

# Guideline # 12

## Permissible Differences in Compensation

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### PAY EQUITY IMPLEMENTATION SERIES

The *Pay Equity Implementation Series* is designed to help employers, employees and bargaining agents to achieve pay equity and to understand their rights and obligations under the *Pay Equity Act*, R.S.O. 1990, c. P7, as amended (the *Act*). These guidelines do not restrict review officers of the Commission or the Pay Equity Hearings Tribunal in their interpretation of the *Act*. The series is published in a sequence that generally reflects the steps for implementing pay equity. (**Revised Summer 2002**).

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### SIGNIFICANCE

The *Pay Equity Act* allows certain exceptions to using the maximum job rate when calculating the differences in compensation among incumbents of a job class and between job classes. These exceptions are called permissible differences, and where applicable, they allow employers to exclude a portion of the compensation of male and female job classes when making pay equity comparisons to determine pay equity adjustments.

The five permissible differences are:

- a formal gender neutral seniority system
- a temporary training or development assignment
- a merit compensation plan based on formal performance ratings which has been brought to the attention of the employees
- red-circling
- a skills shortage causing a temporary inflation of compensation.

The use of a permissible difference to exclude a portion of the compensation of a male job class from the comparison process does not exclude the male job class itself from being used as a comparator. Also, the workplace parties must follow the process for determining job rate, as set out in Guideline #11. Given the purpose of the *Act* to remedy discrimination against women's jobs, permissible differences should be construed narrowly. The onus is always on the employer to show that a permissible difference exists. Any permissible difference used must be clearly described in the pay equity plan.

## EXPLANATION

### 1. Formal Seniority System

Seniority systems provide increased pay to employees based on their length of service, so that incumbents within a job class may be making different rates. However, all incumbents in the job will be able to achieve the maximum rate. The maximum rate, which is achieved after the required length of service, is the job rate for the job class.

When comparing male and female job classes, either of which are paid on a seniority system, the maximum rate is used as the job rate. An incumbent in a male job class may be paid a higher rate because of a greater length of service. However, the two comparable job classes must have the same job rate or maximum. The difference in pay of the incumbents of the two jobs is permissible provided:

- The seniority system is formalized and known to employees; and
- The system does not discriminate on the basis of gender.

Where an employer has a seniority system, the wage gap between comparable male and female job classes is the difference between the job rate (highest rate) for a female job class and the job rate (highest rate) for its male comparator.

#### Example

ABC Company has compared the female job class of Clerk to the male job class of Driver. The most senior employee in the Clerk job class has been there for 9 months, and the most senior employee in the Driver job class has been there for 3 years. The following wage grids were in place at the effective date of the pay equity plan:

Job Class	Start rate	6 months	1 year	2 years
Clerk	\$10.00	\$10.75	\$11.50	\$12.50
Driver	\$11.00	\$11.90	\$12.75	\$14.00

In this case, the difference between the job rates (highest rates) for the Clerk and the Driver is \$1.50. The actual difference between compensation paid to the incumbents in the female job class (\$10.75) and the male job class (\$14.00), however, is \$3.25. In this case the employer may claim a permissible difference of \$1.75 (the difference between the incumbents' rate and the amount of the wage gap) because the seniority system accounted for an identifiable portion of the difference in rates.

In order to demonstrate that the seniority system does not discriminate on the basis of gender, an employer must be able to show that the job rate for the male job class is equally available to incumbents in the female job class(es) for which it was the comparator, provided that the principles for determining seniority are the same.

### 2. Temporary Employee Training or Development Assignment

Training assignment rates are often different than the regular rate paid to the incumbent of a job class. For example, management trainees are often rotated through a number of non-managerial job classes as part of their training. Their pay may be at the rate of their management job class and higher than that of their co-workers who fill the job classes - lower valued, lower paid job classes - on a permanent basis. On the other hand, sometimes trainees continue to receive the wage of their "home" position throughout the training period, even though they may be performing work of higher value.

If a temporary training assignment meets the following conditions, the portion of the rate paid to the incumbent in training that exceeds or is lower than the regular rate of pay would not be used for comparison purposes. To qualify as a permissible difference, a temporary training or development assignment:

- Is equally available to female and male employees;
- Leads to career advancement for employees in the program;
- Is temporary for each employee involved, either of a fixed duration, or until a specific goal is achieved; and,
- Identifies the normal job rate for the job class.

### 3. Formal Merit System

A merit system may be the basis for a permissible difference in the rates paid to incumbents in compared job classes if an employer is able to show that the difference is based on a performance rating system which:

- Is based on *formal* performance ratings, with systematic ratings of how well employees are performing. These ratings must be applied consistently to employees, at regular and defined intervals and must be related to pay levels or increases;
- Was brought to the attention of employees in some formal and consistent way;
- Does not discriminate on the basis of gender; and,
- Identifies the normal job rate for the job class.

An employer may have a merit system where a “reference rate” is identified for a job class. This reference rate is paid to an employee who performs his/her work in a fully competent manner. Employees that exhibit exceptional performance would be paid above that reference rate.

For example, prior to implementing pay equity, this employer had a merit system that indicated the following pay rates for jobs of different values:

Points	Pay Bands	Start/ Developmental	Full Performance (Reference Rate)	Exceptional Performance
100-150	1	\$8.00	\$9.50	\$11.50
151-200	2	\$9.00	\$10.75	\$13.00
201-250	3	\$10.00	\$12.00	\$14.00

The job rates in the above pay bands are \$11.50, \$13.00, and \$14.00 respectively.

A female job class in band 2 is evaluated for pay equity purposes using a gender neutral comparison system, the outcome of which is that the job class is found to be a Band 3 job. An adjustment of \$1.00 per hour is required (this is the wage gap between band 2 and 3). Nevertheless, the real difference between what is actually paid in band 2 and band 3 may be greater than \$1.00 if, for example, the incumbent in the comparator job class is paid \$14.00 (for proven exceptional performance) and the highest paid to an incumbent in the band 2 female job class was paid \$10.75 (for full performance). It is important to remember that these compensation differences are tied to a merit system that has the characteristics of a formal system as described above.

To ensure that a merit system is gender neutral, an employer should assess its performance criteria in a similar way as they would select sub-factors in a gender neutral comparison system (see guideline #9). Similarly, employers should check the results of their merit systems to ensure that females and employees in a female dominated job

classes are as well represented at higher performance and pay categories as males and employees in male dominated job classes. Where the merit exception is relied upon, the actual job rate, including merit considerations, for the male job class must be equally available to incumbents in the female job class.

#### 4. “Red-Circling”

Red-circling, under the *Act*, has a very limited application:

- The value of a position must *have been* downgraded, based on a gender-neutral re-evaluation process, prior to the effective date of the pay equity plan.
- The compensation of the incumbent *has been* frozen or pay increases *have been* curtailed until the lower compensation rate attached to the new lower-valued position catches up.

For example, if prior to the effective date of a pay equity plan, the duties and responsibilities of a job class changed significantly, the position may have been re-evaluated, and as a result, assigned a lower value. In this case, an incumbent may keep the compensation tied to the former value of the position, but have future increases frozen or curtailed until the lower pay rate attached to the new lower-valued position catches up. The difference between the current pay for the incumbent and the job rate determined for the job class may be excluded for comparison purposes.

Where red-circling is established at or after the time the pay equity plan was to be posted, the red-circling exception cannot apply. The full difference between the job rate for the female job class(es) and the job rate which applied to the male job class at the date that a pay equity plan was due, represents the gap to be addressed. Only after this has been closed can the female job class be red-circled in the same manner as its male comparator.

No employee’s compensation can be reduced in order to achieve pay equity.

#### 5. Skills Shortage

The *Act* permits differences in compensation resulting from a skills shortage if:

- The employer can demonstrate a skills shortage is causing a temporary inflation in compensation;
- The employer can demonstrate difficulties in recruiting employees with the requisite skills for positions in the job class; and
- The job rate for the job class is identifiable.

The Pay Equity Hearings Tribunal gave direction in *Melitta Canada Inc (No.2) (1995) 6 P.E.R. 214*, that an employer must be able to defend that a skills shortage exists and that it has encountered difficulties in recruiting for a job class as a result. For example, an employer should consider whether the job positions have been advertised broadly in the media without success, the length of time the search has gone on and whether internal candidates have been trained and are now available. Employers could refer to outside data, such as labour market surveys, to help demonstrate a skills shortage, but they would still have to show difficulty in recruiting.

Employers are likewise required to demonstrate that any skills shortage upon which they rely are temporary. Skill shortages may be temporary when, for example, there are insufficient graduates in an occupation or specialty at a given time, but there is evidence that more qualified people will be graduating or moving into the relevant market at an identifiable future date. This permissible difference, however, should not be used to

justify all market stresses. Job rates reflecting long standing inflation due to past skills shortages would likely not be exempt under this section.

**Example:** When a company installed a widget-making system in 1982, widget-makers (a male job class) were in high demand and the company had to increase the pay offered to attract and retain staff. Within three years the situation changed. Students, attracted to the increased pay, flocked to widget-making courses. There were plenty of candidates and entry-level salaries did not increase as fast as other salaries. Widget-makers did receive, however, increases in line with others in the company. If a female job class is compared to the male job class of widget-maker, the difference in their salaries would not be justified, on the basis of the original skills shortage. On the other hand, if the skills shortage was still in effect, some differences in compensation based on the skills shortage may be permissible.

## RELEVANT SECTIONS IN THE ACT

Subsection 1(l)	Defines compensation, job rate.
Section 6	Defines the achievement of pay equity using the Job-to-job comparison method.
Subsection 8(1)	Defines permissible differences in compensation.
Section 21.3	Defines the achievement of pay equity using the proportional value comparison method.
Section 21.15	Defines the achievement of pay equity using the proxy comparison method.

## REFERENCES:

*Pay Equity Implementation Series (Revised) - Guideline #5: Determining Job Class*  
*Pay Equity Implementation Series (Revised) - Guideline #7: Determining the Gender Predominance of Job Classes*  
*Pay Equity Implementation Series (Revised) - Guideline 9: Gender Neutral Job Comparison*  
*Pay Equity Implementation Series (Revised) - Guideline #10: Which Job Classes to Compare*  
*Pay Equity Implementation Series (Revised) - Guideline #11: Determining Job Rate*  
*Melitta Canada Inc. (No. 2) (1995) 6 P.E.R. 214*  
*Welland County General Hospital (1994) 5 P.E.R. 12*

## **For More Information:**

We are here to help. We can answer your questions by e-mail at <mailto:Pecinfo.Pecinfo@ontario.ca> or by phone at (416) 314-1896, or toll-free at 1-800-387-8813. You can also register for a free seminar. Visit our website at <http://www.payequity.gov.on.ca/peo/english/seminar.html>

**All communications are confidential.**

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### **The Pay Equity Commission**

**This fact sheet is for information only, and is not intended to restrict Review Officers or the Pay Equity Hearings Tribunal in their determination of matters. Refer to the *Pay Equity Act* for exact interpretation.**

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