

HR Insights

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Different Types of Raises and How to Communicate Them With Employees

Pay increases aren't one-size-fits-all. Employers use several types depending on their goals, budget and workforce needs, and these differences matter more than many organizations realize. A merit increase signals something very different to an employee than a standardized across-the-board adjustment, even if the dollar amounts are similar. Understanding the distinctions helps organizational leaders make more consistent, defensible compensation decisions and have productive conversations with employees when it's time for raises.

Each year, employers make decisions about how they want to approach annual increases. This article provides an overview of the most common types of raises and employer guidance on how to communicate them effectively.

Types of Pay Increases

Compensation decisions are rarely simple. Employers must weigh individual performance, market competitiveness, budget constraints and employee expectations, often simultaneously. It's important to understand the different types of pay increases and what they are meant to accomplish.

Merit Increase

Merit increases reward for individual performance. These pay-for-performance adjustments are designed to improve employee productivity, engagement and retention by tying compensation directly to results. Merit increases are typically awarded during performance review cycles and vary based on employee evaluation outcomes, making clear, consistent

performance criteria essential before any raise conversations happen.

Cost-of-Living Adjustment

A cost-of-living adjustment (COLA) is an annual or biannual increase that accounts for inflation, helping employees maintain their purchasing power. COLAs reflect economic conditions and are not tied to organizational, team or individual performance. This type of increase is meant to help employees maintain a lifestyle, not improve it. Employers often reference national inflation data or even local cost-of-living indexes when determining the appropriate percentage.

Standardized Increase

Sometimes called "peanut butter" raises, standardized increases apply the same percentage or dollar amount to all employees within a department or the entire organization. These increases typically range from 2% to 4%, though this varies by industry, company size and economic climate. While these increases benefit employees because everyone receives the same opportunity for higher wages, top performers may feel frustrated knowing they received the same raise as those who underperformed, which may cause them to disengage. As such, employers who use this approach should be prepared to address that tension directly.

Base Wage Raise

A base wage adjustment, also known as a salary band increase, is tied to the market rate. Employers research salaries at organizations in their industry or region that offer similar job types. The goal is to understand the highest and lowest salaries. From there, employers can set the base salary to remain competitive. These increases are used to ensure the organization's pay bands for roles reflect current market conditions and are competitive with other opportunities.

Promotional Increase

A promotional increase accompanies a change in job title or role, reflecting the expanded scope and responsibilities of the new position. These raises are typically larger than annual merit increases, and the appropriate amount may depend on market value, recent increases and what other teammates in the department are earning. These types of raises should be communicated with an explanation of what the new title or role entails and what was recognized in the employee's performance that led to the promotion.

Other Types

Beyond those popular categories, employees may also encounter other forms of compensation that fall outside the scope of a standard pay increase. Other examples of how organizations can reward employees beyond base salary include equity adjustments (to reduce wage gaps or align pay for tenured employees with new hires), equity compensation (e.g., stock options or restricted stock units that give employees an ownership stake in the organization), bonuses tied to individual, team or company performance, and completion increases for finishing milestones such as training or a probationary period.

These types of adjustments address total compensation broadly, whereas pay increases specifically refer to changes in an employee's base pay. While HR and legal frameworks generally rule these elements, it's still important for employers to acknowledge them to help employees understand their total compensation.

Other Considerations

One particular aspect of pay increases that often catches employees off guard is that different types aren't mutually exclusive. An employee might receive a COLA and a merit increase in the same review cycle. In that case, one reflects economic conditions, while the other recognizes individual performance. Similarly, a promotional increase may be layered on top of an annual adjustment. When multiple increases apply, employers should communicate each one separately and explain the rationale behind each. Bundling them into a single number without context can obscure the meaning behind the decision and make even a generous raise feel arbitrary.

Communicating Pay Increases to Employees

While the raise itself is a top priority for workers, how it is communicated can also make a difference, for better or for worse. Employees who understand why they received (or didn't receive) a certain pay increase are more likely to feel valued and stay engaged. Consider the following scenarios and relevant communication strategies:

- **When increases are standard or strong,** be specific about what drove the decision. Whether it was performance, market alignment or a company-wide adjustment, employees benefit from context. Vague messaging (e.g., "the company values your contributions") could potentially undercut the impact of a meaningful raise.
- **When increases are limited or nonexistent,** communication is critical but often becomes difficult. Communicating limited or no pay increases requires transparency and empathy to maintain trust, engagement and morale. Organizational leaders should acknowledge the situation directly, explain the business or economic context honestly and avoid overpromising future increases. If the organization is struggling financially, employees generally respond better to honesty than to ambiguity.
- **When communicating with underperformers,** a lower-than-expected merit increase should never come as a surprise. If performance concerns reflect an employee's raise, or lack of raise, they should have been documented and communicated throughout the review cycle, rather than introduced during the raise conversation. It's important to frame the salary discussion around what the employee can do differently, and tie any future increases to specific, measurable goals.

Conclusion

Pay increases are one of the most direct signals an employer sends about how it values its people. Getting the type of pay bump right matters, but so does the

conversation around it. Trust is built or maintained when employees understand not just what they're receiving but why, even when the news isn't what they hoped for. A clear, consistent approach to both compensation decisions and communication is what separates organizations that retain top talent from those that don't.

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