

## **Executive compensation: influence and reciprocity effects**

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### **Abstract**

**Purpose** – The purpose of this paper is to understand the effects of influence and reciprocity as elements in the determination of executive compensation.

**Methodology** - A purposive sample was drawn, which comprised 13 respondents chosen for their expertise relating to the determination of executive compensation in state-owned enterprises. A semi-structured interview guide was used as the data-gathering instrument. A thematic analysis technique was used for data analysis.

**Findings** - The findings in this study identified three themes resorting under influence as crucial in the process of determining executive compensation, namely an executive's social capital, intellectual capital and social comparison. Two major themes emerged under reciprocity, namely the pay-performance relationship and role complexity. Lastly, the political-symbolic role emerged as the main theme that described the relationship between influence and reciprocity.

**Practical implication** - The findings provide a more detailed description of the process involved in determining executive compensation in state-owned enterprises.

**Originality/value** - There has been limited if any, empirical study on the process involved in setting executive compensation. The limited focus has always been on accounting measures. Incorporating the socio-psychological view attempts to provide a more comprehensive and conclusive explanation of the process of determining executive pay in theory and practice.

**Keywords:** influence, reciprocity, socio-psychology, state-owned enterprises, executive compensation.

**Paper type** Research paper

## **Introduction**

Although research on executive compensation continues to proliferate and determinants of executive compensation have received substantial attention from both academics and regulators, there is still no interdisciplinary consensus on the primary forces shaping observable patterns of executive compensation (Baxamusa 2012; Shaw and Zhang 2010; Tosi et al. 2000; Van Essen, Otten and Carberry 2012). The lack of consensus is most visible between scholars in economics and finance, who advocate the primacy of market-based explanations and scholars outside these two disciplines, who have challenged these explanations and some of their underlying assumptions by highlighting the importance of the power of socio-psychological processes in the creation of compensation practices (DiPrete, Eirich and Pittinsky, 2010).

Prior to this research, there has been limited, if any, empirical study on the process involved in setting executive compensation. The limited focus has always been on accounting measures and traditional performance measures such as return on assets, return on equity or market performance (stock return) as criteria for determining executive compensation (de Wet, 2012; Li, Lou, Wang and Yuan, 2013). However, research by Wu and Wu (2010) found that, except for the return on assets indicator, there is no obvious positive correlation between executive compensation and other indicators, such as asset convertibility, that represent cash performance and the stock yield representing the wealth of shareholders. In particular, the debate on executive compensation focuses primarily on how much executives are paid (Fleming and Schaupp, 2012; Scholtz and Smit, 2012; Theunissen, 2010) and less on the process that determines executive pay. However, discourse on executive compensation needs to focus on socio-psychological processes in the determination of executive compensation. According to DiPrete et al. (2010), a more conclusive understanding of executive pay would be achieved by considering executive pay as an outcome of a social process in which the actors involved have considerable discretion to influence the outcomes.

Branch, Farris and Haskins (2011) capture the social mechanism of pay determination by stating that ‘the realities that some compensation outcomes are a result of a negotiation as opposed to a quoted market price must be considered’ (p. 83). Similarly, Lorsh and Khurana (2010) contend that for senior executives, the compensation arrangements, in reality, depend heavily on negotiations between the executive, and usually his attorney, and the compensation committee and its advisers. These negotiations cover not only the amounts to be paid but also the form of

compensation, as well as the performance metrics, if any, to which these are to be related (Lorsh and Khurana, 2010). Incorporating the social and psychological views attempts to provide a more comprehensive and conclusive explanation of the process of determining executive pay in theory and practice (Otten, 2007). In the same way, this study is designed to explore mechanisms of which the socio-psychological elements of influence and reciprocity are explored in the process of setting executive compensation.

### **Influence**

A number of studies have demonstrated that executives can increase their pay beyond what is justified by economic determinants through exercising their influence (O'Reilly, Doerr, Caldwell and Chatman, 2014; Shin, 2013; Van Essen, Otten and Carberry, 2014). Many of the empirical and theoretical propositions in contemporary treatments of influence relate variations in influence to other observable variables. For example, studies of the factors associated with leadership, the phenomenon of authority, the persuasion effects of different types of communication content, the formally defined power structure in an organisation and informal relations in a community all assert propositions in which “influence” is a major variable (March 1957).

Similarly, in the current study, influence is expressed in terms of the power an executive possesses. According to Cormier, Lapointer-Antunes and Magnan (2016), one can argue that the formal analysis of power within organisations originates from Maximilian Weber's work on bureaucracies. Weber observes that economic power is the predominant form of power for the modern capitalist and is derived from economic relations arising from control of the means of production (i.e., ownership). Such power is socially constructed and manifests itself in social organisations and networks (Cormier et al., 2016; Lukes, 1974; Stammers, 1999). As explained by Bebchuck and Fried (2003), managers wield substantial influence over their own pay arrangements, and they have an interest in reducing the saliency of the amount of their pay and the extent to which that pay is de-coupled from managers' performance. However, several theories could explain this phenomenon of influence with reference to executive compensation, namely the managerial power theory, the figurehead theory and the social comparison theory.

### *Managerial power theory*

The managerial power theory argues that executive pay is an outcome of power relationships and that pay setters and receivers are able to use discretion in the pay-setting process (Ebert, Torres and Papadakis, 2008; Otten, 2007). Chen, Ezzamel and Cai (2011) identified two types of executive power, namely structural power and prestige power. Structural power, on the one hand, relates to formal positions within an organisation and increases as executives move up the hierarchy. The greater an executive's structural power, the greater his/her control over colleagues' actions to pursue self-interests, including obtaining more pay. On the other hand, prestige power relates to the role of outside directorships and education as key components of prestige, which could result in executives receiving more pay (Li, Moshirian, Nguyen and Tan, 2007). Prestige power also manifests as the executive's positional and expert power, which includes the manager's ability to absorb uncertainty from the institutional environment (O'Reilly, Doerr, Caldwell and Chatman, 2014; Shin, 2013; Van Essen, Otten and Carberry, 2014). Thus, executives can use such prestige power to influence and neutralise efforts designed to restrain their compensation (Van Essen et al., 2014; Westphal and Zajac, 1995).

### *Figurehead theory*

The figurehead theory is another theory that would lead to similar predictions. According to this theory, an executive, especially the CEO, plays a political/symbolic figurehead role when communicating within and outside the organisation (Van Essen, Otten and Carberry, 2014). Political connectedness, which is one form of "social capital", consists of resources available through political social networks that a CEO can use to influence policy decisions that are in the interest of both the executive and the firm (Aslan and Grinstein, 2011).

Aslan and Grinstein (2011) found that political networks are positively related to levels of compensation and negatively associated with pay-performance sensitivity. In particular, the results of their study revealed that a political connection is associated with a 9% increase in a CEOs' annual compensation and a 17% decrease in his pay-performance sensitivity, hence the complexity of the symbolic political role as a token of the executive's mandate and ability to manage reflects the level of executive pay.

### *Social comparison theory*

To complement the managerial power theory and the figurehead theory, literature on executive compensation also relates to the social comparison theory. Social comparison literature focuses on determining which individual or groups are likely to serve as influence and reference when determining executive compensation (Boivie, Bednar and Barker, 2015). Social comparison theory on executive compensation finds expression in the fundamental and pervasive psychological process of social influence.

Social influence, also referred to as social capital (O'Reilly and Main 2010), refers to the resources available through social networks and elite institutional ties (such as club memberships) that an individual can use to enhance his or her position (Belliveau, O'Reilly, and Wade 1996). Social capital can provide important cues – such as the credibility and attractiveness of an executive – that people may use in place of facts when the judgement task is ambiguous when deciding on compensation (O'Reilly and Main 2010).

The social capital of executives influences pay through a process in which executives with greater social status or connections than comparison groups receive higher compensation (O'Reilly and Main 2010). Therefore, it is likely that the social comparison process of anchoring executive pay based on readily available and relevant comparison groups will help to increase executive compensation, since individuals would rarely use social referents as justification to decrease their pay (Boivie, et al., 2015).

Following the aforementioned, the current study, therefore, sought to determine the following research objective:

- To investigate the effects of influence in the determination of executive compensation.

### **Reciprocity**

Another element that applies to the process of determining executive compensation is reciprocity. O'Reilly and Main (2010) extend the concept by stating that reciprocity is a fundamental norm in all societies and pervades both economic and social life. Norms are social expectations of how people ought to behave in a given social context (Bandura, 1991). As a norm, reciprocity dictates that 'When one party benefits another, an obligation is generated' (Gouldner, 1960, p.174). Reciprocity finds expression in the psychological contract an executive enters into with the employer that demonstrates their shared expectations (how one should

behave) and sanctions (what happens if one does or does not conform) (O'Reilly and Main, 2010). The current study, therefore, sought to determine the following research objective:

- To investigate the effects of reciprocity in the determination of executive compensation.

### **The relationship between influence and reciprocity as determinants of executive compensation**

The relationship between influence and reciprocity in the determination of executive compensation is demonstrated by how an executive is rewarded for his/her political connectedness, which in turn benefits the organisation. Although Aslan and Grinstein (2011) found that political networks are positively related to levels of compensation and negatively associated with pay-performance sensitivity, supporting evidence is already available that the political social network connectedness of executives increases their compensation, and that connection-based pay is positively associated with future performance (Horton, Millo and Serafeim, 2012). Similarly, Li et al. (2007) contend that the positive association between executives' political influence and the performance of the firm has also been shown empirically, suggesting that increased compensation arising from the executive's political influence may be rooted in increased firm-level performance. Thus, it is reasonable to assume that executives are aware of the performance-enhancing benefits of their political influence, and in return, organisations may be willing to provide greater compensation because of the associated benefits. Politically connected executives may, therefore, demand higher compensation (Aslan and Grinstein 2011).

The relationship between influence and reciprocity is further demonstrated by the nature of benefits an executive could derive. For example, one reason politically connected managers may be willing to accept less compensation is that they take into consideration the potential opportunities of being politically promoted (Aslan and Grinstein, 2011). Even unconnected managers may be willing to accept less compensation because working for the organisation may allow them to develop their own political connections. Based on the aforementioned, the current study, therefore, sought to determine the following research objective:

- To investigate the relationship between influence and reciprocity in the determination of the executive compensation process.

The remainder of this paper is organised as follows: The first section describes a summary of the methodology followed and presentation of the findings. The paper concludes with a discussion of influence and reciprocity, and the relationship between the two constructs in the determination of executive compensation. What follows is a description of the methodology and research design adopted for the current study.

## **Methodology**

Several scholars advocate different paradigms (worldviews) and philosophies that underpin knowledge production (Bryman and Bell, 2011; Guba and Lincoln, 1994; Habermas, 1972; Zikmund, Babin, Carr, and Griffin, 2013). Although there are differences in scholars' advocacy of research philosophies that include among others interpretivism, realism, and positivism (Saunders et al., 2012; Sekeran and Bougie, 2010; Srivasta and Rego, 2011), a common theme is that no knowledge is neutral, and all research is embedded in philosophical preferences. From an epistemological stance, this research adopted an interpretivist approach that advocates subjective views of the phenomenon under study.

## **Research design**

A research design refers to the overall research plan. It is a strategic framework for action that serves as a bridge between research questions and the execution or implementation of the research (Terre Blanche et al. 2006, p. 34). This plan stems from the objective of the study. The research design followed in the current study is discussed according to the sub-headings below.

### *Research strategy*

A research strategy may be defined as a plan of how a researcher will go about answering a research question (Saunders et al., 2012). It is the methodological link between the research philosophy and subsequent choice of methods to collect and analyse data (Denzin & Lincoln, 2005). The research strategy employed in this study consisted of a phenomenological study. The phenomenological study was employed as a means to understand the perception of key informants about executive compensation in the context of South African state-owned enterprises (SOEs). A researcher applying phenomenology is concerned with the lived experiences of the people (Greene, 1997; Holloway, 1997; Kruger, 1988; Kvale, 1996; Maypole

and Davies, 2001; Robinson and Reed, 1998) involved, or who were involved, with the issue being researched (Groenewald, 2004). According to Giorgi (as cited in Groenewald, 2004) the operative word in phenomenological research is 'describe'. The aim of the researcher is, therefore, to describe as accurately as possible the phenomenon, refraining from any pre-given framework, but remaining true to the facts.

### *Participants and setting*

A purposive sample of SOEs was used for the study. In purposive sampling, the sample is chosen for a particular purpose (Leedy and Ormrod, 2013, p. 215). The researcher needs to use judgement to select cases that will best enable him/her to answer the research question(s) and to meet research objectives (Saunders et al., 2012). A key component of a purposive sampling is, therefore, the 'depth' of data in order to gain deeper understanding rather than to generalise or to focus on the frequency (O'Reilly and Parker, 2012; Terre Blanche et. al., 2006).

In order to clarify concerns about the sample size, Cresswell (2007) suggests that a heterogeneous population would require between 25 and 30 interviews, while semi-structured/in-depth interviews require a minimum sample size of between five and 25 (Saunders et al., 2012). In this study, the sample was drawn from the directory of South African SOEs, which entails a population of more than 700 enterprises. However, only those SOEs that had been categorised under Schedule 2 of the Public Finance Management Act of 1999 (PFMA) and fell under the Large Group Business Enterprises category, were considered.

The Schedule 2 group of SOEs consists of 21 SOEs. The reason for selecting only Schedule 2 enterprises was that they were the only entities among all the South African SOEs that were large and competed directly with the private sector in particular.

However, of the 21 Schedule 2 SOEs, only 13 enterprises were interviewed. A single research participant represented each SOE at the interview. The sample size of 13 representatives from various SOEs sufficed for the study, since the sample was from a homogenous population (i.e. Schedule 2 SOEs).

Table 1 shows a list of the participants along with information on their position in their organisations.

**Table 1:** Characteristics of participants

Interviewee	Organisation	Position in the organisation	Gender & Age
1	Company 1: - Development Finance (RP1)	Group Executive HR	Female (33)
2	Company 2: Development Finance (RP2)	Senior Manager Remuneration	Female (40)
3	Company 3: Development Finance (RP3)	Senior Manager Reward and Remuneration	Male (37)
4	Company 4: Aviation 1 (RP4)	Manager Remuneration and Benefits	Female (45)
5	Company 5: Freight and Logistics (RP5)	Divisional Executive Manager HR	Male (42)
6	Company 6: Energy (RP6)	Manager HR	Female (36)
7	Company 7: Telecommunications (RP7)	Manager HR	Female (39)
8	Company 8: Communications (RP8)	Manager Remuneration	Male (40)
9	Company 9: Aviation (RP9)	Senior Manager	Female (46)
10	Company 10: Aviation (RP10)	Human Resource Manager	Male (43)
11	Company 11: Communications (RP11)	Manager Remuneration	Male (45)
12	Company 12: Energy (RP12)	Remuneration and Rewards Manager	Female (40)
13	Company 13: Defence (RP13)	Human Resources Manager	Female (48)

\*(RP) represents research participant

#### *Data collection*

Data were collected using one-to-one semi-structured interviews (one hour in length) with representatives and experts in the field of executive compensation in South African SOEs. Semi-structured interviews were preferred, since they usually have an overarching topic, general themes, targeted issues and specific questions, with a predetermined sequence for their occurrence (Lee, 1999). In addition, a conversational interview technique was used to collect data. The conversational interview technique was deemed suitable since its major characteristic

is its openness. It also allows the researcher to address several issues of thematising, design, situation, criteria for evaluation and transcription as they relate to conversational interviews (Lee, 1999, p.81)

### *Procedure*

Participants were interviewed in a secured office away from their desks and free from interruption by a ringing phone or working colleagues. The researcher asked permission to use a tape recorder to capture a verbatim account of the interview for processing at a later stage. The participants consented to have interviews tape-recorded. However, the participants remained anonymous.

### *Trustworthiness*

The issue of trustworthiness in qualitative research is important to the practice of good science (Streubert and Carpenter 1999, p.61). Several writers on research methods have demonstrated how qualitative researchers can incorporate measures that deal with these issues in their own qualitative studies (Shenton, 2004). For this study, Guba's model for qualitative research was used with the aim of ensuring the trustworthiness of the findings. The four criteria to ensure the trustworthiness of this research were credibility, transferability, dependability and confirmability (Guba, 1981; Krefting, 1991; Lincoln & Guba, 1985; Terre Blanche and Durrheim, 2002).

In addressing credibility, investigators attempt to demonstrate that a true picture of the phenomenon under scrutiny is being presented (Shenton, 2004). In this study, to achieve credibility, the interviews were all tape-recorded and notes were transcribed with the assistance of a professional transcriptionist. The transcribed responses were checked against the tape recordings for consistency, in order to ensure the integrity of the research data (Guba and Lincoln, 1994; Krefting, 1991; Schurink; Fouche and de Vos, 2011; Terre Blanche and Durrheim, 2002). As a follow-up from the initial interviews, the researcher wrote analytic notes and held analytic meetings with other experts in qualitative analysis to capture the initial thinking and tentative ideas about the data. This was done to ensure that the views of the participants and the reconstruction of those views by the researcher coincided (Schurink et al., 2011). Transferability in this study was achieved by the researcher richly describing the data and providing exact definitions of constructs as determined by the literature reviewed and cross-

validation with experts in executive compensation. To achieve dependability, the researcher entered the interviews with a predetermined interview schedule containing specific questions with the intention to pursue emergent topics and to probe more deeply than the initially planned questions (Lee, 1999, p.62). Subsequently, the researcher documented the research process in a logical and well-structured manner for ease of coherence and understanding (Schurink et al., 2011). Finally, regarding conformability, bracketing was used throughout the data collection process so that the researcher could suspend any preconceived notions or personal experiences that would unduly influence what he 'heard' the participants saying (Saunders et al., 2012).

### *Data analysis*

Thematic analysis was adopted as a method to analyse data. As described by Braun and Clarke (2006), thematic analysis is a method for identifying, analysing, and reporting patterns (themes) within data. It is for its contextualist strength that thematic analysis was chosen for the current research. The mode of thematic analysis followed for this study was the meaning condensation technique (Lee, 1994). As the name suggests, meaning condensation involves data reduction, while simultaneously articulating the key emerging themes from transcripts containing interview data (Boyatzis, 1998; Braun and Clark, 2006; Lee, 1994; Yin, 1994).

Meaning condensation as adopted in this study involved five basic steps (Lee, 1994). First, the author read the entire transcript of the interviews. Secondly, portions of the text that were judged to relate to an identifiable theme were identified. Subsequently, the natural meaning units were clearly defined and arranged into themes with subthemes based on the actual responses of the participants, using a software package (Atlas ti.).

## Findings

Findings were condensed under the two variables investigated, namely influence and reciprocity. Under influence, three themes emerged, namely social capital, intellectual capital and social comparison. Two main themes emerged under reciprocity, namely the pay-performance relationship and role complexity. Lastly, the political-symbolic role of the executive emerged as the theme that described the relationship between influence and reciprocity. The findings are presented next.

## Influence

### *Social capital as influence in the determination of executive compensation*

Table 1 indicates the broad theme and the sub-theme, including examples of original responses that were analysed.

Table 1: Social capital

Theme	Sub-themes	Response
Social capital as influence	Executives' relationships and stakeholder engagement	<p><i>"... being able to engage a stakeholder is critical because this is about relationships and making sure that you leverage into the customer ..."(RP2)</i></p> <p><i>"... So you have to manage stakeholders that are very critical to the economy of the country to grow. And that becomes a big determinant of the level of compensation, "(RP9)</i></p> <p><i>"... this is somebody who is able to leverage relationships, this is somebody who is a strategist, somebody who is international savvy in the sense that he can talk to investors from China that are coming to help us build work for locomotives for one of our operating divisions ..." "(RP7)</i></p>

(RP stands for research participant)

The main theme that emerged from the interviews was the executives' social capital as an influence in executive compensation. Social capital was described as the executives' relationships and network with key government stakeholders. The executives' influence was expressed as the ability to command respect among their peers and the international community at large. Thus, social capital was perceived as the executives' ability to network and engage with critical stakeholders for the success of the organisation and in turn, be rewarded accordingly.

Similarly, the importance of the stakeholder relationship was extended to relate to the executives' ability to subscribe to the regulatory bodies that govern SOEs.

Overall, the responses of the participants indicated that executive compensation is determined by executives' ability to engage with various stakeholders who are critical to the delivery of the organisations' strategic intent that would, in turn, influence the level of executives' compensation. Thus, the executive is able to influence his or her level of compensation through social networking.

*Intellectual capital as influence in the determination of executive compensation*

Table 2 indicates the broad theme and the sub-theme, including examples of original responses that were analysed.

Table 2: Intellectual capital

Theme	Sub-themes	Response
<b>Intellectual capital as influence</b>	Leveraging on institutional knowledge	<p><i>"... somebody that has a big picture view of the company." (RP8)</i></p> <p><i>"... there is a lot of institutional knowledge which we need somebody to leverage on and to be able to deliver." (RP4)</i></p> <p><i>"... we look at the experience ... what the incumbent has done previously ..." (RP9)</i></p> <p><i>"... as a state-owned enterprise you need to be aware of the environmental legislation, you need to be aware of PFMA, Treasury regulations." (RP3)</i></p> <p><i>"... there is a lot of socio-economic factors at play. It has to be somebody that understands our labour union environment because a strike could have a catastrophic impact on the economy. "(RP11)</i></p> <p><i>"It is purely based on the knowledge and on what you could offer as an incumbent ..."(RP6)</i></p>

Research participants were of the opinion that executives with advanced institutional knowledge of the organisation were at an advantage in negotiating better pay and increases than executives who had joined the organisation later. They believed that knowledge acquired over time on the functioning of an SOE and the environmental legislation that governed such entities gave an

executive an edge to negotiate for better compensation, compared to other executives who might be lacking such institutional knowledge. In addition, research participants contended that as part of institutional knowledge, the educational background together with acquired experience facilitated understanding of the socio-economic factors that put an executive at an advantage to ‘manage effectively and in turn be rewarded accordingly’.

Overall, it is apparent from the responses of the participants that an executive is able, to some extent, to influence his or her level of compensation using institutional knowledge. Such knowledge is acquired over time on the functioning of an SOE and the environmental legislation that governs the entities. Executives use acquired institutional knowledge to negotiate for better compensation, compared to that of other executives who may be lacking such knowledge.

*Social comparison as influence in the determination of executive compensation*

Table 3 indicates the broad theme and the sub-theme, including examples of original responses that were analysed.

Table 3: Social comparison

Theme	Sub-themes	Response
<p><b>Social comparison</b></p>	<p>Benchmarking</p>	<p>"... I probably can be able to easily find an executive of human capital than find a CFO." (RP8)</p> <p>"... In our organisation branding is important, thus the communication executive would be considered to be very important, maybe more than a finance person..." (RP4)</p> <p>"... When you talk resource management, the CFO will have more responsibilities to manage financial resources compared to the human resources executive" (RP10)</p> <p>"... the corporate services executive, which is responsible for more than what a human capital executive does outside our organisation? So they are in charge of the human capital, in charge of marketing, in charge of IT and facilities. So we look at what's the content of their jobs, and what is the influence to the organisation as a whole ..."(RP 9)</p>

The theme that emerged in the interview was the role of comparison as a key determinant in setting executive compensation. Research participants contended that SOEs deliberated on which peer groups to consider when setting executive compensation relevant to a specific executive. However, arriving at the level of a suitable compensation package was in most cases informed

by the job function of the executive compared to other executive positions within and beyond the SOE. Research participants mentioned that the setting of executive compensation involved the remuneration committee that was tasked with making sure that the proposed packages were competitive enough to attract and retain an executive.

Research participants highlighted the fact that it was important to identify the correct market or industry in order to make comparisons and to benchmark executive compensation accordingly. However, research respondents mentioned that the competitive market according to which executive compensation could be set was not clearly defined for ease of reference and comparison. Overall, the nature of the market or typical industry that SOEs used to set executive compensation was important. In order to identify the correct benchmark, SOEs employed the services of external consultants to assist them. Consultants are used to interpreting the trends and to come up with estimates of executive compensation. This would seem to mean that the type of industry would be more influential in the determination of the level of executive compensation.

## Reciprocity

### *Pay performance relationship*

Table 4 indicates the broad theme and the sub-theme, including examples of original responses that were analysed.

Table 4: Pay performance relationship

Theme	Sub-theme	Response
<b>Pay performance relationship</b>	Shareholder expectations	<p><i>"... the executive understands that you have to do certain things that give investors the comfort that the organisation is run very well, which is efficient with all the measures, the internal controls are there. You are taking care of the brand." (RP7)</i></p> <p><i>... the comfort that the organisation is run on well-established business principles and processes ..." (RP2)</i></p> <p><i>"... executives should perform their deliverables in terms of what is stipulated in the strategy ... the annual salary increase will be linked or will be performance based ..." (RP6)</i></p> <p><i>The Board do the final approval of the executive compensation. So they will provide inputs, they will provide a whole range of things they feel should be taken into consideration from the strategy point of view ...." (RP12)</i></p>

Research participants perceived remuneration as being determined by performance measures that are aligned to the strategic intent and business plans of the organisation. The strategy details key performance indicators and focuses the effort and attention of individuals on the strategic deliverables for long-term sustainability, as well as on short-term business plan deliverables for profitability, both of which are imperative to shareholder value creation. Thus, an executive will be compensated for delivering results according to the performance targets of the organisation. Overall, executive compensation is perceived as performance-driven and depends on its affordability for the organisation. Market conditions, which determine the supply of and demand for executive skills, also play a role in the determination of executive compensation.

*Role complexity*

Table 5 indicates the broad theme and the sub-themes, including examples of original responses that were analysed.

Table 5: Role complexity

Theme	Sub-themes	Response
<b>Role complexity as influence</b>	Impact considerations	<p><i>"... with the organisation that needs to be turned around, you may decide to compensate the chief executive more, because turning around the organisation is different from maintaining what is already the status quo." (RP2)</i></p> <p><i>"... if this executive makes a decision which is wrong, what would be the impact on the economy ..." (RP4)</i></p> <p><i>"... For a company like ours which has a definite link to the performance of the entire South African economy, the role of an executive becomes a critical factor in the determination of pay." (RP8)</i></p> <p><i>"... not all executives are created equally. You always consider what the impact of the role to the position is ... and then reward the executive accordingly" (RP10)</i></p>

Respondents viewed the complexity of the role as influential in the determination of executive pay. The complexity of the role of an executive was viewed in terms of its impact not only on the organisation in relation to other executive positions but also in terms of its contribution to the economy of the country. According to the research participants, the executive's role and mandate are intended for social and economic advancement.

In addition, the research participants emphasised the impact of the role as the main differentiator in the level of executive compensation, but also extended the impact element to include the dynamics of size and complexity of the organisation as influential in the determination of executive compensation.

Overall, the complexity of the role as an influence on the level of compensation involves the executives' ability to manage size not only in terms of the number of employees but also in terms of the complexity and ability to generate and manage large amounts of revenue. In turn, the challenge and difficulty of the position in generating the necessary revenue are reflected in the level of compensation due to the executive.

### **Relationship between influence and reciprocity**

#### *Political symbolic role*

Table 6 indicates the broad theme and the sub-theme, including examples of original responses that were analysed.

Table 6: Political symbolic role

Theme	Sub-theme	Response
<b>Political symbolic role</b>	Political mandate	<p data-bbox="824 1129 1432 1318"><i>“The Minister has always intended to set parameters for SOEs for a long time. So when we give him our final recommendations for salaries for noting, he does come back with comments and say listen beware of the media, and if you going to give high bonuses you must understand its implications to the public” (RP8)</i></p> <p data-bbox="824 1348 1432 1495"><i>“... we run the risk of offending the Minister should we dare to compete with the private sector by paying huge salaries. Taking that risk will invite unnecessary press attention. And the media also becomes a challenge.” (RP2)</i></p>

The relationship between influence and reciprocity finds expression in the complexity of the political role played by the executive. Research participants highlighted the importance of the political mandate that executives should carry in order to fulfil the developmental mandate of the SOEs. The critical stakeholder is the government represented by the Minister, who indirectly

influences the level of executive compensation. Executive compensation is expected to be in alignment with the expectations of the Minister and members of the public.

The overall finding is that executives are compensated for the political role they play to the benefit of the SOEs in meeting their obligation in terms of the developmental mandate. Moreover, it is important that executive compensation does not exceed the expectations of members of the public and does not spark unnecessary debates about social inequality.

### **Discussion and conclusion**

The findings support the role of the two main elements under study, namely influence and reciprocity, in the determination of executive compensation. Influence has been described in terms of the social capital, intellectual capital and comparability of an executive in relation to compensation. Reciprocity has been described by the pay-performance relationship and the complexity of the executive role, while the relationship between influence and reciprocity has been described by the political-symbolic role of the executives in the determination of executive compensation.

### **Influence**

Based on the findings, one of the themes that emerged under the heading of influence is that executive compensation is influenced by the social capital of the executive. Social capital has been described as consisting of the social networks established by the executive. The social networks and stakeholder engagement are mostly political in nature. Thus, the executive is recognised and rewarded for his or her political networks and leadership role demonstrated in translating the vision of the SOE to be adopted by employees and accepted by the broader stakeholders who include the main shareholders (the government) and the third parties (communities) they serve.

The findings of the study seem to align with previous literature. For example, Aslan and Grinstein (2011) found that political networks are positively related to levels of compensation. That is, the more the executive is able to establish a network with most of the critical decision makers, especially those with political influence, the easier it becomes for the executive to carry out his or her mandate and thus deliver the required performance. With an increase in the level

of performance comes compensation commensurate with the level of influence exerted by the executive.

The findings of the study also indicated that executives with advanced institutional knowledge of the organisation were at an advantage in negotiating for better pay and increases. Institutional knowledge finds expression in the intellectual capital of the executive. As explained by the research respondents, part of institutional knowledge consists of experience acquired over time on the functioning of an SOE and the ability to apply this and comply with the environmental legislation that governs such entities. Based on the findings, it would also appear that intellectual capital is not considered in isolation, but to the extent to which it contributes to the ability of the executive to establish the necessary social and political networks and to contribute to the developmental mandate of the organisation. Overall, institutional knowledge was perceived as the edge used by the executive to negotiate for better pay.

The findings of the study seem to corroborate previous studies. For example, Greve et al. (2010) contend that the more knowledgeable and experienced the executive is, the better the compensation. Similarly, figurehead theory considers an executives' political connectedness and social networks in general as the most important social capital that can be used to influence policy decisions that are in the interest of the organisation.

The findings of the interviews also highlighted comparison of executives as another influential element in the determination of executive compensation. Research participants mentioned that a number of referent and comparable peer groups were considered when SOEs set executive compensation. The findings of the current study seem to concur with those of previous studies. For example, social comparison theory focuses on determining which individuals or groups are likely to serve as referents when making comparisons (Graffin, Wade, Porac, and McNamee, 2008; Wade, Porac, Pollock, and Graffin, 2006). As a result, executives with greater social status or connections than comparison groups would receive more favourable compensation (Belliveau, O'Reilly, and Wade, 1996; Westphal and Zajac, 1995). However, the findings of the current study revealed that the Minister as a representative of the Government and as a stakeholder had a direct influence on executive compensation. All SOEs had to check with the Minister, especially when the package seemed to be higher than expected.

## **Reciprocity**

Based on the findings, executive compensation is seen as resulting from a relationship between the achievement of performance targets aligned to the strategic intent and business plans of the SOE by the executive. The research respondents asserted that the strategic objectives focus on strategic deliverables for long-term sustainability, as well as on short-term business plan deliverables for profitability, both of which are imperative to shareholder value creation. In turn, the executive would be compensated for reaching the set performance targets. Thus, the determination of executive compensation is reciprocal in that the remuneration philosophy for the executive is designed to align remuneration with long-term shareholder growth and sustainable profitability of the SOE.

Further, it seems from the participants' responses that executive compensation results from deliberations based on the mutual exchange that involves more than just the interaction between the executive and the organisation. The interactive process takes into consideration the complexity of the role of the executive and the extent of the collective engagement according to which the SOE would establish parity in executive compensation. These findings of the study again seem to align with previous studies. For example, according to Farid, Conte and Lazarus (2010), executive compensation does not flow from predictions of narrow self-interest. As captured by Rhee (2014), executive compensation is no longer purely a matter of private contracting. In other words, executives' selfishness does not determine executive compensation.

## **The relationship between influence and reciprocity in the determination of executive compensation**

The relationship between influence and reciprocity in the determination of executive compensation finds expression in the setting of executive compensation as a symbiotic exercise. Symbiosis in this context involves the incorporation of influence that facilitates the negotiation of expectations between an executive and the organisation, as well as an element of reciprocity, which defines the agreed amount of compensation to be given to the executive for the achievement of the predetermined set of performance targets. Thus, the makeup of the pay mix depends on the complexity of the political role of the executive that serves the best interest of the organisation, which in this context, is the ability of the SOE to meet its developmental mandate to society. The findings on the relationship between influence and reciprocity seem to

align with previous studies. For example, according to Aslan and Grinstein (2011), Francis et al. (2009), Horton et al. (2012) and Li et al. (2008), influence and reciprocal exchange produce beneficial effects for both the individual executive and the organisation.

### **Overall implications of influence and reciprocity as determinants of executive compensation**

The findings of this study, unlike those of previous economic and financial studies, have demonstrated that executive compensation is a product of endogenous and exogenous factors. Endogenous factors include an important individual attribute such as the executive's influence. The executive is recognised and rewarded for his or her leadership role demonstrated in translating the vision of the SOE to be adopted by employees. Exogenous factors entail the accepted predetermined performance standards between the executive and the broader stakeholders who include the main shareholders (the government), and expectations from the third parties (communities) they serve.

As an endogenous factor, the determination of the executive compensation process finds expression in the managerial power theory and the figurehead theory that illustrate how the individual executive uses his/her influence and political social networks to achieve organisational objectives required to determine compensation. As an exogenous factor, the determination of executive compensation finds expression in the social comparison theory, which demonstrates how executive compensation entails consideration of the executive's counterparts, to arrive at the final compensation package.

However, the findings of this study have demonstrated how executive compensation not only depends on the power of the executive as referred to by the managerial power theory, but also takes into consideration the executive's role in meeting expectations from the organisation as articulated by the social mandate. The social mandate dictates the psychological contract, which determines the performance expectations required between the executive and other critical stakeholders. Above all, the social mandate serves as a criterion used to determine the compensation level of an executive.

In addition, the findings of the current study have demonstrated that executive compensation is contextual and reciprocal in nature. That is, the determination of executive compensation involves not only the strength of the social networks and political connectedness as alluded to

by the figurehead theory, but also compliance with expectations from the critical stakeholders such as the minister as the representative of the government and the members of the public.

Overall, this study has demonstrated how socio-psychology is able to surpass the economic and accounting disciplines. For example, the socio-psychological approach provides a more detailed description of the nature and application of executive compensation from a process perspective than the economic and financial sciences do. The economic and financial sciences are limited in that they emphasise economic or agency perspectives focusing on how executive pay varies with performance while ignoring the manner in which executive compensation is decided.

The findings of this study contribute to the advancement of compensation theory and research by introducing an alternative perspective by which compensation in SOEs can be analysed. Findings of this study centre on the sociological conception of the process in the determination of executive compensation. This theoretical analysis stresses the abstract specificity of the process and the employment relationship between the executive, his/her organisation and the external environment in the determination of executive compensation.

In particular, the findings of this study have demonstrated how the process of determining compensation is characterised by a significant departure from conventional management practices that emphasise economic and accounting factors. The findings of this study provide new insight into the conceptualisation of the process and the possible relationships of the constructs (influence and reciprocity) as determinants of executive compensation.

The findings also contribute to the field of personnel psychology. As a sub-discipline of industrial and organisational psychology, personnel psychology is concerned with the scientific study of individual differences in work settings, and includes activities such as employee reward and remuneration, employee performance evaluation, attracting and retaining scarce and critical talent, and encouraging adherence to employment-related legislation, among others (Schreuder and Coetzee, 2010). As a contribution to the field of personnel psychology, the findings of this research serve as a baseline study towards understanding the development and implementation practices on compensation.

In addition, the practical implications of the findings of this study seem to place more emphasis on the determination of executive compensation as a collective process. That is, the determination of executive compensation is not merely the result of a selfish demand by the executive, but of a mutual agreement with all the other stakeholders involved in the process. A

more conclusive understanding of the process of setting executive compensation is therefore seen as a socially constructed process that takes into consideration the effects of influence and the reciprocal nature of the relationships of all stakeholders in arriving at the level of executive pay. However, the challenge that arises from the current study is how to measure executive influence and its impact on executive compensation in a manner that is standard across all SOEs. There is also a need for further study on how to measure the level of reciprocal interaction as a determinant of executive compensation.

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