**TITLE: DETERMINANTS OF EMPLOYEE COMPENSATION IN AN ORGANISATION: AN EXPLORATORY STUDY**

A Research Article presented to the

**GRADUATE SCHOOL OF BUSINESS LEADERSHIP**

**UNIVERSITY OF SOUTH AFRICA**

In partial fulfillment of the requirements for the

**MASTERS DEGREE IN BUSINESS**

**LEADERSHIP**

**UNIVERSITY OF SOUTH AFRICA**

by

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**NOVEMBER 2011**

**DECLARATION**

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I, FRANS MALOA, hereby declare that the dissertation "**Determinants of employee compensation: An exploratory study"** is my own work and that all the sources that I have used or quoted have been indicated and acknowledged by means of complete references.

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# ABSTRACT

Compensation is a discretionary concept whose determinants may not necessarily be the same in all organisations. This study reports on the extent to which a limited number of determinants of compensation, as identified in this study, namely job performance, external equity, job families, organisational tenure and employee skill, predict employee compensation in an organisation.

A convenience sample was drawn from the target population in the Gauteng area. Three small and medium-sized organisations were included in the sample, which consisted of a state-owned organisation in the aviation sector, a parastatal company in the finance development sector, and a private company in the banking sector. A categorical multiple regression analysis was conducted.

The findings of this study reflect a greater consistency in four of the six variables as strong predictors of employee compensation, namely employee skill, employee performance, job family and job grade. These factors are strongly related to employee compensation and are regarded as strong predictors of it. The other predictors, namely external equity and tenure, can be considered to be of marginal significance as predictors of employee compensation. However, the results also indicate that these predictors may be more significant in state-owned and parastatal companies, in comparison to private companies. In addition, the determinants of employee compensation may also depend on the type and size of the organisation.

Keywords:

Job performance; job grading; employee skill; external equity; job family; job tenure; Employee compensation.

**ACKNOWLEDGEMENTS**

The work presented in this research report was carried out under the supervision of Prof. Mahamed Rajah. My gratitude therefore goes to him for his assistance, guidance and supervision during the course of this research.

I also wish to thank the following people/organisations:

- The institutions that provided data for this study
- My colleagues, who assisted me by giving advice
- Mr Andries Masenge, statistician at UNISA's BMR (Bureau of Market Research)
- Last but not least, my family, who supported me throughout my studies.

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# CHAPTER 1 ORIENTATION

## 1.1. Introduction

One would think that employees performing the same kind of work and located in the same working environment would be compensated equally. Workers performing almost identical work that requires the same skills and who are organised by the same union and in the same geographical area are receiving a rate of remuneration that is markedly different among different employers, with a sixty per cent difference not being uncommon (Gomez-Mejia, Beronne & Franco-Santos 2010).

Employee compensation is a product of many factors within an organisation. It may or may not include work-related behaviour, especially employee performance (Gomez-Mejia, Beronne & Franco-Santos 2010; Corby & Lindop 2009:34; Zingheim & Schuster, 2007).

According to Zingheim and Schuster (2007), research suggests that the compensable elements most often used to determine the value of work to an organisation vary widely in their ability to predict the market value of work performed. However, the most important determinants of market worth of a job have been found to be in the functional area in which the work is performed, for example, accounting, computer systems, sales management and quality control.

Determinants of pay may also not be limited to within an organisation but can be influenced by factors outside the organisation. For example, Giancola (2009) states that in many organisations, the internal pay structure and salary increase plans are heavily influenced by the actions of other companies. There may be more variables explaining employee compensation than merely the strategic direction which an organisation has chosen to adopt. Boyd and Salamin (2001) indicate that base salary could be viewed as being determined by individual characteristics (gender, age, hierarchical position) rather than strategic orientation, while a bonus is largely explained by strategic orientation rather than individual factors.

Current compensation practitioners have attempted to address concerns about determinants of employee compensation by relying primarily on equity and market data. According to Gomez-Mejia et al. (2010), both equity and labour market models and their operationalisation (namely job evaluation and market surveys) have a largely deterministic view of the world. This deterministic view has been questioned by practitioners and academics alike in a number of related ways. Rather than regarding pay as being determined by job evaluation and market surveys, some practitioners still believe that employee compensation is mainly determined by job performance.

According to Bevilacqua and Singh (2010), the foundation of any pay-for-performance system is the establishment of an accepted method of performance evaluation – one that is fair and transparent. However, methods of evaluation are often fraught with problems. Frequently, pay-for-performance systems become encumbered by complex, multi-layered formulae that attempt to reward such a large number of behaviours, to such an extent that employees are unable to keep their priorities straight (Bevilacqua & Singh 2010). In addition, the results of a study conducted by Bol (2011) further attest to the problems from performance management by mentioning that managers respond to their own incentives and preferences when subjectively evaluating performance and that performance evaluation biases affect not only current performance ratings, but also future employee incentives.

Determinants of employee compensation seem to also be influenced by whether the company is a public company or a private company. For example, Llorens (2008) assert that to identify competitive pay rate levels, most public sector organisations rely on salary surveys of comparable positions in the private sector. As these positions are the most likely alternative for potential or current public sector employees, it is the goal of public sector organisations to offer pay rates that are at or at least near private sector rates. These rates are commonly referred to as “prevailing rates.” However, there are a number of issues that arise when seeking to identify prevailing rates for public sector occupations.

Firstly, if there are patterns of wage discrimination present in the private sector labour market, then basing public sector pay rates on this market only perpetuates these patterns of discrimination (Nigro et al. 2007). Secondly, policy makers must determine which labour markets are most appropriate for a comparison of pay rates. Inappropriate comparisons could potentially lead to higher- or lower-prevailing rates than needed or desired (Llorens, 2008).

The dependency of the public sector on the private sector and issues about the correct market to determine pay, seems to suggest that there is no immediate solution to the problems surrounding employee compensation. For example, Gomez-Mejia et al. (2010) findings are that, firstly, most organisations have considerable discretion in terms of pay allocation, basis for pay decisions, and administrative procedures. Secondly, compensation problems and challenges in each firm are usually more unique and less structured than the traditional models would lead one to believe.

In a study conducted in the public sector by Masibigiri and Nienaber (2011), it was indicated that employees complained about their employer in the public sector, who did not pay for their skills. In addition, employees were of the opinion that salary should match the service of a person and that salary should not get behind in terms of inflation. From the findings of the study, one could draw an inference that employees do regard their skill and tenure as important determinants of employee compensation. The question then is to establish as to what the public sector as an employer in turn regards as an important determinant of employee compensation.

Masibirigi and Nienaber (2011) further assert that retaining Generation X employees, in particular, is important for both the private and public sectors. The retention problem may even be worse for the public sector as there are fewer financial rewards in the public service than in the private sector (Niewenhuizen, 2009).

In the case of public servants like nurses (Perrine, 2009) and engineering and technical professionals (Rose & Gordon 2010) competitive remuneration is another factor that affects the retention of Generation Xers (Masibirigi & Nienaber 2011).

A study by Van Zyl (2010) contend that there is currently an important general debate in South Africa (among employer organisations, labour unions, politicians etc.) on the size and fairness of perceived employee-remuneration gaps among the different employment levels in organisations.

Labour unions, in particular, are of the opinion that these remuneration gaps are expanding and that the situation constitutes a major threat to job creation and the fair distribution of income in the workplace and the economy as a whole. Employer organisations, however, argue that employee-remuneration gaps are, in the main, the result of the shortages of higher-skilled employees in the workplace and differences in labour-productivity levels between the different employee segments (Van Zyl 2010).

Van Zyl (2010) comes to a conclusion that irrespective of whether the relation between employee-remuneration gaps and labour productivity is positive or negative, all the research findings clearly indicate three important aspects that need to be considered, namely (1) employee characteristics, (2) the difference in the skill levels of employee segments and (3) the level of uncertainty in the business or economic environment in which a particular employer operates. Van Zyl's study relates partly to the intentions of the current study in that it puts emphasis on employee skill and the market which relates to aspects of external equity.

Previous research on employee compensation focused mainly on performance-based compensation, employee skills, tenure, job grade, and job family/job function as determinants of employee compensation but did not emphasise the extent to which each variable contributes to employee compensation (Gomez-Mejia et al. 2010; Corby & Lindop 2009:34; Zingheim & Schuster 2007). In contrast, this study focuses on the extent to which each variable predicts employee compensation.

This study offers several contributions to the literature on employee compensation. Firstly, it intends to add new insight to the body of knowledge on employee compensation by measuring the extent to which each identified variable contributes to employee compensation. Secondly, this study being sheds light on the employee compensation process in different kinds of organisations, both private and public. Thirdly, it aims to bring about improvement in establishing standardised practices in structuring compensation, by taking the relevant variables applicable to the type of organisation into account. Lastly, more knowledge on compensation will assist in creating fairness and equity in the design and implementation of compensation strategies within organisations.

In the following section, the problem statement and objectives of this study report are provided. The purpose of the study will be explained followed by the assumptions and Hypotheses. The delimitation of the study, benefits, new contributions and conceptual description will be presented. The chapter concludes with an outline of the research report.

## 1.2. Problem statement

Compensation is a discretionary concept and the determinants of compensation may not necessarily be the same in all organisations. There are various factors that may contribute to the discrepancy in determining employee compensation within an organisation. Employee experience and level of education are signals to organisations about employees' knowledge and skill levels, and thus the labour market rewards employees for acquiring more human capital with access to better jobs, higher earnings, and greater incentives to remain (Ng & Feldman, 2010).

According to Gomez-Mejia et al. (2010) each employee in an organisation exchanges a set of inputs or contributions (e.g., education, effort, and long-term commitment) for a set of outputs or contributions (e.g., pay, promotion, prestige). This exchange process takes place not in isolation but within a social setting. Thus, employees are constantly comparing their inputs relative to their outcomes vis-vis other employees (called referent others) inside and outside the organisation (Gomez-Mejia et al. 2010).

The going rate in the labour market becomes the key factor for ascertaining job value or worth and, hence, external equity is defined as the extent to which the firm's pay rate for a given job matches the prevailing rate for that job in the external market (Fitzpatrick & McMullen, 2008). The salary survey data, in general is used for each job within a given grade level and is used to price all jobs previously classified into that grade. It is possible to use regression procedures to link market data with job evaluation scores (Rosen, 2008) to determine employee compensation. However, there seems to be challenges in determining which labour markets are most appropriate for a comparison of pay rates between the private and the public sector organisation.

Gomez-Mejia et.al (2010) argue that both equity and labour market models and their operationalisation (namely job evaluation and market surveys) had a largely deterministic view of the world. This deterministic view has been questioned by practitioners and academics alike in a number of related ways. The deterministic view may thus imply that the determinants of employee compensation may not be restricted to only equity and market data, but other variables should be taken into consideration.

It has been shown in the literature review that employee compensation is a product of many factors within an organisation which may or may not include work related behaviour, especially employee performance (Gomez-Mejia et al 2010; Corby, Palmer & Lindop 2009:34; Zingheim & Schuster 2007). In practice, where a given employee will be positioned in terms of salary depends on a number of factors, of which the most common are previous experience, company tenure and assessed job performance (Hellerman & Kochanski, 2008; Amuso & Knopping, 2008; Wilson & Malanowski, 2008; Grote, 2008; Niven, 2008; Graham-Brown, 2008).

The problem statement of this study can thus be expressed as follows:

Job performance, external equity, job families, organisational tenure, and employee skills as determinants of employee compensation.

1.2.1 . Sub-problems:

**Sub-problem 1:** To what extent does job performance determine employee compensation in an organisation?

**Sub-problem 2:** To what extent does external equity determine employee compensation in an organisation?

**Sub-problem 3:** To what extent does a job family determine employee compensation in an organisation?

**Sub-problem 4:** To what extent does Organisational tenure determine employee compensation in an organisation?

**Sub-problem 5:** To what extent does employee skill determine employee compensation in an organisation?

**Sub-problem 6:** To what extent does a job grade determine employee compensation in an organisation?

### 1.3. Objectives of the study

The primary objective of this research was to gain a better understanding of the determinants of employee compensation in an organisation.

The secondary research objectives include the following:

- To determine the extent to which job performance determines employee compensation in an organisation.
- To determine the extent to which external equity determines employee compensation in an organisation.
- To determine the extent to which organisational tenure determines employee compensation in an organisation.
- To determine the extent to which a job family determines employee compensation in an organisation.
- To determine the extent to which employee skill determines employee compensation in an organisation.
- To determine the extent to which job grade determines employee compensation in an organisation.

The last objective was to formulate recommendations from the results for use in the organisation as well as in further research in the fields of human resources management and compensation in particular.

### 1.3.1 . Purpose of the study

The aim of this study is to explore and describe the extent to which job performance, external equity, job family, organisational tenure and employee skill determine employee compensation in an organisation.

## 1.4. Assumptions of the study

Based on the literature review and the chosen theoretical framework, namely socio psychology (motivational theories) and neoclassical labour market theories, this study was based on the following working assumptions concerning possible trends.

Firstly, as per the equity paradigm, it is assumed that each employee in an organisation exchanges a set of inputs or contributions (e.g., education, effort, and long-term commitment) for a set of outputs or contributions (e.g., pay, promotion, prestige). This exchange process takes place within a social setting, not in isolation. Thus, individuals are constantly comparing their inputs relative to their outcomes vis-vis other employees (called referent others) both inside and outside the organisation (Gomez-Mejia et al. 2010).

Secondly, and related to the first assumption, the going rate in the labour market becomes the key factor for determining job value or worth and, hence, external equity is defined as the extent to which the firm's remuneration rate for a given job matches the prevailing rate for that job in the external market (Fitzpatrick & McMullen 2008).

The salary survey data for each job within a given grade is used to price all jobs previously classified according to that grade. It is possible to use regression procedures to link market data with job evaluation scores (Rosen, 2008), in order to determine employee compensation.

Experience and education are signals to organisations about employees' knowledge and skill levels, and the labour market therefore rewards employees for acquiring more human capital with access to better jobs, higher earnings, and greater incentives to stay (Ng & Feldman 2010).

Lastly, the position of a given employee's pay within a pay range depends on a number of factors, most notably previous experience, company tenure, and assessed job performance (Hellerman and Kochanski, 2008; Amuso and Knopping, 2008; Wilson and Malanowski, 2008; Grote, 2008; Niven, 2008; Graham-Brown, 2008).

### 1.5. Hypotheses

A total of 6 hypotheses that indicate statistically significant relationships between the independent and dependent variables are highlighted in this study. The null hypotheses with statistically significant relationships are the following:

**Null hypothesis (H0) 1:** Job performance does not determine employee compensation to a large extent in an organisation.

**Alternative hypothesis (H1)1:** Job performance determines employee compensation to a large extent in an organisation.

**Null hypothesis (H0) 2:** External equity does not determine employee compensation to a large extent in an organisation.

**Alternative hypothesis (H1) 2:** External equity determines employee compensation to a large extent in an organisation.

**Null hypothesis (H0) 3:** Job family does not determine employee compensation to a large extent in an organisation.

**Alternative hypothesis (H1) 3:** Job family determines employee compensation to a large extent in an organisation.

**Null hypothesis (H0) 4:** Organisational tenure does not determine employee compensation to a large extent in an organisation.

**Alternative hypothesis (H1) 4:** Organisational tenure determines employee compensation to a large extent in an organisation.

**Null hypothesis (H0) 5:** Employee skill does not determine employee compensation to a large extent in an organisation.

**Alternative hypothesis (H1) 5:** Employee skill determines employee compensation to a large extent in an organisation.

**Null hypothesis (HO) 6**: Job grade does not determine employee compensation to a large extent in an organisation.

**Alternative hypothesis (H1) 6**: Job grade determines employee compensation to a large extent in an organisation.

### 1.6. Delimitations of the study

The origins of the selected topic of this study are in the fields of human resource management and compensation in particular. The traditional foundations of compensation as an academic sub-field are found in both social psychology (motivational theories) and labour economics (labour markets) (Gomez-Mejia et.al, 2010). Scientific management has also played a role in its development.

The topic of compensation was chosen due to its nature as a multidisciplinary concept which can be embraced fully within the field of human resource management (HRM). Unlike most HRM variables, compensation is directly related to the conceptual frameworks of other mainline business fields, (such as finance and accounting (Gomez--Mejia et.al, 2010: 4). Thus, one is able to draw upon a wealth of theoretical models and empirical research from various disciplines.

As mentioned by Gomez-Mejia et al. (2010), productive research and theory development in compensation may be enhanced in the future by greater cross-fertilisation with other disciplines. This will allow compensation to transcend the traditional paradigms grounded in industrial/social psychology and labour economics.

Within the South African context, compensation is also informed by regulatory agencies such as sectoral determination and collective bargaining. Sectoral determination refers to a sectoral determination made under Chapter Eight of the Basic Conditions of Employment Act of 1997. In terms of Section 55(1) of the Basic Conditions of Employment Act no 75 of 1997, read together with Section 18(4) of the Skills Development Act no. 97 of 1998, conditions of employment and rates of learners, as well as allowance for learners in South Africa, were established. The provision of the determination is binding upon all employers and learners in all sectors where Sector Education Authorities (SETAs) have been established. This study concentrates on employees whose compensation is independent from sectoral determination and collective bargaining.

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There are a number of interesting research questions that could have been asked by this study but which are not pursued, such as the following: "What are all possible and known determinants of employee compensation in an organisation?"

This question is not pursued in this study because (a) the focus of the inquiry is on developing new insight into the extent to which each of the identified determinants of employee compensation contributes to employee compensation, and not on all possible and known determinants of employee compensation in all organisations, and (b) the inclusion of this question, while interesting, would be beyond the scope of the researcher, given the limited time and resources available for conducting this study.

### 1.7. Preliminary literature review

The broader theoretical framework that serves as a foundation to understanding the concept of employee compensation in an organisation includes motivational theories (i.e. equity theory), institutional theory, principal-agent theory, the structural model, and the human capital theory. Firstly, according to Gomez-Mejia et al (2010) equity theory as part of the motivational theories has played a predominant role in traditional compensation theory and practise.

Equity theory posits that an individual's motivation is affected by how he or she perceives the ratio of inputs (i.e., work performance) to outcomes (i.e., rewards) relative to referent others. Consequently, from a motivational perspective, the organisation must provide rewards that are proportionate to individual inputs.

A second possible theoretical viewpoint of employee compensation is the institutional theory. Balkin (2008) argues that it is impossible to explain the observed differences in pay level and compensation without examining the role of institutional forces such as mimetic isomorphism (practices of peer organisations), normative isomorphism (norms that develop in professions that receive similar training) and coercive isomorphism (corporate governance system, practices and regulations).

A third theoretical viewpoint from which employee compensation can be explained is the principal-agent theory, also known as the agency theory. According to Perkins and White (2010), agency theory hold that the size of the reward offered may be linked to the level of complexity (and associated transactional cost to principals) in monitoring agent's behaviour (employee behaviour).

A fourth possible theoretical viewpoint is the structural models of pay, which holds that the compensation received by top ranks in a firm is a direct function of the number of organisational levels below them. Other things equal, the taller the organisational structure, the greater the earnings of top executives (Gomez-Mejia et al. 2010).

The last theoretical viewpoint discussed here is human capital theory, which focus on individual characteristics as predictors of pay (Buck, Liu, & Skovoroda 2008; Finkelstein, Hambrick, & Cannella 2009; Combs & Skill 2003; Carpenter, Sanders, and Gregersen 2001). According to Ng and Feldman (2010), human capital theory suggests that long-tenure workers are better performers because they have accumulated more job-related knowledge and work experience. Experience and education are signals to organisations about employees' knowledge and skill levels, and thus the labour market rewards individuals for acquiring more human capital with access to better jobs, higher earnings and greater incentives to remain. In turn, employees with longer tenure have greater incentives to perform well in the future.

### 1.8. Research methodology

A quantitative approach will be used because of its positivist foundation (Babbie 2007). The quantitative approach suits the purpose of this study since it helps to establish the existence of facts (i.e. the extent of the determinants of employee compensation) in a distanced and quantitative manner.

The study is exploratory in nature and reports on new insights in employee compensation. An in-depth analysis of a salary data corpus of various organisations will be conducted. Documented survey data will be used to benchmark external equity.

A secondary data analysis approach will be adopted for this study. A secondary data analysis approach is relevant for the study since, as posited by Mouton (2009), using existing data (mostly quantitative), secondary data analysis aims at reanalysing such data in order to test hypotheses or to validate models.

### 1.8.1. Population and unit of analysis

The population and the unit of analysis comprise of salaried employees from three organisations: two financial institutions (a private company and a parastatal enterprise) and the third company, a state owned company in the aviation sector. The unit of analysis consist of employees that do not fall under sectoral determination. Thus, employee compensation in this research is not determined by a Bargaining Council.

Owing to the nature of this study, a convenience sample will be drawn from small to medium-sized companies. A complete salary data corpus consisting of all three organisations will be studied for purposes of analysis. The reason for adopting such an approach is because an in-depth analysis of the available data of the three companies was necessary.

### 1.8.2. Data Collection and methods

Secondary data will be collected by means of an extensive literature study that will include journals and textbooks on employee compensation. Empirical data will consist of a salary data corpus, information about current job grades, information on job tenure, information on employee skill and information on performance appraisal scores of all employees in the three organisations under study.

### 1.8.3. Data processing and analysis

The data analysis will be in the form of statistical analysis. The statistical procedures chosen for this research will be based on the applicability to the exploratory nature of the research design. SPSS (a statistical program for the social sciences) will be used to perform statistical analysis. Since this study involves a multi-variable problem, that is, more than one independent variable is studied; the categorical multiple regression analysis will be adopted.

### 1.8.4. Methods used to ensure reliability and validity

#### 1.8.4.1. Validity

According to Terre Blanche and Durrheim (2002), both internal and external validity are important and desirable for a research design. The aim of the research design is to plan and structure the research project in such a way that it would ensure that the literature review and empirical study is valid in terms of the variables in this study.

The validity of the literature review will be ensured by using relevant literature to the study, problem statement and objectives. In the empirical study, the validity of the study will be ensured by using standardised instruments of measurement. The validity was determined by how appropriate, meaningful and useful the instrument was, and where validity coefficients were calculated, they usually ranged between a low score of zero and a high score of one (Gregory 2007).

#### 1.8.4.2. Reliability

Reliability is the extent to which a test is repeatable and yields consistency of the results indicated by that which is measurable. Reliability in the literature review will be addressed by using existing literature sources, theories and models that are available to researchers (Foxcroft & Roodt 2009).

## 1.9. Ethical Considerations

Issues which the proposed study will contend with refers to informed consent by participants, gaining access and acceptance into the research data, confidentiality and responsibilities to the research community. Consideration of ethical issues is important since various kinds of problems may arise from methods which are used to obtain valid and reliable data (Cohen et al. 2007). The researcher therefore ensures the highest degree of caution in collecting, storage and management of information. The researcher will always maintain confidentiality of the study participants.

## 1.10. Benefits of the study

This study offers several contributions to the literature on employee compensation. Firstly, it intends to provide new insights for the body of knowledge on employee compensation, by measuring the extent to which each of the identified variables contributes to employee compensation. Secondly, this study sheds light on the employee compensation process in different kinds of organisations, both private and public. Thirdly, it aims to bring about improvement in terms of establishing standardised practices in structuring compensation, by taking the variables applicable to the type of organisation into account. Lastly, more knowledge on compensation will assist in creating fairness and equity in the design and implementation of compensation strategies within organisations.

### 1.11. Contribution of the study

Previous research on employee compensation has focused mainly on performance- based compensation, competency-based compensation, and compensation based on tenure, job grade and job family/job function (Gomez-Mejia et al, 2010; Kessler, 2001; Thompson, 2000; White & Druker, 2009). However, previous studies did not put emphasis on the extent to which each variable predicts employee compensation.

This study focuses on the extent to which each variable predicts employee compensation. It is based on data obtained from South African-based organisations in both the private and the public sector.

### 1.12. Conceptual definitions

#### 1.12.1 Employee Compensation

According to Perkins and White (2011), employee compensation, remuneration or reward may be defined as “all forms of financial returns and tangible services and benefits employees receive’ (Milkovich and Newman, 2004:3).

### 1.12.2 Job performance

According to Ng and Feldman (2010), the conceptualisation of job performance has been expanded in recent years to include core task performance, citizenship performance, and counterproductive performance. Core task performance refers to the basic required duties of a particular job. Citizen performance refers to those extra behaviours engaged in by employees (e.g. helping co-workers), over and above their core task requirements, which actively promote and strengthen the organisation's effectiveness.

### 1.12.3 External equity

External equity is defined as a perception resulting from comparisons with a referent other that performs a similar job in another organisation (Shore et al. 2006).

### 1.12.4 Organisational tenure

According to Ng & Feldman (2010), organisational tenure is defined as the length of employment in an organisation.

### 1.12.5 Job function/Job family

Incomes Data Services (2006b, p.3) defines job families as clusters of jobs or roles that share similar characteristics. While the exact level of responsibility, skill or competence required of roles within a job family may vary, the essential nature of the activities carried out and the skills used tend to be the same.

### 1.12.6 Employee skill

According to Spector (2011), employee skill refers to a person's current level of proficiency in a particular task or family of tasks.

## 1.13. Outline of the study

This study consists of six chapters, and a brief description of the various chapters is provided below.

Chapter 1: Orientation

This chapter provides a background to and overview of the scope and context of this study. The problem statement is introduced and the research objectives are set. The research hypotheses are then stated, followed by a discussion on the assumptions, delimitations and benefits of the study. The contribution of the study to research is outlined, and a few key conceptual definitions are provided. The chapter concludes with a summary of the chapters in this study.

Chapter 2: Theoretical/Conceptual Framework

This chapter provides a theoretical overview of the concept of compensation. Five theoretical models are discussed, namely equity theory, structural theory, agency theory, institutional theory and human capital theory. These theories will account for each determinant of employee compensation, as stated in the previous chapter.

Chapter 3: Literature Review

This chapter presents a review of relevant literature used in this study. The discussion focuses on all the variables mentioned as determinants of employee compensation, namely job performance, external equity, organisational tenure, job families (job function), job grade and employee skill. The variables are discussed in detail, using literature to support the findings with regard to their relationship to employee compensation.

Chapter 4: Research design and methods

This chapter will discuss the research methods and research design used in this study. A detailed description of the research paradigm, data collection and sampling methods, and data analysis techniques will also be provided. This is followed by a description of the methods used to ensure validity and reliability of data, and ethical considerations are also discussed.

Chapter 5: Research Results

This chapter includes the presentation, statistical analysis and interpretation of the results obtained in this study. The extent to which each variable, namely job performance, external equity, organisational tenure, job family, job grade and employee skill determine employee compensation will be indicated in this chapter, based on the findings of the study.

Chapter 6: Conclusion, Recommendations and Limitations

This final chapter provides a conclusion to the study, and makes recommendations for future research the conclusion attempts to indicate the extent to which job performance, external equity, organisational tenure, job family, employee skill and job grade are determinants of employee compensation. The limitations of the study will involve reviewing the particular shortcomings of the research, followed by suggestions as to how these shortcomings might be avoided by future research.

# CHAPTER 2: CONCEPTUAL AND THEORETICAL FRAMEWORK

## 2.1. Overview of the chapter

This chapter provides a theoretical overview of the concept of compensation. The chapter is divided into two parts - the first part gives a brief explanation of the theory, and the second part discusses the five theoretical models, namely equity theory, structural theory, agency theory, institutional theory and human capital theory. These theories account for each determinant of employee compensation, as mentioned in the first chapter.

## 2.2. Explanation of the theory

Given that the employment system is both an economic and psychological relationship, literature in these two disciplines is drawn upon in order to deepen the understanding of employee compensation. Literature in the fields of economics and psychology bring different assumptions and perspectives to bear on compensation, as posited by Thompson, in White and Druker (2009).

Since the researcher is investigating a multi-faceted concept, namely employee compensation, in order to conceptualise compensation, there is the need for a broader theoretical framework that will permit generalisation to most compensation situations. The broader theoretical framework that will serve as an anchor for understanding the concept of employee compensation in an organisation includes motivational theory (i.e. equity theory), institutional theory, principal-agent theory, the structural model, and human capital theory. According to Thompson, as stated in White and Druker (2009), each theory emphasises different aspects of compensation and therefore provides new insights into the functioning of pay systems, including salary progression systems, in practice.

## 2.3. Five theoretical models

The five theoretical models that serve as a framework for employee compensation are discussed below, namely human capital theory, equity theory, principal agency theory , institutional theory, and structural theory.

### 2.3.1. Human capital theory

The first possible theoretical viewpoint of employee compensation is human capital theory. This theory focuses on individual characteristics as a predictor of pay (Buck, Liu, and Skovoroda, 2008; Finkelstein, Hambrick, and Cannella, 2009; Combs and Skill, 2003; Carpenter, Sanders, and Gregersen, 2001). According to Ng and Feldman (2010), human capital theory suggests that long-tenure workers are better performers because they have accumulated more job-related knowledge and work experience. Experience and education are signals to organisations about employees' knowledge and skill levels, and the labour market therefore rewards individuals for acquiring more human capital with access to better jobs, higher earnings and greater incentives to stay. In turn, employees with longer tenure have greater incentives to perform well in the future.

According to Perkins and White (2008:39), human capital theory is an economic theory that is relevant to employee reward. This theory is based on the fact that individuals accumulate human capital by investing time and money (including deferred earnings) in education, training, experience and other qualities, in order to increase their productive capacity and thus worth to an employer. While all employees bring some skill and experience to the performance of their tasks, accumulated educational achievements and experience give rise to differentiation in the level of reward needed to attract and retain certain people.

According to Hijazi and Bhartti (2007), the amount of human capital that a worker possesses influences his/her productivity, which in turn influences earnings. This theory can also be applied to executive compensation. Another explanation for the positive effect of human capital on compensation is that an executive with a greater amount of human capital is better able to perform his/her job and, as a result, is paid more.

Perkins and White (2008) assert that managerial discretion with regard to pay may also be linked to the job or, in less bureaucratic contexts, to role design. Roles are viewed as socially determined signals to individuals about what is expected of them. A balance needs to be achieved between how a role is paid and how the individual's contribution to organisational performance is reflected in terms of reward. Pay rates based on the job or role indicate how individuals are expected to align themselves with the overall work system.

2.3.2. Equity theory

The second theoretical viewpoint of employee compensation is equity theory. According to Gomez-Mejia et al. (2010), equity theory, which is part of motivational theory, has played a predominant role in traditional compensation theory and practice. Equity theory posits that an individual's motivation is affected by how he or she perceives the ratio of inputs (i.e. work performance) to outcomes (i.e. rewards) in relation to referent others. Consequently, from a motivational perspective, the organisation must provide rewards that are proportionate to individual inputs.

According to Thompson in White and Druker (2009) equity theory is based on the proposition that people make judgements about the fairness of their pay on a comparative basis. People in the same job role, doing similar work under a pay progression system determined by issues such as merit or appraisal, will make an assessment regarding whether or not the effort-reward outcomes are fair.

Equity theory can also be further explained by expectancy theory, based on a combination of three factors, namely the expectancy factor, instrumentality factor, and valence factor (Perkins and White, 2008).

The expectancy factor in an individual's own assessment involves determining whether or not performing in a certain way will lead to a measurable result. The instrumentality factor is the perceived likelihood that such a result will, in turn, lead to a given reward, and the valence factor refers to the likelihood of them being satisfied with the reward obtained. Wright, in White and Druker (2009), assert that expectancy has been used in research relating to reward from the early twentieth century, but tends to focus on cash-based rewards, rather than benefits.

According to Perkins and White, the model was further refined in view of the research conducted by Porter and Lawler, so as to include the motivational influence of active self-reflection on the individual's abilities and other traits, the perceived nature of the role to be performed, and the degree of equity attributed to both extrinsic and intrinsic rewards likely to result from the endeavour (Perkins and White, 2008:45).

Perkins and White (2008) state that expectancy theory indicates that if a person sees that performing in a certain way will bring about a reward which he or she values, then this individual is more likely to attempt to perform in that way than if the relationship between effort and measured performance, or measured performance and reward, is weak or uncertain.

In addition, Perkins and White (2008:59) assert that individuals may focus less on the content of the reward and more on comparing the informational signals regarding the relative recognition that they receive with organisational peers (Chen et al, 2002). Equity and comparability are factors that may not actively motivate, but may be anticipated to have a depressing effect on the motivational influence associated with extrinsic rewards for employment and performance if mismanaged.

### 2.3.3. Principal agency theory

The third theoretical viewpoint according to which employee compensation can be explained is the principal agent theory, also known as the agency theory. According to Perkins and White (2008), principal agency theory holds that the size of the reward offered may be linked to the level of complexity (and associated transactional cost to principals) involved in monitoring an agent's behaviour (employee behaviour).

According to Errikson (2000), agency theory, in terms of which the firm (principal) observes individual output, contains less information about its determinants, including worker effort. Agency theory provides the following three explanations for variations in performance pay among individuals:

The first is risk aversion - individuals with a preference for more stable earning flows are more likely to have contracts with weakened incentives. A second reason is differences in the noisiness of the performance measures. The noisier the signals are, the less often they are used. Finally, there is multi-tasking. Under pure performance pay, individuals performing several tasks will devote too much effort to those tasks which are easy to observe, and too little to the hard-to-measure tasks. Consequently, firms are expected to mute incentives when employees are able to "game" the system.

Many authors have chosen principal agency theory as their theoretical framework, in order to characterise the compensation processes in organisations (Gomez-Mejia, Larraza, & Makri, 2003). According to Thompson (2008), principal- agent theory has become the most important framework informing the design of executive compensation reward schemes, but the general principles can be applied to any situation in which delegation of decision-making occurs, and is therefore relevant to the design of reward systems in general. The agency perspective has greatly increased the understanding of executive compensation, but has not been applied as much to compensation at the lower levels in firms.

Little is known about the determinants of employee compensation contracts from an agency perspective (Werner, Tosi, & Gomez- Mejia, 2005). This is somewhat surprising, considering that the study of employment compensation has major practical implications. Employee compensation costs often exceed 80% of total operating expenses (Gomez-Mejia & Balkin, 2006), and these costs provide a more realistic picture of firms' costs than of executive compensation costs.

Different types of compensation contracts are designed according to the possible interest groups. Owners are unable to directly observe the behaviour of employees at the base of the firm or fix their contracts in order to align the interests of both parties (Bolton & Dewatripont, 2004).

According to Perkins and White (2008), pay rates may be set below market 'guaranteed' levels, but workers are offered the opportunity to earn above-average total remuneration, contingent on higher performance. An agency-based approach to reward strategy may be associated with notions of incremental pay progression as individuals ascend internal job ladders, with the reasoning being that the expectation of earning a full return on their human capital investment only over a lengthy employment career will encourage people to stay beyond the below-market-paid phase in the early period of employment.

Within this agency context, in which various levels made up of many agents exist, the compensation contracts fixed at each level are important, since they can be used to align the interests of all the agents and hence reduce possible agency risks (Carrasco-Hernandez et al., 2007). In the case of multiple agents, these may act uncooperatively and seek their own benefits (a worker wants to rely on the other workers to do the work), or they may act cooperatively with other agents for their mutual benefit, to the detriment of the principal (Bolton & Dewatripont, 2004). Thus, the principal must monitor or reward the agents to ensure that they all work, and that no agency problems exist.

The suitable compensation design for employees may vary according to the type of firm (Carrasco-Hernandez et.al, 2007). This implies that pay in the public sector will not necessarily be the same as in the private sector. The differences may also occur in organisations within the same industry or sector, depending on the type of product or service it offers to its customers.

Few studies relate employee pay levels to the ownership structure, and those that do focus on executives (Core, Holthausen, & Larcker, 1999; Ramaswamy, Veliyath, & Gomes, 2000), indicating that managers' pay level decreases as the CEO's level of ownership increases. With regard to the rest of the employees, the same conclusions have been reached (Werner et al., 2005).

### 2.3.4. Structural theory

The fourth theoretical viewpoint to be discussed is the structural model of pay, which holds that the compensation received by top ranks in a firm is a direct function of the number of organisational levels below them. Other things being equal, the taller the organisational structure, the greater the earnings of top executives (Gomez-Mejia et al., 2010).

According to the structural theory, the differences between ranks are not determined by economic forces, but rather through cultural processes that create relevant norms of social stratification. The resulting pay scale will comply with cultural "norms of proportionality" between the earnings of superiors and those of subordinates.

In a manner somewhat akin to the traditional economic models, the structural perspective is very deterministic, with the earnings of executives being mechanically established as a function of the number of levels below them and a fixed percentage difference between their pay and those of subordinates (Gomez-Mejia et al, 2010).

### 2.3.5. Institutional Theory

The last theoretical viewpoint is institutional theory. Balkin (2008) argues that it is impossible to explain the observed differences in pay level and compensation without examining the role of institutional forces such as mimetic isomorphism (practices of peer organisations), normative isomorphism (norms that develop in professions that receive similar training), and coercive isomorphism (corporate governance system, practices and regulations).

According to Scott (2004), from the institutional perspective, organisations are the way they are because this is the legitimate way in which to organise themselves (Meyer & Rowan, 1977). The key behind institutionalisation is that most organisational action reflects a pattern of doing things that evolves over time and becomes legitimated within an organisation and an environment. Therefore, it is possible to predict practices within organisations from perceptions of legitimate behaviour derived from cultural values, industry tradition, firm history, popular management folklore and the like. In other words, things are done in a certain way simply because it has become the only acceptable way of doing them (Zucker, 1977).

According to Scott (2004), consistent with conventional accounts, organisations were recognised as “rationalised” systems—sets of roles and associated activities established to reflect means-end relationships geared towards the pursuit of specific goals. The key insight, however, was the recognition that models of rationality are themselves cultural systems, developed to represent appropriate methods for achieving goals. A wide variety of institutional systems have existed over space and time, providing diverse guidelines for social behaviour, many of which sanction quite arbitrary behaviour. However, the modern world is dominated by systems that embrace rationality and these, in turn, support the proliferation of organisations. Norms of rationality play a causal role in the creation of formal organisations (Meyer and Rowan, 1977), and can thus be seen as playing an important role in determining compensation.

According to Scott (2004), institutional theory models exert their power, not through their effect on the task activities of organisational participants, as work activities are often decoupled from rule systems or the accounts depicting them, but via stakeholders and audiences external to the organisation. Their adoption by the organisation garners social legitimacy.

Relatively little research has explored the influence of institutional pressures on the outcomes of pay determination. However, research on the institutionalisation of organisational forms would suggest that they might have an important impact on the nature and outcomes of pay determination (Gerhart & Rynes, 2003).

According to institutional theory, norms, which include rules, rituals and beliefs, influence organisations and their actors at multiple levels: at the individual level, they inform the values of decision makers; at the firm level, they influence the culture and politics of the organisation; and at the inter-organisational level, there are industry-wide norms (Kessler, 2001). Thus, employee compensation can be regarded as being determined by all these levels within an organisation.

With regard to mimetic processes, pay specialists frequently refer to the experiences and practices of others, often emulating what is considered to be successful elsewhere, in order to inform choice and mediate risk in the form of failed change (Corby et al, 2009:27).

According to Perkins and White (2008), a new institutional approach to strategy theory, paying attention to the various political and social pressures confronting people in organisations, both internally and externally, may facilitate more effective employee reward decision-making. Over time, employers and employees in specific contexts may build a shared history of effort-reward determination. This may involve accumulated learning on how to interpret factors such as internal norms and values, as well as external indicators (e.g. comparison with other employers, as well as from state legislation and trade union interventions). The understanding reached carries with it a shared legitimacy regarding employee reward-setting processes and outcomes. Underlying differences of interest may be held in check, as the parties trust one another enough, given their common experience, to follow the ‘ rules of engagement’ that are slow to change.

### 2.4. Summary

This chapter highlighted the five theoretical models that serve as a framework for research on employee compensation. Each theoretical model addresses employee compensation from a different perspective, and a clear understanding of employee compensation can thus be obtained by taking all these perspectives into consideration when conducting a study on employee compensation.

## CHAPTER 3: LITERATURE REVIEW

### 3.1. Overview of the chapter

The purpose of this chapter is to conduct a review of the literature on employee compensation, which forms the foundation on which this study is based, by facilitating an understanding of previous research and insight into current trends in the field of employee compensation. This chapter describes how literature on employee compensation has evolved to provide more insight into the determinants of employee compensation. Compensation or remuneration philosophy is discussed, followed by a description of the determinants of employee compensation in this study. Previous studies on employee compensation are reviewed, followed by a discussion of the similarities between this study and other recent studies.

### 3.2. Evolution of compensation

For most people, pay is a primary reason for working. Indeed, compensation is at the core of any employment exchange, and it serves as a defining characteristic of any employment relationship (Glassman et Al., 2010). Pay is an important work outcome for most employees, as employees often regard pay as an indicator of their achievement and recognition (Goodman, 1974, in Shore et Al., 2006).

Linked to the theoretical framework, the literature review conducted in this study indicates that determinants of employee compensation are not stagnant but evolve over a period of time. According to Palmer (2009), pay trends in the past thirty or so years, particularly in the private sector, have shown a move away from quasi-automatic incremental progression based initially on service to systems based on assessments of individual performance, and more recently, to systems based on performance and competence, or some other combinations. This has gone hand in hand with moves away from narrow grades to the use of broader bands or grades, possibly with internal zones or sectors, job families or career grades.

Similarly, Thompson noted that during the course of the previous decade, "the dominant shift has been away from progression scales based on seniority or age to a consensus that some form of performance measurement should be the main determinant" (Thompson, 2000:147).

### 3.3. Compensation or remuneration philosophy

Compensation systems do not exist in a vacuum. At a very basic level, an organisation's compensation system reflects a reasoned strategy on the part of organisational decision makers with regard to how vigorously an organisation is going to compete within a competitive and constantly changing marketplace. In the public sector, this often involves deliberate decisions by appointed or elected policy boards, acting upon the recommendations of professional administrative staff. Over time, creative thinking by both public and private sector managers has resulted in the development of theories of compensation that purport to increase employee motivation, job satisfaction and, in turn, organisational performance and productivity (Davis, 2007).

There is a common approach that seems to establish a foundation for determining employee compensation, namely a compensation or remuneration philosophy. According to Weinberger (2010), a compensation philosophy is an overarching statement for managing a company's compensation resources. It is a declaration of intent to align compensation with the mission, goals and values of the company. Many companies have prepared a philosophy document as a basis on which to articulate their pay policies and guiding principles for developing pay programmes and plans.

Henneman (2011) states the following in this regard: “A compensation philosophy explains the values and objectives guiding compensation policies; which skills the organisation rewards; whether the company pays at the median of the market or above or below it; and which types of rewards are available. For instance, the values guiding Hartford Financial Services Group Inc.'s policies include aligning its workforce's interest with its shareholders' interest and linking pay to performance”.

Employee satisfaction with a company’s pay practices depends, in part, on validating the compensation philosophy (i.e. “walk the talk”). However, owing to limitations of situational awareness, it is not always apparent to employees whether or not pay practices are consistent with stated principles. Within the company setting, employees will process and evaluate ambiguous events (i.e. “cues”) that are seen as having pay implications. Consequently, employees are liable to draw mistaken inferences of compensation philosophy violations from observed or reported pay cues that arise inside or outside the company (Weinberger, 2010:215).

In concrete terms, the compensation philosophy statement guides the deployment of pay across jobs and employees. The statement content provides the rationale for originating and perpetuating pay practices that will enable the company to meet its business objectives (Weinberger, 2010). The type of compensation system or philosophy utilised by an organisation plays an important role in determining its overall level of efficiency and effectiveness (Davis, 2007).

Weinberger (2010:.215) asserts that an effective compensation philosophy presents a clear direction for integrating pay programmes with the talent needs engendered by the company’s strategic plan. The aim is to implement pay practices that will secure and reward high-calibre employees in those jobs that are most instrumental to attainment. However, challenges with regard to compensation still appear to exist. For example, Gomez-Mejia et al. (2010:17) posits that many compensation textbook authors and consultants realise that a more professional image of the field of compensation becomes a business discipline, rather than a personnel tool kit. This calls for a broader perspective on analysing internal and external forces that impact the organisation and the ability to devise pay systems to cope with them.

There seems to be no immediate solution to the problems surrounding employee compensation. For example, Gomez-Mejia’s findings are that, firstly, most organisations have considerable discretion in terms of pay allocation, basis for pay decisions, and administrative procedures. Secondly, compensation problems and challenges in each firm are typically unique and less structured than the traditional models would lead one to believe (Gomez-Mejia et al., 2010).

Furthermore, a traditional compensation system based on job evaluation cannot be easily adapted to volatile economic environments or rapid technological change. There is also difficulty in defining the market in which an organisation belongs (Gomez-Mejia et al., 2010).

Determinants of pay also depend on whether a company falls under the public or the private sector (Corby, 2009). As posited by Palmer, in Corby (2009:72), the private sector is much more likely to use a combination of individual pay, broad bands, and job families than either the voluntary or public sectors. This is particularly the case with larger organisations. As a result, private sector organisations have fewer grades by broad occupational classification than the public sector, and market rates are clearly the main determinant of pay rates, followed by the ability to pay. According to Palmer, in terms of pay progression, given the weight that the private sector gives to performance and the market, the main progression emphasis is on a combination of performance, skills, competences, and individual performance (Corby, 2009).

### 3.3. Job performance as a determinant of employee compensation

According to Gomez-Mejia et al. (2010), when performance is used as a basis for distributing rewards, payment is provided for individual or group contributions to the firm. Strict performance–contingent compensation delivers payment for the output or outcome, and most closely resembles the operation of traditional piece-rate plans or sales commissions. Pay-for-performance systems are frequently used by companies in an effort to link compensation to improved employee performance (Bevelacqua & Singh, 2009).

The trend towards the greater use and incidence of performance-related pay continued through the 1990s and into the new century (Kersley et al., 2006). The early days of performance-related pay effectively resulted in pay progression based on service being replaced with pay progression based on an appraisal against agreed objectives (Corby et al. 2009).

According to Dohmen (2004), it is clear from knowledge of the salary system that a higher performance rating triggers a wage increase. Cross-sectional wage regressions partly indicate the weaker impact of supervisors' evaluations on earnings profiles because the positive relationship between performance and wages is dissociated by nominal rigidity, which creates an asymmetry in the relationship between performance and wage changes.

While performance improvements do trigger wage increases, a decline in performance ratings does not cause wages to fall, which means that two (identical) workers with the same job assignment, performance rating history, and earnings history currently receive identical wages, even though one worker's evaluation score has decreased.

Looking back over the previous decade, Thompson noted that “the dominant shift has been away from progression scales based on seniority or age to a consensus that some form of performance measurement should be the main determinant” (Thompson, 2000:147; Corby et al., 2009).

Rather than restricting pay to being determined by job evaluation and market surveys, some experts still believe that employee compensation is mostly determined by job performance. According to Hansen (2009), pay for performance has become increasingly important: “The trend to strengthen performance management programs to better differentiate strong from average or weak performers will only gain more traction in future”.

With all that has been written about pay for performance, considerable doubt still remains among sceptics. Some critics object to pay for performance due to the absence of measurable results that will justify an organisation’s expenditure in terms of time and effort (Zingheim and Schuster, 2007)

According to Bevilacqua and Singh (2010), the foundation of any pay-for-performance system is the establishment of an accepted method of performance evaluation—one that is fair and transparent. However, methods of evaluation are often fraught with significant problems. Often, pay-for-performance systems become encumbered by complex, multilayered formulae that attempt to reward such a large number of behaviours that the employees are unable to stick to their priorities (Bevilacqua and Singh, 2010).

In the view of Gomez-Mejia, et al (2010) a focus on performance for distributing rewards is most appropriate when relevant performance indicators are available, the firm competes through continuous innovation, and the available information technology facilitates the storage and use of performance data for compensation purposes .These conditions are perhaps not always easily met, as performance-contingent compensation is not always feasible.

Dohmen (2004) attempts to account for performance as a determinant of employee compensation by providing for the use of performance scores. According to Dohmen, five different performance evaluation scores determine the attainable wage ceiling within a salary scale's wage range. The wage ceilings for performance scores 1, 2 and 3 are, respectively, at 80%, 90% and 100% of the reference wage. The wage ceiling associated with the highest score coincides with the maximum wage of a scale, and the midpoint between this maximum wage and the reference wage indicates the highest attainable wage for those by means of score 4.

According to Gomez-Mejia (2010), firms continue to search for better ways to assess employee performance, but in their professional experience, they still find widespread dissatisfaction with the appraisal process, and much of it is attributed to the fact that emotions influence both the supervisor’s and the employee’s perceptions of individual contributions. Besides mandated salary increases, other compensation practices include additional guaranteed cash payments (payments provided to employees beyond their salary but independent of performance) such as cash allowances for transportation, meals or holidays ( Hansen, 2010).

According to Bevilacqua and Singh (2010), the foundation of any pay-for-performance system is the establishment of an accepted method of performance evaluation—one that is fair and transparent. However, methods of evaluation are often fraught with significant problems. Often, pay-for-performance systems become encumbered by complex, multilayered formulae that attempt to reward such a large number of behaviours that the employees are unable to stick to their priorities (Bevilacqua and Singh, 2010).

### 3.4. Job grading as a determinant of employee compensation

Job grading, which is also known as a job evaluation system, as suggested by Hastings in White and Druker (2009), involves developing a job hierarchy, either by putting jobs in a ranking order on the basis of information about the jobs as a whole, or by matching them against criteria in a job classification system.

The creation of a grading or pay structure provides the basis for differentials and also identifies what is expected from the bargaining effort for different levels of pay. It does not, however, create the basis for pricing individual jobs. The pricing of jobs, as opposed to their internal evaluation or ranking, is usually done with some reference to external economic indicators such as the cost of living or the average earnings movement (White and Druker, 2009:25).

The hay system and most other job evaluation techniques have the following in common: firstly, the analysis of jobs according to a set of factor headings agreed on for the job population in question; and secondly, the assessment of each job in terms of factor scales, which are usually, but not always, predetermined to give a total score for each job. The third feature of these techniques is the weighting of factors, initially to reflect the perceived value placed by the labour market on each, but subsequently modified to reflect organisational values Hastings, in White and Druker (2009).

According to Hastings in White and Druker (2009:81), there are a number of possible reasons for the increased use of job grading, particularly in the public sector. Firstly, changes in technology and work organisation have, in practice, led to job grading becoming more flexible. Secondly, job grading systems are no longer restricted to traditional collective bargaining groups, but have become broader in techniques - for example, making factor-level definitions more generic to cover different families or types of jobs. Thirdly, instead of evaluating narrowly defined sets of tasks, job grading has been adapted to include more flexible, sometimes multi-skilled roles.

Organisational policy dictates that newly appointed employees with limited experience are brought in near the salary minimum, that competent employees should receive merit increases which allow them to rise to the midpoint, and that stellar employees should receive merit increases that allow them to progress towards the maximum (Heneman, 1992). Employees can also receive pay increases by accepting a job that is on a higher salary grade (with a higher salary range).

Many organisations have opted for monetary reward practices that are far more complex than the traditional “rate for the job” and narrow-graded structures: everything from broad-banded structures and “person-based” base-pay progression to sophisticated individual and group cash incentives and employee equity plans (Shields et al., 2009).

According to Dohmen (2004), upward job transitions are typically associated with advancement on the salary scale ladder, as jobs on higher hierarchical levels are associated with higher wage scales. Blue-collar workers climb one grade each year until they have reached the highest grade of a scale. During this period, their contractual wages rise annually by a fixed amount. A worker receives additional (or less) wage growth if his performance rating improves (or declines). A one-score improvement in performance triggers, on average, a wage gain of about 2%, which is less than the contractual annual wage increases associated with grade advancement, which range from 2.4% to 3.2%. Having attained the highest wage on a specific scale, a worker can only enjoy further wage growth upon promotion to a higher scale.

In general, workers gain only part of the difference between the highest contractual wages of two adjacent wage scales, ranging from 4.4% to 9.7%, immediately upon promotion, since they are typically placed on a lower grade of the higher scale. The other part, i.e. wage growth until the highest grade of the new scale is reached, takes the form of deferred contractual wage growth.

Dohmen (2004) states that the remuneration system for white-collar workers differs slightly from that for blue-collar workers. A minimum and a maximum wage are defined in each scale as a percentage of the scale-specific reference wage. The minimum wage always amounts to 80% of this reference wage. The maximum wage escalates in the form of 2 percentage points from 106% of the reference wage in scale 12 to 118% of the reference wage in scale 18, so that higher scales span wider wage ranges. The wage path towards the respective wage ceiling is characterised by annual contractual percentage wage raises. The system is created in such a way that a worker whose performance rating remains unchanged advances from the minimum wage in a scale to his relevant wage ceiling after six raises. Percentage wage growth is higher when the performance rating is better, and, for a given evaluation score, the further a worker's current wage is below the relevant wage ceiling, the higher it will be (Dohmen, 2004).

The historical development of pay progression, as indicated by Palmer (2009), has seen pay being determined by staff development and based on promotion within the organisation. The 1980’s marked a move towards a more transactional model, and one casualty was incremental payment systems with service as the prime determinant of pay progression. Some of the reasons for this were decentralisation and individualisation, as well as economic pressures occasioned by open markets and fierce competition (Palmer, 2009). There seems to be little doubt that large organisations will need to value and grade jobs for the foreseeable future (White & Druker, 2009:95).

### 3.5. Employee skill as a determinant of employee compensation

Employee skill as a determinant of employee compensation is explained through the human capital theory, which contends that skills are viewed as enablers of According to Gomez-Mejia (2010) Skills based pay (also known as knowledge-based pay), employees are paid based on the jobs they can do. That is the abilities they have can be successfully applied to a variety of tasks and situations.

Martocchio (2011) assert that skill based pay reward employees for the range, depth, and types of skills they are capable of applying productively to their jobs. Employees can earn more rewards by acquiring new horizontal skills, vertical skills, or a greater depth of skill. The more “hats an individual can wear,” the higher his or her pay. Thus skill based pay rewards the individual for the versatility rather than for actual tasks performed.

Under a skill-based system, employees are rewarded horizontally through the expansion of their knowledge, skills and abilities, which enhance their specific job expertise. Wallace and Fay (1988), however, point out that skill-based systems often suffer from the following problems: (1) narrow pay ranges, causing employees to quickly “top out” on the pay scale; (2) an inadequate process of defining and measuring various qualification levels, thereby transforming the pay plan into a mere credentialing scheme for employees to qualify for higher wages; and (3) greater employee training costs, making employee turnover even more costly. Moreover, skill-based systems are in direct conflict with traditional job evaluation plans, where a worker’s pay is based on the position held, rather than his or her individual skill set. Ultimately, however, exactly how or whether or not skill-based pay systems are correlated with significant organisational performance increases has yet to be the subject of extensive empirical research (Davis, 2007).

Dohmen (2004) asserts that heterogeneity in earning dynamics might be informative in terms of ability differences among workers if ability determines the rate at which workers enhance their skills. If more able workers learn faster, i.e. accumulate skills at a higher rate, they are more likely to climb the within-job wage ladder and be promoted faster. This results in heterogeneous experience profiles, even if observed measures such as educational level or years of experience are the same.

According to Klarsfeld, Balkin and Roger (2003:47), the application of skill-based pay challenges the traditional logic of pay determination, which assumes that the firm pays for the job and not the person. Skill-based pay focuses on the individual employee as the source of value and the specific bundle of skills that an individual brings to the employer becomes the basis for determining the rate of pay. In other words, the depth and breadth of each employee’s skills determines the rate of pay. This is a very different philosophy from the conventional approach to worker compensation, where the worker starts out at a flat hourly rate and then receives pay increases as he or she learns how to perform a certain job better, or how to perform other jobs within the same plant or department. The worker gets this hourly rate regardless of his or her job assignment.

Competencies are not necessarily intended to determine reward, but the emphasis in some employment areas, especially customer-facing roles, on behaviours rather than outputs, and the view that performance could be enhanced by doing so, has led some employers to use competency frameworks to replace, or at least modify, progression based simply on performance. In these systems, competency assessments determine movement either through pay ranges or solely above the range mid-point (Corby et al., 2009).

The skills-based approach relates pay progression to the acquisition of new skills, typically to enable manual or craft employees to operate and maintain high-tech equipment. It is based on reward for specific skills (Corby et al., 2009). According to Palmer, as quoted in Corby et al (2009), progression pay trends over the past thirty or so years, particularly in the private sector, show a move away from quasi-automatic incremental progression based on service to systems based on assessments of individual performance and, more recently, to systems based on performance and competence, or some other combinations. This has gone hand in hand with moves away from narrow grades to the use of broader bands or grades, possibly with internal zones or sectors, job families or career grades.

Zingheim and Schuster (2007) emphasises that organisations and various governmental agencies remain concerned about the potential discriminatory nature of any tools or yardsticks that organisations use to determine the value of work in monetary terms. Because of this, many believe that the best way to address the issue of fair pay is to base how employees are paid upon accurate descriptions of skills, competencies, work and job content, but then also to identify the features and characteristics of these that are most correlated with how the market determines what makes people who perform valuable (Zingheim et al., 2007:79).

According to Zingheim and Schuster (2007), research suggests that the compensation elements most often used to determine the value of work to an organisation vary widely in their ability to predict the market value of work performed. However, the most important determinant of the market worth of a job is the functional area in which the work is performed – for example, accounting, computer systems, sales management, quality control, etc.

### 3.6. Job family as a determinant of employee compensation

Incomes Data Services (2006b:3) defines job families as clusters of jobs or roles that share similar characteristics. While the exact level of responsibility, skill or competence required of roles within a job family may vary, the essential nature of the activities carried out and the skills used tend to be similar.

Armstrong and Brown point out that this approach of using job families in compensation is likely to occur when management believes that different occupations require different reward and/or career development practices. Job families are therefore usually arranged by functional groups - for example, finance, information technology (IT) or personnel, or by work categories such as administration or customer services, or by occupation - for example, scientists or IT specialists. Each family is divided into 'levels' or (grades) to reflect the knowledge or competency required of different roles. Levels can vary across families, depending on their complexity. Job families often entail fewer and wider grades than traditional structures, and can therefore be accommodated within broad-banded structures (Armstrong and Brown, 2001).

### 3.7. External equity as a determinant of employee compensation.

External equity refers to the fairness of the pay for a specific job in an organisation in comparison to the pay for similar jobs in other organisations in the relevant labour market. Wage and salary surveys are typically employed in an attempt to achieve external equity (Terpstra and Honoree 2003). According to Martocchio (2010) paying well below or well above the typical market rate for jobs can create a competitive disadvantage for companies. Thus it is important that companies set pay rates by using market pay rates as reference points. To this end, regression analysis, which is a statistical analysis technique is used to enable compensation professionals to establish pay rates for a set of jobs that are consistent with typical pay rates for jobs in the external market.

Researchers of equity theory (Adams 1964) have long recognized that salary expectations may depend on various reference points. The most common reference point considered in this research is salary of a relevant other. For example, Scholl, Cooper, and McKenna (1987) found that people often used others in their occupational field as standards of comparison. Starting salaries of similar graduates have also been used as reference points (e.g., Ordonez, Connolly, & Coughlan, 2000). Bazerman, Schroth, Shah, Diekmann, and Tenbrunsel (1994) found that graduating MBAs utilised social comparison information when only one job offer was available but ignored such information when two competing job offers were available" (Highhouse et al. 2003:71).

Corby et al (2009) assert that pay systems that give primacy to labour market considerations essentially disregard the fact that individuals are influenced by relative, not absolute rewards, and compare their pay with 'referent others'. These are typically their fellow employees (internal equity), but may extend to those in other organisations (external equity). If employees are of the view that others are paid more for the same effort and that their pay is not fair, they will react negatively (by, for example, shirking their duties) in order to balance their effort with their reward. Corby et al (2009) contend that pay systems that give primacy to equity considerations essentially disregard the fact that the labour market for the same or similar jobs may vary significantly in different parts of the country. Equally, there may be major market variations between different jobs at the same level - for instance, between the pay for a marketing manager and a production manager.

According to White and Druker (2009:25), external comparability has been central to pay theory and practice for two reasons. Firstly, as Fay (1989) indicates, jobs have no demonstrable, inherent value and hence, employers gauge the value of a particular post with reference to external counterparts. Secondly, the pay package is the only part of a job offer which applicants can readily compare with other offers. Hastings (2009:79) asserts that organisations use market rates as the basis for determining internal relativities. They are thus allowing the external market to determine their internal relativities.

**3.8. Job Tenure as a determinant of employee compensation**

Corby et al (2009:13) contend that payment for the person, rather than the job, can be achieved either through recognition of length of service, on the assumption that the longer the person does the job, the more skills and knowledge are acquired , or through some form of performance pay. The latter can be either a mechanistic link between pay and output or after evaluation of behavioural characteristics.

Seniority pay and longevity pay relate to job tenure and reward employees with periodic additions to base pay according to employees' length of service in performing their jobs. According to Martocchio (2010) these pay plans assume that employees become more valuable to companies with time, and that valued employees will leave if they do not have a clear idea that their salaries will progress over time.

Martochhio (2010:60) assert that the object of seniority pay is to reward job tenure or employees' time as members of a company explicitly through permanent increases to base salary. Employees begin their employment at the starting pay rate established for the particular jobs. At specified time intervals, which can be as short as 3 months and as long as 3 years, employees receive designated pay increases. These pay increases are permanent additions to current pay levels. Over time, employees will reach the maximum pay rate for their jobs. Companies expect that most employees will earn promotions into higher paying jobs that have seniority pay schedules.

**3.9. Previous research on determinants of employee compensation**

Findings by Dohmen (2004) articulated a strong relation between some of the variables within the current study. Dohmen demonstrated the relationship between employee performance, job grade and tenure in relation to employee compensation. To illustrate how heterogeneous tenure profiles evolve for workers who start doing the same job, Dohmen (2004) considers the example of assembly workers in aircraft construction. An assembly worker who starts on the lowest grade of scale 5 can advance to the highest grade on scale 8 after 8 years, provided his performance ratings remain sufficiently high. On such a path, a worker initially proceeds to the second lowest grade on scale 5 and, receiving a performance evaluation score of 4, he is promoted to the third lowest grade on scale 6 after his second year of tenure.

Upon promotion to a higher scale, a worker is commonly placed on the lowest grade for which the wage exceeds what a worker would have earned if he had only proceeded along the contractual tenure wage path on the lower grade. Typically the worker's performance rating drops upon this transition, but after it has improved again after the second year of tenure, the worker might be promoted to scale 7, at which point he starts to climb the salary scale grade ladder. If the worker's performance increases beyond score 4, he is likely to be promoted to scale 8 before reaching the highest grade on scale 7. In this exceptional case, he might even jump one wage grade on scale 8, thus reaching the top grade of scale 8 after 8 years (Dohmen, 2004).

If performance ratings are less favourable, it takes longer for workers to reach the within-job wage ceiling. Assembly workers whose performance rating is lower than score 3 never proceed to a higher salary scale. A profit analysis reveals that high performance ratings have a particularly strong positive impact on early promotion chances of workers on the bottom grades of a salary scale (Dohmen, 2004).

Moreover, higher performance ratings become generally more important for promotions to the top salary scale of a job. In order to proceed beyond salary scale 8, an assembly worker has to advance to a job with a higher pay range. Such a job change might either involve a transition to a higher job level, for example by becoming a team leader of an assembly group and thereby extending the potential wage range to salary scale 10, or a lateral job change—a quality controller of an assembly line, for example, can proceed to salary scale 9 (Dohmen 2004).

Dohmen (2004) assert that it has been shown that the institutional rules of formal salary systems, which commonly characterise the wage policies of large firms, make the observed positive relation between seniority and earnings appear to be largely independent of performance ratings in standard cross-sectional wage regressions despite the fact that better performance leads to considerably higher life-cycle earnings. Several features cause this deception.

Firstly, performance evaluation is not only contingent on the job level, but also depends on the contemporaneous assignment to a salary scale within the job's wage range. Performance ratings tend to fall upon advancement to a higher scale. This does not only suggest that performance requirements are more stringent on higher salary scales but also means that two workers in the same job might have the same contemporaneous performance rating even though the more productive of the two earns more being assigned to a higher salary scale because of better performance in the past (Dohmen 2004).

Secondly, nominal wage rigidity creates an asymmetric relationship between changes in the salary system and wage changes. Promotions, typically initiated by high ratings, result in wage increases, while decreases in  salary, which commonly result from a decline in performance, do not have wage consequences (Dohmen, 2004).

Thirdly, higher performance ratings increase promotion prospects, but much of the life-cycle earning gains associated with a promotion are neglected in cross-sectional analyses, because the largest portion of the discounted value of a promotion takes the form of contractual entitlements to future wage raises. While better performance increases and prolongs life-cycle earnings growth, wage gains resulting from better performance only accrue gradually with tenure (Dohmen, 2004).

According to Dohmen (2004), deferred compensation is thus an important element of the wage policy, but upward-sloping tenure profiles are not a mere reflection of institutional seniority provisions. Instead, the size of contractually promised future wage growth depends on performance, and performance ratings determine the steepness of individual wage-tenure profiles. Such a salary system, with a deferred compensation component, is likely to encourage workers to make productivity enhancing investments that are difficult to verify, as it creates confidence among workers that they will be rewarded for improving their productivity, and it is also likely to reduce turnover.

The fact that the firm strictly adheres to the formal rule structure, even during periods of adverse economic conditions, emphasises that reliability, trust and reputation are crucial elements of the wage policy. Over time, creative thinking by both public and private sector managers has led to the development of theories of compensation that purport to increase employee motivation, job satisfaction and, in turn, organisational performance and productivity (Davis, 2007).

In the public sector, the dominant compensation system or philosophy has generally centered around two basic concepts: the classic civil service pay system and performance-based (or merit-based) pay. Under the classic civil service pay system, employees are classified or categorised according to specific grades and steps, determined in part by rank, function and seniority. These grades and steps are then linked to specific pay scales and ranges, which are then rigidly applied and rarely deviated from. Employees at the same grade and step throughout an organisation, although performing substantively different jobs, should receive approximately the same pay. Thus, the classic civil service pay system strives to maximise internal equity (Wallace & Fay, 1988), while simultaneously rewarding long-tenured employees with automatic step increments. Such a system, however, does little, if anything, to enhance individual employee performance. During the 1970's and 1980's, performance-based pay emerged as an impetus for increasing employee performance and productivity.

### 3.10. Similarities and differences with reference to this study

As a result of the limited amount of empirical research conducted on this topic within the South African context, this study used Dohmen's (2009) approach, but supplemented it with the latest study on compensation, which was conducted by Gomez-Mejia et al (2010). Gomez-Mejia has written extensively on the topic of compensation and is regarded by most practitioners in this field as an authority on the subject. This study used most of Gomez-Mejia's (2010) findings to study the relationship between the independent variables and the dependent variable. However, this study used the Social Science Research Program (SSP) to score data.

### 3.11. Summary

This chapter entailed a review of relevant literature that was used in this study. The discussion covered all the variables mentioned as determinants of employee compensation, namely job performance, external equity, organisational tenure, job family (job function), job grade and employee skill. These variables were discussed in detail, using the literature to support findings in this study with regard to their relationship to employee compensation. Previous research on determinants of employee compensation was also explored, and the chapter concluded with a discussion of the similarities and differences between previous research and this study.

# CHAPTER 4: RESEARCH METHODOLOGY

## 4.1. Overview of the chapter

The purpose of this chapter is to outline the methods used to conduct this study. Reviewing the information provided in this chapter should allow the reader to make a reasonable judgement in terms of the reliability and validity of the research methods used in this study (Saunders et al., 2007).

## 4.2. Research approach

The research approach describes the way in which a theory is formulated and then tested. There are two major approaches to research, namely deductive and inductive. The deductive approach formulates the theory first and then seeks out data to confirm or disconfirm this theory. The inductive approach begins with the data first and then formulates a theory based on the data gathered. This study employed the inductive approach. A research question was formulated prior to gathering the data, however, as no theory had been proposed. The data that was gathered and analysed guided the formulation of the resulting theory.

## 4.3. Research design

A research design refers to the overall research plan. This plan stems from the objective of the study. This study aimed to explore and describe the extent to which job performance, external equity, job family, organisational tenure and employee skill determine employee compensation in an organisation. In this particular study, the focus was on employee compensation. The study explored the determinants of employee compensation and sought to bring new insight to the body of knowledge on employee compensation.

The design of this study incorporated the inductive approach mentioned above. It also employed the case study method, and conducted an interpretive, in-depth analysis of the data. The following sections of this chapter will provide detailed information on each component of the research design.

### 4.4. Research Strategy

The overall topic of this study is employee compensation. This study focused on employee compensation in particular sectors of industry and a specific company. The case study approach seemed to be most appropriate for this study, as it investigates a research question in its real-life context (Saunders et al., 2007). Employee compensation is studied at all levels within an organisation, ranging from the executive management to the lowest level employee within an organisation, in both the private and public sector.

### 4.5. Research methodology

The research methodology refers to the techniques used in data collection and data analysis processes (Saunders et al, 2007). For this study, the researcher chose the quantitative method for gathering and analysing data. The emphasis was on documented data containing nominal, ordinal and numeric data. This data was gathered through an interpretive, in-depth analysis of secondary sources

A quantitative approach is used because of its positivist foundation (Babbie, 2007). It suits the purpose of this study, since it helps to establish the existence of facts (i.e. the determinants of employee compensation) in an objective and quantitative manner.

This study uses the inductive research approach. The data gathered during the study was analysed to identify the determinants of employee compensation.

This study is exploratory in nature and provides new insights into employee compensation. An in-depth analysis of a salary data corpus of various organisations is conducted, and documented survey data is used to benchmark external equity.

A secondary data analysis approach was adopted in this study. This approach was relevant since, as posited by Mouton (2008), using existing data (mostly quantitative), secondary data analysis attempts to re-analyse such data in order to test hypotheses or validate models.

**4.6. Population and unit of analysis**

The population and unit of analysis were comprised of salaried employees from three organisations: two financial institutions (a private company and a state-owned enterprise), and a company in the aviation sector.

The unit of analysis consisted of employees who do not fall under sectoral determination. Thus, employee compensation, in this study, is not determined by a bargaining council.

Owing to the nature of this study, a convenience sample was drawn from small to medium-sized companies. A complete salary data corpus consisting of all three organisations was studied for purposes of analysis. The reason for adopting such an approach was because an in-depth analysis of the available data of the three companies was necessary.

### 4.7. Data collection

A contextual descriptive approach seemed to be most appropriate, since this study is interested in studying the population within a particular time period. The total timeframe of the research is the 2011 academic year. This includes the research proposal, literature review, data collection, data analysis and final reporting of results and conclusions.

This study relied solely on secondary data. Thus, it is appropriate to consider the advantages and disadvantages of using secondary data. One of the primary advantages of using secondary data is the low cost of obtaining the data. Secondary data is usually obtained from published reports, articles and books. Another advantage is that secondary data is more readily available, and can be obtained in a short period of time. Collecting primary data may take longer, especially in the case of longitudinal studies. And finally, secondary data can result in the discovery of unintended information, thus leading to conclusions initially not predicted. This is especially beneficial for inductive studies that seek to explore a subject (Saunders et al., 2007).

However, there are some disadvantages to using secondary data. One disadvantage is that secondary data may have been collected for a purpose other than what was intended for the study. This can cause the data to be unusable or diminish its effectiveness. Secondly, there is very little control over the quality of secondary data. The original researcher may have had different standards of quality to those required by this study. In addition, secondary data may be presented in a way that served the original purpose, but which may not be effective or credible for this particular study (Saunders et al., 2007).

Despite the disadvantages of using secondary data, the researcher believes that the benefit is greater than the cost. The ability to access secondary data quickly and at a low cost made this study possible. Significantly higher resource requirements would have made this study prohibitive to the researcher. Furthermore, secondary data enabled the researcher to get access to a wider range of sources than time would have allowed if primary data was being collected. The data available through secondary sources was collected by people, in some cases, who had greater access to the original sources than the researcher did. And finally, because secondary data offers the possibility of discovering unintended information, it enhanced the exploratory nature of this study.

Secondary data was collected by means of an extensive literature review, which included journals and textbooks on employee compensation. The SDA approach is relevant for this study, as posited by Mouton (2009), in that by using existing data (mostly quantitative), SDA aims at reanalysing such data in order to test hypotheses or validate models.

A theoretical orientation and a study of the appropriate published research data precede the empirical study. A literature review of the research reports and journal articles related to employee performance, external equity, organisational tenure, job families, and employee skill was conducted to test the extent to which these factors are determinants of employee compensation in an organisation.

Empirical data collected consisted of a salary corpus, as well as information about current job grades, job tenure, employee skill and performance appraisal scores of all employees in the three organisations under study. The data gathered was in the form of an excel spreadsheet of the organisations under study. The salary corpus consisted of existing salary information of each employee within the organisation, and thus served as part of the secondary data analysis.

Furthermore, an analysis of the National Remuneration Survey, which also serves as part of the secondary data analysis, was used to benchmark the salaries paid by the organisation under study against those paid in the market within the same industries. The purpose of using the national benchmark was to measure the external parity of the jobs in the organisation under study with those contained in the national industry data.

Data from the salary dump, the grading system information, performance rating scores from the performance appraisal system and the National Remuneration Survey were transferred to an Excel spreadsheet in order to code and analyse the data.

### 4.8. Data processing and analysis

The data analysis was in the form of statistical analysis. The statistical procedures chosen for this study were based on their applicability to the exploratory nature of the research design. Salary data corpus available on an excel spreadsheet containing information about employee job grade, tenure, job function, performance rating, employee skill was exported into SPSS (a statistical program for the social sciences) in order to perform statistical analysis. After editing and capturing, the data were processed to provide descriptive measures in order to describe the data set according to its shape. Data were summarised for individual variables in the form of frequency tables. Descriptive statistics were also calculated to describe variables numerically (Saunders et al. 2007).

Since this study involved a multi-variable problem - that is, when more than one independent variable is studied, categorical multiple regression analysis was used. This multiple regression analysis was used because, according to Albright et al. (2006), multiple regressions represent an improvement over simple regressions, and they allow any number of explanatory variables to be included in the analysis. For this particular study, a categorical regression analysis was used to specify the extent of the relationship between the variables. Categorical regression was conducted because the variables being studied differ, and this includes a combination of numerical, ordinal and nominal data.

The statistical analysis makes use of a categorical regression model to facilitate the investigation of causal relationships in the data. This model was preferred over other categorical association measures, such as chi- square, Cromer's V and Lamda, which would not have allowed the same level of analysis, especially with regard to causal relationships. A further reason for using a categorical regression model is the usage of both ordinal and nominal data in the model (Ligthelm, 2010).

In this study, leading extant sources on employee compensation were studied to derive the content of the measurement items. In order to control the extent of the research, only employee compensation variables mentioned for this particular study were considered for analysis. As a result, the data analysis aimed to empirically validate the variables believed to have an impact on employee compensation through an extensive literature review of the particular variables.

**4.9. Methods used to ensure validity and reliability**

**4.9.1. Validity**

According to Terre Blanche and Durrheim (2002), both internal and external validity are important and desirable in a research design. The aim of the research design used in this study was to plan and structure the study in such a way that it would ensure that the literature review and empirical study are valid in terms of the variables used in this study.

The validity of the literature review was ensured by using literature that was relevant to the research topic, problem statement and objectives. In the empirical study, the validity of the data was ensured by using standardised measuring instruments, namely the SPSS. In this regard, validity was determined by how appropriate, meaningful and useful the instrument was, and where validity coefficients are calculated, they will usually range between zero and one (Gregory, 2007).

### 4.9.2. Reliability

Reliability is the extent to which a test is repeatable and yields consistent results in terms of that which is measurable. In the literature review, reliability was addressed by using existing literature sources, theories and models that are available to researchers (Foxcroft & Roodt, 2009).

The data in this study was related only to those variables that were mentioned previously. Employee compensation can be determined by a wide variety of factors, but in this particular study, the focus is on a few of the variables that may be regarded as determinants of employee compensation.

The limitation of this approach in terms of reliability is that there may be variables that are regarded as significant determinants of employee compensation, besides the ones identified and included in this study. However, it is not possible to test all the known variables, given the limited time and resources available to conduct this study.

## 4.10. Ethical considerations

Ethical issues with which the research had to contend were the following: informed consent, gaining access to and acceptance of the research data, confidentiality, and responsibilities to the research community. A consideration of ethical issues is important, since various types of problems may arise from methods which are used to obtain valid and reliable data (Cohen et al., 2007). Since this study involved sensitive information regarding employee compensation, the researcher ensured that the highest degree of caution in the collection, storage and management of information was taken. The researcher always maintained the confidentiality of the respondents and the research data used in this study.

The researcher ensured that harm to participating organisations was avoided by fully informing participants of the research procedure and clearly outlining potential risks. Permission was sought for the use of the salary data corpus provided by the participating organisations. Participants were informed that the findings would be used for purpose of completing an academic study and for publication of results in a credible journal. In order to protect the privacy of participants, personal details such as names of employees, identity of the respective organisations and salary data were kept in confidence during the study. Thus the researcher always maintained confidentiality of the research respondents and the research data used during the study.

### 4.11. Summary

This chapter presented the research methodology and design strategy used in this study. A detailed description of the research paradigm, data collection and sampling methods, as well as data analysis techniques, was provided. A discussion on the methodology was followed by an outline of the methods used to ensure validity and reliability. The chapter concluded with an overview of the ethical considerations that applied to this study.

## CHAPTER 5: RESEARCH RESULTS

### 5.1. Overview of the chapter

The purpose of this chapter is to outline the results of the study and present a discussion based on the findings. The chapter will include statistical methods, presentation and discussion of results, and limitations of the study.

The analysis of the research findings is based on statistical methods. The research findings are discussed in terms of categorical and quantitative data. The data obtained was purely quantitative, and the analysis therefore used only quantitative methods. The research results are discussed in terms of the descriptive statistics and tables are used to represent the statistical findings.

Descriptive statistics are used to explore the samples used for determining employee compensation. Data preparation and coding are also discussed in this chapter, which concludes with a presentation of the results which indicate the extent to which each variable, namely job performance, external equity, organisational tenure, job family/job function and employee skill, determines employee compensation within the three organisations in this study. The results are then also analysed and interpreted.

### 5.2. Descriptive statistics

The predictor variables are discussed in terms of job family, job grade, employee skill, external equity, organisational tenure, job performance and employee compensation. Descriptive statistics provide an initial indication of the research data.

The total population of 459 employees' salary information from three different organisations was studied. Table 1 below shows the total population percentage distribution per company, and Table 2 presents the summary statistics of the job family. Table 3 indicates the frequency distribution of job grades among the 459 employees represented in this study.

**Table 1: Statistical information on all represented companies**

| Company | | Frequency | Percentage | Valid Percentage | Cumulative Percentage |
|---|---|---|---|---|---|
| Valid | 1.00 | 75 | 16.3 | 16.3 | 16.3 |
| | 2.00 | 137 | 29.8 | 29.8 | 46.2 |
| | 3.00 | 247 | 53.8 | 53.8 | 100.0 |
| | Total | 459 | 100.0 | 100.0 | |

Table 1 above provides information regarding company statistics. Company 1 represents a state-owned company in the development finance sector, Company 2 represents a state-owned company in the aviation sector, and Company 3 represents a private company in the banking sector.

The most represented company in the population was Company 3, with 247 employees, resulting in a percentage distribution of 53.8%. The second highest represented company was Company 2, with 137 employees, resulting in a percentage distribution of 29.8%. The least represented company was Company 1, with 75 employees, resulting in a percentage distribution of 16.3%.

**Table 2: Statistical data on job family**

| Job family | | Frequency | Percent | Valid Percent | Cumulative Percent |
|---|---|---|---|---|---|
| Valid | Administration | 17 | 3.7 | 3.7 | 3.7 |
| | Finance | 91 | 19.8 | 19.8 | 23.5 |
| | Human Resources | 19 | 4.1 | 4.1 | 27.7 |
| | IT | 56 | 12.2 | 12.2 | 39.9 |
| | Risk | 33 | 7.2 | 7.2 | 47.1 |
| | Operations | 243 | 52.9 | 52.9 | 100.0 |
| | Total | 459 | 100.0 | 100.0 | |

Table 2 above presents information regarding job families. The most represented job family in this study is Operations, with 243 employees, resulting in a percentage distribution of 52.9%. The second highest represented job family is Finance, with 91 employees, resulting in a percentage distribution of 19.8%.

The third highest represented job family is Information Technology, with 56 employees, resulting in a percentage distribution of 12.2%, followed by Risk, with 33 employees, resulting in a percentage distribution of 7.2%.

The second lowest represented job family in this study is Human Resources, with 19 employees, resulting in a percentage distribution of 4.1%, followed by the least represented job family, which is Administration, with 17 employees, resulting in a percentage distribution of 3.7%.

**Table 3: Statistical data on grades**

| Grades | | Frequency | Percent | Valid Percent | Cumulative Percent |
|---|---|---|---|---|---|
| Valid | BL | 9 | 2.0 | 2.0 | 2.0 |
| | BU | 15 | 3.3 | 3.3 | 5.2 |
| | CL | 31 | 6.8 | 6.8 | 12.0 |
| | CU | 110 | 24.0 | 24.0 | 35.9 |
| | DL | 153 | 33.3 | 33.3 | 69.3 |
| | DU | 85 | 18.5 | 18.5 | 87.8 |
| | EL | 51 | 11.1 | 11.1 | 98.9 |
| | EU | 5 | 1.1 | 1.1 | 100.0 |
| | Total | 459 | 100.0 | 100.0 | |

Table 3 above shows that the highest grade represented in this study is DL, which represents lower level management, at 33.3%, followed by supervisory staff (CU) at 24%. Upper management (DU) represents 18.5% of the population, with senior management (EL) representing 11%. The least represented grade is the executive management (EU), at 1%.

### 5.3. Combined Results

**Table 4: Model summary**

The model summary indicates the correlation between employee compensation and its determinants, with all the organisations being treated as one company.

Model summary

| | Multiple R | R Square | Adjusted R Square | Apparent Prediction Error |
|---|---|---|---|---|
| Standardised Data | .892 | .796 | .786 | .204 |

Table 4 above shows that 79% of the variance in employee compensation in all companies combined is explained by the determinants of employee compensation.

**Table 5: Analysis of variance**

| | Sum of squares | df | Mean square | F | Sig. |
|---|---|---|---|---|---|
| Regression | 360.525 | 20 | 18.026 | 84.211 | .000 |
| Residual | 92.475 | 432 | .214 | | |
| Total | 453.000 | 452 | | | |

Dependent Variable: Employee Compensation

Predictors: Hot Skills External Equity Tenure Employee Performance Company Job Family Grades

The results from the analysis of variance are depicted in Table 5 above. The model fit is significant, since the p value is less than 0.05. The results show that the model variances (18.026) are considerably higher than the error variances (.214), indicating that the different determinants succeed in predicting employee compensation at a 95% level of certainty.

**Table 6: Regression coefficients**

| Variables | Standardised Coefficients | | df | F | Sig. |
|---|---|---|---|---|---|
| | Beta | Bootstrap (1000) Estimate of Std. Error | | | |
| Employee Skills | .125 | .035 | 1 | 12.493 | .000 |
| External Equity | .080 | .051 | 1 | 2.421 | .120 |
| Tenure | .030 | .025 | 1 | 1.374 | .242 |
| Employee Performance | -.081 | .033 | 3 | 6.104 | .000 |
| Company | .151 | .034 | 2 | 19.390 | .000 |
| Job Family | .132 | .024 | 5 | 30.412 | .000 |
| Job Grades | .671 | .050 | 7 | 178.832 | .000 |

According to Table 6 above, the following determinants have a p-value less than the significance level of 0.05, and can therefore be regarded as being strongly related to employee compensation: employee skill, employee performance, job family and job grade. The variable of job grade (.671) has the highest beta coefficient, followed by job family (.132) and employee skill (.125) respectively. This implies that job grade, as a determinant of employee compensation, is the strongest predictor, followed by job family, employee skill, external equity, tenure and employee performance respectively.

There is a negative relationship between employee compensation and employee performance. This implies that there is an inverse relationship between employee compensation and employee performance, which implies that when employee performance is low, employee compensation will be high. The standardised coefficients with regard to the six variables indicate that employee skill, employee performance, job family and job grade are strongly related to employee compensation, and are regarded as determinants of the latter. The other determinants, namely external equity (.120) and tenure (.242), can be considered as non-significant, since they are both e way above the 0.05 level of significance.

### 5.4. Overall results and summary by company

The previous section reported on the overall findings of all the organisations combined. However, there seems to be discrepancies when reporting on the determinants of employee compensation at the individual organisation level. The following section reports on findings for the individual organisations in this study.

**Table: 7 Model summary**

| Standardised Data | Multiple R | R Square | Adjusted R Square | Apparent Prediction Error |
|---|---|---|---|---|
| Company 1 | .969 | .939 | .921 | .061 |
| Company 2 | .911 | .829 | .811 | .171 |
| Company 3 | .892 | .796 | .786 | .204 |

Dependent Variable: Employee Compensation

Predictors: Hot Skills Score External Equity Tenure Employee Performance Job Family Grades

Table 7 above shows the correlation between employee compensation and its determinants. The predictor variables of employee compensation for Company 1 explain 92% of the variance, for Company 2, 81% and for Company 3, 79% of the variance. This indicates, on the one hand, that the type of organisation has an effect on employee compensation. On the other hand, the results also indicate that the determinant variables are significant in state-owned companies, in comparison with companies.

**Table: 8 Regression coefficients**

| | **Company 1** | | | **Company 2** | | | **Company 3** | | |
|---|---|---|---|---|---|---|---|---|---|
| Determinants | Standardised Coefficients Beta | F | Sig. | Standardised Coefficients Beta | F | Sig. | Standardised Coefficients Beta | F | Sig. |
| Employee Skills | 0.209 | 3.214 | 0.080 | 0.057 | 0.536 | 0.465 | 0.122 | 7.82 | 0.006 |
| External Equity | 0.282 | 3.273 | 0.077 | 0.632 | 28.283 | 0.000 | 0.205 | 14.04 | 0.000 |
| Tenure | 0.081 | 1.996 | 0.165 | -0.097 | 5.423 | 0.022 | 0.029 | 0.565 | 0.453 |
| Employee Performance | -0.08 | 1.322 | 0.256 | -0.091 | 3.335 | 0.039 | -0.129 | 9.729 | 0.000 |
| Job Family | 0.083 | 3.968 | 0.005 | 0.161 | 10.369 | 0.000 | 0.142 | 19.978 | 0.000 |
| Job Grade | 0.476 | 8.281 | 0.000 | 0.27 | 4.86 | 0.003 | 0.593 | 89.902 | 0.000 |
| Model | | | 0.000 | | | 0.000 | | | 0.000 |

### 5.4.1 Results for Company 1

According to Table 8 above, job grade (0.000) and job family (0.005) have a p-value less than the significance level of 0.05, and can therefore be regarded as determinants of employee compensation. Their beta coefficients are .476 for job grades and 0.083 for job family. This implies that job grade is the strongest determinant of employee compensation, followed by job family.

The other predictors, namely employee skill (.080), employee performance (0.256), external equity (.0.077)) and tenure (.165), can be regarded as non-significant, since they are above the 0.05 level of significance.

### 5.4.2 Results for Company 2

According to Table 8 above, external equity (0.000), job family (0.000), job grade (0.003), tenure (0.022) and employee performance (0.039) have a p-value less than the significance level of 0.05, and can therefore be regarded as determinants of employee compensation. Their beta coefficients are (0.632) for external equity, 0.161 for job family, 0.27 for job grade, (-0.097) for tenure and -0.091 for employee performance. This implies that external equity is the strongest determinant of employee compensation, followed by job grade. However, there is a negative relationship between tenure (-0.097), employee performance (-0.091) and employee compensation. This means that there is an inverse relationship between tenure, employee performance and employee compensation.

### 5.4. 3 Results for company 3

According to Table 8 above, the following have a p-value less than the significance level of (0.05) and therefore can be regarded as determinants of employee compensation: employee skill (0.006), external equity (0.000), employee performance (0.003), job family (0.022), and job grade (0.039). Their beta coefficients are as follows: external equity (0.205), job family (0.142), job grade (0.593), employee skill (0.122) and employee performance (-0.091). This implies that job grade is the strongest determinant of employee compensation, followed by external equity, job family, employee skill and employee performance. However, there is a negative relationship between employee performance (-0.129) and employee compensation. This implies that there is an inverse relationship between employee performance and employee compensation.

The other variable, namely tenure (.453), can be considered as being non-significant, since it is way above the 0.05 level of significance. Thus, tenure is not significant as a determinant of employee compensation within this private company in the banking sector.

## 5.5. Summary

This chapter entailed the presentation, statistical analysis and interpretation of results. The chapter is preceded by the preparation of data for analysis, the exploration and interpretation of data using statistics. The extent to which each variable namely, Job performance, external equity, organisational tenure, Job family, Job grade, and employee skill determine employee compensation was presented.

# CHAPTER 6: CONCLUSION, RECOMMENDATIONS AND LIMITATIONS

## 6.1. Overview of the chapter

The purpose of this chapter is to provide a conclusion for this study and present a discussion based on the findings. The chapter will include a presentation and discussion of the results, as well as the implications of these results for each company.

## 6.2. Discussion

This research offers a new approach to compensation in terms of the determinants of employee compensation within an organisation. In addressing employee compensation the extent of each determinant of compensation was considered in terms of the extent it predicts employee compensation. Overall, findings from the research suggest a greater consistency in four of the six variables as strong predictors of employee compensation. These include employee skill, employee performance, job family and job grade. These factors relate strongly to employee compensation and are thus regarded as strong predictors of employee compensation. Moreover, the findings show the other predictors namely external equity and tenure as of marginal significance as predictors of employee compensation.

The participant organisations were from various sectors of the industries one a private company in the banking sector and another, a parastatal in the development finance sector and a state owned company in the aviation sector. In interpreting the results, the differences between public and private organisations were kept in mind.

Since the findings were different in different organisations depending on the nature of the business and the number of employees per organisation, that seem to suggest that type and size of a company be taken into consideration when studying the extent of the determinants as predictors of employee compensation in an organisation. The findings seem to suggest that the determinants may be more significant in a state owned and a parastatal company compared with a private company. A brief exposition of this analysis per organisation is presented.

### 6.2.1. Results for Company 1

According to the results of Company 1, job grade and job family, with a p-value less than 0.05 and a beta coefficiency of .476 and 0.083 respectively, appear to be strong determinants of employee compensation. The differences in beta coefficiency imply that job grade is the strongest determinant of employee compensation, followed by job family. This finding agrees with the literature reviewed, in that salary survey data is generally used for each job on a given grade level, as well as to price all jobs previously classified according to a specific grade. It is possible to use regression procedures to link market data with job evaluation scores (Rosen, 2008), in order to determine employee compensation. Research also suggests that the most important determinants of the market worth of a job have been found to be in the functional area in which the work is performed - for example, accounting, computer systems, sales management and quality control (Zingheim & Schuster, 2007).

The results also agrees with the structural theory as explained by Gomez-Mejia et al. (2010), that compensation received by top ranks in a firm is a direct function of the number of organisational levels below them. Other things equal, the taller the organisational structure, the greater the earnings of those that are on top of the organisational structure.

Rosen (2008) further assert that it is possible to use regression procedures to link market data with job evaluation scores to determine employee compensation. In addition to Rosen's assertion, research also suggests that the most important determinants of the market worth of a job have been found to be in the functional area in which the work is performed, for example accounting, computer systems, sales management and quality control (Zingheim & Schuster 2007).

However, in this particular company, other predictors, namely employee skill (.080), employee performance (0.256), external equity (0.077)) and tenure (.165) were non-significant since they scored above the 0.05 level of significance.

**6.2.2. Implications of results within Company 1**

The employee skill which is non significant in this particular company seems to suggest that the company does not have serious challenges from the market in as far as fighting for scarce skills is concerned. With the company also scoring low on tenure and external equity, the results seem to suggest that its employees are not poached by other companies , which may be the reason why tenure is low and non significant as a determinant of employee compensation.

Employees within this company remain longer with the company, but are not rewarded accordingly. Since employees are not resigning, there seems to be no pressure to compensate employees according to market rates. Thus, external equity is not significant as a determinant of pay in this development finance company.

The finding may further suggest an inverse relationship between employee skill and organisational tenure. That is, when employee skill is in demand, organisational tenure would become significant since more employees would live the organisation for competitors. When the demand for employee skill in the market is low the organisational tenure would increase with the effect that employees remain longer with the organisation and thus the organisation may not be pressured to increase pay in an attempt to retain employees.

Considering the overall relative significance of job grade and job family, the results seem to suggest that with less challenges in retaining skilled employees, an organisation would put much emphasis on internal factors such as placing employees in the correct grades and jobs and paying them according to predetermined salaries as per the level and the type of job an employee occupies within the company.

### 6.2.3. Results for Company 2

External equity (0.000), job family (0.000), job grade (0.003), tenure (0.022), and employee performance (0.039) have a p-value less than the significance level of 0.05 and can therefore be regarded as strong determinants of employee compensation within company 2.

The beta coefficients with external equity (0.632), job family (0.161), job grade (0.27), tenure (-0.097) and employee performance (-0.091) indicate that external equity is the strongest determinant of employee compensation followed by job grade. However, there is a negative relationship between tenure (-0.097), employee performance (-0.091) and employee compensation. The findings indicate that there is an inverse relationship between employee tenure and employee compensation, That is, when tenure is high, employee compensation would remain low. The finding seems to indicate that employees may have joined the company at the "going rate", since external equity is the highest determinant of employee compensation within the company.

The impact of external equity has the effect of overriding employee performance. Employee compensation remained high irrespective of the employee's performance in this specific organisation. This seems to agree with the motivational theories as posited by Perkins and White (2008, p.59) that individuals may focus less on their own performance and more on comparing informational signals regarding relative recognition they receive against organisational peers. Equity and comparability are factors that may not actively motivate, but they may be anticipated to have a depressing effect on the motivational influence associated with extrinsic rewards for employment and performance in the job if mismanaged. Thus, it seems like within company 2 employees are compensated according to the type of job an individual performs and the job grade, with the effect that employees remain longer with the organisation.

The other predictor, namely employee skill (.465), can be considered as non-significant, since it is way above the 0.05 level of significance. Thus, employee skill is not a significant determinant of employee compensation within this particular aviation company.

### 6.2.4. Implications of results within Company 2

The findings of this study imply that Company 2 does not experience problems with employee skills and is able to secure all the required skills in the market, without having to consider them as a determinant of employee compensation. It may also mean that there is a low turnover of staff, and it is thus not a serious challenge for the organisation to recruit aggressively in the market. It may also suggest that the organisation does not have stiff competition from the market and is therefore not forced to consider paying for skills at a competitive level.

### 6.2.5. Results for Company 3

Employee skill, external equity, employee performance, job family and job grade are strongly related to employee compensation within Company 3, and are thus regarded as strong determinants of employee compensation within this private company in the banking sector. These findings are aligned with the neoclassical model and the literature review. For example, Fitzpatrick and McMullen (2008) state that in order to attract and retain a qualified workforce, the firm must first identify what the prevailing wage is for each of its jobs. Secondly, the going rate in the labour market becomes the key factor in determining job value or worth and, hence, external equity is defined as the extent to which the firm's pay rate for a given job matches the prevailing rate for that job in the external labour market. According to Perkins and White (2010), agency theory holds that the size of the reward offered may be linked to the level of complexity (and associated transactional cost to principals) in monitoring an agent's behaviour (employee behaviour).

The other variable, namely tenure (.453), can be considered to be non-significant, since it is way above the 0.05 level of significance. Thus, tenure is not significant as a determinant of employee compensation within this private company in the banking sector.

### 6.2.6. Implications of results within Company 3

The findings of this study imply that Company 3 focuses their compensation on retaining employee skills, which may be in demand by competitive organisations in the market. In order to retain such skills, the company benchmarks employee compensation against the market and applies appropriate grading of positions, in order to arrive at a competitive scale of employee compensation. It may also mean that there is high turnover of staff, which poses a serious challenge if the organisation fails to pay employees at the market rate. This supports the literature, which argues that in many organisations, the internal pay structure and salary increase plans are heavily influenced by the actions of other companies (Shore et al., 2006).

## 6.2. Conclusion

The aim of this study has been to gain a better understanding of the determinants of employee compensation in an organisation. The preceding discussion addressed the extent to which certain variables, namely job performance, external equity, job family/job function, tenure, employee skill and job grade, determine employee compensation.

The determinants of employee compensation have been discussed from the perspective of a broad theoretical framework, which would permit generalisation to most compensation situations. The applicable theoretical framework consisted of motivational theories (i.e. equity theory), institutional theory, principal-agent theory, structural theory, and human capital theory.

A quantitative approach was used, since this helps to establish the existence of facts (i.e. the extent to which the variables determine employee compensation) in an objective and quantitative manner.

The population and unit of analysis comprised salaried employees from various organisations and included two financial institutions, i.e. one private company and one state-owned enterprise. The third company came from the aviation sector.

Convenience sampling was used to select three companies from different industrial sectors. A complete salary data corpus consisting of information from all three organisations was studied for purposes of analysis. This study was exploratory in nature and provided new insights into employee compensation. An in-depth analysis of the salary data of various organisations was conducted, and documented survey data was used to benchmark external equity.

The study was exploratory in nature and reported on new insights in employee compensation. An in-depth analysis of salary data of various organisations was conducted. Documented survey data was used to benchmark external equity.

The secondary data analysis (SDA) approach, as posited by Mouton (2009), was relevant for the study. Secondary data analysis was used because it facilitates the reanalysis of existing (mostly quantitative) data in order to test hypotheses or to validate models. Secondary data were collected by means of an extensive literature study that included journals and textbooks on employee compensation. Empirical data consisted of a salary data corpus and information about current job grades, job tenure, employee skill and performance appraisal scores of all employees in the three organisations under study.

Findings from the research reflect a greater consistency in four of the six variables as strong predictors of employee compensation. Employee skill, employee performance and job family were found to be strongly related to employee compensation and regarded as strong determinants of it. The other determinants, namely external equity (.120) and tenure (.242), could be considered to be non-significant, since they both were above the 0.05 level of significance.

However, the results may also imply that the predictors may be more significant in a state owned and a parastatal compared to a private company. In addition, the implications of the findings may also suggest that the type and size of the company be taken into consideration when studying the determinants of employee compensation.

Determinants of employee compensation were also discussed at an individual organisation level. It was demonstrated that the significance of determinants of employee compensation also depends on the type of company. In Company 1, a parastatal development finance company, the determinants were 92% predictable and in Company 2, a state-owned company in the aviation sector, the determinants were 81% predictable, compared to a private company, where the determinants were 79% predictable. Thus, the results indicate that the determinants were more significant in state-owned companies than in private companies.

### 6.3. Recommendations

The findings have confirmed previous research that suggests that the compensable elements most used to determine the value of work to an organisation vary widely in their ability to predict the market value of work performed (Zingheim & Schuster 2007). Thus, organisations and compensation practitioners may have to consider the type of organisation and the sector in which an organisation belongs in order to design an ideal compensation strategy that would be suitable for a particular organisation.

Since this research focussed on single organisations from different sectors, future research may need to investigate the extent to which each variable studied for this research contributes to employee compensation within organisations of a similar type within the same industry or sector.

The nature of the sample based on a convenient sampling may also limit the generalisability of the findings. Stratified sampling would be ideal for future studies on the subject since the study is about different categories of employees in the organisation. Since employees are classified according to different job functions, job grades, job performance and organisational tenure, Stratified sampling would assist in providing information about the different subgroups as well as information about the overall population of employees in the study.

According to Peck et al. (2001), stratified sampling can be used if it is important to obtain information about characteristics of the individual strata as well as of the entire population.

The subject of compensation remains a challenging concept that cannot be confined into a single theoretical perspective but should continue to be approached from a broad perspective that involves an interdisciplinary background.

The research findings suggest that in this time of rapid change in compensation, a new paradigm of employee compensation and research is needed; and that compensation practitioners and Human resources managers need help and professional development to prepare them for challenges around designing effective compensation strategies specific for their own organisations.

While the author is keenly aware of and sensitive towards the limitations of using the secondary data analysis and own capacity to provide meaningful advice to South African organisations, the research discussed some of the more important issues of employee compensation development in South Africa, illustrated by examples from literature and from the empirical research conducted. This research attempted to avoid the generic manner in which employee compensation is addressed. Instead it focussed on specific and popular determinants of employee compensation in practice and evaluated the extent each variable predicts employee compensation within an organisation. The authors' approach suggests that the crux of employee compensation lies in understanding the extent of each determinant in predicting employee compensation.

It is hoped that this research will trigger discussion among compensation practitioners and Human resources managers about how they might structure employee compensation by taking into account the extent each determinant assist in predicting compensation in their particular organisations. In most organisations the extent to which each of the determinant predicts employee compensation maybe a taken for granted aspect but is may be the core of what separates one organisation from another as an employee of choice.

### 6.4. Limitations of the research

This study has several limitations. It investigated only one type of organisation in each sector studied. Care should be taken when extending the research results beyond the three organisations studied. Although the determinants of employee compensation studied may be common among most organisations, this however may not necessarily have the same applications to other similar organisations. Thus, it is critical for firms to take into account the extent of each determinant when determining employee compensation in their particular environment.

A convenience sample was drawn from the target population in organisations based in the Gauteng area, which could have impacted on the representativeness of the sample. Mainly small and medium-sized organisations were included in the sample. Larger organisations might have different impact regarding the determinants of employee compensation in an organisation.

The study focussed on the few identified determinants for this study, however there may be other unobserved determinants of employee compensation that were not taken into account. Moreover, individual differences between the organisations may have contributed to the differences in the extent of the determinants of employee compensation in the different organisations.

This study relied on secondary data. Although there were advantages to using secondary data, such as ease of access and low cost, the use of such data presented some limitations. The greatest limitation in this regard was the acceptance of the captured information as being correct. A study that incorporates interviews of employees would be able to provide more insight, especially with regard to performance and how fairly it is measured. This study was dependent on documented information received from the organisations that participated in this study. Data on employee remuneration is very confidential and institutions are therefore reluctant to divulge information. This study is also dependent on the accuracy of the data provided by these institutions.

More informative data was obtained from a consulting firm that specialises in remuneration. This information assisted in providing best practice and benchmarked survey data. Even though the organisations under study possessed recent benchmarked data, they did not, however, use the same service provider or consultant, and the figures may thus vary.

The other challenge was the limited time allowed for this study. With more time, it would be possible to collect and analyse a larger set of data. This would potentially provide deeper insight into the determinants of employee compensation in an organisation. Such a study would be able to gather data from more organisations in a wider range of industries, in both the private and the public sector.

**6.5. Summary**

This chapter outlined the findings of the study. The major theme that emerged from the data was that the extent to which the different variables studied are determinants of employee compensation is not the same in all organisations.

Through the analysis of the data, it became clear that the extent to which each variable is a determinant of employee compensation depends on the type of organisation. The determinants of employee compensation which were more evident and significant included job grade and job family. The significance of the other determinants, however, depended on the type of the organisation. Determinants of employee compensation may be informed by whether an organisation is from the public or the private sector.

The data made it clear that there is no "one size fits all" in employee compensation. The determinants of employee compensation may be different at group level - that is, when all the organisations are treated as one organisation, than when the variables are predicted at an individual organisation level.

The findings have confirmed previous research that suggests that the compensable elements most used to determine the value of work to an organisation vary widely in their ability to predict the market value of work performed. Thus the recommendation made was that organisations and compensation practitioners may have to consider the type of organisation and the sector in which an organisation belongs in order to design an ideal compensation strategy that would be suitable for a particular organisation

The limitations of this study were discussed, and were seen to be based on the restrictive nature of the secondary data analysis, which relies on already documented data which cannot be altered.

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