



Employee compensation: The neglected area of HRM research



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ABSTRACT

This Introduction offers a plea for more research in the area of compensation. The reasons why compensation research is important are discussed. The introduction also provides an overview of the papers in this issue. It suggests the kinds of questions that are in critical need of comprehensive answers.

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1. Introduction

When we look across the topics that have been the focus of attention in HRM and organizational behavior research, we find thousands of studies on employee selection, performance appraisal, and turnover. So much research has been devoted to these topics that researchers have resorted to review the reviews (e.g., Price, 1989) to get some sort of grasp of the underlying lessons to be gleaned. By contrast, research on employee compensation is sporadic and sparse. A meta-analysis of 40 years of research on financial incentives and performance yielded only 39 studies, about one per year (Jenkins, Mitra, Gupta, & Shaw, 1998). The situation has not improved in recent years. Tables of content in the major journals and recent major conference programs yield only a scant few articles on the topic. For example, of more than 1200 sessions at the 2013 annual meetings of the *Society for Industrial and Organizational Psychology* (SIOP), only three are related to compensation, rewards, or benefits. Similarly, the program of the HR division of the *Academy of Management* featured only three sessions on compensation, among hundreds devoted to other topics, at the 2012 annual meetings. Of 111 articles published in *Personnel Psychology* in 2003–2007, only two focused on compensation issues; the parallel proportion was seven of 457 in *Journal of Applied Psychology* (Cascio & Aguinis, 2008).

The relative dearth of research on employee compensation is problematic for a variety of reasons. One, compensation is arguably one of the most critical influences (if not the most critical influence) on the quality and effectiveness of human capital. Compensation influences the quality of the people who apply, the quality of those hired, the likelihood of job acceptance, the motivation and performance level of the workforce, and the quality of who stays with the company (Dineen & Williamson, 2012; Saks, Wiesner, & Summers, 1996; Shaw & Gupta, 2007). Despite a surfeit of vociferous opinions to the contrary (e.g., Kohn, 1993; Pfeffer, 1998; Pink, 2009), the evidence is quite clear; compensation has powerful incentive and sorting effects (Gerhart & Rynes, 2003; Jenkins et al., 1998). In virtually every aspect of organizational functioning, compensation can shape employee behavior and organizational effectiveness.

Two, from a psychological standpoint, compensation affects employee attitudes and behaviors. Simple and minimal reminders of money (e.g., a U.S. dollar bill on a screen saver) can increase feelings of self-reliance (Vohs, Mead, & Goode, 2006, 2008) and increase pain tolerance (Zhou, Vohs, & Baumeister, 2009). From the perspective of organizations, it is almost axiomatic that, unless the compensation system is done right, other organizational policies and procedures cannot have their desired effects. The centrality of compensation systems is amply displayed in our everyday life in phrases such as “money talks,” “follow the money,” and “pay the piper.” Indeed, the design and implementation of compensation systems not only can affect employee motivation, but also can be harnessed to improve safety, quality, creativity, innovation and a myriad other outcomes critical in a successful workplace.

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Three, many compensation decisions are not particularly expensive. It would, of course increase payroll costs to raise salaries for the entire workforce. On the other hand, the same level of total payroll dollars can be distributed across employees in a variety of different ways (Gupta, Conroy, & Delery, 2012). All employees in a job category can be paid the same, or pay can vary based on performance, seniority, skill, competency, etc.; distinctions in pay across employees can be large or small; the system can be hierarchical with most of the compensation dollars going to top executives whereas lower-level employees are paid the lowest possible rates, or the compensation system can be more egalitarian, with greater parity across organizational echelons; etc. Organizational decisions on these kinds of issues have the potential to have a profound influence on the kinds of employees who are attracted to and stay with the organization, and on the attitudes and behaviors toward which employee motivation and effort are directed. This is particularly significant because these effects occur while the total payroll dollars expended on employees are held constant. Indeed, employee compensation remains perhaps the most powerful tool for engineering successful management of human capital and thereby promoting organizational effectiveness.

Besides, it is evident from everyday life and conversations that compensation matters to people. If we read the newspapers, we find many stories about issues and benefits related to compensation and incentive systems – just recently, one report indicated that weight loss was facilitated by the use of financial incentives (Kullgren & Norton, 2013); another report suggested that teachers who were given incentives at the beginning of a school year, but had to return the incentive money if they did not meet performance goals during the year, outperformed teachers who were simply promised an incentive at the end of the year if performance goals were met (Fryer, Levitt, List, & Sadoff, 2012); another sensational report announced the indictment of the Atlanta Public School superintendent and others in a massive cheating scandal attributed to incentives offered for the improvement of student performance (Winerip, 2013). The list goes on. These reports show that financial incentive systems are effective; sometimes they are too effective.

Compensation systems are important; they are also interesting. It is fascinating to examine the tug-of-war between supervisors and subordinates over incentives. It is fascinating to evaluate the pronouncements about incentives that come down from on high and explore the correspondence between rhetoric and reality – for example, companies are fond of saying that their employees are their most valuable asset, but does employee pay reflect this? Often not. It is also intriguing to consider the wide gap between what people say motivates them and what the evidence says actually does (Rynes, Gerhart, & Minette, 2004).

Other reasons for the importance of compensation and incentive systems can be enumerated. Nevertheless, the fact remains that compensation and incentive systems are among the most under-researched areas in HR. This issue of HRMR seeks to begin correcting this neglect. Of course, a single journal issue cannot do this alone, but we hope that this is the beginning of a spate of good compensation thinking and research. We also hope that better thinking and better evidence will, ultimately, enable payroll expenses to be targeted better to achieve the recruitment, selection, and retention of a highly-motivated, high-performing workforce. These, after all, are the espoused goals of compensation systems.

This issue of HRMR covers a variety of compensation topics. One aspect of compensation that has, for some reason, stirred up a lot of debate is whether pay is actually motivating. The empirical evidence on this issue is unambiguous – pay can be and has been used effectively to motivate employees. Still, as noted above, consultants, motivational speakers, and some academics continue to denounce the use of extrinsic motivators, especially pay. This is in spite of the fact that most research showing the corrosive effects of extrinsic rewards was not conducted in work settings, and workplace research shows that extrinsic rewards can work quite effectively. The problem in workplace settings is not whether extrinsic rewards can be effective (they can be), but rather the conditions under which they are likely to be most effective. These and other issues are addressed in greater detail by Gerhart and Fang. This paper focuses on the claims and assertions with respect to pay for individual performance, and presents the scientific evidence regarding these claims and assertions. It points to many areas of performance-based pay that could benefit from further research.

If pay systems can be effective in motivating better performance, can they be used to motivate other desired behaviors as well? We often hear that people show the behaviors that are rewarded. This suggests that compensation systems could be powerful tools in motivating a multitude of desired behaviors. Mattson, Torbiörn, and Hellgren address this issue in their paper. They use a qualitative approach to decipher the effects of bonus systems on safety behaviors in nuclear plants. The data suggest that financial incentives can in fact promote safety. It is particularly noteworthy that no major problems or downsides are evident from the use of money in the safety context they describe.

A different behavior is of interest in the paper by Merriman. Here the role of pay systems in employee choice of the number of hours to work is explored. Non-exempt employees often work overtime hours, partly due to the inducement of premium pay. But this paper explores the role of regular pay in decisions about how many hours to work, suggesting that there is a curvilinear relationship between the two. The propositions offered in this paper present interesting opportunities for empirical exploration.

Ironically, the argument that incentive compensation is not effective is sometimes countered by the argument that it is too effective. This position proposes that when money is attached to employee behaviors, employees evince functional as well as dysfunctional behaviors in order to ensure that they do indeed obtain the desired money. The cheating scandal in the Atlanta school system exemplifies this argument – in order to get the desired incentives, teachers, principals, and the superintendent focused on improving student performance scores not necessarily student performance. Sometimes this focus entailed functional behaviors (trying to enhance student learning), and sometimes it entailed dysfunctional behaviors (erasing incorrect answers on the test, and filling in the correct answers). Thus, when assessing the effectiveness of financial incentives, it is critical to consider both functional and dysfunctional consequences. Samnani and Singh do so in their paper. The authors offer a framework for explaining how performance-enhancing compensation practices can lead to workplace bullying and can be counterproductive. The insights offered in this paper can be expanded to explore how, when, and where financial incentives can lead to

counterproductive work behaviors. This issue was highlighted about forty years ago in [Steve Kerr's \(1975\)](#) pioneering article. It continues to have resonance today.

Regardless of the specifics, most pay systems make distinctions in pay across employees. Distinctions are made virtually universally across hierarchical echelons; distinctions are made quite often within lateral levels as well. It is these distinctions that presumably lead to the sorting, incentive, and dysfunctional consequences of financial incentives. Distinctions in pay among employees result in pay dispersion. Pay dispersion has been the subject of some debate in the literature. At this point, it is quite clear that pay dispersion per se is neither good nor bad. Rather, it is the factors that dispersion is based on (performance, seniority, politics, etc.), the proper communication of pay information to employees, the workplace structures, etc., that determine whether pay dispersion is beneficial or harmful. Even so, some research continues to insist that the evidence supports a direct negative relationship between pay dispersion and organizational performance. Downes and Choi address the issues inherent in pay dispersion. These authors offer a typology of existing pay dispersion research as it affects employee reactions. This paper should be useful in laying to rest the mistaken belief that, in and of itself, pay dispersion is good or bad. It should also be instrumental in triggering more nuanced approaches to pay dispersion.

The final article by Baeten takes a broader perspective on compensation. How compensation is conceptualized and managed affects many constituencies. It affects employees, managers, owners, customers, clients, and the larger society, to name a few. Sometimes the effects on these varying constituencies mesh well with one another. At other times, they are in conflict. These synergies and clashes must be considered in designing compensation systems. The article by Baeten helps in doing so.

Several papers in this issue also address global concerns in compensation management. Gerhart and Fang have a separate section on these issues. Baeten offers a Belgian perspective and Mattson and colleagues take a Swedish perspective. Just as it is the case that an incentive system working quite well in New York City can encounter significant problems in rural Alabama, so it is probably also the case that the same incentive system will not work equally effectively in all countries and cultures across the world. It is imperative that compensation research address these cross-country and cross-cultural differences if it is to have relevance in a global economy.

In all, this issue of HRMR begins to address many vital topics in compensation research. But these topics represent only a small fraction of the issues that need to be better understood. For instance, many companies claim to use performance-based pay, but a closer examination unearths many differences in the specifics of the pay-for-performance plans across companies. A number of such differences are crucial in affecting the success of the pay-for-performance plan. Examples of dimensions along which differences could occur include:

- Is pay based on organizational, group, or individual performance?
- Is pay based on objective measures such as piece-rate or subjective measures such as supervisory ratings?
- What proportion of pay is variable?
- How big are performance-based pay differences between good and bad employees?
- Are pay criteria clearly specified to employees in advance?
- Is there a policy of pay secrecy?
- In group-level performance-based pay plans, is pay distributed to group members equitably or equally?
- Is performance-based pay supplemented with other rewards?

Other dimensions could easily be identified as well. So are performance-based-pay plans that differ on these characteristics the same plan or different plans? If different, which of these dimensions are critical? In selection research, interviews are often compared with cognitive ability tests of the Big Five personality dimensions, but some scholars have pointed out that these comparisons involve a construct (e.g., cognitive ability) on the one hand and a method (interview) on the other – a comparison of apples and oranges ([Arthur & Villado, 2008](#)). Likewise, in compensation research, when different performance-based pay plans are grouped together, are we grouping together a method? If so, what construct does this method represent? We would have much greater clarity about performance-based pay if some of these issues were addressed directly.

As an example at a macro level, some researchers would like to assert that pay dispersion is either good or bad for the organization. But before such a claim can be justified, we need again to address a variety of issues:

- Is the dispersion vertical, horizontal, overall, or some other variation?
- What is the basis of the pay variation – performance, seniority, skill, a combination, other?
- Are employees working independently or interdependently?
- How much control do employees have over their outputs?
- Are organizational processes egalitarian or elitist?

Again, numerous other differences could be listed, but the same point remains. We have to focus on the nuances if we are to obtain in-depth understanding.

We list these examples at the micro and macro levels simply to illustrate how much complexity exists in compensation research, and to issue a plea to researchers not to gloss over these complexities. Among these and other areas in need of research, there remains much to be learned about the multi- and cross-level effects of compensation systems on employee attitudes and behaviors. Although authors such as [Trevor and Wazeter \(2006\)](#) have taken up the challenge, we have simply scratched the surface in terms of understanding how pay decisions play out similarly and differently across levels within the organization. Nuanced approaches can offer rich soil for research endeavors; we strongly encourage them going forward. In short,

compensation is important to employees. We hope that this issue of HRMR motivates more of us to focus on compensation issues in our research. Clearly, if we could also tie substantial compensation to these endeavors, we might see more dramatic effects! For the moment, however, we hope that this research continues for intrinsic reasons alone. The time is now, the opportunities are endless.

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