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## JUSTICE AND CULTURE IN THE PERCEPTION OF COMPENSATION FAIRNESS*

*Abstract*

While compensation is a central component in the relationship between employees and employers, it is a relatively under-researched area within human resource management and industrial-organisational psychology. Instead, where much of the compensation research has occurred is within the disciplines of economics and finance, areas where agency theory dominates. This article explores the relationship between culture and compensation practices through the lens of organisational justice theory and contrasts the role of distributive justice with the more recent procedural and interactional justice theories.

The article articulates how fairness perceptions are instrumental in determining which compensation practices fit different cultures. The consideration of individual perception is important as there is considerable variability within cultures and many organisations have to deal with increasingly multicultural workforces. A particular contribution of this paper is that it explicitly discusses justice perceptions as an explanatory variable of the relationship between culture and compensation practices, something that frequently has been omitted in prior scholarship. The article further explores the extent to which employee participation in compensation decisions may modify perceptions of fairness, and subsequently how this participation effect may be modified by culture.

**Keywords:** compensation, cultural values, fairness perception, organisational justice, participatory decision-making.

### 1. Introduction

While compensation is a central component in the relationship between employees and employers, it is a relatively under-researched area within

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human resource management and industrial-organisational psychology. Instead, where much of the compensation research has occurred is within the disciplines of economics and finance, areas where agency theory dominates. An alternative perspective for studying compensation is through the lens of organisational justice. While distributive justice, mainly in the form of equity theory (Adams 1963), has been the primary theory, more recent scholarship has also focussed on procedural (Thibaut & Walker 1975) and interactional justice (Bies & Moag 1986).

In this paper, I explore the relationship between theories of organisational justice and perception of fairness as they relate to compensation and rewards. A consequence of the subjective nature of perception is that a reward system that is perceived to be fair by some people may not be seen as fair by others. In the examination of the reasons for these differences, I invoke a cultural perspective, relying on Hofstede’s (2001) cultural typology. In addition, I explore the extent to which employee participation in compensation decisions may modify the perceptions of fairness, and subsequently how this participation effect may be further modified by culture. One particular contribution of this paper is that I explicitly discuss justice perceptions as an explanatory variable of the relationship between culture and compensation practices, something that frequently has been omitted in prior scholarship (e.g. Schuler & Rogovsky 1998). It is this particular role of the justice perception that forms the basis of the discussion on the potential role of employee participation.

2. Compensation Systems

Compensation systems come in many flavours. Generally speaking, the core components are base pay, performance based pay, bonuses, skill based pay, fringe benefits, and non-monetary benefits and rewards. Compensation can be awarded on an individual basis, group basis, or organisational basis (Gagné & Forest 2008). The overall characteristics of a compensation system are determined by the particular mix of these components. As each of these components can be administered in a vast range of ways and combined in an equal number of different ways, it is impossible to list all the combinations. The best we can do is to group the systems into general characteristics based on their predominant features. For example, many organisations offer a combination of base pay and performance-based pay or bonuses, and some also offer a combination of individual performance
rewards and group / organisation performance rewards. Some of the main compensation practices are listed Table 1.

Table 1. Compensation Practices

<table>
<thead>
<tr>
<th>Compensation practice</th>
<th>Criteria</th>
<th>Level of Determination</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base pay</td>
<td>Position and rank</td>
<td>Individual / organisational</td>
</tr>
<tr>
<td>Pay-for-performance</td>
<td>Per-unit output</td>
<td>Individual</td>
</tr>
<tr>
<td>Merit pay</td>
<td>Performance appraisal</td>
<td>Individual</td>
</tr>
<tr>
<td>Bonus</td>
<td>Performance appraisal</td>
<td>Individual</td>
</tr>
<tr>
<td>Skill based</td>
<td>Training / education completed</td>
<td>Individual</td>
</tr>
<tr>
<td>Gain sharing</td>
<td>Achievement of goal or target</td>
<td>Group</td>
</tr>
<tr>
<td>Profit sharing</td>
<td>Profitability</td>
<td>Organisation</td>
</tr>
<tr>
<td>Stocks / options</td>
<td>Stock market performance</td>
<td>Organisation</td>
</tr>
<tr>
<td>Benefits</td>
<td>Loyalty / seniority</td>
<td>Individual / organisation</td>
</tr>
<tr>
<td>Cafeteria plans</td>
<td>Employee choice</td>
<td>Organisational policy Individual choice</td>
</tr>
<tr>
<td>Non-monetary</td>
<td>Informal</td>
<td>Informal</td>
</tr>
</tbody>
</table>

Source: based on Gagné & Forest (2008).

3. Organisational Justice

Perceived fairness is critical for any effective compensation system as it is instrumental for employee pay satisfaction without which organisations will be faced with a wide range of undesirable outcomes such as increased turnover, absenteeism, and reduced performance (Williams, McDaniel & Nguen 2006). In many respects, fairness perception can be said to be the most critical consideration in the development of a compensations system, as it (as a component of the overall HRM system) has to be congruent with overall organisational culture and strategy (Taggar, Sulsky & MacDonald 2008).

In the organisational justice literature, the distributive justice theory has had the longest currency. According to Adam’s equity theory (1963), employees make comparison of their input as a proportion of output and with those of other employees. Fundamental to this appraisal is the perception of fairness. If an employee puts in twice as much effort as the worker next to him or her but does not receive a proportionately higher award, he or she
may perceive the balance as unfair. As a response, the employee will likely reduce the effort in order to rebalance the situation.

It is worth noting, however, that perception of fairness is more complex than a simple comparison of relative distribution of input and output, as per equity theory. Recent decades have seen increasing attention paid to the fairness of process, as in procedural justice (Thibaut & Walker 1975), and to the fairness of interaction, as in interactional justice (Bies & Moag 1986). Thibaut and Walker originally conceptualised procedural justice in the context of legal disputes. The point was that it was not only the outcome of the dispute that mattered in the perception of fairness but also the process that led to the outcome, the main idea being that disputants would be more likely to find an otherwise not optimal outcome acceptable if they perceived the process as being fair and unbiased. Noting the applicability to non-legal contexts, the concept was expanded to include organisational settings. For such settings, Leventhal (1980) defined and proposed six criteria that would guide perception of fairness. These include: (a) consistency of application, (b) suppression of bias, (c) information accuracy, (d) correctability of flawed or inaccurate decisions, (e) representativeness of ethical and moral standards, and (f) inclusion of the opinion of those affected.

As procedural justice relates mainly to the formal aspects of justice, Bies and Moag (1986) introduced the notion that the less formal aspects of interpersonal treatment are also an important component in people’s perception of fairness. Bies and Moag referred to this as interactional justice. Later, other scholars proposed that a distinction be made between different components of interactional justice: (i) one that addresses the manner in which people are related to, referred to as interpersonal justice; and (ii) one focusing on the level, accuracy, and quality of information that is shared with those affected, referred to as informational justice (Greenberg 1993a, 1993b). While Greenberg’s illustrations of informational justice involve mainly interpersonal communication, informational justice could conceptually just as well apply to information communicated through the more impersonal formal channels of the organisations, and thus could be considered a part of procedural justice.

4. Compensation and Fairness Perceptions

In addition to the actual compensation and rewards employees are offered, the process which determines the rewards is an important consideration. This is the case both with the variable rewards and the fixed
rewards. For example, satisfaction with the actual payout of performance based pay is dependent on the perceived fairness of the process of determining that pay.

*Pay for Performance*

Sometimes, objective measures are available, such as piece rate, and as these do not involve a subjective evaluation of the third person, these are often seen as more acceptable to employees. However, these can be problematic for a number of reasons: 1) employees may find the rate per piece unacceptably low, and history with piece rate pay is fraught with issues of increased productivity only resulting in a lower piece rate. Rather than being an issue of comparative fairness between employees – i.e. Adam’s problem of inequity is resolved – it becomes an issue of fairness between company profit and employee payout; 2) piece rate pay rewards quantity, and thus such a system risks creating a climate that compromises on quality; 3) in many industries, objective measures of performance output are unavailable or unreliable; 4) in industries were production levels vary, a pure piece rate system can result in extreme fluctuations of pay for employees, which may be perceived as unfair considering the employees’ commitment to work for this particular company over taking another job. In order to alleviate some of these problems, combinations of variable and fixed / base pay are common (Dessler & Cole 2008).

*Bonuses*

Individual bonuses and merit pay are systems where rewards are based on slightly longer-term performance measures. Rather than paying for individual pieces, they reward performance over a longer period of time. These performance evaluations may include qualitative measures, such as performance appraisal from a supervisor, but could also include quantitative measures such as financial performance or sales over a period of time. Again, objective measures may be perceived as more reasonable and visibly more directly related to input, but these too are not perfect. Financial performance and sales are not always related to effort; the business and economic environment can have big impact on performance. Also, a problem with these measures is that they generally reward short-term performance over long-term objectives (Kerr & Slocum 2005).
Skill-based Pay

Instead of rewarding performance output, some organisations use a skill based pay system. Rather than paying everyone doing the same type of job the exact same wage, employees are rewarded according to their skill level, often assessed by the level of education. For example, someone acquiring a master’s degree might immediately be bumped up to high salary grade (Murray & Gerhart 1998). This system is relatively objective – and typically quite formalised – but it has problems with recognising alternative avenues of skills acquisition, and some people may see this as unfair.

Criteria: Individual vs Group

A compensation and reward problem that is frequently discussed is the distinction between individual rewards and group- or organisation-based rewards. The problem is the paradox of encouraging team work and team mentality while also wanting to reward individual performance. These are often seen as being incompatible (Hollensbe & Guthrie 2000). While many have argued that individual rewards encourage competition between employees, which is inconsistent with a team approach (Kerr 1975), others have pointed out that only rewarding based on team performance can lead to an unequal amount effort among the team members, causing “loafing” (Dessler & Cole 2008). Furthermore, high achievers may perceive it as unfair that individual effort and contribution is not rewarded.

Benefit Plans

An important component of a total compensation system that has received a notable lack of research attention (Dulebohn et al. 2009) is employee-sponsored health benefits, pensions, and other “fringe benefits”. Employers have for decades offered health benefits and pensions plans, partly with the intention to retain employees by rewarding long-term commitment, in particular through defined benefit pensions plans (Dulebohn & Werling 2007).

A more recent issue is the potential disconnect between plans offered and the needs and wishes of employees. Recognising that not all employees have the same preferences and priorities, many companies have started to offer flexible or “cafeteria” plans where employees have options in which provisions to pick. However, as it still is difficult to determine which types of options will be of interest to employees, Dencker, Joshi, and Martocchio (2007, p. 209) suggest employees engage in a “rewards dialogue” in order to
find the ultimate combination of benefits. Interestingly, research has shown
a stronger relationship between benefit satisfaction with “perceived level”
benefits than with the “true” actuarial value of benefits (Williams 1995), and
support has not been found for any relationship between actuarial value of
benefits and benefit satisfaction (Dulebohn et al. 2009).

Non-monetary Rewards

Non-monetary benefits are a part of the total compensation package
that should not be neglected. Some of these are formal and specified,
such as holidays, vacation, and sick leave, while others are either informal
or discretionary, such as employer-sponsored training, perquisites, status,
and promotions. Non-monetary benefits also include flexible in-work
schedules, accommodation for care of family, as well as job security. While
these benefits may be considered extra and non-essential, they still are an
important factor of the work climate and overall organisational culture
(Yeganeh & Su 2011). The intangible benefits are difficult to assess in terms
of fairness, but the more specified ones, such as vacation or sick leave, are
directly comparable to what other employers are offering and thus something
employees will take into account when appraising the overall fairness of the
compensation they receive.

5. Culture and Justice Perception

Next, using Hofstede’s culture framework (2001), I will examine
how employees with different cultural values may respond to different
compensation practices. I do so informed by Bruner’s (1957) theory of
perception according to which perception involves a process of categorisation
into learned categories, a learning process that to a considerable degree is
informed by culture (Mendoza-Denton & Mischel 2007). Transactions are
only going to be perceived as fair, or unfair, if the appraiser perceives them
as such, and what is perceived as fair by one person may well be perceived
as unfair by another. From the viewpoint of perception as a learned process
of categorisation, it only makes sense that perception of justice will be
culturally determined.

In management literature, culture is frequently conceptualised into
categories. By far the most popular conceptualisation of culture is the
framework developed by Hofstede (1980). Hofstede originally proposed
four main dimensions to measure and explain differences in cultural
values between different countries: Power Distance (PDI), Individualism
vs Collectivism (IDV), Masculinity vs Femininity (MAS), and Uncertainty Avoidance (UAI). While Hofstede’s model has been criticised for being overly simplistic, such as not being equipped to deal with value variability within nation boundaries and including too few dimensions (McSweeney 2002), it is still considered a highly useful model, particularly as it is the model that everyone knows and one that is parsimonious and easy and clear to communicate (Triandis 2004, Williamson 2002). The reason for using the Hofstede model over GLOBE (House et al. 2004) or the model by Schwartz (1992, 1994) is that the GLOBE model to a large extent is an extension of Hofstede, replicating many of the same cultural dimensions (Peterson 2004), while the Schwartz model has primarily been used as a measure of individual-level values, with relatively few empirical studies using Schwartz’s (1994) culture-level dimensions. The Hofstede model is also particularly important as it has served as a foundation and inspiration for many subsequent models (e.g. Triandis 1995, Trompenaars 1993, Wagner III 1995), many of which include similar dimensions, individualism-collectivism, and power distance in particular.

Individualism vs Collectivism (IDV) describes the extent to which societies value individual agency and attributes in contrast to collectivist societies where people identify primarily with their group and where group needs usually trump individual needs. Considering these differences, it is expected that compensation that is based on individual criteria is going to be most congruent with individualist cultures while collectivist cultures are going to be more consistent with group- or organisation-based criteria. Thus, based on the categorisations in Table 1, I propose:

**Proposition 1a:** Employees with an individualist orientation will perceive individual performance pay as fair and group performance rewards or lack of performance rewards as unfair.

**Proposition 1b:** Employees with a collectivist orientation will perceive group rewards as fair and individual rewards as unfair.

Power Distance (PDI) relates principally to how societies deal with differences in power, in particular how accepting members are of inequality and of a hierarchical structure. People in high power distance cultures do not expect power and resources to be distributed equally and think of hierarchical order as natural and therefore do not question it. In low power distance culture, however, people are interested in equality and equal distribution of power and resources. In terms of compensation, it follows that:
Proposition 2: Employees with low Power Distance orientation will perceive high wage dispersion as unfair. Employees with high Power Distance orientation will perceive high wage dispersion as fair.

Hofstede defines Masculinity vs Femininity (MAS) on the basis of stereotypical male and female traits. Whereas masculine cultures are defined as valuing competition, assertiveness, and aggression, feminine cultures are characterised as nurturing, caring, and cooperative. It follows that compensation structures based on competition between individuals will be inconsistent with feminine cultures. Such compensation practices include bonuses based on ranked performance evaluations and variable pay practices that put employees in direct competition with each other. At the same time, however, variable pay practices – where there is not a fixed amount of added compensation to be spread around, such as a piece-rate system where increased individual performance is directly linked with total group or organisational output – can be consistent with feminine cultures. Conceptually there is some overlap with other dimensions, e.g. individual competition is a masculine characteristic that is also associated with individualist cultures and the feminine characteristic of cooperation is also associated with collectivism. Accordingly, I propose:

Proposition 3: Masculine culture will be consistent with pay-for-performance, merit pay, and bonuses, while feminine culture will be consistent with profit sharing, gain sharing, and generous benefits.

Uncertainty Avoidance (UAI) is defined by the extent to which people are comfortable with uncertainty and ambiguity. Uncertainty avoidance cultures are typically risk-averse and usually have a more rigid code of practices. It should follow, then, that fixed pay will be consistent with high uncertainty avoidance and variable pay with low uncertainty avoidance. In a similar vein, people in low uncertainty avoidance cultures will prefer flexibility in compensation practices and systems such as cafeteria plans will be preferred by them. Accordingly, I propose:

Proposition 4a: High-UAI culture will be consistent with base pay and long-term benefits and inconsistent with variable pay practices, such as pay-for-performance, merit pay, bonuses, gain sharing, profit sharing, and stocks / options.

Proposition 4b: Low-UAI culture will be consistent with pay-for-performance, merit pay, bonuses, gain sharing, profit sharing, stocks / options and cafeteria plans, and inconsistent with pure base pay.
6. A Participative Solution?

As indicated in the description of organisational justice theory, there is more to perception of fairness than a mere evaluation of outcomes. According to procedural justice theory, outcomes and decisions are much more likely to be perceived as fair if they are perceived as being arrived at through a process that is consistent, free of bias, incorporates accurate information, is correctable, representative of ethical standards, and incorporates the opinions of those affected. Furthermore, according to theories of interactional justice, including interpersonal and informational justice, perception of fairness will also depend on the manner in which people feel they have been treated as well as the extent to which information regarding the decision has been shared. As most of these elements relate directly to the practice of participative management (Cotton et al. 1988, Miles 2012), it is highly plausible that employee participation might increase the perception of fairness regarding compensation decisions and system. Research has already indicated that employee participation in goal setting leads to increased acceptance and commitment to goals, which in turn leads to increased motivation (Locke & Latham 2002, Roberson, Moye & Locke 1999). Other empirical research has also supported the notion that participative decision-making is associated with a higher level of perceived fairness (Cohen 1985). As process and information-sharing are key determinants of fairness perception, I propose the following:

Proposition 5a: Employees participating in setting criteria for performance-related pay, such as setting piece rate, performance goals and standards as well as performance evaluation criteria and process, will be more likely to perceive compensation as fair and more motivated to meet targets, goals, and objectives.

Proposition 5b: Employees participating in determining specific components of benefits will perceive them to be of higher value than those employees who do not.

Proposition 5c: Employees participating in determining standards for skill-based pay will be more likely to perceive compensation as fair.

Culture and Participative Decision-making

The relationship between culture and participatory decision-making (PDM) has been relatively underexplored. Responding to the absence of the cultural context in the PDM literature, Hofstede writes, “one cannot write meaningfully about organisational participation without embedding it within
a national cultural context” (Hofstede 2001, p. 109). Sagie and Aycan (2003) acknowledge that while some authors have mentioned the importance of cultural considerations, there are has been almost no empirical testing of the relationship between culture and PDM. It is notable that now, more than ten years later, such research is still very limited.

Hofstede, himself, primarily discussed participation in relation to power distance, suggesting that people in low-PDI cultures will be more interested in participation than people in high-PDI cultures, where people are more likely to accept hierarchical structure and decision-making. The GLOBE study on leadership (House et al. 2004), which includes dimensions that are similar to Hofstede’s, found that low uncertainty avoidance, low power distance, high collectivism, and high “gender equalitarianism” were all associated with a participative leadership style. As participative leadership conceptually is strongly related to participative decision-making, I propose:

*Proposition 6*: Participation in compensation decisions will only increase the perception of fairness in cultures that are low-PDI, low-IDV, low-UAI or low-MAS

### 7. Discussion and Conclusion

While there is some previous research on the relationship between culture and compensation practices (Schuler & Rogovsky 1998) as well as between compensation and perceptions of fairness (Shao *et al.* 2013), there is little research that has explored these concepts together. By linking these concepts together, I have proposed explanations for the reasons why various compensation practices may have different success in different cultures. In this regard, I have highlighted the role of justice perception as an explanatory variable.

In addition to enhancing the theoretical understanding of the link between culture and compensation practices, the consideration of how justice is perceived has practical significance for organisations operating in different cultures. It is often not sufficient for managers to know which compensation practices typically work in a particular cultural location since different types of business have different needs. Furthermore, if companies want to use compensation practices strategically to gain competitive advantage, it is not enough to know what typically works. A deeper understanding of the relationships between culture, justice, and compensation will help managers interested in developing innovative compensation approaches. This is
particularly important because cultures are not as homogenous as culture indices may tempt us to believe (Fischer & Schwartz 2011). This is especially relevant for organisations with multicultural workforces and organisations with a mix of native and expatriate employees.

I have proposed that employee participation in decision-making may increase the odds of particular practices having the desired effects and will help organisations devise systems that have the desired effect in terms of meeting justice expectations. However, I have also raised the issue that participation will not have the same effect in all cultures. Thus, while employee participation will be useful for some, it will likely not be universally useful. Bringing participatory decision-making into the discussion with culture and compensation not only strengthens our understanding of the relationship between culture and compensation but also strengthens our understanding of the relationship between culture and participatory decision-making.

**Limitations and Future Research**

A potential limitation of this paper is that I have limited the considerations of culture to the four original Hofstede dimensions. A consequence of this choice could be that certain cultural influences on fairness perception have been neglected. It is possible that utilising a culture model with a broader set of cultural dimensions, such as Schwartz (1992, 1994) or GLOBE (House et al. 2004), would have provided for a more nuanced exploration. However, I have chosen Hofstede’s model primarily for its conciseness and parsimony, and because its predominance and popularity as a cross-cultural values model makes it more easily accessible to a broader range of readers.

The propositions presented here still need empirical testing. While some empirical research has examined the relationship between culture and compensation, the relationship between employee participation and culture has been relatively neglected. Future research will need to examine not only the cultural effects on participation but also how these interact in shaping the perception of fairness with regard to compensation. In particular, future research needs to take into account justice perception and pay satisfaction as explanatory variables.

Culture is by definition a macro-level construct, which means that investigations into the effect on individual perception and satisfaction may need to involve multi-level methods (Chao 2000). Such research may need to consider measuring culture at the macro-level and individual level (in the
form of individually held values), the moderating and mediating effects of personality and organisational characteristics, as well as outcomes measured both at individual and organisational levels.

Overall, this paper has attempted to bring together in discussion a number of critical variables relevant to organisations either operating in different cultural settings or employing multicultural workforces. As such, I believe this discussion will be relevant for both researchers and practicing managers.

**Bibliography**


Abstract

Sprawiedliwość i kultura w postrzeganiu sprawiedliwego wynagradzania

Mimo że wynagrodzenie stanowi istotny komponent w relacji pomiędzy pracownikami a ich pracodawcą, w badaniach z zakresu zarządzania zasobami ludzkimi oraz psychologii industrialnej i organizacyjnej wciąż nie przykłada się do nich wystarczającej wagi. Dziedzinami, w których poświęca się temu zagadnieniu najwięcej miejsca, są ekonomia i finanse, czyli obszary, w których dominują teorie agencyjne przedsiębiorstwa. W artykule zaprezentowano powiązania pomiędzy kulturą a praktykami wynagradzania z perspektywy teorii sprawiedliwości, a także zestawiono rolę teorii sprawiedliwości dystrybutywnej z bardziej aktualną teorią proceduralną oraz sprawiedliwości interakcyjnej.

Wskazano, w jaki sposób postrzeganie sprawiedliwości determinuje dopasowanie praktyk wynagradzania w stosunku do różnych kultur. Uwzględnienie opinii jednostkowego pracownika w tym zakresie nabiera znaczenia, gdyż istotnie zmienia się w zależności od kultury narodowej, a coraz więcej organizacji ma do czynienia ze wzrostem liczby pracowników wywodzących się z różnych kręgów kulturowych. Dokładnie przeanalizowano także postrzeganie sprawiedliwości jako zmiennej objaśniającej związek pomiędzy kulturą a praktykami wynagradzania, co często było pomijane we wcześniejszych pracach badawczych. Ponadto zwrócono uwagę, jak partycypacja pracownicza w zakresie wynagradzania może wpływać na postrzeganie sprawiedliwości, a następnie – jak stopień partycypacji może być modyfikowany przez kulturę.

Słowa kluczowe: wynagrodzenie, wartości kulturowe, postrzeganie sprawiedliwości, sprawiedliwość organizacyjna, partycypacja w podejmowaniu decyzji.