

Executive remuneration: Considerations of South African remuneration committees

**A research report submitted by
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Abstract

South Africa is ranked as one of the countries in the world with a big wage gap. The debate in academic communities, the business world and for policy makers is that there appears to be no explanation for the variations in executive pay and research has been inconclusive about the factors which are used by remuneration committees to determine the pay of these executives. This research aimed to gain deeper insight into the determination of executive remuneration, including the factors that are typically considered by South African remuneration committees, with a view to providing these committees with standard criteria to assist in ensuring that the interests of all stakeholders are considered by these committees in the future.

A convenience sample of 13 remuneration committee members participated in semi-structured interviews. Findings indicate that a similar process is followed and similar factors are considered by remuneration committees in South Africa. Relevant information is gathered around executive considerations, legal and ethical considerations and market considerations, and then scrutinised in line with a package that addresses fixed pay, short-term incentive pay and long-term incentive pay for the executive. Governance of the process is considered to be non-negotiable.

Keywords: Agency theory, Corporate governance, Executive remuneration, Wage gap, Remuneration committee

Declaration

I declare that this research project report is my own work. It is submitted in partial fulfilment of the requirements for the degree of Master of Business Administration at the Gordon Institute of Business Science, University of Pretoria. It has not been submitted before for any degree or examination in any other university. I further declare that I have obtained the necessary authorization and consent to carry out this research.

Signed: 

Name: Wilfred Mwiwa

Date: 07 November 2018

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Chapter 1: Introduction to Research Problem

1.1 Introduction and Background to the Research

South Africa is ranked as one of the countries in the world with a big wage gap. This is evidenced by the way Chief Executive Officers (CEOs) of the top South African companies listed on the Johannesburg Stock Exchange (JSE), are earning as much as 725 times what their workers earn (Bronkhorst, 2014). This difference in earnings has resulted in much controversy and ethics debates in the media, as well as in the business and academic space, about the level of remuneration and the amount of performance pay for South African CEOs (Core, Holthausen & Larcker, 1999; Edmans & Gabaix, 2016). This debate has been observed in different fields like economics, corporate finance, contract theory and through the inequality theory in South Africa (Edmans & Gabaix, 2016).

CEO remuneration can be described as an economic reward which is composed of a basic salary, incentives and share options (Murphy, 2013). The South African Companies Act (Companies Act 71 of 2008) contains numerous criteria relating to executive remuneration. These include the disclosure of all remuneration and benefits for all directors of the organisation in the annual financial statements, and for companies listed on the JSE there is a requirement to comply with the King Code of Governance Principles (“King Code”) for the determination of executive remuneration (VDMA, 2011). The Institute of Directors, South Africa (2016) recommends in the King IV Report™, herein referred to as King IV, that the board of directors should make sure that the director’s remuneration is used to ensure that the company creates value in a sustainable way within the social, environmental and economic context in which the company operates. In addition, the board should establish a remuneration committee (REMCO) which will be tasked with recommending to the board, a fair and responsible remuneration policy which will be able to create value in the foreseeable future. This policy should be able to address the following factors in the long term: the base salary; variable remuneration; termination pay; sign on; retention and restraint payments; provisions of claw backs; commissions; and fees for non-executive directors. These factors, which are included in the policy, should be aligned to the terms of the company’s act. King IV also states that the board of directors must ensure fair and responsible executive remuneration practices when compared to overall employee remuneration to safeguard the company’s alignment with the principal of ethical leadership. King IV goes

ahead to highlight the key areas in which the board need to adhere to while implementing the remuneration policy, these areas are attracting, motivating, rewarding and retaining executives, promoting the strategic objective of the company, promoting positive outcomes, promoting ethical culture and good corporate citizenship. There is a strong suggestion in King IV that the remuneration policy should be approved by the shareholders and this is to make sure that the interests of shareholders are taken in to consideration when rewarding the executives (Institute of Directors, South Africa, 2016).

Despite the requirement of the South African Companies Act and the King IV report, the remuneration of chief executives in South Africa has been in the press for a long time as it has become a very intriguing and popular topic that has piqued public interest. The interest around executive remuneration in academic communities, the business world and for policy makers has occurred because there appears to be no explanation for the variations in executive pay (Graham, Li & Qiu, 2011).

According to Shah, Jared and Abbas (2009), much research has been conducted in the 20th century with a lot of attention and controversy around CEO remuneration. However, the research has been inconclusive about the factors which are used by remuneration committees to determine the pay of these executives. There is also controversy regarding which of these factors are considered the most important when it comes to determining CEO remuneration, what attributes are used, and how this influences CEO remunerations. In addition, researchers see CEO remuneration from different perspectives which creates disagreement about which factors are really used by remuneration committees to determine executive remuneration. Shah et al. (2009) continue to argue that there is still much needed research to determine the factors which are used by the remuneration committee of companies to determine CEO remuneration because of internalisation, diversification at the work place, maximisation of shareholder value and the current collapse of various large organisations.

Irvine (1987, p. 236) introduces the principle of enablement which argues that, “it is morally wrong when a person’s actions enable other people to do wrong”. If this principle is used in the corporate context, it implies that shareholders should not do something which will enable the directors to act unethically. This unethical behaviour can be seen as an act of misappropriation of funds but also as doing something which is unjust to the society. Critics of CEO remuneration practices argue that the board does not structure these CEO’s packages so that they can reflect the idea of maximising outside shareholder value because the board of directors is influenced by the CEO (Core et al.,

1999). There have been instances where the CEO remuneration was high even though the company did not add any value to the shareholders, such as in the case of Enron where the long-term goals of the company were compromised due to the executives being highly compensated (Core et al., 1999).

A company board of directors should act in the best interests of the shareholders and should not make decisions that will impact the shareholders negatively. They are also tasked to advise and keep a close eye on the top management of the company and protect the interests of the company shareholders by establishing the remuneration of the executives. At the same time, the company needs to treat employees fairly and in an equal manner as outlined in the companies act.

Executive remuneration in South Africa is a complex and sensitive issue. Preston (as cited in Bronkhorst, 2014, para. 18) states that,

“South African companies and their stakeholders face the challenge of having to compete in a global marketplace but also having to confront the enormous levels of inequality within the South African society.... The current level of income inequality within listed South African companies should be a concern for shareholders, as well as the fact that in some companies this inequality is rising”.

Bronkhorst (2014) cautions that if these matters are not attended to timeously, business operations will be affected negatively by social or political forces. This has been seen in the mining sector where employees were demanding R12 500 per month but the company's management insisted that they had no money to pay this large sum of remuneration. However, they went ahead in awarding executive's large amounts of incentives.

Another aspect that has been a focus of attention is where the contracts of executives are not designed to maximise the shareholders' interests. Remuneration committee have been criticised in the past for not balancing the interests of the shareholders and the executives but rather focusing on the interest of executives (Edmans & Gabaix, 2016). Viviers (2015) states that remuneration committees, of South African JSE listed companies, have moved to justify the amount they pay their executives. They argue that in order to attract, retain and motivate talented executives, they have to offer competitive packages to them. Bronkhorst (2014) agrees and in addition suggests that executives must be well compensated for companies to maintain their competitive position.

However, it remains unclear as to how these remuneration committees balance these packages with the earnings of the rest of the employees.

The executive pay debate is not only a South African problem but rather a worldwide issue. Jensen and Murphy (2010) argue that In the United States of America (USA), for example, executive pay has not been excessive but there are major disconnects have been observed between the performance of the company and the performance incentives paid to executives. They suggest that the board should allocate a bigger percentage of equity to executives, offer cash incentives for great performance and give penalties for poor performance.

The South African companies act lays down certain criteria for determining executive remuneration but it is unclear if this criterion is being carried through to the boardroom by the remuneration committee. Due to this there is a need to come up with a model which remuneration committees can use to rein in any excessive pay to executives and avoid the principle of enablement.

1.2 Research Problem

The research problem is that despite the South African company's act laying down certain criteria for determining executive remuneration, there are no standard or benchmark guidelines of the factors to consider when determining executive remuneration packages within large South African organisations. This has resulted in remuneration committees of different organisations using different criteria, which may not always be in the interests of all stakeholders. The research gap is therefore that there are no standard guidelines for factors to be considered by remuneration committees in South Africa when determining executive remuneration.

The usage of different metrics by different organisations has led to huge pay gaps if you compare the same executive positions of different organisations. In addition, with the high rates of executive remuneration stated in annual reports and the apparent discussions on media platforms, employees perceive that they are underpaid. Therefore, something needs to be put in place which protects both the interest of the shareholders and the employees of the organisation.

Excessive remuneration of CEO's in South Africa has been widely publicised and subjected to public scrutiny because there is an argument that the high remuneration that CEO's are receiving does not take the long-term interest of the company or the interests of the shareholders into account, and at the same time it is widening the wage

gap between executives and ordinary workers. According to Steyn (2012), the chairman of business leadership in the country, Bobby Godsell, recently said that there is a need to establish a commission tasked to investigate the high pay debate in South Africa similar to the one established in the United Kingdom's high pay commission. After studying excessive executive pay, this commission "recommended that company executives are paid basic salaries, remuneration reports are standardised, listed companies produce fair pay reports, employees are represented on remuneration committees and an independent body is permanently established to monitor high pay" (Steyn, 2014, para 16). Similarly, "Gerald Seegers, South African partner of PricewaterhouseCoopers, is of the opinion that new executive reward models are required that can be tailored to specific businesses that are both relevant and simple in terms of design and number of elements" (Theunissen & Oberholzer, 2013, p. 1509).

1.3 Research Purpose

The remuneration committee plays a major role in arriving at, and monitoring, the remuneration of a company's executive. However, the level of remuneration and the amount paid for performance of CEO's, has led to much debate within the South African public and also business community. There is also little evidence of research conducted in the South African environment which identifies awareness of the factors used by remuneration committees when determining executive pay. Therefore, there is a strong need to determine which particular remuneration factors may be used when determining executive pay.

Remuneration committees in South Africa have been criticised for paying too little attention to determining the remuneration of the executives because there is a view that they are influenced by the CEO and they don't structure the CEO's remuneration package to maximise shareholder value. There have also been some accusations of CEOs who have been accused of focusing on short-term goals rather than long-term goals. These CEOs get incentivised based on short-term performance, hence missing performing for the long-term future of the company.

1.4 Scope of the Research

A number of academics (Edmans & Gabaix, 2009; Tosi & Gomez-Mejia, 1994; Yanadori & Milkovich, 2002) who have researched executive remuneration, have narrowed their research to focus only on the remuneration of the CEO because they are the most influential people in the company (Bussin, 2015a). Therefore, this study will also focus on the remuneration of the CEO in the framework of executive remuneration.

1.4.1 Aim and Objectives of the Research

The objectives of the research are to:

- Explore how executive remuneration packages are determined by remuneration committees
- Investigate the use of policies and procedures in determining executive remuneration
- Understand what remuneration committees believe are the most important factors of consideration for executive remuneration
- Understand what remuneration committees believe are the least important factors of consideration for executive remuneration

1.5 Structure of the Research Report

Chapter 1 has introduced the research problem, giving some background to the study and the reason for the need for the study. Chapter 2 provides a discussion of relevant literature and theory relating to the research. The research questions are then listed in chapter 3 while chapter 4 sets out the methodology and design used for the research. A consistency matrix is provided in Appendix C, which illustrates alignment of the research problem presented in Chapter 1, the research questions presented in Chapter 3, the literature discussed in Chapter 2 and the research methodology and design discussed in Chapter 4. The findings of the research are then presented in Chapter 5, in line with the research questions. Chapter 6 discusses these findings together with relevant literature. Chapter 7 concludes the study. It highlights the principle findings of the research and provides recommendations to various stakeholders. Limitations of the study and suggestions for future research are also presented in this chapter.

Chapter 2: Literature Review

2.1 Introduction

Executive remuneration is a widely debated topic amongst academics (Edmans & Gabaix, 2016) and has attracted much public scrutiny due to the large increases apparent in remuneration levels and differing remuneration practises globally (Kumar & Zattoni, 2016). In recent years there has been an increasing interest in executive remuneration among academics in the fields of economics, law, organisation studies, accounting and finance (Pepper & Gore, 2015). The topic also forms a large part of the literature on corporate governance (Kumar & Zattoni, 2016). As such, numerous theories and frameworks within the different academic fields have been developed, discussed and argued among academics. This chapter presents a review of current literature relating to executive remuneration. Firstly, the role of the executive is stated and the shareholder value debate presented. Various types of executive remuneration are then introduced and the role of the remuneration committee discussed. Some of the most common theories on executive remuneration are then presented, followed by a discussion on various factors that could contribute to executive remuneration levels.

2.2 Executives and Executive Remuneration

Executives are the senior people in an organisation, who are tasked by the shareholders, to run the organisation (Finkelstein, Hambrick & Canella, 2009). They are also commonly members of the board of directors (Usman, Akhter & Akhtar, 2015). The chief executive officer (CEO) holds the most senior position among executives. In most cases, the CEO might fulfil the role of chairman in the organisation (Usman et al., 2015).

The CEO of a company has a role to play that is pivotal to managing company resources for the shareholders in an unstable environment (Bussin, 2015a). They hold the power to make decisions and control the company's resources (Fama & Jensen, 1983 and Boyed, 1994 as cited in Usman et al., 2015). These CEO's are then compensated with a remuneration package in return for their services (Finkelstein et al., 2009).

Executive remuneration packages can include various forms of remuneration and incentives (Guay, Core & Larker, 2002; Murphy, 2013). These include, but are not limited to: basic salaries; annual bonuses; restricted shares; performance shares; retirement benefits; travel allowances; and other long-term incentives. Executives can also receive a lump sum amount at different times during their employment, such as with signing on fees, termination pay out or retrenchment pay out (Murphy, 2013).

According to Gayle, Golan and Miller (2015), the structure of executive remuneration packages differs from one organisation to another and these differences can be attributed to various labour market elements, such as, the job description and required tasks, opportunities for development, job security and the work environment. Other factors that may also be taken in account include the number of employees in the organisation, CEO efficiency, CEO availability in the industry, market remuneration rates of other CEO's, listing requirements, regulatory systems, company policies, board size, and the governance system in the company (Conyon, 1997).

2.3 The Remuneration Committee

The remuneration committee, also referred to as the compensation committee, is a subcommittee of the board which is established with a view to assisting the board perform their role because the board has many responsibilities (Tao & Hatchison, 2013). Remuneration committees are tasked with the responsibility of overseeing remuneration matters in the company. This responsibility includes making sure that there is alignment between the shareholders interest and those of the directors, using executive remuneration as a tool (Tao & Hatchison, 2013).

Remuneration committees perform a critical role in the organisation as they determine and monitor the remuneration of the company's executive (Conyon, 1997; Liao & Hsu, 2012). Literature shows that there many factors which remuneration committees can take into consideration when determining CEO remuneration, such as company size, company complexity, company financial performance, number of employees, CEO efficiency, CEO availability in the industry, market remuneration rates of other CEO's, listing requirements, regulatory systems, company policies, board size, and the governance system in the company (Conyon, 1997).

It is also the responsibility of the remuneration committee to align the interests of shareholders to those of the directors by encouraging executive performance, and hence also the company's performance. This can be achieved by using equity remuneration to motivate the executives (Hillman & Dalziel, 2003). This remuneration also enables the company to attract, retain and motivate employees while, at the same time, making sure that the goals of the company are achieved (Liao & Hsu, 2012).

Despite all the factors that remuneration committees examine when determining executive remuneration, there is little evidence of standard practises or a model that can be used to determine the most considered factors. Bussin (2015b) posits that despite

the plethora of factors that can be considered in the executive remuneration decision, the decision makers have little knowledge of how much each of these factors should influence their decisions. The relative weighting of each factor remains unknown which poses problems as remuneration policy tends to be reactive and change as the situation changes.

Conyon (1997) states that the majority of members in a REMCO should be non-executive and that all members should be members of the board of directors. Not only should these non-executive directors be independent, the chairman of the remuneration committee should also be an independent non-executive director. The chairman of the company should not be the chairman of the remuneration committee but should attend by invitation only (Conyon, 1997).

According to Conyon (2014), it has been established that most studies indicate that remuneration committees composed mainly of independent directors, have good corporate governance, which means that these companies tend to comply with the rules and regulations set in the act.

2.4 The Shareholder Value Debate

Bussin (2015a), states that the central role of the CEO is to manage company resources in an unstable environment for the benefit of the shareholder's returns. However, there is much debate amongst academia and the public which argues that executive remuneration is not always aligned to maximising shareholder value (Edmans & Gabaix, 2016).

According to Dunlop and Andelman (1997 as cited in Perel, 2003, p.381), "The best bargain is an expensive CEO.... You cannot overpay a good CEO and you can't underpay a bad one. The bargain CEO is one who is unbelievably well compensated because he's creating wealth for the shareholders. If his remuneration is not tied to the shareholders' returns, everyone's playing a fool's game". Jensen and Murphy (2010) argue that it is okay to pay CEO'S based on the value they create for the shareholders because that is the main objective of the shareholders. Shareholders want to pay the lowest possible remuneration to CEO's for a fixed level of organisational performance, or to pay a fixed level of remuneration for the highest possible organisational performance (Krause, Whitley & Semadeni, 2014). However, Jensen and Murphy (2010) caution that the value created by the CEO for the shareholders is sometimes short-lived and not sustainable for the long-term future of the company and therefore CEO

remuneration packages should not only be based on the value they create in meeting the short-term goals of the organisation but the long-term sustainability of the company should also be taken in to account. They state that many companies have failed due to being short sighted in basing the CEO's remuneration on their short-term performance and forgetting that the long-term future of the company needs to be the main factor otherwise short-term gains will be wiped out in the future. Murphy (2013) also highlight that although basic salaries, bonuses, retirement benefits and allowances can be easily measured because they are paid on a regular basis, there are many other types of remuneration which are not easily measured as they are determined based on the performance of the company over a year or more.

Almost 30 years ago Jensen and Murphy (1990) argued that appropriate CEO remuneration should be based on shareholder wealth as this aligns to the objectives of the shareholders. This argument, according to Krause et al. (2014), was the initiator of the debate around the relationship between CEO remuneration and organisation performance, as well as the factors that influence this relationship. Ntim, Lindop, Osei and Thomas (2015) argue however, that the focus of the debate around executive remuneration and performance, stems from two opposing theoretical points of view, namely the optimal contracting theory or agency theory and the managerial power theory.

2.5 Agency Theory

The determination of executive remuneration levels and remuneration practises has been widely studied and a number of frameworks have been developed around executive remuneration (Kumar & Zattoni, 2016). Although some view executive remuneration as being optimised for shareholder value (Gabaix & Landier, 2008 and Rosen, 1992 as cited in Kumar & Zattoni, 2016), scholars in the field of corporate governance have adopted a number of theories to explain the high rates of executive remuneration over average worker remuneration (Kumar & Zattoni, 2016). Among these, agency theory has become the most dominant (Bratton, 2005 as cited in Pepper & Gore, 2015).

Agency theory relates to the relationship between two parties which occurs when the shareholder of a company is a different person to the individual who manages the same company. In this case, the shareholder of the company is referred to as "the principal" and the manager for the principal is referred to as the "agent" (Bussin, 2015a).

Agents are used by shareholders to run the organisation as these agents do not share the emotional burden of any investor risk and they can maintain a better focus in running the organisation (Jones, 1995). A principal-agent problem occurs when the shareholder of a company and the directors have different views of how the company should be run (Hope & Thomas, 2008). The shareholders desire is to make a return while the director is concerned with the remuneration he/she receives, for the work he/she does (O'Reilly & Main, 2010). This becomes a problem when the different views are not in the best interests of the company (Bebchuk & Fried, 2003).

The conflict that arises between the principal and the agent is a result of each the individual's differing levels of risk experiences. The CEO as an agent is unlikely to experience the same kind of risk as the company shareholders because in most cases the CEO has not invested their own equity into the company as the shareholders have done (Jensen & Meckling, 1976). Agency theory suggests that the principal can limit any conflict of interest with the agent by putting together appropriate incentives for the agent. These incentives will try to align the interest of the agent and those of the principal who is the shareholder. These incentives are referred to as monitoring costs. When the principal incurs these monitoring costs it limits any opportunistic action the agent may have which could affect the overall return to the principal. The principal may also incur costs, referred to as bonding costs, which are paid to the agent in order to acquire resources. This guarantees the principal that the agent will not take any actions that will affect the principal negatively but rather ensures that the principal is rewarded for his or her investment in the company through appropriate actions taken by the agent. However, even when the principal pays all these costs, some conflict between the principal and the agent remain because the principal experiences a residual loss on their investment. The combinations of the principal's monitoring cost, the agents bonding cost and the residual loss is referred to as the agency costs (Hill & Jones, 1992).

Optimal contracting occurs where remuneration practises ensure that the goals of the executives and of the shareholders are in agreement (Van Essen, Otten & Carberry, 2015). An efficient contract or optimal contract minimises agency costs and "maximizes the net expected economic value to shareholders after transaction costs (such as contracting costs) and payments to employees" (Guay et al., 2002, p. 27). Ntim (2015) explains that with optimal contracting, the executive has little contact with independent executive boards who determine the appropriate managerial contracts and incentives aligned to the executive's performance, thereby lessening the control of the executive to influence their remuneration.

2.6 Managerial Power Theory

The managerial power theory builds on to agency theory by addressing the power that CEO's often have over board members due to both structural and social-psychological influences on executive remuneration decisions. These mechanisms dissuade shareholders from challenging high levels of remuneration for executives or remuneration agreements which do not adequately align to company performance and can in fact exacerbate agency problems (Van Essen et al., 2015) and lead to the executive influencing their own pay in a positive way (Guthrie, Sokolowsky & Wan, 2012).

According to Essen, Otten and Carberry (2012 as cited in Bebchuk & Fried, 2004), there are many reasons why directors would not have an incentive to negotiate for the best interest of the shareholders but rather choose to have a remuneration arrangement that will suit the executives. The first reason is the director's need for a powerful status and to be re-elected into their status positions on the board. They will therefore favour the executives during remuneration discussions as the executives have a major influence during director selection to the board (Main, O'Reilly & Wade, 1995). Secondly, there is the social and psychological situations which have been found to be common within small groups of people, such as friendship within a group and loyalty within a certain group. These social and psychological mechanisms are also common to boards of companies and make directors less likely to challenge the CEOs running these companies (O'Reilly & Main, 2010). Thirdly, CEOs are in a powerful position to compensate directors with director fees or remunerations, allowances, and donation contributions. These rewards could be used by the CEO to make it likely that they can exert power over board members to their advantage, thereby giving them a competitive edge when negotiating for their remuneration (O'Reilly & Main, 2010).

Guthrie et al. (2012) state that the power of influence that executives have can be limited by appointing more independent directors which will improve the governance of the company. They found that CEO remuneration changed by 17% more in non-compliant companies than in compliant companies, and that compliance was stronger in companies that had more independent directors. Governance is improved by independent directors on the board as they are able to reduce the power of the CEO and hence ensure that the correct process to determine CEO remuneration is followed whereby the executives' remuneration is linked to performance.

Company leaders also use forecasts to determine short-term goals that will maximise profits for the company. Adjustments are made to the performance of a company when

short term targets are not met in order to justify the executive pay. In some instances, financial statements can be seen, with adjustments like extraordinary items or non-recurring expenses, which are excluded from the performance ratios to make the company performance look better. Other expenses which are not operating expenses, like taxes, may also be excluded, which poses the question of where the money will come from to pay these taxes if they are not included (Guthrie et al., 2012).

2.7 The Principle of Matching Theory

Principle matching theory is another theory used to explain executive remuneration decisions. The matching principle is where CEO pay does not match their contribution and services rendered during that period. Guthrie et al. (2012), discusses that while serving as Apple's interim CEO from September 1997 to December 1999, Steve Jobs was only paid two dollars despite the share price of the company quadrupling during this period. However, to reward Jobs for the good performance, the board of Apple compensated him with a bonus, in the form of an aircraft valued at 90 million dollars, which was only recorded in the 2001 and 2002 financial statements of the company. The salary of two dollars was not the correct remuneration for Jobs as he was not paid a salary in line with his good performance. This indicates an issue from a corporate governance perspective. In addition, the bonus received was only recorded in the organisation's financial statements two years later. This is a matching principle issue because the bonus should have been recorded at the time the performance of Jobs was evaluated. Sometimes the reverse happens where CEO's are paid when they have not made an excellent contribution and this presents corporate governance issues. Expenses which are incurred by the business should be reflected in the same period in which the revenue related to those expenses are reported. This will make sure that the company's results are correctly reflected which will make sure that if the executives are rewarded based on their performance, the remuneration which is paid to them is correct (Dechow, 1994).

2.8 The Conflicted Remuneration Consultants Theory

According to Murphy and Sandino (2010), some large corporations make use of external executive remuneration consultants to guide the board on suitable pay for the executives. These consultants can help in determining remuneration levels; implement the company's short and long-term executive incentives; do a benchmarking exercise to compare the current executive remuneration to those of the industry and the market; as well as help in designing the employment contracts of the executives, perform complex

tax calculations for the executive remuneration and also offer regulatory advice to the board. However, Murphy and Sandino (2010) caution that these consultants, who give advice to the board, face a possible conflict of interest and may therefore recommend a higher remuneration for the CEOs. This is because the consultants also derive large sums of money from these companies and the companies are run by the CEOs who they are recommending the remuneration for.

2.9 Factors to Consider in Determining Executive Remuneration

2.9.1 Legislation

CEO remuneration in the United States of America (USA) has attracted a lot of attention, as it has in the rest of the world, especially towards public listed companies. This attention has been discussed in public and also in the press for some time. With all this attention, there is still an incomplete understanding of the contractual terms which are inserted into executives' contracts that essentially determine CEO remuneration and their incentives and how the remuneration committee ties up the remuneration of the CEO and the performance of the company he leads. The fact that these contracts cannot be observed, has led to doubt among the public that these contracts usually optimally align the CEO remuneration to the performance of the company (De Angelis & Grinstein 2014).

According to Bebchuk and Fried (2003), companies have both masked and become inconsiderate to the amount of executive remuneration and pay for performance. As a result, the securities and exchange commission in the United States of America has issued a rule in which companies are required to disclose how they match the amount they pay their CEO with the performance of the company the CEO manages. This decision by the commission, to force disclosure of the remuneration, was driven by investors who argued that CEO remuneration packages were not disclosed properly or could not be understood by the investors. Under this rule, companies must provide more information about their CEO remuneration agreement; they also need to adhere to the disclosure measures which the company uses to determine the CEO remuneration, performance targets and the time frame of these performance targets. This type of disclosure is aimed at limiting the issue of agency problems and the pay is tied to the performance of the CEO.

2.9.2 Corporate Governance

According to Fama and Jensen (1983), agency theory leans towards a selection process that favours governance structures which reduce agency costs. These governance structures provide agents with actions to follow which are intended to reduce agency problems. They include the following factors: the law governing corporate behaviours; monitoring mechanisms like the company board and other control mechanisms.

Many companies have established committees to promote corporate governance, such as remuneration, audit, and risk committees, amongst others. The members of these committees are recommended to be independent because independent directors will monitor the work performed by the executive directors thereby reducing and limiting the powers the CEO might have in the company. It is through this monitoring that committees are likely to maintain higher level of corporate governance (Guthrie et al., 2012).

2.9.3 Performance Contracts

Fama and Jensen (1983) argue, that to limit this agency problem the company needs to motivate the CEOs by paying them incentives as the company performance changes. According to Angelis and Grinstein (2014), companies use different performance measures to monitor how their executives have performed in the company. These are then used by the remuneration committee to determine the CEO remuneration. The performance measures can be based on accounting performance measures, share performance measures, which is market-based performance, and non-financial measures. Accounting measures are estimated to account for 79 percent of the estimated value of performance remuneration, while 13 percent is attributed to market-based performance measures, which is share performance, and 8 percent is from non-financial measures. Accounting measures can include revenue, margin, net income, return on equity contributed by shareholders, economic profit, profit before interest and taxes, cost reduction, return on assets, cash flow improvements and earnings per share. Income measures account for 56 percent of the total accounting measures, 12 percent on revenue and 17 percent on returns.

There are major differences in the way companies use performance measures. Most of these companies rely on accounting-based performance measures which rely mainly on sales, profit and returns for the shareholders. This is mostly used for CEO'S with longer tenures as more mature companies tend to have more stable strategies. Where companies have complex business activities and more growth opportunities, the CEO'S are rewarded based on market measures instead of accounting measures (Angelis &

Grinstein, 2014). Angelis and Grinstein (2014) go on to argue that the lack of proper transparency of the CEO remuneration contracts leads to powerful CEO'S having the ability to reward themselves with performance pay for self-gain, rather than create value for the shareholders, hence increasing the agency problem.

Krause et al. (2014) argue that shareholders of companies who are referred to as principals, will not approve CEO remuneration which is high when there is poor company performance. In addition, it was found by Jensen and Murphy (1990) that pay performance for CEO'S indicates that their wealth changed by 3.25 dollars for every 1000 dollars the shareholders wealth changed. They also state that if the shareholder of the company had all the information about the CEO activities and the company's investment opportunities, the shareholder would be able to design a contract which would specify and enforce the actions the shareholders will be taking. Due to the fact that shareholders are unable to foresee the actions of the CEO and which of the actions they take will create shareholder value, it leads to agency problems. When this happens, agency theory predicts that the remuneration policy of the company should be drafted to incentivise the CEO so that he can select and implement decisions which will add value to the shareholders. In addition to remuneration contracts, there are other mechanisms which can be used to ensure that both the agent and the principal's interests are aligned. These include mechanisms like corporate governance which aims to reduce agency costs through the alignment of the interests of the parties (McKnight & Weir, 2009).

2.9.4 Company Size

Shah et al. (2009) argue that different studies have found that there are economic factors, social factors and agency theory factors which are used to explain the factors used to determine the CEO remuneration. These factors are very complex and they have led to much debate about them. They go ahead to mention these factors being such things as company size, market risk, company performance, power, CEO tenure, ownership by the CEO, and the growth of the company.

Academic research done in the past shows a strong relationship between company size, which is measured according to revenue and resources, and the CEO remuneration (Shah et al., 2009). According to Core et al. (1999), CEO'S get paid more when the size of the company is big, compared to their counterparts who run small companies in comparison. McGuire, Chiu and Elbing (1962) maintain that CEO remuneration is related to company size. Roberts (1956) argues that even though CEO remuneration is linked to company size, the relationship to the level of earnings is artificial and not considered

when the influence of size is taken in to account. CEOs who run companies which have more turnover and at the same time high profit should be compensated more than those who run companies with less sales and profits as this is a good indication of a good return to the shareholders. Shareholders will reward the CEO's who run big companies more as they have more responsibilities than the CEO's who run small companies. Big companies are very complex in terms of structure, operations, number of employees, revenue generated and profits compared to small companies. The revenue and profit turnover are very debatable as these are not the only indicators that the CEO is creating wealth to the shareholders. Other factors like return on assets, market price, net asset value, economic value added, price per share, return on equity, cash flow improvement, earnings before interest tax and depreciation, are some of other factors which should be also be looked at. We have seen in recent times most companies mainly reward their CEO's based on the bottom line performance but this should not be the only factor because overlooking the other factors could have a negative impact of the company in the long term.

Finkelstein and Hambrick (1989) mention that CEO pay depends on various factors like company size, company complexity, company performance, CEO power, the board vigilance and the CEO's human capital. They continue to argue that CEO remuneration is linked to the company and the profits generated by the company. Finkelstein and Hambrick (1989) also include other factors which determine CEO remuneration, like industry factors which might be a concentration, or barriers to entry of other companies which can create slack conditions, and the CEO labour market which could affect the supply and demand of CEOs in the industry. They also argue that some external factors like product differentiability or growth rates will also have an impact. Simon (1957) disagrees that company size is linked to CEO remuneration by arguing that it is based more on the demand for CEO's, the ability to pay them and the reporting structures which are established in big companies. Even though company size matters when determining the CEO remuneration, some CEO's are involved in more complex structures, demanding expectations compared to others, The structure a company creates is also critical, companies with a lot of subsidiaries, divisions, or reporting structures, will reward their CEO more than companies which do not have that complexity. This means that these CEO's are in demand in the market and will require more incentives in the labour market as their talents will be scarce (Agarwal, 1981).

2.9.5 Organisation Complexity/ Diversity

According to Finkelstein and Hambrick (1989), company complexity may include multinational operations or a politicized environment, but the one which is critical in determining the CEO remuneration, is corporate diversity. Finkelstein and Hambrick (1989) argue that the more diverse the company is, the higher the remuneration of the CEO. This is because the CEO will have to deal with more complex issues in this company than the CEO who leads a company which is not that diverse.

Finkelstein and Hambrick (1989) indicate that CEO's who have made investment in themselves, in form of acquiring education and training, should be able to earn more than their counterparts who are less educated and experienced. This is because these CEO's bring training to the company and because they are educated and experienced they could be more productive than those who are not. There is also the argument that you might be well educated but if you do not have the required experience you might not perform to the required level, which means that experienced CEO's will be rewarded more than the ones who are not experienced. The CEO's who are experienced are in demand which means that they will demand more money in the market.

2.9.6 Competitor and Market Information

Remuneration committees use competitive benchmarking in the market to gather information which is used to determine executive pay. Properly structured information from peer groups provides great information to the board for designing a competitive pay level which is necessary to attract, retain and motivate top executives. This is done by comparing the executive pay levels with that of other organisations which are of similar industry, size, performance, capital markets, customers and suppliers (Bizjak, Lemmon & Nguyen, 2011).

Benchmarking for CEO pay should be driven by available information obtained in the market. This information should only be used if the CEO has viable employment options in this market. The information which is used for benchmarking provides strong evidence for determining a remuneration package for a CEO coming from outside the organisation, whereas the evidence used for an internal candidate includes a number of additional internal factors (Martijn Cremers & Grinstein, 2013).

According to Cordeiro, He, Conyon and Shaw (2013), executives are rewarded and penalized based on the performance of the company compared to industry and regional benchmarks. If a CEO performs well compared to his peers in the same industry, he will

be rewarded with a good remuneration package and the contrary would happen if he does not perform well.

2.10 Conclusion

Recent years have shown increased interest from academics and scholars around executive remuneration with a number of theories on executive remuneration having been developed. Literature highlights the important role of executives in managing company resources in order to create value for the shareholders. As a reward for their services, the executive receives a remuneration package which is typically determined by a remuneration committee. This committee may take various factors into consideration when determining the executive remuneration package, however, there is still much debate around what factors should be considered and how these can be incorporated into balancing the executive remuneration package to the performance of the company. In addition, there is little literature available pertaining to the determination of executive remuneration in South Africa. This gap in the literature is what has prompted this research project to gain a deeper understanding of the factors that are considered by remuneration committees in large South African organisations, when determining executive remuneration. Chapter 3 outlines the research questions formulated for this research project.

Chapter 3: Research Questions

3.1 Research Questions

Research question 1: How are executive remuneration packages determined by remuneration committees in South Africa?

This question aims to understand what the top of mind thoughts are of the remuneration committee members as these will provide insight into the influence that the CEO or the executive has in determining the package and whether the shareholders are regarded as top priority.

Research question 2: What policies and procedures do remuneration committees follow when determining executive remuneration?

This question aims to identify if legislated processes are being followed such as those laid out in the companies act. In addition, are there internal policies and processes that the organisations have in place and to what extent are these being followed?

Research question 3: What do remuneration committees believe are the most and least important factors of consideration for executive remuneration?

This question will aim to identify the most critical and least factors which the remuneration committee will consider. The most critical factors are like experience of the executive, performance, company size, complexity of the company, regulatory requirements, (Conyon, 1997).

3.2 Conclusion

It is envisioned that by gathering an understanding of the factors that are typically considered by remuneration committees in South Africa when determining executive remuneration, and the importance placed on these factors, the research will provide insight into standard criteria that can be used by remuneration committees in the future. This can then assist with ensuring that the interests of all stakeholders are considered by these committees.

Chapter 4: Research Methodology

4.1 Introduction

The purpose of this research was to gain deeper insight into how executive remuneration is determined by remuneration committees in large South African organisations. The research intended to understand what factors are commonly considered by the remuneration committees when determining executive remuneration packages as well as which of these are deemed the most and least important to the remuneration committee members. In addition, Furthermore, aside from understanding what the factors are in determining executive remuneration, the research aimed to gather an understanding of the extent to which various policies and procedures may be followed by the remuneration committees. Although some research has dealt with executive pay, the results vary and there is no clear explanation of the variation in executive pay due to the fact that different researches have looked at different factors which are used by remuneration committees to determine executive pay (Graham, Li & Qiu, 2011).

4.2 Introduction

This section provides an overview of the research methodology and design used for the study. Firstly, the research philosophy and approach are outlined, followed by the rationale for choosing a qualitative research design. The chapter includes a discussion of the population and sampling procedures used and describes the unit of analysis, the research instrument, the process of data collection and the procedure for analysis of the data. Finally, limitations to research are considered, trustworthiness stated and ethical considerations given.

4.3 Choice of Methodology

4.3.1 Research Philosophy

To design a good research strategy, a researcher should be aware of their ontology and epistemology which are their philosophical assumptions about the world around them, and about research, as these will affect how they carry out their research (Klakegg, 2016). According to Ritchie, Lewis, Nicholls and Ormston (2013, p.1), ontology refers to the researcher's "beliefs about the nature of the social world and what can be known about it" and epistemology refers to the researcher's "nature of knowledge and how it can be acquired".

In social research one's ontology is based on their perceptions of social reality either as being independent of one's awareness and interpretations or developed through one's experiences and perceptions, and whether the nature of social behaviour is shared and generalisable. On the other hand, one's epistemology concerns their way of acquiring knowledge about social reality. In this case, the researcher must question their influence on the information gathered, the truth of information gained, and their method of finding patterns and associations in the information (Ritchie et al., 2013).

The philosophical assumptions of how a researcher views the world, are the foundation to the research approach and strategy used by the researcher (Saunders, Lewis & Thornhill, 2009). This research followed an interpretative philosophy as the researcher was interested in the views and perceptions of the subjects to the research. Interpretivism implies that the researcher uses his own **judgement to make sense of the data** during the process of enquiry. Interpretivism is the opposite of positivism which assumes that hypothesis can be tested from the objective data collected. However, interpretivism allows the researcher to be subjective and develop an accurate understanding of the phenomena (Bryman & Bell, 2015).

4.3.2 Research Approach

Deductive and inductive research approaches are used to evaluate an argument (Creswell, 2014). A deductive approach is followed when the reasoning process starts with general knowledge and then becomes specific through a line of logical arguments, such as with the testing of hypotheses in quantitative research. On the other hand, qualitative research usually follows an inductive approach where the reasoning involves forming general conclusions by way of a number of observations (Ary, Jacobs, Sorensen & Walker, 2013). This research followed an inductive approach whereby exploratory data was gathered through semi-structured interviews and then simplified through a process of synthesis and grouping to find meaning in the data and determine various factors that can be considered by a remuneration committee when determining CEO remuneration.

4.3.3 Research Strategy and Choice of Investigation Design

A phenomenological research strategy was considered the most appropriate strategy for this research. Phenomenology is a form of qualitative research whereby the researcher tries to understand the experiences of the participants and then uses the data obtained from these experiences to analyse and interpret that information (Petty, Thomson & Stew, 2012). Qualitative research was considered a good fit for this study as the study

intended exploring the participant's inputs and developing an understanding of the factors that could be considered when determining CEO remuneration.

4.3.4 Research Design

A research design can be cross-sectional or longitudinal (Becker, Bryman & Ferguson 2012). According to Creswell (2014), when a researcher is trying to understand an issue at a specific time, a cross-sectional design is used, but when the researcher wants to study an issue over a longer period of time, a longitudinal research design is more appropriate (Neuman & Robson, 2012). Time and cost constraints for the research would not allow for the collection of data over an extended period of time and therefore a longitudinal design was not appropriate for this research. Instead, this research was cross-sectional in nature and involved collecting data at a specific point in time.

4.4 Population and Sampling

4.4.1 Population

According to Sekaran and Bougie (2016), a population is described as the entire group of entities, such as people events or items of interest which the researcher aims to study or make assumptions about. The target population for this research was all remuneration committee members of corporations in South Africa.

4.4.2 Unit of Analysis

A unit of analysis refers to the entity to be analysed in a study. It is the "what" or "who" that is being studied (Sekaran & Bougie, 2016). In this research, the unit of analysis is the individual remuneration committee individuals who participated in the research.

4.4.3 Sampling

A sample is a sub group of the population which the researcher can draw results from and to which they can generalise the results to the population being studied (Sekaran & Bougie, 2016). Selecting a sample or small group of the population to conduct research with is common practice as the cost and time frame in which the research needs to be conducted means that it is not always possible to do research on the entire population (Acharya, Prakash, Saxena & Nigam, 2013). Being aware of the sampling designs and sample size helps someone understand why a particular method of sampling is used by the researcher, this will in turn help them understand the cost implications of different methods.

Research sampling can be classified as probability or non-probability sampling. Probability sampling is where the likelihood of a researcher selecting any unit from a population is equal and known, while with non-probability sampling the chances of the researcher selecting a particular unit, is unknown (Bryman & Bell, 2015). Non-probability sampling involves targeting potential research participants because of known characteristics that will be beneficial to the research, such as having specific knowledge on the topic (Sekaran & Bougie, 2016).

A sample of 13 participants were targeted to conduct the research with. These participants were selected because they were remuneration committee executives who were believed to have the necessary knowledge about the topic and were therefore deemed capable of providing relevant inputs to the research. The selection of these participants therefore involved the use of the researcher's judgement. The researcher also used their judgement on the sample size to determine at which point the data collected, reached a level of saturation (Kumar, 2011). It was estimated that a sample of 13 executives would be adequate to reach data saturation point.

Convenience sampling and quota sampling are non-probability sampling techniques which were used in the selection of the participants (Sekaran & Bougie, 2016). Convenience sampling allowed the researcher the freedom to choose whoever was available for inclusion and who agreed to participate in the research. However, it was also deemed critical to ensure that these individuals fit the required respondent profile for the study, to get value out of the research. Therefore, besides the fact that the participants need to be knowledgeable in the subject at hand, it was also believed that a quota sample should be selected where half the participants were male and half were female as these gender groups could have had differing perceptions of the phenomena. The sample for the research was therefore made up of eight men and seven women who form part of a remuneration committee within various large organisations in South Africa.

4.5 Research Instrument

Research instruments can be defined as measurement tools which are mostly designed to obtain data on a research topic (Myers, 2013). For this study a semi-structured questionnaire or interview guide (Appendix A) was designed to assist the researcher in conducting the semi-structured interviews. The semi-structured interview guide contained questions to be asked of each participant, ensuring that all participants were asked the same general questions. These questions were aligned to the research objectives to ensure that relevant data was gathered. However, the researcher had the

freedom of asking the questions in any order that made sense during the interview discussion. According to Bryman and Bell (2015), semi-structured questionnaires allow for the collection of consistent data by ensuring that all participants are asked a standard set of questions. However, a more in-depth understanding can be gathered through probing of the participants responses. The use of a semi-structured questionnaire was therefore also beneficial as it allowed the researcher to probe further when a deeper understanding was needed or when the participant mentioned something that the researcher wished to explore further. The questionnaire consisted of three sections. The first section gathered demographic data which was intended to put the participants at ease and to gather an understanding of some of their background. The second section contained the main questions intended to answer the research objectives and these were in three parts, each part addressing one of the research objectives. Finally, the last section brought the interview to a close by asking the participants if they wished to share anything further or provide recommendations going forward. This also provided them with the opportunity to ask any questions of the researcher.

The semi-structured questionnaire was piloted with two participants to ensure that there was a full understanding of the questions by the participants, that relevant information was being collected to answer the research objectives and that the length of the interview was comfortable for the participants. After the pilot there were no changes to the questionnaire as all the questions answered the research objectives.

4.6 Data Collection Process

Personal semi-structured interviews were conducted with 13 individuals who were currently serving on one or more remuneration committees in mid to large organisations and within a variety of industries in South Africa. In total, the participants represented 13 different industry sectors. The interviews were conducted over a 10-week period and lasted between 40 minutes and one and a half hours.

In order to collect data for the research, potential participants were contacted and invited to participate in the research. They were provided with some background to the research and were informed of what their participation would entail. The participants were also assured of their confidentiality and anonymity in participating in the research. Upon agreement to participate, interviews were scheduled with the participants and they were requested to block time out in their diaries so as to ensure that the interview can run smoothly without interruptions and that the researcher does not run out of time to conduct the interview.

Prior to the interviews taking place, the participants were sent an e-mail and provided with some of the general questions that would be covered during the interviews so that they could prepare themselves. However, they were not provided with the complete research instrument so as to prevent any bias responses occurring. Included in this email, the participants received an information sheet which explained the background to the research and their role in the research, as well as reassurance again of their confidentiality and anonymity.

At the start of each interview, the participants were given an opportunity to ask any questions they may have. Thereafter, they were asked to sign an informed consent form (Appendix B) which confirmed that they were participating voluntarily and that they had been informed of their rights to confidentiality, anonymity and that they had the right to exit the interview at any time. They were also informed that the interviews would be audio recorded with their permission and that the audio recordings would be used only for the purposes of transcribing the interviews for analysis of the data.

The use of a semi-structured questionnaire provided flexibility for the researcher to explore the participants responses in-depth but also provided for consistency of data collection across participants (Smith, 2015). The audio recording of interviews, which were later transcribed, ensured that there was an accurate record of the participants responses. In addition, brief notes were taken by the researcher during the interviews, which enabled him to reflect on the most critical aspects to be probed further to gain greater insights. However, the researcher ensured that the note taking was not extensive as it could detract from the flow of the discussion. These notes were also used for reflection during data analysis.

4.7 Analysis Approach

Data collected was analysed using ATLAS-ti, a software analytics tool for qualitative data analysis. The analysis involved the coding of data, following which codes were grouped into themes pertaining to each of the research objectives. These themes are used as the basis of discussion in Chapter 5 which presents the results of the research.

According to Elo, Kääriäinen, Kanste, Pölkki, Utriainen & Kyng (2014), there are three main steps to analysing qualitative data. These main steps are preparing the data; organising the data; and the final step is reporting of the research findings. Content analysis or thematic analysis are methods used in qualitative research to code and

interpret patterns of data which are then grouped into concepts or themes for reporting (Braun & Clarke, 2014).

Thematic analysis is used when the words from the participants are used to create codes and the codes are then grouped into themes based on the literature. Content analysis is used when the researcher codes the data and groups it (Cho & Lee, 2014). The analysis of data for this research was done using a combination of content and thematic analysis techniques.

The transcripts of each of the semi-structured interviews was used as the base to prepare and organise the data. Firstly, the researcher read through the transcripts to ensure familiarity and understanding of the content of the data. After this, the process of coding the data could take place whereby the researcher coded the participants' responses line by line from the transcripts.

The ontology of the researcher was that the reality of what the participants shared originates from a degree of shared understandings which has been shaped by their lived experiences (Ormston, Spencer, Barnard, & Snape, 2014) as a remuneration committee member. The codes that were used emerged from what the participants said or from concepts identified in the literature.

After coding, the codes were split, merged, grouped and ungrouped repetitively in order to simplify the data into manageable concepts or themes (Appendix F). This was done within the context of each of the research objectives. During both the coding process and the theme development, the researcher reflected on his epistemology by questioning his influence on the information gathered and the methods used in finding patterns in the data, so as to find the true meaning of the data (Ritchie et al., 2013). Making sense of what the data was saying was key to developing the relevant themes or concepts. The resulting themes or concepts were then used as the basis of interpreting and reporting on the research findings.

4.8 Limitations

According to Creswell (2015), limitations to the research are any issues that the researcher has no control over and can therefore potentially undermine the research. These limitations need to be considered and documented as part of the research. This research project had the following limitations:

- The relatively short time slot available for the researcher to conduct the interview with each of the participants, limited the quantity of data that could be collected. This highlights the importance of using a semi-structured interviewer questionnaire as the researcher was able to ensure that all the questions were covered during the interview.
- Another limitation to this research was that the sample was small, hence the findings of the research cannot be generalised to the entire population. The research was intended to explore the issue at hand and further research with a larger sample may be required to confirm the findings.
- The researcher had no prior experience in this industry and his knowledge base of the topic was from his learnings during the review of literature. Therefore, there are potentially questions that the researcher may have omitted to ask.
- There is a potential for participant bias as there was a limitation of being able to source the participants due to their high-ranked positions at director level. The researcher made use of his own network of individuals in these senior roles to gain access to potential participants.
- The credibility of the participant's answers could potentially be a limitation in that the individuals may have withheld certain information that they wished to remain private. However, the researcher made every attempt to ensure that the participants were comfortable to provide truthful and complete answers to the research questions by assuring them of their confidentiality and anonymity.

These limitations were identified prior to the collection of data and where possible, measures were put in place to reduce any impact on the trustworthiness of the study. However, some of the limitations may be addressed through future research which is outlined in Chapter 7.

4.9 Trustworthiness

Ritchie et al. (2013) explain that the measures of reliability and validity used in quantitative research which involves mathematical measurements, are not really appropriate in qualitative research studies. However, the principles of validity and reliability are still appropriate. To explain further, in qualitative research reliability can be translated to 'sustainable' or 'replicable' and validity to being 'well grounded'. These principles can help to assess the strength of the data.

The principle of "trustworthiness" is often used to describe validity and reliability in qualitative research literature (Anney, 2014). According to Connelly (2016), the four

criteria for assessing trustworthiness in qualitative research that are accepted by most qualitative researchers today, are those outlined by Lincoln and Guba (1995) and include credibility, transferability, dependability and confirmability. Ritchie et al. (2013, p. 271), state that “all of these features lie at the heart of reliability in its broadest sense and are key to appraising the soundness of a study”.

4.9.1 Credibility

The **credibility** criteria relate to the truthfulness of the data and the rigour in which the data was collected and analysed to provide a correct interpretation of the participant’s views (Anney, 2014). There are a number of ways that a researcher can ensure that their research is credible, including being reflective of their role in the research, providing transparency of the data collection and analysis process, as well indicating methods used to minimise any bias that may have resulted (Twining, Heller, Nussbaum & Tsai, 2017). In order to enhance the credibility of this research study, the approach to the research design, data collection and analysis process has been clearly outlined and detailed.

During the research design, strategies for ensuring attention to detail were considered so that the researcher remained focused. Morse, Barrett, Mayan, Olson and Spiers (2002) indicate that the researcher must remain focused and systematically check, monitor and make certain that the data fits within the conceptual work of analysis and interpretation”. During data collection, the researcher took care not to influence the participant’s responses and ensured that he understood what the participant was saying by repeating what was being said in his own words and getting confirmation from the participant that this is what was meant. In addition, the researcher asked further questions of the participant to ensure a clear understanding.

Generally, the phenomenological philosophy can be compromised by the subjectivity of the person doing the research and an inferior reliability of the findings. This means that two people doing the same research can arrive at different results based on the same problem observation at the same time (Kline, 2008). During the data analysis stage, the researcher read through the transcripts a number of times to ensure familiarity with the data. Coding the data involved a reiterative process and in order to circumvent researcher subjectivity, the common views of the research participants were used to develop the themes or patterns in the data. In addition, the analysis of data considered the findings from the literature to confirm constructs and participant verbatim comments were used to support the findings.

4.9.2 Transferability

The *transferability* criteria relate to the degree of generalisability of the findings to other contexts, other participants or wider theory (Anney, 2014; Ritchie et al., 2013). Bitsch (2005) recommends that in order to facilitate another researcher conducting the same study, a ‘thick description’ of the research process and design should be provided. This study has outlined the reasoning for the choice of a qualitative research design using semi-structured interviews. The research instrument has also been detailed and it was highlighted that this research instrument was used to ensure that all participants were asked the same basic questions.

Bitsch (2005) highlights the importance of describing the sampling procedure and purposeful sampling criteria, in order to ensure transferability. Participants to the research were purposefully selected based on their role as remuneration committee executives who were believed to be knowledgeable in the topic being discussed and therefore able to answer the research questions. It must also be noted that the sample was relatively small, and as indicated by Twining et al. (2017) the data can only be considered generalisable in a similar setting with similar participants. In this case, the participants were all from large organisations in South Africa and a quota was set on gender to gather the viewpoints of both men and women. The research findings were also considered in light of current literature from a global context.

4.9.3 Dependability

The dependability of the research refers to “the stability of findings over time” (Bitsch, 2005, p. 86). Ritchie et al. (2013, p. 285) describe this as the “security and durability of a research finding”. In order to enhance the dependability of this research the coding process involved a thorough examination of the interview transcripts and a reiterative process of coding and recoding. In addition, the researcher discussed the research findings with his supervisor as a form of peer examination to enhance reflexivity.

4.9.4 Confirmability

The confirmability criteria relate to the extent that the findings of the research can be confirmed by another researcher (Baxter & Eyles, 1997 as cited in Anney, 2014). Many of the actions taken in this research to enhance the credibility, transferability and dependability of the research, are also relevant in ensuring confirmability. All aspects of the research process have been clearly outlined, a detailed description of the sampling procedure, data collection and data analysis techniques has been given, and the findings have been discussed in line with existing literature.

4.10 Ethical Considerations

There are a number of ethical considerations that were considered whilst conducting this research. Firstly, the researcher ensured that he acted with professionalism at all times. The researcher made every effort to ensure that there were no adverse consequences for the participants to the research and that the reputation of GIBS, the researcher and the organisations in which the participants work, were upheld. Data collection therefore, did not take place until approval of the proposed questionnaire was received from the research supervisor.

It is also good practise to ensure that there is transparency for the participants to the research. As such, on inviting potential participants to the research, they were informed of the purpose and objectives of the research and that their input would only be used for the purposes of the research. They were also informed of their rights to confidentiality and anonymity, as well as their right to exit the interview at any point. Prior to conducting any interview, these issues were again discussed with the participants who were then able to ask any further questions they may have had.

Chapter 5: Results

5.1 Introduction

The results presented within this chapter are aligned with the research questions listed in Chapter 3. The research was exploratory in nature and therefore data collective was qualitative in nature, using semi-structured interviews for data collection. The rationale for using semi-structured interviews was to provide a level of adaptability to uncover insights on the research topic, as discussed in Chapter 4.

The presentation of results begins by describing the sample in order to lend understanding to the credibility of the participants to have the relevant knowledge to answer the questions posed. This is followed by a discussion of the findings according to the themes identified within the data analysis process. Where appropriate, selected participant verbatim comments are included to support the findings presented within each theme.

5.2 Research Findings

5.2.1 Description of the Participants

Non-probability, convenience sampling was used to select the participants to the research. This enabled the researcher to use his own judgement to select participants who were knowledgeable in the field of study. The 13 participants interviewed were all currently involved in remuneration assignments and had extensive knowledge on executive remuneration and rewards. With both current and past experience on remuneration assignments within various organisations and industries, the participants' cumulative experience spanned over 13 industry sectors (Figure 5.1). Their current job designations included executive chairmen, REMCO members/chairmen and heads of rewards/human capital with the majority of participants having between 21 to 30 years work experience (Table 5.1) and all of them had achieved some degree of tertiary education. The achieved sample had a mixture of both male and female participants of various ages. The youngest participants were in the 30 to 39 age group but the majority were between the ages of 50 and 59 years (Table 5.1). The fact that there were no younger participants could be attributed to the fact that younger individuals do not have the necessary experience to fulfil these senior executive roles.

Table 5.1: Description of Participants

Industry Sector Experience in Executive Remuneration	Number of Participants
Consulting	6
Banking	4
Employee Benefits and Insurance	4
Telecommunications	3
Public Sector	3
Healthcare	2
Energy	2
Mining	1
Retail	1
FMCG	1
Media	1
Tertiary Education	1
Non-profit	1
Total	13
Job Designation	Number of Participants
Head of Rewards / Human Capital	6
REMCO Member/ Chairman	4
Executive Chairman	3
Total	13
Participant Work Experience	Number of Participants
11 to 20 years	1
21 to 30 years	9
31 to 40 years	3
Total	13
Gender Distribution	Number of Participants
Female	5
Male	8
Total	13
Age Distribution	Number of Participants
30 to 39 years old	1
40 to 49 years old	3
50 to 59 years old	9
Total	13

Source: Authors own

5.2.2 Research Question 1: How are executive remuneration packages determined by remuneration committees in South Africa?

5.2.2.1 The Role of REMCO

In order to understand how executive remuneration packages are determined by REMCO, it was deemed prudent to first understand the role of the remuneration committee as a board sub-committee in the company. According to participant 11 the primary purpose of REMCO is that “*it is a sub-committee of the board*” and that there are four main functions of remuneration committees in organisations (Figure 5.1).

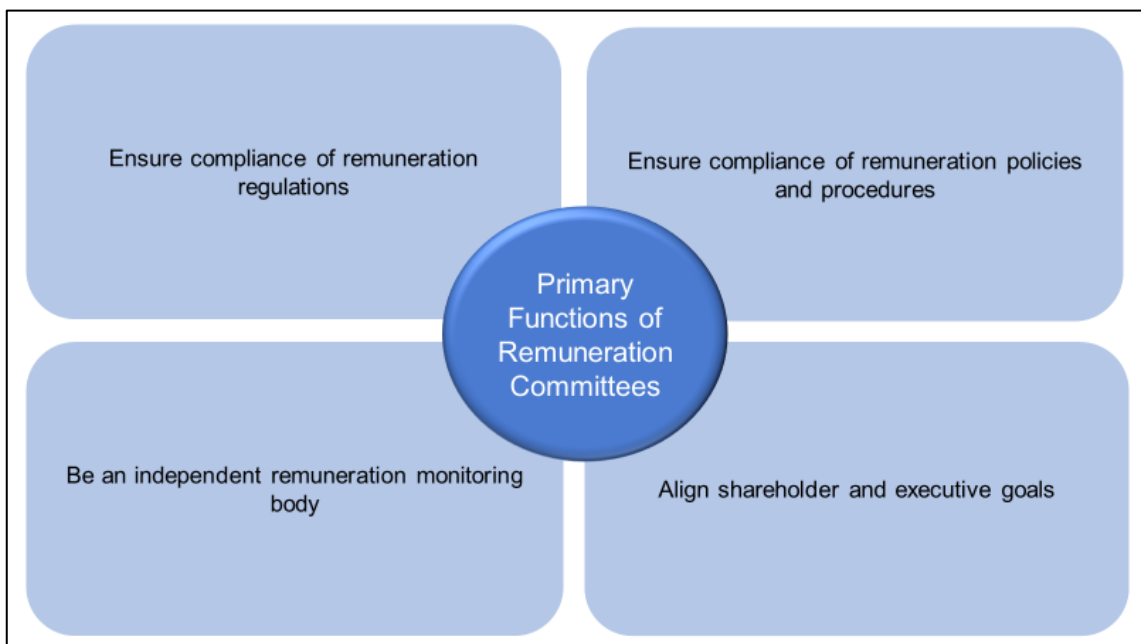


Figure 5.1: Primary Functions of Remuneration Committees

Source: Authors own

Firstly, the remuneration committee must ensure that the organisation complies with the remuneration regulations as set out in legislation such as the labour relations act, the companies act and the code of good practice identified by King IV. This means that they need to ensure transparency of executive pay. In addition, the boards of companies consider governance to be a serious issue which has resulted in many REMCO’s making governance key to their agenda when executing their mandate.

“King IV... requires far more transparency. So, you can read a REM report and you can get a good handle of how much [executives] get paid, the likelihood of investing, the performance conditions” (Participant 4)

“First of all, governance is a key thing on the REMCO’s agenda and they see that as their mandate and part of the charter.... So, I would say that South

African companies, in my view, are fairly governed. I'd say it's very good and [the board of] companies take it pretty seriously" (Participant 2)

From a compliance perspective, the remuneration committee acts as a watchdog on remuneration practices. This is because the shareholders need to be assured that remuneration policies are consistently applied across short-term and long-term incentives so that good corporate governance is maintained.

"You must make sure that your policies and your framework is being applied correctly because when shareholders vote, they vote not only the reward practise but they also reward on how well you apply. So, you can have these rules and then do the other. So, you have to make sure that you apply according to the rules" (Participant 2)

"They have to set targets for incentive plans to ensure that all good corporate governance is applied in terms of all the incentive plans. They apply the rules for your long-term incentives, the rules for your short-term incentives" (Participant 6)

In order to maintain good corporate governance, the board establishes REMCO to be an independent remuneration monitoring body. The independence of REMCO members is important to ensure that principles are consistently applied without any influence of bias. However, this does not imply that all REMCO members must be independent of the organisation, but rather that there needs to be at least three external independent members as outlined in King IV and that the interests of the executive should not be priority.

"Governance is about them being objective. So, governance is about principles that should be followed that are not influenced by personal bias or personal relationships" (Participant 8)

"You need an independent remuneration committee. Those are people that are frankly disinterested in the outcome for the CEO" (Participant 4)

"My experience in market practise is that usually the remuneration committees usually have a minimum of three independents and that kind of aligns with King. Some remuneration committees allow executives to either sit in the committee as a member or by invitation only. Generally, they won't let the CEO sit there. And that will be by invitation" (Participant 2)

It is important that REMCO ensures that there is alignment between the interests of the shareholders and that of the executive. Executives are appointed to run the organisation in the interests of creating value for the investment of the shareholders. REMCO therefore, must consider that executive remuneration packages align to the value created by the executive, without also disregarding that the remuneration package should benefit the executive as well.

“REMCOM also wants the best for the employees but they are there to protect the shareholders’ interests” (Participant 6)

“You are trying to act for the shareholder but also come up with something that is attractive and competitive for the executives but fair to shareholders and other stakeholders” (Participant 11)

5.2.2.2 Process Followed in Determining Remuneration Package

A lot of emphasis is placed on gathering relevant information and analysing this information, in order to determine a fair remuneration package for the executive which also considers the interests of the shareholders. The process for determining executive remuneration is conducted in four main phases and both the executives and the REMCO play a role in this process (Figure 5.2).

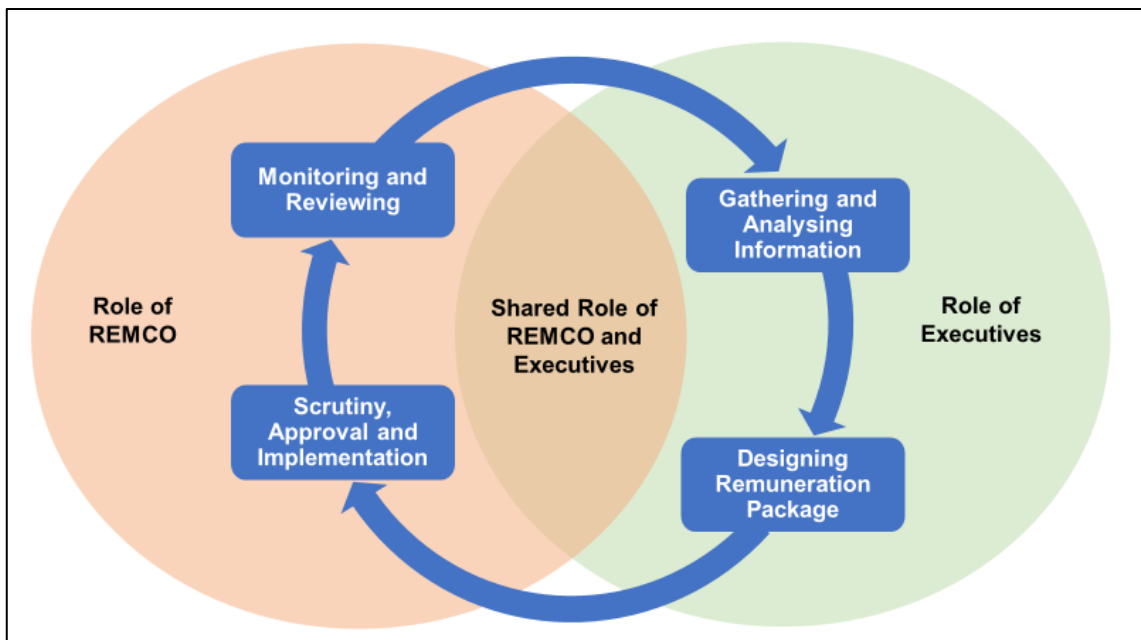


Figure 5.2: The Process for Determining Executive Remuneration

Source: Authors own

REMCO members may serve on multiple committees and they tend to have a great deal of knowledge about business in general as well as the regulatory environment. However,

they may require further information about a specific company to make informed decisions. This additional information relates to market information, company information, and executive information. Coupled with their existing knowledge, the sum of the information gathered, is analysed and used to arrive at a remuneration package (Figure 5.3). The information gathered may also be used to back up REMCO’s final decisions with the shareholders, if needed.

“...REMCO members tend to be extremely knowledgeable about the business Most of the REMCO members either are executives in other parts of the business but the non-exec members tend to serve on several other committees. So, they actually tend to be very well informed about business” (Participant 1)

“... it is really important from our perspective, why we always back it up with very good knowledge, so that if any shareholder walks in and says, tell me, where did you get that amount, where does that come from, or show me where the auditors have signed off on this incentive plan or this target that has been reached, that you have that material available” (Participant 6)

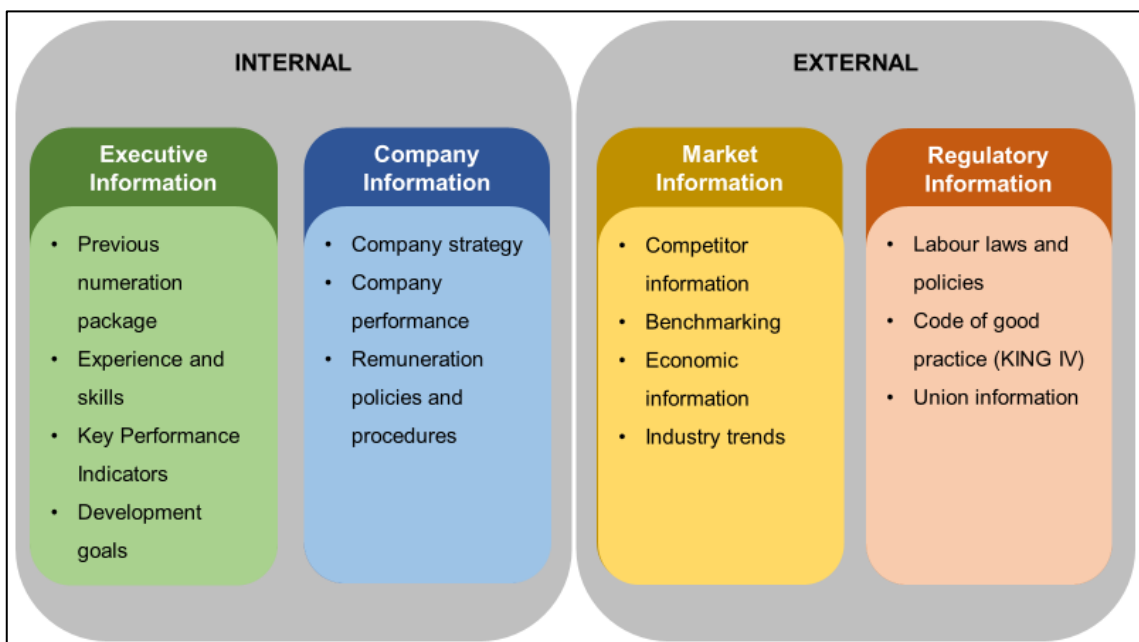


Figure 5.3: Types of Information Gathered for Determining Executive Remuneration Package

Source: Authors own

After all relevant information has been gathered and analysed, the remuneration package can then be designed. In the remuneration package design, REMCO looks at

“...it in terms of three pillars of remuneration. So, guaranteed package, variable pay [which is] the bonus piece, and then the long-term incentive” (Participant 1). These different elements of reward are considered to determine what proportion of the remuneration package should be guaranteed and how much should be performance driven (Figure 5.4).

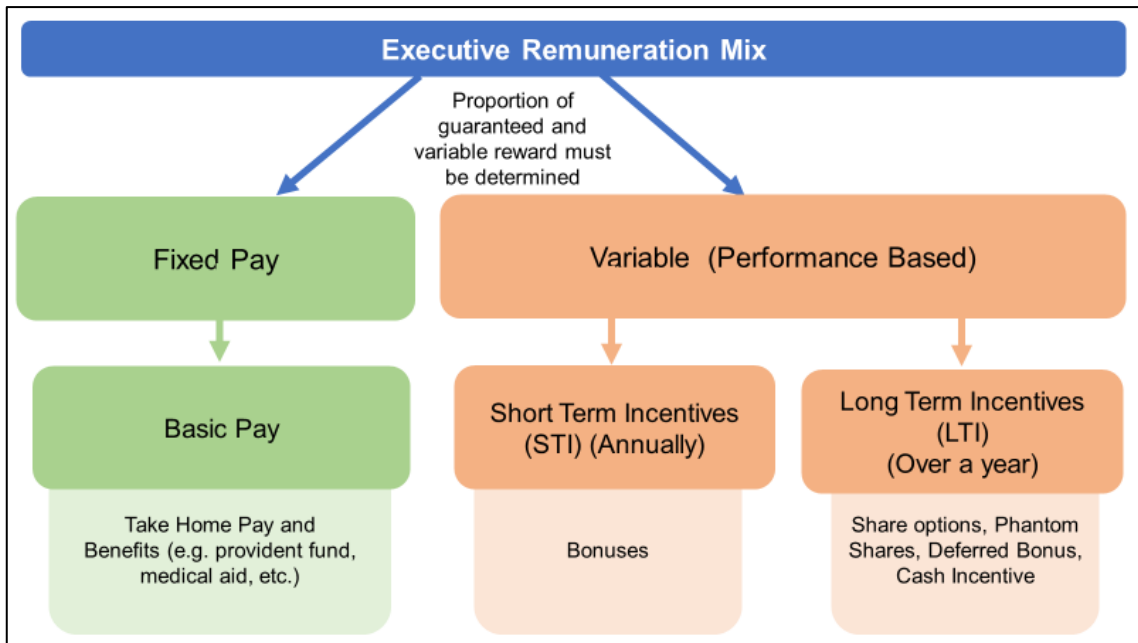


Figure 5.4: Elements of the Executive Remuneration Mix
Source: Authors own

When determining a remuneration package, a lot of focus is placed on the performance driven elements of the remuneration mix. This is because variable pay, the bonus-pay part of short-term incentives, as well as the long-term incentives, are designed in line with the company strategy and executives are rewarded according to the performance of both the company and the executive themselves, over the period in question.

“... on the variable pay side ... we design short incentives and long-term incentives and that pay mix which is part of the strategy And then on the variable pay side, the short-term incentives including everything. That's just kind of looking back a year. And then on the long term, looking forwards, usually 3 - 5 years and that revolves around shares. If the company is a public company, so the shares are available. If it's a private company, maybe phantom shares, cash schemes, deferred bonus schemes, anything that really underpins the remuneration strategy that the company is trying to achieve” (Participant 3)

“Of course, there's different elements of reward, guaranteed pay, short term and long-term incentives. So basically, depending on the remuneration philosophy of the business, to what extent do you want to reward performance. What percentage of the package should be performance driven and how much should be guaranteed.”

The remuneration package is then presented to REMCO alongside a summary of gathered information so as to substantiate the remuneration package design. It is then the responsibility of REMCO to make sure that the designed package is fair and relevant and that remuneration policies and procedures have been followed by the executives. This may require them to request further information, if needed. After the remuneration package has been approved, it is then sent back to the executives for implementation and communication to relevant parties.

Finally, after implementation, REMCO continues to monitor and review the remuneration packages. This involves examination of the performance metrics and regular feedback from the executives, to ensure that the remuneration package is promoting the right behaviour to ensure the sustainability of the company and that the interests of shareholders are protected.

“... as a remuneration committee you've got to make sure that executives ... remuneration drives the behaviour that you want, and that it rewards performance as well as penalises performance. So, if you reward in tandem with performance, I think you know that your reward instrument is working well ... So, your remuneration must be able to attract, retain, as well as drive performance” (Participant 2)

5.2.1 Research Question 2: What policies and procedures do remuneration committees follow when determining executive remuneration?

As REMCO committees are tasked with the responsibility of overseeing the determination of remuneration practices, they use policies and procedures as guidelines. These policies and procedures can either be determined external to the company or internally by the company.

5.2.1.1 External Remuneration Policies and Procedures

External policies and procedures which the REMCO need to adhere to, include the Companies Act, which incorporates the King IV code of good practice, as well as the Labour Relations Act. Remuneration committees consider these very seriously as

deviation from them could lead to governance issues as well as criminal charges being instituted against the company and directors.

“You know that King IV requires companies that are listed, because the JSE listing requirements makes it mandatory, to put the remuneration policy and the implementation of board to shareholders REMCO's are very alert to that reputational damage” (Participant 9)

“REMCO ... follow the different governance codes as close to dammit as they can because they don't want to deviate and then there's a liability on execs. So, I would say that ... companies take it pretty seriously” (Participant 2)

“In terms of King, King obviously advises that the members of the REM committee should be independent, particularly the chairman of the committee.... usually the remuneration committees usually have a minimum of three independents and that kind of aligns with King most REMCO's do have 50% that are independent and they do run fairly independently” (Participant 3)

“When it comes to remuneration we go through a process of salary negotiations because we are unionised” (Participant 13)

5.2.1.2 Internal Remuneration Policies and Procedures

Internal remuneration policies and procedures are written by the executives and approved by REMCO. They are designed in line with legislation and are continuously reviewed for company and market relevance. Although they are followed strictly by the company, REMCO does have the mandate to deviate from such should unexpected circumstances arise, however, not where legislative requirements are concerned.

“The one thing that will limit the frustration is that we have very strict reward guidelines This is what you can offer... and if you want to offer anything more, these are the approvals you need to get. I think if ever there was an environment where I was frustrated is if there was no clear policy on reward” (Participant 9)

“...to set the remuneration policy and principle for the entire organisation and it's a very important matter” (Participant 11)

“...as the remuneration committee, you have to have discretion as a committee member, to pull back the levers of reward if something big or a

negative oversight from management, ... You should be able to work outside the policy if you find that management have been negligent in whatever way, whatever is in their control has gone off track” (Participant 2)

5.2.2 Research Question 3: What do remuneration committees believe are the most and least important factors of consideration for executive remuneration?

There are a number of factors that are considered by remuneration committees, in order to structure an executive remuneration package in terms of the three areas of guaranteed pay, short term incentive pay and long-term incentive pay. These three types of remuneration are aligned to three main areas of consideration, namely organisation and executive considerations, legal and ethical considerations and market considerations. The majority of factors within these areas of consideration, were consistently mentioned as top of mind considerations, implying that they are all considered to be important by the remuneration committee. Other factors that were prompted, were found to be less important considerations (Table 5.2).

Table 5.2: Most and Least Important Factors for Consideration in Determining Executive Remuneration

Area of Consideration	Most Important Factors	Least Important Factors
Organisation and Executive Considerations	<ul style="list-style-type: none"> • Organisation Structure and Complexity • Performance Metrics and Affordability 	<ul style="list-style-type: none"> • Executive Qualifications • Executive Mobility
Legal and Ethical Considerations	<ul style="list-style-type: none"> • King IV • Companies Act • Labour Act • Ethical 	<ul style="list-style-type: none"> • Wage Gap
Market Considerations	<ul style="list-style-type: none"> • Economic Conditions • Industry Considerations • Competitor Considerations 	

Source: Authors own

5.2.2.1 Organisation and Executive Considerations

When determining executive remuneration packages, remuneration committees examine the structure and complexity of the organisation as well as the financial performance of the organisation, the performance of the executive and affordability for the company. Factors that are considered to a lesser extent are the qualifications of the executive and the mobility of the executive (Figure 5.5).

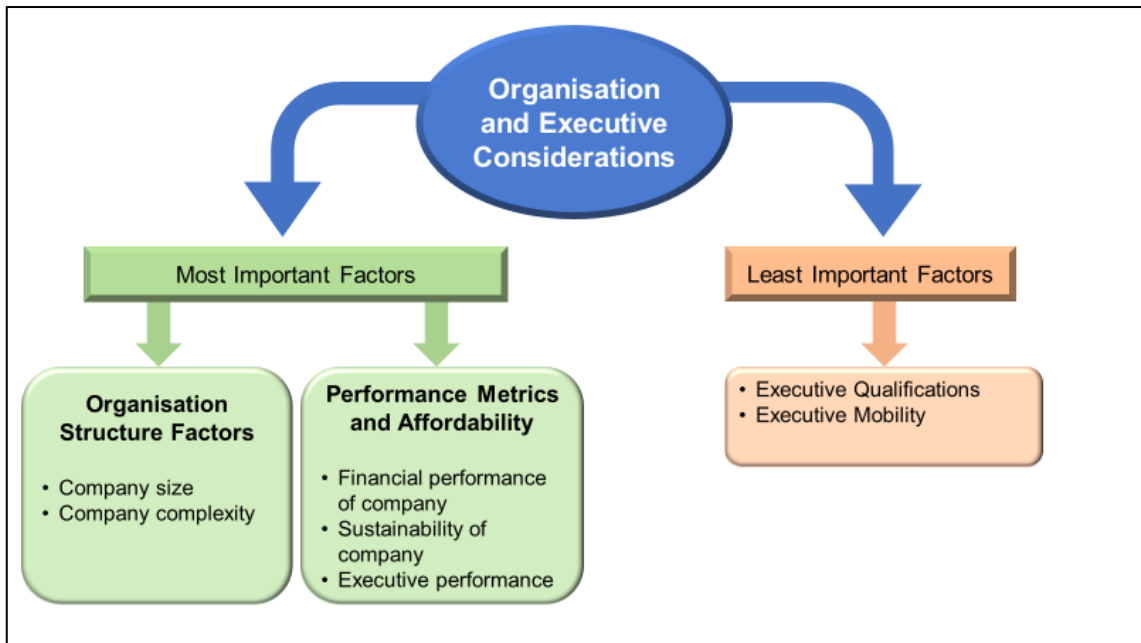


Figure 5.5: Organisation and Executive Considerations

Source: Authors own

There are a number of things that may be looked at in terms of the structure and complexity of the organisation. The size of the company is one such element and may be determined differently by different organisations and their REMCO's. Some of the ways in which the company size may be determined are by the revenue, total assets, the number of employees in the company, or by market capital. According to participant 13, *“Basically, our remuneration philosophy, structure, strategy moves from the kind of revenue that we have, we generate as an organisation. So, the size of the organisation. And therefore, our remuneration structure moves from the size of the revenue we generate”*.

“The target package and the fixed incentive is from the size and complexity of your organisation. Size is determined by very specific things: revenue; total assets; number of employees; in some cases, people also look at PBT or earnings and market capital” (Participant 11)

The more complex the organisation structure, the higher the executive remuneration package should be as the tasks the executive needs to perform are more complex. The elements that contribute to the complexity of the role include the company size in terms of turnover or number of employees, but also the location and footprint of the company and the complexity of shareholding and subsidiary companies. These elements are not considered in isolation as it is the sum of them that determines the complexity of the executive role.

“So, in our experience its size and complexity of the business. You could even have businesses that are the same size revenue wise but one is much more complex than the other one.... It helps you to get a sense of how big the job is, how big the exec job is, but it also helps you to look at other comparatives” (Participant 8)

Executives have a more complex role where the company has a footprint across multiple locations. However, the number of locations alone does not determine the complexity. A global footprint places far more responsibility on the executive than a local footprint due to the differing laws, cultures and economies across different countries, that the executive needs to consider. In addition, the shareholding structure of subsidiary companies may pose additional complexities on the executive in terms of reporting structures.

“... grade the job in line with the responsibilities. I think also, what South African companies need to be very careful with, ... is that there are South African multinationals who've got companies in multiple countries and therefore they should be having a multinational salary if they are looking after six or seven countries, but when single market countries start using that as a benchmark, that's where things go wrong. Sometimes they have five people in three countries, Swaziland, Lesotho and South Africa. They are not really multinational companies, they are just sales offices. The complexity is very different where there is a mine in five different countries, you have staff in five countries, you have to pay taxes in five countries. So, it's very different. So, complexity and size are important to determine and then you must play in line with market there” (Participant 2)

Shareholder return on equity is an extremely important consideration in determining executive remuneration. Participant 1 explains that, *“...our remuneration decision [must] align with the shareholders' interests and align with the long-term sustainability of the company”*. This means that the financial performance of the organisation and the performance of the executive needs to be taken into consideration. Participant 4 explains that *“You choose this basket of performance conditions and then you have to set a performance range So, you need stretch in the targets because that's fair to shareholders. You need the performance conditions to be ones that promote sustainability and then finally you need this thing to be fairly simple because otherwise if your executives don't understand it, you are just wasting everyone's time”*.

Shareholders want higher returns and therefore push for the remuneration package to have a higher variable pay element, in order to drive performance. The executive remuneration package is designed in light of the organisation's strategy and business objectives whereby performance standards are agreed upon for the short and long term. These performance targets are aligned to the executives variable short and long term pay and are intended to promote the right behaviour from the executives.

“So, the market is fairly similar and shareholders are also pushing for similar things which is bring down your guarantee and have variable pay higher so you can drive performance, have your measurements more like mine as a shareholder so you are rewarded the same, so you also have skin in the game. So, management is not getting big bonuses when I am not getting dividends. So, what shareholders want is shareholder alignment. All shareholders in all sectors want that” (Participant 2)

“So, for me it's a ... understanding where the business is going and designing your programs to make it sure it supports the business objectives because you don't want behaviours to be going in one direction and the business to be going somewhere else” (Participant 5)

Affordability and sustainability for the organisation is examined, not only through financial performance metrics but also in light of the life stage of the organisation. Judgement may have to be used in determining executive remuneration where specialised skills are required in a new business but the affordability of the organisation will lead the decision.

“And also important is the stage of the company. So, a new company, it's a start up, there isn't a hell of a lot of cash...you know the guaranteed pays a little bit less and there's a lot more on the equity because now we're driving growth ... and a very mature business, almost a decline, that's where your guaranteed pay would be a lot higher and the type of benefits that you have must be more towards retirement or towards exit of the business” (Participant 2)

“We started [some] businesses a couple of years ago which are both new and require some skills which are not necessarily things we've had before. And then you do find yourself saying how much should you be paying a CFO [with these particular skills]. And then the benchmarking can help but it's also a bit of a judgement call and also what can the business accommodate, what can you afford” (Participant 1)

One of the least important factors that remuneration committees look at when determining executive remuneration is the qualifications of the executive. Although the executives experience may be looked at when recruiting a new executive, it is the reputational proven track record of the executive that is important.

“For people in exco together, your qualifications are not important. It's what you have brought on the table” (Participant 10)

“We do look at time in role and their experience. I mean things like qualifications, not really. You know when you get to be the CEO of a company, what you did 20 or 30 years ago in terms of qualifications becomes increasingly irrelevant.... It's their proven track record in running a business” (Participant 11)

Another factor considered to be of least importance for determining executive remuneration, was found to be the perceived mobility of the executive. This is because not all executives want to relocate as they would prefer to stay in their home country with their family.

“Not all CEO's are mobile because they've got family, they don't want to move, and actually maybe the other country doesn't want you, maybe they've got their own better people there.... So, the global mobility thing is not a big thing to be honest. I think it is overused and it's an executive ploy to use that (Participant 2)

5.2.2.2 Legal and Ethical Considerations

Legal and ethical considerations include non-debatable factors that are implemented during the process of designing an executive remuneration package. It is believed that without conformance to the legislation, codes of good practise and ethics, companies may incur reputational damage and they would not be able to exist.

Companies incorporate legal requirements into the design of their remuneration policies and procedures as well elements of the King IV Code of good practice and any ethical requirements that they want to employ. In this way, following their remuneration policies and procedures ensures good corporate governance is followed and that they are compliant with any legal requirements should they need to defend their decisions. They may also incorporate ethical elements such as employment creation or rules for addressing the wage gap imbalances created through legacy.

“Governance is about them being objective. So, governance is about principles that should be followed that are not influenced by personal bias or personal relationships. The governance is about policies that can be defensible, the implementation of policies that were agreed so that the end decision lines up with the policy and it isn't a random decision that ignores the set policy. So, I think governance is also about the process. Governance is about the end outcomes, that the outcomes are robust and defensible”
(Participant 8)

“I think just overall, governance and being ethical and responsible is just so important” (Participant 5)

In terms of legal considerations, it was found that the Companies Act and the Labour Relations Act are the most prominent laws to be considered and it is vital that there is compliance with these legal requirements. Other laws were also mentioned including the Treasury Act, The Banking Act and the Insurers Act but these are very industry specific and not considered as factors for all companies.

“So corporate governance absolutely. The constitution of the REMCO, the terms of reference, how that's run and shared, corporate governance is key. So, King IV and the companies Act and the Banks Act and the Insurers Act, all of these things, we have to be very prised and very careful in refence to how we do it” (Participant 11)

“And of course, we have to make sure that we are compliant in as far as labour relations is concerned...If we look at schedule 8 of the labour relations act, the code of code practice, it tells us things that organisations need to do”
(Participant 13)

The King IV code of good practise is one of the top factors of consideration when determining executive remuneration and is regarded to be as important as following regulatory requirements. King IV provides guidelines on fair remuneration, transparency and disclosure of executive remuneration, shareholder considerations and the balancing of shareholder and executive interests to avoid agency issues as well as to avoid any reputational damage.

“...first of all, governance is a key thing on the REMCO's agenda and they see that as their mandate and part of the charter. Secondly, they follow the different governance codes as close to dammit as they can because they

don't want to deviate and then there's a liability on execs. So that's the first thing that will come up, how does this align with King IV" (Participant 2)

The legal requirements and King IV also provide some ethical guidelines for determining executive pay. However, other ethical factors may also be considered but to a lesser degree. Compliance with the laws and King IV requires that there is fair and responsible pay. Participant 4 explains that, *"We worry about what we should do rather than what we must do.... REMCO's are very alert to that reputational damage.... We are fundamentally focused on that. King IV has been instrumental in making sure that we design fair and responsible pay. Responsible is another word for sustainable and fair is ethics"*.

Ethics also plays a role in determining executive pay. According to participant 2, *"That's a corporate citizenship that that you must have"*. This is because the remuneration and performance metrics should promote the right behaviours and not be detrimental to the society.

"You've got to be sure you're promoting the right behaviours. So, it's the ethical aspect... you can't have just one short term measure which is financial. You can imagine the intended consequences" (Participant 4)

"How do you still perform and keep the health and safety of not only your employees but of the community at large as well?" (Participant 2)

Ethical factors include considerations of the wage gap and a living wage. Internal remuneration policies may incorporate elements that address these issues such as ensuring that salary increases for executives are not higher than the salary increases of the rest of the employees so that the wage gap can be reduced over time. Although the wage gap is seen to be of less importance in determining executive remuneration, the general feeling is that this is because a solution has not been found and that one can only really try to ensure that the gap does not widen further.

"When it comes to remuneration we go through a process...of salary negotiations because we are unionised.... Whatever we have agreed on with the unions, our managers are going to receive x minus.... That's per the board and we are not going to go above that" (Participant 13)

"I don't think that it is not important for the REMCO to look at the wage gap but why I haven't put it in that list is because I don't know how you fix it and I don't think anyone knows how to fix it actually.... So, we say as long as your

wage gap is moving in the right direction because you can't fix it overnight” (Participant 3)

“By the way, in terms of the wage gap I think we need to be clear. You need to understand that there must be a wage gap. The problem is, it shouldn't be growing. So, I always maintain that people should understand what their wage gap is.... But, we should be using it as an internal measure because if that is growing then that's a problem. It shouldn't be growing” (Participant 4)

5.2.2.3 Market Considerations

Factors relating to the organisation, the executive, legislative requirements, and ethics that REMCO looks at, can all be influenced by various market considerations which are also considered by REMCO. The most important factors include the economic conditions of the country, competitor information and industry conditions.

The financial performance and sustainability of a company has much to do with the economic conditions in the country. The rate of economic growth impacts the company's performance and this is taken into consideration when setting performance targets for the organisation and the executive. Salary increases are also affected by inflation and REMCO needs to ensure that the executive remuneration package is able to attract and retain talent. In essence, organisations in a high growth environment are able to pay higher remuneration but in a low growth environment executive are challenged in ensuring that shareholders receive return on their investment.

“So, in that case they will look at the market and look at CPI and look at attraction and retention elements” (Participant 3)

“...as a remuneration committee you've got to make sure that executives are paid in line with the market and that their remuneration drives the behaviour that you want” (Participant 2)

“We are guided by the CPI. So, CPI tells us that your basket of goods for 2018 has increased by x percent so management of the organisation makes a decision, we are going to pitch all our salaries at x percent increase” (Participant 13)

The industry in which the organisation operates has its own growth cycle and where there is positive growth, employment creation is near the top of the agenda so as to try and lower the high unemployment rate in the country. However, if the industry is experiencing declining growth, organisations are sometimes forced to downscale and

with that comes retrenchments. It is believed that morally and ethically, REMCO's must factor in job creation where possible, or assist with retrenchments.

"This is where the board plays a big role and depending on the sector that you are in. If you're in a growth sector and you are a corporate citizen of the country, you know that there is high unemployment, this is where the board should be looking at what are we doing to create employment. But if you are in a declining sector, you know that it's a problem. Then the discussion there should be, to what extent do you manage the exit, to what extent do you get them to land as soft as possible" (Participant 2)

Industry and competitor benchmarking are used extensively by REMCO's to determine executive remuneration packages. Comparisons are made in regard to both industry conditions, such as growth or decline of industry, as well as competitor conditions. All REMCO's look at executive remuneration benchmarks in conjunction with other factors mentioned. They are clear that these benchmarks need to be comparative to the role of the executive, the industry segment, the complexity of the role performed and the size, footprint and complexity of the organisation, amongst others.

"So, we start with a benchmark and the benchmark is more than just a number, the benchmark is also a construct. So, we have a peer group and that peer group is selected in terms of a similar business model, a similar geographical footprint and a similar market capitalisation" (Participant 6)

"When you start plotting your pay levels, your organisational pay levels against organisations in the market place, there's got to be some level of similarity. So, our CEO job must then have similar seniority with other CEO's of similar companies" (Participant 6)

It is important for REMCO to look at benchmarking as they have to ensure that there is alignment between the tasks of the executive and other executives in the industry or with competitor executive packages. Therefore, both internal equity and external equity are important factors that need to be considered by REMCO's to ensure that executive pay is fair and that it is a competitive package. The requirements for transparency in King IV allow the REMCO to scrutinise remuneration reports of competitors which has helped them realise that most organisations use similar performance conditions.

"No, you must take two things into account, internal equity as well as external equity. So, your exco is a certain grading plus the grade must pay

within certain range. and remember now, if the market also uses the same grading system, the range is similar anyway so in essence you choose whether you want to pay your people in the upper quartile or medium as well as the lower. So that's where you must choose where it is you want to play" (Participant 2)

"For executives it's a bit of an issue because there's three major factors that will affect them. Number one, what the executive is currently earning.... Secondly, you have to look at the peers in the market. Well let's just start with the peers in the company. What are you offering as a company? And then thirdly, you've got to look at the peers in the market" (Participant 9)

"Not necessarily a copycat behaviour but we watch intensely what our competitors are doing because we see remuneration as a critical tool that makes us competitive. And you know with this age of transparency with King IV, it's far less prescriptive than King III but it requires far more transparency. So, you can read a REM report and you can get a good handle of how much they get paid, the likelihood of investing, the performance conditions and events back to back. So, you can see we've all got pretty much the same performance conditions" (Participant 4)

In line with the company strategy for sustainability and affordability, remuneration policies of the organisation usually dictate pay scales or in what percentile executives should be paid. REMCO takes this into consideration as it not only ensures that the package agreed on is affordable for the company, but it also prevents copycat behaviour with competitors and contributes to responsible decisions as it is believed that organisations should not all pay in the upper quartiles because if they do it just grows the benchmark and contributes further to the wage gap issue.

"There are very specific procedures around benchmarking where you compare your pay as fairly and reasonably as possible to your comparatives and you also try to do that in a responsible way so as not to contribute to the upgoing cycle of paying more because in past years people were always trying to outdo the competitors by paying in the upper quartile. That's partly what's led to the upward spiralling of pay" (Participant 11)

"...that is why I am saying companies must do what they have to do, they must do what they can afford. You must know what it is that you want. If you don't know what it is that you want or what you can afford, you will end up

doing what everybody else says. And executives, when they want to be paid more, they will follow the market more. Then you have to say no, we hear what the market is doing, this is what we want to do” (Participant 2)

5.3 Conclusion

Remuneration committees in South Africa have four main functions, that is to ensure compliance with regulation, ensure compliance with remuneration policies and procedures, act as an independent remuneration monitoring body and ensure that there is alignment between the interests of the executives and the shareholders. The determination of executive remuneration follows a similar process in all organisations and similar factors may be considered by REMCOs when determining the executive remuneration package.

Prior to the design of a remuneration package, various kinds of information are gathered. This information is used to determine various elements of the remuneration package but also to support the proposed remuneration package and performance measures. After the remuneration package is designed, REMCO has the responsibility to scrutinise the data and the proposed package, requesting additional data if necessary, before they approve the remuneration package. They also have to monitor and review the performance metrics and remuneration package used.

In order to ensure that executive remuneration packages are designed appropriately, REMCO committees pay particular attention to governance issues through ensuring that internal and external remuneration policies are followed correctly. It is acknowledged that compliance is vital to ensuring fairness and maintaining the corporate reputation and is central to all activities conducted by the remuneration committee.

During the process of determining executive remuneration and ensuring governance, REMCO will look at various factors for consideration. These include factors relating to the organisation and the executive, legal compliance and ethical considerations, and factors relating to the economy, industry conditions and competitor considerations. The degree to which each of these are considered varies from one organisation to the next. The size and structure of the remuneration package and agreed performance metrics are then approved and REMCO continues to monitor and reassess the situation.

Chapter 6: Discussion of Results

6.1 Introduction

This chapter provides a discussion of the findings presented in Chapter 5, together with the findings from the literature review in Chapter 2 and is the basis of the conclusions drawn and recommendations made in Chapter 7. The research intended to gain insight into the factors that are considered by remuneration committees in the determination of executive remuneration. Qualitative semi-structured interviews were conducted with 13 remuneration committee executives from different industries. Sampling of these executives was purposeful and convenient so as to ensure that a good mix of knowledgeable participants with different level of experience and from various industries were interviewed. However, the sample was relatively small and it must be noted that a larger sample will be required in order to generalise these findings to all organisations.

Chapter 5 presented the findings of a content analysis of the interviews in light of each of the research questions. This chapter reviews these findings and provides an interpretation of the data in light of existing literature in the executive remuneration field. The discussion is presented in line with each of the research questions, as was the case in Chapter 5. This analysis then concludes with a conceptual model of factors to be considered when determining executive remuneration packages in South Africa which has been designed using the data gathered from both interviews and the literature reviewed.

6.1.1 The Determination of Executive Remuneration Packages by Remuneration Committees in South Africa?

6.1.1.1 The Role of REMCO

King IV recommends that the board establish a remuneration committee with the objective of recommending a fair and responsible remuneration policy to the board, in order to create value in the foreseeable future (Institute of Directors, South Africa, 2016). South African remuneration boards were found to believe that the primary purpose of REMCO is to be a sub-committee of the board that is an independent remuneration monitoring body. This independent sub-committee must ensure compliance of remuneration regulations and remuneration policies and procedures. In so doing, they are also required to ensure that there is alignment of executive and shareholder goals.

In regards to remuneration regulations, many REMCO's were reported to have made governance key to their agenda when executing their mandate because the boards of

companies consider governance to be a serious issue. As such, REMCO's pay careful attention to abiding by the remuneration regulations set out in the South African Companies Act and the labour relations act, as well as any specific industry regulations that may apply. The King IV Code is also considered to be a regulatory requirement by REMCO's. However, the South African Companies Act (Companies Act 71 of 2008) only requires companies listed on the JSE to comply with the King Code of Governance Principles ("King Code") for the determination of executive remuneration (VDMA, 2011).

The South African Companies Act (Companies Act 71 of 2008) requires the disclosure of all remuneration and benefits for all directors of the organisation in the annual financial statements. REMCO's were found to pay close attention to ensuring the transparency of executive pay in their reporting so as to abide by this requirement. The remuneration committee also understand that shareholders need to be assured that remuneration policies are consistently applied across short-term and long-term incentives which requires governance of internal remuneration policies and procedures as well as legal requirements. As such, the remuneration committee acts as a watchdog on remuneration practices to create value and ensure fair and responsible executive remuneration practices when compared to overall employee remuneration in line with King IV and the requirement for ethical leadership (Institute of Directors, South Africa, 2016).

Fama and Jensen (1983) state that by maintaining governance structures such as following laws governing corporate behaviour and using monitoring mechanisms such as corporate control, agency problems can be minimised. In order to maintain good corporate governance, the board establishes REMCO to be an independent remuneration monitoring body so as to ensure that principles are consistently applied without any influence of bias. In addition, the independence of REMCO in line with the King IV code was found to mean that at least three of the independent members must be external members of REMCO and that the interests of the executive should not be priority. However, Conyon (1997) states that the majority of the members should be non-executive members and that the chairman of the remuneration committee should also be an independent non-executive member. In addition, the chairman of the company should only attend REMCO meetings by invitation. This because studies have found that remuneration committees composed mainly of independent directors have good corporate governance and therefore tend to comply with the rules and regulations set in the act (Conyon, 2014).

REMCO's believe they are appointed to run the organisation in the interests of creating value for the investment of the shareholders and therefore that they must not only consider that the remuneration package is beneficial for the executive, but that they must also consider if the executive remuneration package aligns to the value created by the executive for the shareholders. According to Tao and Hatchinson (2013), executive remuneration can be used by remuneration committees as a tool to ensure that there is alignment between the interests of the shareholders and those of the directors. This is because the executive remuneration package can be designed to encourage executive performance and therefore also the company's performance (Hillman & Dalziel, 2003). In addition, remuneration packages can enable the company to attract, retain and motivate employees while still making sure that the goals of the company are achieved (Liao & Hsu, 2012).

6.1.1.2 Process Followed in Determining Remuneration Package

The process for determining the executive remuneration was found to be conducted in four main phases. The first two phases involve extensive input from the executives in gathering information and designing a remuneration package. REMCO has a focus on the next two phases where they scrutinise the information gathered in line with the proposed executive remuneration package, and following that they are involved in the continuous monitoring and review of executive remuneration

Remuneration committees place a lot of emphasis in analysing relevant information in order to determine a fair remuneration package for the executive which also considers the interests of the shareholders. According to Conyon (1997), remuneration committees may take a number of issues into consideration when determining CEO remuneration, such as company size, company complexity, company financial performance, number of employees, CEO efficiency, CEO availability in the industry, market remuneration rates of other CEO's, listing requirements, regulatory systems, company policies, board size, and the governance system in the company.

Remuneration committee members are believed to be highly experienced and knowledgeable about business and the regulatory requirements in South Africa. However, due to various labour market elements such as the job description and required tasks of the executive, the executives' opportunity for development, job security and the work environment, executive remuneration packages tend to differ from one organisation to another (Gayle, Golan & Miller, 2015) and the knowledge of the remuneration committee members about the specific company they are serving on the REMCO for,

may be limited. Therefore, the first stage of determining the executive remuneration package involves the executives gathering relevant information to be presented to the remuneration committee along with a proposed executive remuneration package.

The second phase occurs where the proposed executive remuneration package is designed by the executives using the information gathered. There are various forms of remuneration and incentives that may be incorporated into the executive remuneration package (Guay, Core & Larker, 2002; Murphy, 2013) including, basic salaries, annual bonuses, restricted shares, performance shares, retirement benefits, travel allowances and other long-term incentives. Executives can also receive a lump sum amount at different times during their employment, such as with signing on fees, termination pay out or retrenchment pay out (Murphy, 2013).

Once the executives have gathered the relevant information and designed a proposed remuneration package, REMCO is responsible for scrutinising the data. The proposed remuneration package is presented to REMCO alongside a summary of gathered information to substantiate the remuneration package design. It is then the responsibility of REMCO to make sure that the designed package is fair and relevant and that remuneration policies and procedures have been followed by the executives. Where necessary, REMCO may require further information to be gathered by the executives. This information could relate to market information, company information, and executive information. It may also be gathered and used by REMCO to back up their final decisions with the shareholders, if needed.

REMCO also scrutinises the information gathered and the proposed executive remuneration package in line with the remuneration mix. They describe this as the “three pillars of remuneration” which includes the executives fixed pay or guarantee package, the short-term incentive pay and the long-term incentive pay. The short-term and long-term incentive pay are both variable pay elements which are aligned to the performance of the executive and the performance of the company. Once the executive remuneration package has been agreed upon, it is sent back to the executives for implementation and communication to relevant parties.

Finally, after implementation, REMCO continues to monitor and review the remuneration of the company’s executive (Liao & Hsu, 2012). This involves examination of the performance metrics and regular feedback from the executives to ensure that the remuneration package is promoting the right behaviour to ensure the sustainability of the company and that the interests of shareholders are protected (Tao & Hatchison, 2013).

6.1.2 Policies and Procedures Followed by Remuneration Committees when Determining Executive Remuneration

Executives play a pivotal role in running organisations for shareholders (Finkelstein, Hambrick & Canella, 2009) and the CEO, who is the most senior of these executives (Usman et al., 2015) is expected to create value for the shareholders (Bussin, 2015a). This is because the CEO has the power to make decisions and control the company's resources (Fama & Jensen, 1983 and Boyed, 1994 as cited in Usman et al., 2015). As a reward for their services, executives are then compensated with a remuneration package (Finkelstein et al., 2009). However, literature highlights that there is a shareholder value debate that executive remuneration is not always aligned to maximising shareholder value (Edmans & Gabaix, 2016). This is because executive remuneration packages tend to focus on the value created for the shareholders in the short-term and not on the long-term sustainability of the company (Jensen & Murphy, 2010).

One of the reasons for the focus on the short-term achievements is that the shareholders and the executives have different goals. The shareholders want to make a return on their investment and the executives are concerned about the remuneration they receive (O'Reilly & Main, 2010). As such, the shareholders and the executives may have differing views about how the company should be run which may not be in the best interest of the company (Bebchuk & Fried, 2003) and as a result, a principal-agent problem occurs (Hope & Thomas, 2008). Secondly, the executive may have the power to influence their remuneration in a positive way (Guthrie, Sokolowsky & Wan, 2012) through structural and social-psychological influences or social and psychological influences they have over board members (O'Reilly & Main, 2010; Van Essen et al., 2015).

In order to minimise agency problems or managerial power issues, Guthrie et al. (2012) recommends strong governance of the company which can be achieved through appointing independent directors to the board who are able to reduce the power of the CEO and hence ensure that the correct process to determine CEO remuneration is followed whereby the executives' remuneration is linked to performance. Remuneration committees can also be tasked with determining and monitoring the remuneration of the company's executive (Canyon, 1997; Liao & Hsu, 2012) so as to ensure that the remuneration provided to the executives align the interests of the shareholders and those of the executives (Tao & Hatchison, 2013). Remuneration committees in South Africa place great importance on using both external and internal remuneration policies and procedures as guidelines for determining executive remuneration as they need to ensure

good governance practises that align the interests of the shareholders and the executives, while also ensuring that there is compliance with legislation and King IV in order to protect the stakeholders from criminal or reputational damage.

6.1.3 Remuneration Committee Perceptions of the Most and Least Important Factors of Consideration for Determining Executive Remuneration

It was found that remuneration committees consider a number of factors when determining executive remuneration packages. Contrary to Jensen and Murphy's (2010) view and Edmans and Gabaix's (2016) view that executive remuneration packages often don't align to maximising shareholder value because they have too much focus on the short-term performance, it was found that South African REMCO's have a number of factors that they consider within three areas of the remuneration package design, namely guaranteed pay, short-term incentives and long-term incentives.

South African REMCO's were found to all use similar factors of consideration which fell into three main areas of consideration including organisation and executive considerations, legal and ethical considerations and market considerations. The majority of factors considered were regarded as being important considerations. However, as posited by Bussin (2015b), there is no understanding of weighting metrics attached to these factors by the South African remuneration committees.

6.1.3.1 Organisation and Executive Considerations

In order to determine executive remuneration, REMCO's will look at the structure and complexity of the organisation as well as the financial performance of the organisation, the performance of the executive and affordability for the company. Finkelstein and Hambrick (1989) agree that CEO pay is linked to factors such as company size, complexity of the company, the performance of the company, the power of the CEO and CEO's human capital. He adds however that board vigilance is another factor that should be considered.

Core et al. (1999) state that CEO'S get paid more when the size of the company is big, compared to their counterparts who run small companies in comparison. Shah et al. (2009) reports that a strong relationship has been found between company size, which is measured in terms of sales and assets, and the CEO remuneration. South African REMCO's view the size of the organisation through financial metrics such as revenue, assets or market capital. However, the number of employees in the company may also be considered. According to Roberts (1956), revenue and profit turnover are not the only

indicators of creating wealth for the shareholders and overlooking the other factors such as return on assets, market price, net asset value, economic value added, price per share, return on equity, cash flow improvement, earnings before interest tax and depreciation could have a negative impact on the company in the long term. REMCO members agree that shareholder return on equity is an extremely important consideration in determining executive remuneration and the financial performance of the organisation as well as the performance of the executive needs to be taken into consideration.

The structure and complexity of the organisation is viewed by REMCO's in terms of the location and footprint of the company and the complexity of shareholding and subsidiary companies. REMCO members believe this is important because it provides an indication of the complexity of the executive role and the responsibility that the executive has. According to Roberts (1956), executives who run big companies have more responsibilities than those who run small companies because big companies are very complex in terms of structure, operations, number of employees, revenue generated and profits. Agiwal (1981) argues that although the size of the company is important, the structure of the company is also an important consideration as executives in companies with a lot of subsidiaries, divisions, or reporting structures have scarce talents and are therefore in high demand in the market place. REMCO's were also found to believe that all these factors should not be viewed in isolation and it is the sum of them that determines the executive's role responsibilities.

One of the least important factors that remuneration committees look at when determining executive remuneration is the qualifications of the executive. They are more concerned with the proven track record of the executive. Another factor considered to be of least importance for determining executive remuneration, was found to be the perceived mobility of the executive. This is because not all executives want to relocate as they would prefer to stay in their home country with their family.

6.1.3.2 Legal and Ethical Considerations

Agency theory favours governance structures in terms of the law governing corporate behaviours; monitoring mechanisms like the company board of directors; and enforcement mechanisms such as corporate control and managerial labour markets, or order to reduce agency problems (Fama & Jensen, 1983). Guthrie et al. (2012) posit that it is through the remuneration committee that corporate governance can be promoted. Legal and ethical factors for REMCO's are non-debatable.

South African REMCO's were found to incorporate policies and procedures as well elements of the King IV Code of good practice and any ethical requirements that they want to employ. In this way, following their remuneration policies and procedures ensures good corporate governance is followed and that they are compliant with any legal requirements should they need to defend their decisions. They may also, it was found that the Companies Act and the Labour Relations Act are the most prominent laws to be considered and it is vital that there is compliance with these legal requirements. Other laws were also mentioned including the Treasury Act, The Banking Act and the Insurers Act but these are very industry specific and not considered as factors for all companies.

The King IV code of good practise is one of the top factors of consideration when determining executive remuneration and is regarded to be as important as following regulatory requirements.

Ethics plays a role in determining executive pay. According to participant 2, *"That's a corporate citizenship that that you must have"*. This is because the remuneration and performance metrics should promote the right behaviours and not be detrimental to the society.

6.1.3.3 Market Considerations

Market considerations including economic conditions of the country, competitor information and industry conditions, are also factors that the remuneration committee looks at. The economic conditions in the country affect financial performance and sustainability of the company and therefore the executive remuneration as well. The life cycle of the organisation may also enable companies to pay more in a good economic condition.

Industry and competitor benchmarking are used extensively by REMCO's to determine executive remuneration packages. Properly structured information from peer groups provides great information to the board to be able to design a competitive pay level which will be necessary to attract, retain and motivate top executives. This is done by comparing the executive pay levels with that of other organisations which are of similar industry, size, performance, capital markets, customers and suppliers (Bizjak et al., 2011).

It is important for REMCO to look at benchmarking as they have to ensure that there is alignment between the tasks of the executive and other executives in the industry or with

competitor executive packages. The information which is used for benchmarking provides strong evidence for determining a remuneration package for a CEO coming from outside the organisation, whereas the evidence used for an internal candidate includes a number of additional internal factors (Martijn Cremers & Grinstein, 2013). The requirements for transparency in King IV allow the REMCO to scrutinise remuneration reports of competitors which has helped them realise that most organisations use similar performance conditions.

6.2 Conclusion

This chapter has discussed the finding of the interviews conducted and the literature reviewed. Based on the findings of the research and on the literature reviewed, a conceptual model of factors to be considered when determining executive remuneration packages in South Africa has been designed (Figure 6.1), which could assist remuneration committees in South Africa to have a standardised process for determining executive remuneration.

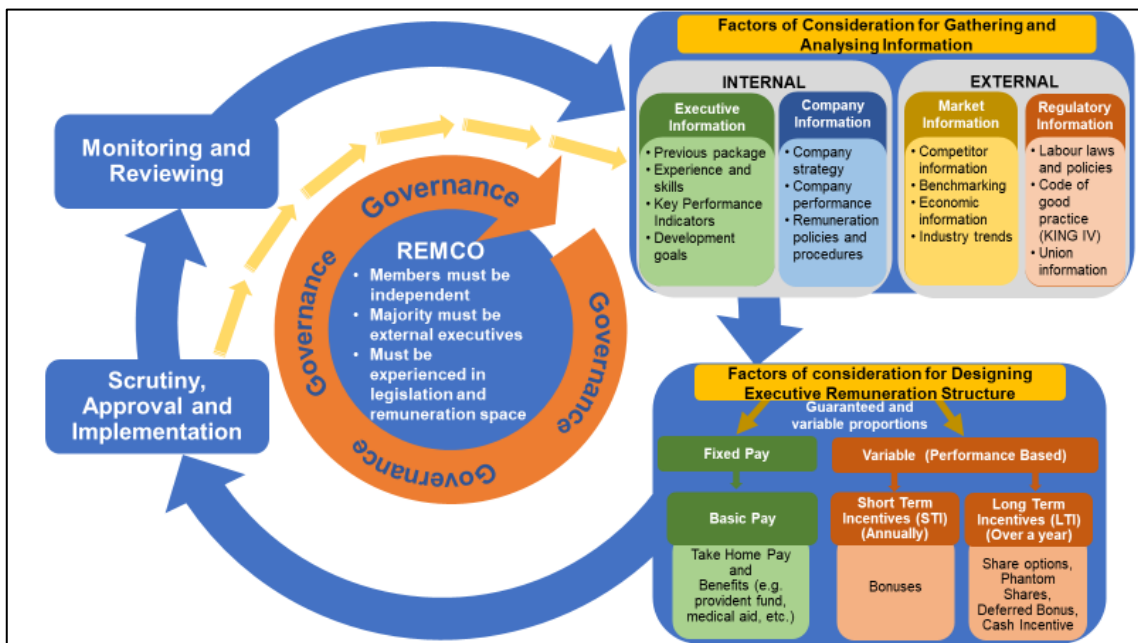


Figure 6.1: Conceptual Model of Factors to be Considered when Determining Executive Remuneration in South Africa

Source: Authors own

This conceptual model illustrated in Figure 6.1 shows the process followed by remuneration committees in South Africa when determining executive remuneration. The process follows four-phases and includes a feedback loop. The factors that remuneration committees in South Africa consider in the determination of executive remuneration, are similar across remuneration committees and therefore could be

standardised as factors that should be considered by all remuneration committees. Also highlighted is the fact that remuneration committees regard governance as being highly important throughout the four-phases and therefore should be included as part of the model. The following chapter provides a conclusion to the research through a summary of key findings, as well as recommendations for organisations and future research.

Chapter 7: Conclusion

7.1 Introduction

In this chapter a summary of the principal findings of the research is presented in line with each of the research questions. The implications of the findings of this study for remuneration committees are then discussed, highlighting the factors which are considered by remuneration committees when designing executive pay and the implications to the overall organisation and stakeholders. The chapter concludes with a discussion on the limitations of this research and recommendations for future research.

7.2 Key Findings

7.2.1 Summary of Finding for Research Question 1: The determination of remuneration packages by remuneration committees in South Africa

Remuneration committees in South Africa are very focused on ensuring governance, not only in terms of organisational policies and procedures, but also in terms of legislation which is considered when the internal remuneration policies and procedures are designed. The remuneration committees are independent with at least three external executives although literature advises that the majority of these members should be external independent members (Institute of Directors, South Africa, 2016). This focus on governance helps organisations to avoid agency problems (Fama & Jensen, 1983). REMCO members are considered to be highly skilled and experienced but may lack knowledge about the specific company.

Executives are compensated with a remuneration package in return for their services (Finkelstein et al., 2009). Remuneration committees are tasked with recommending these remuneration packages to the board after ensuring that they are fair and responsible (Institute of Directors, South Africa, 2016) as well as ensuring that they align the interests of the executive and the shareholders (Tao & Hatchison, 2013).

Executive remuneration packages can include various forms of remuneration and incentives (Guay, Core & Larker, 2002; Murphy, 2013) but Jensen and Murphy (2010) caution that CEO remuneration packages should not only be based on the value they create in meeting the short-term goals of the organisation but the long-term sustainability of the company should also be taken in to account. The remuneration package which EXCO recommends must have three components of pay, including a fixed portion, a short-term incentive portion and a long-term incentive portion. These components are

scrutinized by REMCO to ensure that they are attractive to the executive and they will promote performance which contributes to the organisational strategy and goals in order for the organisation to remain sustainable.

There are four main stages in the determination of executive remuneration. The first two involve both the executives and REMCO, where information is gathered and analysed, after which the proposed executive remuneration package is provided to REMCO for scrutiny and approval. Information about the company and regulatory systems are needed by remuneration committees (Conyon, 1997).

REMCO then uses both their knowledge and the provided information to determine if the package and performance measures are relevant, attractive and fair. This may require the executives to provide further information. Once the package has been approved by REMCO and the board, REMCO is then responsible for monitoring (Liao & Hsu, 2012) to make sure that the executive is paid according to the approved parameters.

7.2.1 Summary of Finding for Research Question 2: Policies and procedures followed by remuneration committees when determining executive remuneration

Companies often use committees to promote corporate governance, such as a remuneration committee, an audit committee, and a risk committee, amongst others. It is through this monitoring that committees are more likely to comply with corporate governance (Guthrie et al., 2012).

REMCO committees in South Africa use approved remuneration policies and procedures as guidelines for determining executive remuneration. External policies and procedures used by these remuneration committees include the companies act, which incorporates the King IV code of good practise, as well as the Labour Relations Act. These are considered seriously by the remuneration committee in order to avoid reputational damage for the company or shareholders. The internal remuneration policies and procedures are continuously reviewed to ensure alignment to legislated requirements and are usually also followed quite strictly. However, REMCO can analyse each specific scenario and may deviate from company specific requirements in order to remain fair to the executive and the shareholders.

7.2.2 Summary of Finding for Research Question 3: Remuneration committees' perceptions of the most and least important factors of consideration for determining executive remuneration

Remuneration committees need to take the structure of the executive remuneration package into account when designing the executive remuneration package. Fixed pay short-term incentives and long-term incentives must be looked at in line with various other factors of consideration in determining executive remuneration. These other factors are aligned to three main areas of consideration, including organisation and executive considerations, legal and ethical considerations and market considerations. However, different remuneration committees will explore different metrics within each of these factors meaning that there are differences in the weighting applied to the importance of each in determining the executive remuneration package.

Under the organisation and executive considerations remuneration committees consider organisational structure and complexity of the company, performance metrics and affordability of the company as main factors, as these will align the shareholder's interest with those of the directors. Academic research done in the past shows a strong relationship between company size, which is measured in terms of sales and assets, and the CEO remuneration (Shah et al., 2009).

Least important executive considerations for the remuneration committees which are sometimes considered are the qualifications of the executive and the executive mobility. However, Finkelstein and Hambrick (1989) argue that the power of the CEO and the CEO's human capital should also be considered as it is linked to the company and profits the company generates.

The legal and ethical considerations of REMCO highlight the importance they place in ensuring governance. All legislative requirements form the basis of internal remuneration policies and procedures and these legislative requirements are never deviated from. In addition, King IV which is compulsory only for private companies listed on the JSE (Institute of Directors, South Africa, 2016), are also followed strictly by all REMCO's regardless of the company's listing.

Guidelines provided by King IV also list some ethical considerations which are incorporated into the internal remuneration policies and procedures of companies. King IV highlights that the company must create value in a sustainable way within the social, environmental and economic context in which the company operates (Institute of

Directors, South Africa, 2016). Fair and responsible pay are considered to be ethical factors by REMCO's to ensure corporate citizenship, to promote the right behaviours and to not be detrimental to society. Agency theory suggests that promoting the right behaviour with appropriate incentives for executives, limits agency issues (Hill & Jones, 1992).

Ethical factors also include considerations of the wage gap and a living wage. The difference in earnings between executives and general workers has resulted in much controversy and ethics debates in the media, business and academic space (Bronkhorst, 2014; Core et al., 1999; Edmans & Gabaix, 2016). REMCO's believe that this issue is addressed to some degree in the company policies and procedures in order to reduce the wage gap over time. However, since no solution has been found to resolve the issue, this factor is not considered to be very important when determining executive remuneration.

Market considerations include factors that remuneration committees consider when collecting information, including economic, industry and competitor considerations. The information is often collected through benchmarking. Bizjak et al. (2011) suggest that gathering information through competitive benchmarking in the market provides properly structured information from peer groups to REMCO so that they are able to design a competitive pay level which will be necessary to attract, retain and motivate top executives. This is done by comparing the executive pay levels with that of other organisations which are of similar industry, size, performance, capital markets, customers and suppliers (Bizjak et al., 2011).

7.3 Implications for Management

The remuneration committee need to be aware that they have to balance the executive interest to the interest of stakeholders of the company (Edmans & Gabaix, 2016). According to Bronkhorst (2014) the issue of executive pay needs to be addressed before there are negative social consequences, regulatory or political interference which could ultimately stifle the business operations.

Remuneration committees need to make sure that there is a close alignment of the goals of the executives and those of the shareholders using remuneration practices (Van Essen, Otten & Carberry, 2015) This can be done by making sure that there is an efficient contract or optimal contract, maximising agency cost and at the same time maximising the net expected economic value to shareholders (Guay et al., 2002).

The shareholders of the company will not approve executive remuneration which is higher while the expected performance is not achieved by the executives (Jansen & Murphy (1990).

The remuneration committee need to make sure that executives have no power on the determination of their pay as this can influence the amount they get paid. To make sure that the executives do not have more power than the remuneration committee the board need to make sure that the remuneration committee is made up of more independent directors (Guthrie et al., 2012).

Another aspect which remuneration committee need to take in to account is that of the matching principle where the executive pay needs to be aligned to the contribution and services the executives have rendered to the company during a certain period of time.

The remuneration committee also needs to make sure that the contractual terms in the executive contracts are tied to the remuneration of these executives and they can be understood by the shareholders. When setting these contracts and remuneration the remuneration committee needs to make sure that the proper governance is followed so as to eliminate non-conformance to any act. The aspects which need to be adhered to are corporate governance, companies act, King IV, shareholder authorisation, board approval or any process which has been established by the company.

Remuneration committees can also consider company size, market risk, company performance, and power of executive, executive tenure, growth of the company when determining executive pay (Shah et al., 2009).

7.4 Limitations and Suggestions for Future Research

Based on the limitations of the research as identified in Chapter 4, recommendations for future research are provided below:

- This research involved a small sample; hence the findings of the research cannot be generalised to the entire population. The research was intended to explore the research problem and gain insights which can be tested with further research involving a larger sample of participants.
- This sample included in this research was conducted with representatives of mostly private companies. The inclusion of more public companies and non-profit organisations in a larger sample could be beneficial to give a broader perspective of the determination of executive remuneration in South Africa.

- This research was conducted with participants from large organisations in South Africa. It is recommended that gathering the perceptions of remuneration committees from small organisations in South Africa could add more insight into the findings.
- The research explored the factors that are considered by remuneration committees in South Africa. However, it was outside of the scope of the research to delve into the specifics of percentage weightings of these factors. It would be beneficial for further research into these weightings so as provide South African remuneration committees with weighting metrics for each of these factors.

7.5 Conclusion

Executive remuneration is a hotly debated topic in South Africa due to the value differential between the executives and general employees. Due to the attention this topic receives, remuneration committees in South Africa which are composed mainly of non-executive independent directors, place high importance on proper governance by ensuring that they follow approved organisation policies and procedures and also the legislation. They make certain that they comply with the company's act and also King IV in order to avoid any non-compliance issues or reputational damage to any of the stakeholders.

Factors of consideration for the remuneration committees when designing the executive remuneration package, fall into three main areas of consideration, namely, organisation and executive considerations, legal and ethical considerations and finally market considerations. The specific factors considered within each area however, differ from one company to the next resulting in the remuneration committees applying different metrics to arrive at the executive pay package.

Remuneration committees need to make sure that they align the interests of the shareholders to that of the executives through the design of their executive pay packages. This can only be achieved if there is proper weighting on the factors considered.

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APPENDIX A: SEMI-STRUCTURED QUESTIONNAIRE

Semi-Structured Questionnaire

Introduction and Background Information

1. To start, please can you give me some details about yourself?

Background on Remuneration Committee

2. Please tell me a bit about the remuneration committee or consulting work you do?

Determining Executive Remuneration

3. What is the role of remuneration committee?
4. Please explain briefly how executive remuneration packages determined by the remuneration committee? *(This question aims to understand what factors are top of mind for the participants before any probing is done)*
5. Do you have any models or policies and procedures for determining executive pay? Please describe them
6. When going through the process of determining executive remuneration, what factors relating to the executive are considered?
7. When going through the process of determining executive remuneration, what factors relating to the company are considered?
8. Are the shareholders' interests considered when determining executive remuneration? To what degree are these considered; are they at the forefront of the decision?
9. What role does corporate governance play in determining executive remuneration?
10. What do you believe are the most important factors to consider when determining executive remuneration? Why are these important?
11. What do you believe are the least important factors to consider when determining executive remuneration? Why are these not as important?

Closing

12. Is there anything else you would like to share about determining executive remuneration?

APPENDIX B: CONSENT FORM

CONSENT FOR RESEARCH INTERVIEW

**Dear
Participant**

You are invited to participate in an academic research study conducted by an MBA student (Wilfred Mwiwa, student number 16008724) from the GIBS Business School at the University of Pretoria. **The purpose of the study is to gain a better understanding of the considerations of South African remuneration committee when determining executive remuneration.**

Please note the following:

- This is an anonymous study survey and your name will not appear on any document published as a result of this study. The answers you give will be treated as strictly confidential.
- Your participation in this study is very important to us. You may, however, choose not to participate and you may also stop participating at any time during the interview without any negative consequences.
- Our interview is expected to last about an hour and will help us understand the considerations of the South African remuneration committee when determining executive remuneration.
- With your kind permission, the interview will also be audio-recorded to facilitate collection of accurate information and later transcribed for analysis. All information you provide is considered completely confidential. Your name will not appear in any publication resulting from this study and any identifying information will be omitted from the report. However, with your permission, anonymous quotations may be used. Data collected during this study will be retained on a password protected computer for a short period of time. There are no known or anticipated risks to you as a participant in this study.
- Should you have any questions or concerns, please do not hesitate to either consult me, or my supervisor. My details and the supervisor's details are as follows:

Researcher: Wilfred Mwiwa
e-mail: wilfredmwiwa@gmail.com
Phone: 079 329 6511

Supervisor: Dr Mark Bussin
e-mail: drbussin@mweb.co.za
Phone: 082 901 0055

Please sign the form to indicate that:

- You have read and understood the information provided above.
- You give your consent to participate in the study on a voluntary basis.

Signature of participant: _____

Date: _____

Signature of researcher: _____

Date: _____

APPENDIX C: CONSISTENCY MATRIX

TITLE: EXECUTIVE REMUNERATION: CONSIDERATION OF SOUTH AFRICAN REMUNERATION COMMITTEES.

QUESTIONS	LITERATURE REVIEW	DATA COLLECTION TOOL	ANALYSIS
<p>Research Question 1</p> <p>Explore how executive remuneration packages are determined by remuneration committees.</p>	Murphy (2013)	<p><u>Qualitative Methodology</u></p> <p>Semi-structured interview with remuneration committee member</p>	Excel and external research analyst
<p>Research Question 2</p> <p>Do remuneration committees use policies and procedures when determining executive remuneration?</p>	<p>Murphy, & Sandino (2009).</p> <p>Guthrie, Sokolowsky, & Wan (2012)</p>	<p><u>Qualitative Methodology</u></p> <p>Semi-structured interview with remuneration committee member</p>	Excel and external research analyst
<p>Research Question 3</p> <p>What are the most important factors of consideration for executive remuneration?</p>	<p>Guthrie, Sokolowsky, & Wan (2012)</p> <p>Van Essen, Otten, & Carberry (2012)</p>	<p><u>Qualitative Methodology</u></p> <p>Semi-structured interview with remuneration committee member</p>	Excel and external research analyst
<p>Research Question 4</p> <p>Do remuneration committee comply with corporate governance when determining executive remuneration?</p>	<p>Van Essen, Otten, & Carberry (2012)</p> <p>Bebchuk & Fried (2004)</p> <p>Guthrie, Sokolowsky, & Wan (2012)</p>	<p><u>Qualitative Methodology</u></p> <p>Semi-structured interview with remuneration committee member</p>	Excel and external research analyst

APPENDIX D: ETHICAL CLEARANCE LETTER

Gordon Institute of Business Science

University
of Pretoria

07 June 2018

Mwiwa Wilfred

Dear Wilfred

Please be advised that your application for Ethical Clearance has been approved.

You are therefore allowed to continue collecting your data.

Please note that approval is granted based on the methodology and research instruments provided in the application. If there is any deviation change or addition to the research method or tools, a supplementary application for approval must be obtained

We wish you everything of the best for the rest of the project.

Kind Regards

GIBS MBA Research Ethical Clearance Committee

APPENDIX E: CERTIFICATION OF ADDITIONAL SUPPORT

I hereby certify that ***I RECEIVED*** additional/outside assistance for editorial services on my research report.

Name and contact details of editor:

NAME: ...Sandra Reinbrech.....

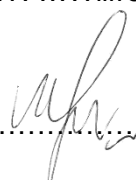
EMAIL ADDRESS: ...sandra@librasquared.com.....

CONTACT NUMBER: ...+27 61 442 6182.....

TYPE OF SERVICE: ...Editorial assistance.....

I hereby declare that all interpretations (statistical and/or thematic) arising from the analysis; and write-up of the results for my study was completed by myself without outside assistance

NAME OF STUDENT: ...Wilfred Mwiwa.....

SIGNATURE: .....

STUDENT NUMBER: ...16008724.....

STUDENT EMAIL ADDRESS: ...16008724@mygibs.co.za.....

APPENDIX F: DATA ANALYSIS CODES AND CONSTRUCTS

Objectives	Themes	Constructs	Codes		
Objective 1	Role of REMCO	Sub-committee to the board Governance	Ensure compliance of remuneration policies and procedures		
			Ensure compliance of remuneration regulations		
			Align shareholder and executive goals		
			Independent remuneration monitoring body		
			No influence of bias		
			Consistent application of policies and procedures		
	Process followed for determination of executive remuneration	Gathering and analysing information		Company strategy	
				Company Performance	
				Previous remuneration package of executive	
				Executive experience and skills	
				Executive performance (KPI's)	
				Development goals of executive	
				Competitor information	
				Benchmarking	
				Economic information	
				Industry trends	
				Labour laws and policies	
				King IV	
				Union information	
				Designing remuneration package	
		Fixed pay /guaranteed pay/ take home pay			
		Benefits			
		Variable pay			
		Performance metrics			
		Performance pay			
		Long-term pay			
		Short-term incentives			
		Bonus			
		Share options			
		Deferred bonus			
		Cash incentive			
		Phantom shares			
Scrutiny, approval and implementation			Remuneration policies and procedures		
			Governance		
			REMCO, board and shareholder approval		
Review and monitoring			Annual review and monitoring		

Objectives	Themes	Constructs	Codes
Objective 2	Remuneration policies and procedures	Internal policies and procedures	HR and remuneration policies
			Continuous review of company policies and procedures
		Legislated policies and procedures	Companies Act
			King IV
			Labour Act
			Authority of REMCO to deviate from internal policies and procedures
Strict governance of legislation			
Objective 3	Organisation and Executive Considerations	Organisation structure and complexity	Company size
			Company complexity
			Company turnover
			Footprint of company
			Global location complexities (laws, taxes, cultures, reporting structures)
			Number of subsidiaries in executive responsibility
			Number of employees for executive to oversee
			Complexity of executive tasks
			Company revenue, total assets, the number of employees in the company, or by market capital
			Total assets of company
			Shareholder return on equity
			Shareholder risk
			Market capital of company
			Sustainability of company
		Life stage of company	
		Executive Considerations	Executive performance in line with performance targets
			Executive qualifications less important than proven track record
	Executive mobility less important		
	Legal and Ethical Considerations	Legislation	Compliance necessary to defend decisions
			Companies Act and Labour relations Act highly important
			Industry specific acts
			King IV as important as legislation
		Transparency and disclosure	
		King IV	Risk of reputational damage
			Fair and responsible remuneration
			Equity
		Internal Policies and Procedures	Legal requirements included in company policies and procedures
		Unions	Employment creation
		Ethical	Wage gap less important

Objectives	Themes	Constructs	Codes
			Living wage
			Consideration of society
			Balance of shareholder and executive interests
	Market Considerations	Economic conditions Industry considerations Competitor considerations	Rate of economic growth
			Company performance projections
			Compensation package to attract and retain executive
			Inflation
			High and low growth industry environment
			Job creation versus retrenchments
			Comparative benchmarks
			Affordability
Determination of pay scales and percentile pay outs			