

## **Portuguese People's Views Regarding the Legitimacy of Bonuses for Senior Executives in Time of Global Crisis: A Preliminary Study**

Joana Margarida Sequeira Neto\*

*University of Oporto, Portugal,*

*and Institute of Advanced Studies (EPHE), France.*

We applied a technique that has already been implemented in studies conducted in the field of bioethics to map people's views regarding senior executive compensation. Fifty participants were presented with a number of concrete scenarios depicting the circumstances in which senior executives have received bonuses of variable amount, and they were asked to indicate the extent to which such bonuses may be considered as legitimate. The scenarios were created by varying four factors likely to impact of people's views: (a) the extent to which the objectives fixed by the company have been attained or not, (b) the global, economic context in which the company has performed, (c) the availability of experienced senior executives in the sector considered, and (d) the amount of money that has been attributed, in terms of pay multiple. Three different personal positions were found. The most common position was that the legitimacy of bonuses mainly depends on the degree to which the company's objectives have been attained. A small minority of people considered that bonuses were never legitimate, and another minority of people considered that they were never fully legitimate but that in at least one case – comparatively low amount of money and the surpassing of objectives, bonuses can be viewed as somewhat legitimate.

“For more than a decade, executive compensation in the United Kingdom (UK), United States (US) and other jurisdictions has attracted unfavorable attention from practitioners, academics and the media, who have focused on the large amounts received by executives, both in absolute terms and in comparison with the pay received by employees lower down the corporate hierarchy. Much of this commentary is about whether the level of pay is ‘fair’” (Bender & Moir, 2006, p. 75). This preliminary study

---

\* Address correspondence to Joana Sequeira, e-mail: [netojoana@hotmail.com](mailto:netojoana@hotmail.com)

was aimed at examining lay people's views on the fairness/legitimacy of bonuses for senior executives, and at assessing the effect of level of knowledge in economic science on these views.

Few studies on lay people's views regarding the ethics of business in general or the ethics of executive compensation in particular have been reported (e.g., Borkowski & Ugras, 1992). This is surprising given most people's concerns about social justice in time of crisis (Jousenvirta, 2012). This is also surprising given that whether one believes that senior executives are excessively compensated (or not) is a personal judgment (Nichols & Subramaniam, 2001). Lay people's judgment capacities are probably not lesser than experts' ones when societal issues are at stake, and their views deserve to be carefully examined and taken into consideration, would it be just for preventing political exploitation of public discontent by extremists groups.

The present study applied a technique that has already been implemented in studies conducted in the field of bioethics (see Mullet et al, 2012, for an overview). Participants were presented with a number of concrete scenarios depicting the circumstances in which a senior executive has received a bonus of a variable amount, and they were asked to indicate the extent to which such a bonus may be considered as legitimate.

The scenarios were created by varying four factors likely to impact of people's views. The first factor was the extent to which the objectives fixed by the company have been attained or not (Nichols & Subramaniam, 2001). The second factor was the global, economic context in which the company has performed. It is in this context that the level of attainment of objectives must be assessed (Angel & McCrabe, 2008). The third factor was the availability of experienced senior executives in the sector considered (Angel & McCrabe, 2008). Finally, the fourth factor was the amount of money, in terms of pay multiple; that is, the ratio of senior executive pay and the average employee compensation (Cai, Jo & Pan, 2011).

### **Hypotheses**

The first hypothesis was that, as in most previous studies on people views regarding ethical matters (see Mullet et al., 2012) several qualitatively different personal positions would be encountered among participants. As suggested by Nichols and Subramaniam (2001), each people has probably his/her personal answer. One of these positions would be that bonus are never legitimate, irrespective of circumstances (Angel & McCrabe, 2008). Another of these positions would be that what matters most for judging of the legitimacy of bonuses is the degree to which

economic objectives have been attained. This position would reflect people's endorsement of what is called Agency Theory (Jensen & Meckling, 1976). Alternative positions taking mainly into account the situation of the job market regarding talented executives or the pay multiple factor may, of course, also be found.

The second hypothesis was that these qualitatively distinct personal positions would be linked to people's level of knowledge in economics (Borkowski & Ugras, 1992). In particular, if a "never legitimate" position is empirically found, it would be less frequently found among people who have been trained in economics than among people who have not. In contrast, an agency theory-type position would be more frequently found among people who have been trained in economics than among people who have not.

## METHOD

**Participants.** Fifty unpaid individuals (23 females and 27 males), currently living in Oporto, Portugal, participated for this pilot study. Their mean age was 30 years ( $SD = 15.32$ , range = 18-79 years). Thirty-two had been trained in economics, and 18 had never taken any courses in economics.

**Material.** The material consisted of 54 cards showing a story of a few lines and a response scale. Each vignette had four critical items of information in the following order: (a) the availability of "talented" executives in the labor market (easy, difficult, extremely difficult to recruit a talented executive), the extent to which the objectives that were fixed by the company had been attained (not attained, attained, surpassed), the global context (crisis or development), and the amount of money attributed as a bonus (E300,000, E600,000, and E900,000; that is, 30, 60 and 90 times the average workers' income in the country). These three levels have been chosen in order to reflect the range of bonuses attributed to senior executives in Portugal at the time of the study (Comissão do Mercado de Valores Mobiliários, 2012). The vignettes were obtained by the orthogonal crossing of the four factors:  $2 \times 3 \times 3 \times 3 = 54$ .

The question and the response scale were under each story. The question was "To what extent do you think that the attribution of such a bonus is legitimate in this case?" The response scale was an 11 point scale with "Not at all" (0) at the left hand extreme and "Completely" (10) at the

right hand extreme. One example is given in the Appendix A. The cards were arranged in random order for each participant.

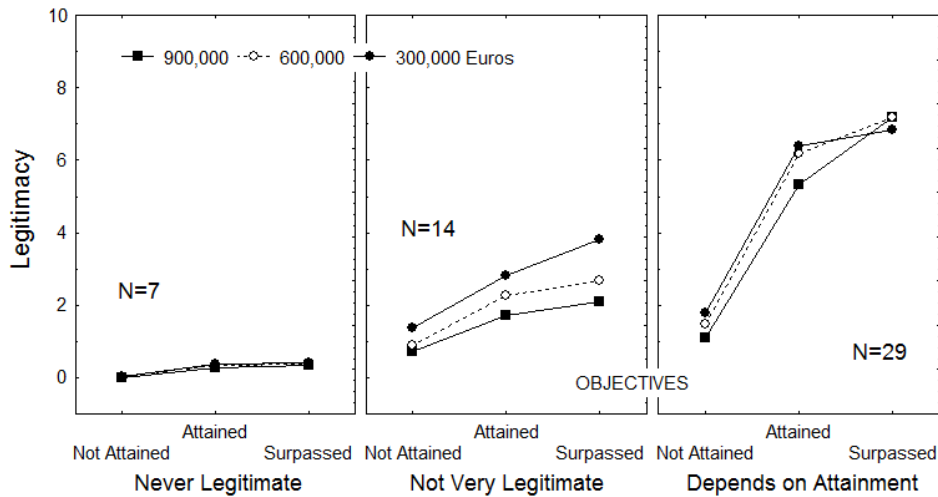
**Procedure.** Each person was tested individually or in small groups of two or three people in his/her own home. The session had two phases. In the familiarization phase, the experimenter explained to participants what was expected from them, in other words, they were about to read a certain number of vignettes depicting the circumstances in which an executive has been attributed a determined amount of money in addition to his/her regular wages, and, for each vignette, they had to indicate the degree to which they would feel legitimate this attribution of bonus. Subsequently, participants were presented with 18 vignettes taken randomly from the complete set. They read each vignette, after which the experimenter reminded them the items of information. Then, the participants made their ratings. After completing the 18 ratings, they were allowed to go back at their responses, compare them, and make changes.

During the following experimental phase, the whole set of vignettes was presented to the participants. They made their ratings at their own pace, but they were no longer allowed to go back and make alterations. Participants took 35 to 50 minutes to complete both phases.

## RESULTS

As expected, participants responded in very different ways, and a cluster analysis was applied to the raw data in order to capture possibly radically different attitudes. K-means clustering – a nonhierarchical centroid based procedure – was applied because it uses all data points, and it is not very sensitive to the distance measure employed or to the presence of outliers (Hofmans & Mullet, 2013). A three-cluster solution was retained. The main results corresponding to these clusters are shown in Figure 1, with mean legitimacy ratings pooled across levels of availability of talented executives and global economic context. Three separate analyses of variance were conducted on the raw data of each cluster with a design of Context x Availability x Objectives x Amount, 2 x 3 x 3 x 3. Owing to the great number of comparisons conducted, the significance threshold was set at .01.

The first cluster was called *Never Legitimate* because the overall mean rating was close to the “Not at all” end of the response scale ( $M = 0.24$ ). This cluster was composed of seven participants (14%): two who have been trained in economics (6%), and five who have not (28%).



**Figure 1. Patterns of results corresponding to the *Never Legitimate* cluster (left panel), to the *Not Very Legitimate* cluster (second panel), to the *Mainly Depending on the Attainment of Objectives* cluster (right panel). In each panel, the mean legitimacy judgments are on the y-axis, the three levels of attainment of objectives are on the x-axis, and the three curves correspond to the three amounts of money. Ratings are pooled across levels of availability of talented executives and global economic context.**

The second cluster was called *Not Very Legitimate* because mean ratings were always closer from the “Not at all” end of the response scale ( $M = 2.04$ ) than from the other end. In the “best” case (objectives that were surpassed and attribution of 300,000 Euros) the mean legitimacy value was 4.29 (out of 10). For the participants in this cluster, legitimacy was higher (a) when the objectives had been surpassed ( $M = 2.86$ ) than when they had simply been attained ( $M = 2.27$ ) or when they had not been attained ( $M = 1.00$ ),  $F(2, 26 = 19.99, p < .01$ , and (b) when the amount of money was 300,000 euros ( $M = 2.66$ ) than when it was 600,000 euros ( $M = 1.94$ ) or 900,000 euros ( $M = 1.51$ ). The Objectives  $\times$  Amount was significant, and its bilinear component was also significant. The effect of the objective factor was stronger when the amount of money was 300,000 euros (a difference of 2.43 points) than when the amount of money was 900,000 euros (a

difference of 1.40 point),  $F(4, 52 = 3.55)$ ,  $p = .01$ . This cluster was composed of 14 participants (28%): eight who have been trained in economics (25%), and six who have not (33%).

The third cluster was called *Depends on the Attainment of Objectives* because the strongest effect was the effect of the objective factor. Overall mean rating was 4.83; that is, close to the middle of the response scale. For the participants in this cluster, legitimacy was higher (a) when few or very talented executives were available in this sector ( $M = 4.95$ ) than in the other case ( $M = 4.58$ ),  $F(2, 56 = 5.39$ ,  $p < .01$ , (b) when the objectives had been surpassed ( $M = 7.07$ ) than when they had simply been attained ( $M = 5.96$ ) or when they had not been attained ( $M = 1.46$ ),  $F(2, 56 = 105.07$ ,  $p < .01$ , and (c) when the amount of money was 300,000 euros ( $M = 5.00$ ) than when it was 900,000 euros ( $M = 5.53$ ). The Objectives x Amount was significant, but its bilinear component was not. The effect of the amount of money factor was inverse when the objectives were not attained (from 1.79 to 1.09) or where simply attained (from 6.38 to 5.32), and direct when the objectives have been surpassed (from 7.19 to 8.83),  $F(4, 112 = 5.35$ ,  $p < .01$ . This cluster was composed of 29 participants (58%): 22 who have been trained in economics (69%), and seven who have not (39%).

An ANOVA was also performed on all the raw data. The design was Cluster x Context x Availability x Objectives x Amount,  $3 \times 2 \times 3 \times 3 \times 3$ . The Cluster effect was, of course, significant, and post hoc analyses showed that the means between all clusters differed significantly. Two interactions involving the cluster factor were significant: Cluster x Objectives and Cluster x Objectives x Amount. The effect of the attainment of objectives was significantly stronger in the *Depends on the Attainment of Objectives* cluster than in the other clusters. The shape of the Objectives x Amount interaction was very different from one cluster to the other.

An ANCOVA was conducted with Training as the between-subject factor, and gender and age as the covariate. The mean rating of the participants who had been trained in economics ( $M = 4.10$ ) was significantly higher than the one of the other participants ( $M = 2.17$ ),  $F(2, 48) = 12.88$ ,  $p < .01$ . The Training x Context was significant. Among the participants who had not been trained in economics, legitimacy ratings were lower in the context of crisis ( $M = 1.86$ ) than in the context of development ( $M = 2.49$ ), which was not the case among the other participants. Not surprisingly, among the participants who had been trained in economics, the Objectives factor had a stronger effect than among the other participants.

## DISCUSSION

Lay people views on the fairness/legitimacy of bonuses for senior executives have been explored using a technique that had successfully been implemented in previous studies conducted in the domain of bioethics. As hypothesized, qualitatively different personal positions were found. The most common position was that the legitimacy of bonuses mainly depends on the degree to which the company's objectives have been attained. When the objectives have been surpassed, bonuses appeared as fully legitimate, and comparatively high bonuses appeared as even more legitimate than comparatively lower ones. When the objectives have simply been attained, bonuses appeared as largely legitimate but high bonuses appeared as less legitimate than lower ones. When the objectives have not been attained, bonuses appeared as illegitimate. People endorsing this position did not think (a) that the global context or (b) the situation of the job market regarding talented executives must be taken into account for judging legitimacy. They probably assume that (a) the objectives of the company have been determined as a function of this context, and (b) the senior executives' talent was already fully reflected in the company's actual performance. As also hypothesized, people with a background in economics were more likely to hold this view than other people. This result was consistent with findings by Borkowski & Ugras (1992).

A small minority of people considered that bonuses were never legitimate, and another minority of people considered that they were never fully legitimate but that in at least one case – comparatively low amount of money *and* the surpassing of objectives, bonuses can be viewed as somewhat legitimate. The cognitive rule at work here was  $\text{Legitimacy} = f(\text{Money} \times \text{Objectives})$ . As hypothesized, people with a background in economics were less likely to hold these two views than other people. This result was consistent with findings by Borkowski & Ugras (1992).

Future studies on larger samples should check whether the three-position taxonomy found in this preliminary study fully reflects the diversity of opinions in the general public. They also should also examine whether performance should be the only criterion to be considered to determine senior executive compensation, or whether other criteria should be added (e.g., respect for the environment and responsible governance) (Angel & McCrabe, 2007).

Finally, future studies should explore the role of culture on lay people's ethics thinking regarding the conduct of economic affairs. For instance, it has been suggested that economic decisions in Asian countries are usually taken by teams rather than by a single individual, which may

strongly impact on the way rewards must be shared (Walters, Hardin, & Schick, 1995). Previous studies have shown that the approach used in the present study is flexible enough to allowing meaningful comparisons between samples from many countries (e.g., Kamble, Ahmed, Sorum, & Mullet, 2013).

## REFERENCES

- Angel, J., & McCabe, D. (2008). The ethics of managerial compensation: The case of executive stock options. *Journal of Business Ethics*, *78*, 225-235.
- Bender, R., & Moir, L. (2006). Does "Best Practice" in setting executive pay in the UK encourage "Good" behavior? *Journal of Business Ethics*, *67*, 75-91.
- Borkowski, S. & Ugras, Y. (1992). The ethical attitudes of students as a function of age, sex and experience. *Journal of Business Ethics*, *11*, 961-979.
- Cai, Y., Jo, H. & Pan, C. (2011). Vice or virtue? The impact of corporate social responsibility on executive compensation. *Journal of Business Ethics*, *104*, 159-173.
- Comissão do Mercado de Valores Mobiliários (2012). *Relatório anual sobre o governo das sociedades cotadas em Portugal*. Lisboa: CMVM.
- Hofmans, J., & Mullet, E. (2013). Towards unveiling individual differences in different stages of information processing: A clustering-based approach. *Quality and Quantity*, *47*, 555-564.
- Jensen, M. C., & Meckling, W. H. (1976). Theory of the firm: Managerial behavior, agency costs, and ownership structure. *Journal of Financial Economics*, *3*, 305-360.
- Joutsenvirtia, M. (2012). Executive pay and legitimacy: changing discursive battles over the morality of excessive manager compensation. *Journal of Business Ethics*. Advance online publication.
- Kamble, S., Ahmed, R., Sorum, P. C., & Mullet, E. (2013). The acceptability among young Hindus and Muslims of actively ending the lives of newborns with genetic defects. *Journal of Medical Ethics*, in press.
- Mullet, E., Sorum, P. C., Teyssere, N., Nann, S., Morales, G. E., Ahmed, R., Kamble, S., Olivari, C., & Munoz Sastre, M. T. (2012). Functional Measurement in the field of empirical bioethics. *Psicologica: International Journal of Methodology and Experimental Psychology* [Special Issue on Functional Measurement], *33*, 665-681.
- Nichols, D., & Subramaniam, C. (2001). Executive compensation: Excessive or equitable? *Journal of Business Ethics*, *29*, 339-351.
- Walters, B. T., Hardin, T., & Schick, J. (1995). Top executive compensation: Equity or excess? Implications for regaining American competitiveness. *Journal of Business Ethics*, *14*, 227-234.



## APPENDIX A

O Dr. Fonseca é o Director Executivo da PINTO MAGALHÃES, uma das maiores empresas do país.

O Dr. Fonseca está no cargo há dois anos. Tem sido muito difícil para a empresa recrutar um Director Executivo competente porque o número de especialistas nesta área é muito limitado.

Este ano, os objectivos da empresa foram atingidos. As vendas da empresa aumentaram de 5%. Contudo, o Produto Interno Bruto do país tem estado estagnado.

Tem sido atribuído ao Dr. Fonseca um bónus de 600 000€. Esta quantia equivale a 1 vez o seu salário base e 60 vezes o salário médio do país.

*Até que ponto acha que a atribuição de uma quantia de dinheiro, neste caso particular se justifica?*

Nada o-----o-----o-----o-----o-----o-----o-----o-----o-----o Completamente