

WHEN PAY IS KEPT SECRET, THE IMPLICATIONS ON PERFORMANCE ARE REVEALING

Key Findings

- Pay secrecy (in contrast to pay transparency) negatively affects the performance of individuals who are less tolerant to inequity;
- Pay secrecy negatively affects the perception of the link between performance and pay in individuals intolerant to equity, which in turn, decreases their performance;
- In contrast, pay secrecy is associated with significantly better task performance than pay transparency for individuals who are more tolerant to inequity.

Topic: A Person's Tolerance For Inequity May Affect Performance When it Comes to Pay Secrecy

Public companies are required to share compensation packages for their top executives. And yet, pay secrecy for most other employees remains an established practice in many workplaces both in America and abroad (Day, 2007; Gely & Bierman, 2003). Many organizations believe that pay secrecy eliminates jealousy among employees. Indeed, well over a third of those American employers surveyed indicated that they provide only a limited amount of pay information to their employees and enforce rules prohibiting employees from discussing their wages with coworkers (HRnext.com Survey, 2001). This research examines the impact of pay secrecy on employees' performance.

Researchers set out to draw from expectancy theory notions to explain how the effects of pay secrecy on perceived performance-pay instrumentalities are likely to cause a generally adverse effect on individual task performance. In addition, the study drew from equity and justice models to suggest that informational and procedural fairness perceptions may also



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play a role in generating such outcomes, partially mediating the effect of pay secrecy on individual task performance. Finally, building on Collela et al's (2007) suggestion that the effects of pay secrecy may not be universal, the researchers explain how this indirect effect of pay secrecy on individual task performance is likely to be moderated by tolerance for inequity.

The study was performed in a lab-based simulation in which base pay was constant, but pay communication policy regarding performance-based bonuses was manipulated. The experiment proposed and tested the following factors:

- (a) the psychological mechanisms linking pay secrecy and individual task performance, as well as;
- (b) a key dispositional factor – namely the individual's tolerance to inequity – as a potential mitigation variable of such relations.

Results

Many managers believe that pay secrecy is better because it avoids the implications if one employee finds out that a coworker makes more than him/her. However, many up-and-coming Generation Y employees have grown up in the public world of social media and have no issues sharing information with one another that used to be seen as private – such as pay. Furthermore, they are more likely to have access to ballpark figures that are easily obtained from any computer or even a smartphone. Even for non-Millennials – or for those who don't go online to try to estimate what others make, people always assume that 1) other people make more money than they do in fact and that 2) they are better performers.

Researchers found that the relationship between pay secrecy (relative to pay transparency) and perceived pay-for-performance link (i.e. instrumentality perceptions) is moderated by an individual's tolerance for inequity. For employees with lower levels of tolerance, this means lower performance.

Method

Pay policy was manipulated for the 144 participants of the study in the following way: **Pay secrecy individuals** received information on their *own* absolute levels of individual performance and bonus pay only. In addition, prior to the first round of the simulation, participants in this condition were told that pay is a personal matter and were

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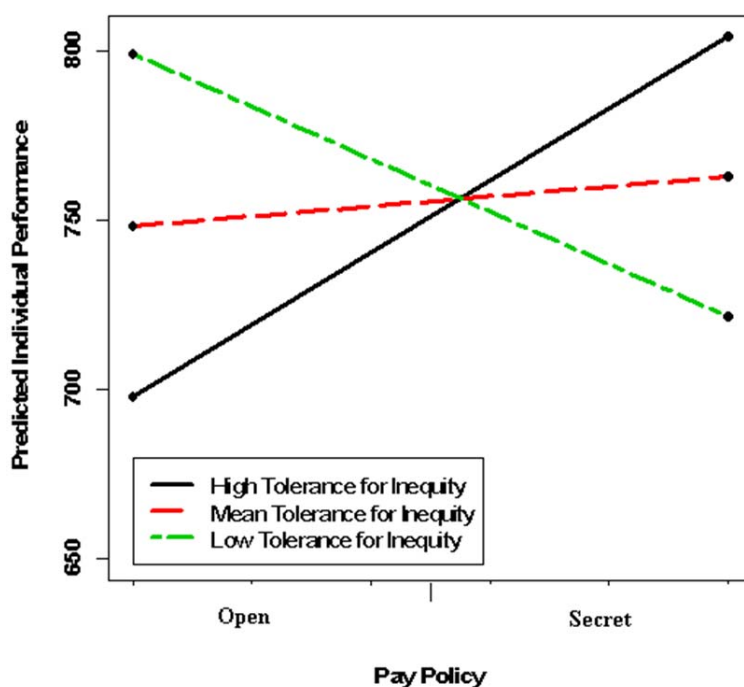
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requested not to discuss any pay-related matter with other participants in the study at any time. All communications between participants was monitored.

In contrast, participants assigned to the **open pay condition** received information regarding their *own* individual performance and bonus pay as well as information regarding the pay (but not performance level) of their fellow group members (listed by code-numbers in order to ensure privacy). Participants in the open condition were told that their post phase, e-mail-based communications with their fellow group members would be completely unrestricted.

Figure 1: Moderated Model of Pay Policy (X) on Individual Task Performance (Y)



The direct effect of pay communication policy on task performance is significantly moderated by tolerance for inequity. The nature of this moderation effect is also consistent with the theory that the relationship between pay secrecy and individual task performance is such that performance is lower among those with lower levels of tolerance for inequity. There is a significant positive effect of secrecy on performance among those more inequity tolerant. In contrast, among those less tolerant for inequity, this effect is not only not significant, it is downward sloping.

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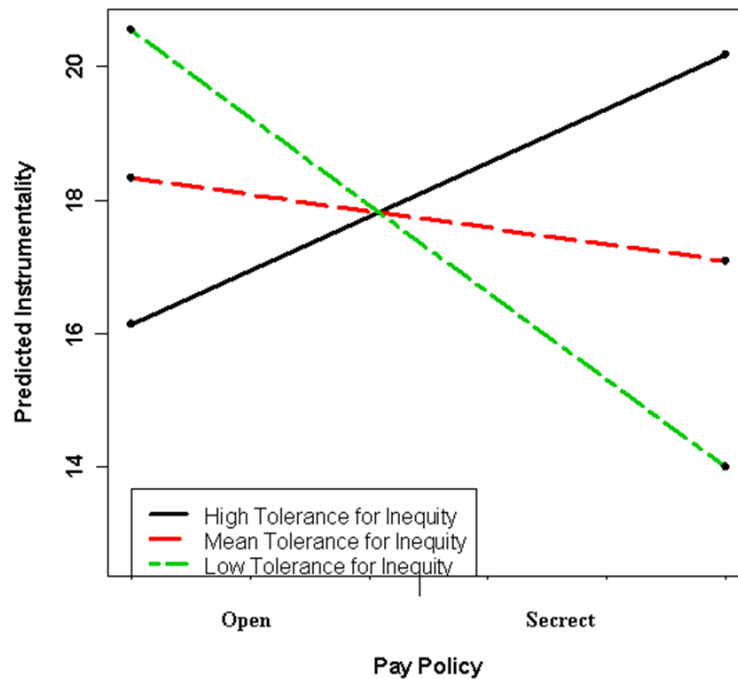
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Figure 2: Moderation of the Effect of Pay Policy on Perceived Instrumentality



The impact of pay secrecy on instrumentality perceptions for those respondents with mean and high tolerance for inequity were insignificant. In contrast, for those with low tolerance for inequity, the negative effect of pay secrecy on individual task performance via perceived instrumentality is more negative among those with lower levels of inequity tolerance.

In other words, when people are in an environment where they have to guess what others make, those individuals who are less inequity tolerant not only think that they deserve to make more money, but they are less motivated to work hard.

Takeaways

- The findings suggest that organizations subscribing a policy of pay secrecy should make additional efforts to help employees with lower levels of tolerance for inequity to more accurately calibrate their perceptions of the link between performance and pay.
- One example could be – rather than enforcing a policy of strict pay secrecy – adopting a pay administration policy of partial openness with the broad parameters of compensation (for example, making bonus associated with a given level of performance or performance improvement more transparent). This option would eliminate the reluctance that managers have shown in the past to overhaul an entire pay policy – a daunting task, to say the least.
- The solution is not to make pay systems completely open, but to make them more transparent and fair, and communicate clearly about them. Employees need to understand how to get from Point A in a salary range to Point B. It's also important to make sure that employees perceive the system as fair – it doesn't matter what you think. If your employees don't perceive it as fair, you're in trouble.

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