

*The relationship between performance indicators and executives' remuneration in the South African higher education sector*

M.J. Maleka  
C.M. Schultz

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**Abstract**

Executive remuneration is a complex topic. Executives (vice chancellors) in the higher education sector serve the interests of many stakeholders such as students, unions, management, community and government. In the main, vice chancellors drive the interest of their major stakeholder, which is the government. They do this by ensuring that their academic institutions produce a workforce needed by the labour market, implement transformation, produce research that addresses societal problems and is published in high-impact journals, and have high graduate employability rates. In addition, executives must ensure that the institutions they lead are financially sustainable. The major financial sources are tuition and publication fees and third-stream income (i.e. offering short learning courses). It can be averred that the performance indicators which lead to executives' remuneration are not purely financial. This article ends by proposing that future research should be conducted to determine how executives' performance indicators are to be weighted as compensational factors within the context of South African universities.

**Keywords:** Agency theory, executive salary, South African universities, sales and enrolled students

## Introduction

Executive remuneration is defined as compensation for achieving the agreed target (Jong & Ho, 2019; Veldsman & Johnson, 2016). Executive compensation consists of base or fixed pay and variable pay. Base pay is mainly determined by market data (i.e. organisational size, labour market/industry/sector and geographical location), while variable pay is linked to performance (Modau, 2014:50). Corporate executives' variable pay entails bonuses and shares, and its contributors are given more weight than those for the base pay. This means that corporate executives' pay is driven mainly by variable pay. On the contrary, in the public sector (including universities), executives' base pay contributes a higher percentage to their remuneration because public-sector institutions do not offer shares (Carlson & Bussin, 2020). At the time this article was written, the performance indicators used to determine the executives' salaries were unclear.

The salaries of executives at South African universities have been heavily criticised in the media (Govender, 2019), and little research has been conducted to determine and measure the performance indicators in order to govern these salaries. This was one of the motivations that drove us to address this void in the South African literature. The other motivation was that executive remuneration has been identified by South African futurist research as a topic that will be salient in human resource management (Wärnich, Carell, Elbert & Hatfield, 2018). Recently, some South African universities have been put under administration, and yet there is no clarity about executives' remuneration (Linden, 2019). Compelling executives to pay back remuneration due to poor performance is known as a clawback when performance targets are not met (Martocchio, 2015).

In the main, universities are put under administration due to lack of financial prudence or not being financially sustainable. One of the factors that puts South African universities under financial pressure is that some of the universities are compelled to cover the costs emanating from students who cannot pay for their tuition. This puts universities under pressure beginning of the 2021 academic year, because students protest especially when they are excluded due to owing tuition fees. In response, the universities end up using money in their fiscus to cover for students who cannot pay off their debts and registration (Nkanjeni, 2021). Based on this, it can be argued that universities' poor financial position and bottom line are not purely due to executives' lack of financial prudence, but also caused by societal problems. In addition, the Council on Higher Education (2018) reports that performance indicators are both financial (i.e. tuition, research and teaching outputs) and non-financial (i.e. full-time equivalent, success rates, number of students registered and success/throughput and full-time equivalent (FTE)). This led to us asking this question: What are the performance indicators that should

be used to determine executives' remuneration in the South African higher education sector?

We hypothesise that:

- There is a relationship between performance indicators and executives' remuneration in the South African higher education sector.

To address this hypothesis, the following objectives have been formulated:

- The relationship between performance indicators and executives will be measured using data from the universities' annual reports from 2015 to 2020.
- Perceptions from remuneration experts will be solicited to establish which performance indicators to prioritise when recruiting and retaining executives.
- A remuneration questionnaire will be developed and validated.

## Agency theory

From an executive remuneration theoretical framework, we deemed the agency theory appropriate in this study. This theory states that the remuneration of agents (i.e. executives) should be determined by "company owners (shareholders)" (Martocchio, 2015:381). The executives referred to here are chief executive officers, not vice chancellors. The problem with agents (i.e. executives) is that sometimes they do not act in the shareholders'/stakeholders' interest, but instead manipulate organisations to focus on short-term financial gains, which will enable them to meet the variable pay performance indicators (Martocchio, 2015). Not serving the stakeholders' interest and focussing on one's personal interest is known as an agency problem (Lee, 2011). The main short-term indicators that shareholders calculated to determine the executives' (i.e. agents) variable pay are return on assets (ROA), return of equity (ROE) and revenue (Nuanpradit, 2019). ROA, for example, is calculated by dividing the net income from total assets and net income and shareholder equity (Van Den Berg & Pietersma, 2003). Scholars such as Cable and Vermeulen (2016) are in favour of abolishing variable pay, which constitutes 60% to 80% of executive salary. Instead, they argue that executive remuneration should be fixed or base pay which is linked to the market.

In order to curb or curtail executives' rogue behaviour in manipulating financial indicators, certain measures have been put in place to protect shareholders' interests. For example, in the United Kingdom, the Cadbury 1982 report recommended that shareholders or the board of directors must appoint a remuneration committee (REMCO) that oversees executives' remuneration and ensures that it is based on the agreed performance targets (Beal, 2016). Similarly,

in South Africa, the King report states that a REMCO should be established, and that public sector universities and other organisations must publish executives' remuneration. The report further mentions that REMCOs should be established in the private sector to determine executives' remuneration based on agreed performance targets (KPMG, 2016). However, since universities do not have REMCOs, it is unclear how their salaries are determined. In the USA, the Dodd Frank Act allows stakeholders to vote how much the executive must be paid. This Act, however, states that the stakeholders' voting is non-binding; instead, it puts the final decision on the REMCO (Bussin, 2014).

## Preliminary study

To explore our research question, we conducted a study on the 2018 data of South African universities. We utilised student numbers as independent variable, because it was the data we could access through the universities' annual reports. The descriptive statistics are shown in Table 1.

**Table 1: Descriptive Statistics**

University	X (number of students)	Mean (students)	SD (students)	Y (VC salary rounded to the nearest million)	Mean (VC)	SD (VC)
Unisa	400 000	70 260	107740.81	5	3.7	1.06
University of Johannesburg	48 500			4		
University of KwaZulu Natal	40 000			3		
University of Witwatersrand	32 700			5		
Stellenbosch University	30 150			3		
University of Cape Town	26 300			4		
North-West University	74 300			3		
Rhodes University	7 000			5		
University of Pretoria	50 000			3		

To determine if the number of students was a significant performance indicator in executive salaries, we ran a regression analysis in Microsoft Excel, and the results are shown in Table 2. From the t-statistic, it can be observed that the number of students enrolled was not a significant predictor, because it was within the  $-2$  to  $+2$  range (The Economist, 2014). Since students' enrollment might contribute 6% of the variance in executive salaries, 94% of the variance is determined by other variables.

**Table 2: Relationship between number of students enrolled and executive salaries**

	<i>Coefficients</i>	<i>Standard error</i>	<i>t Stat</i>
Intercept	3.41	0.48	7.07
373747	1.01E-05	1.28E-05	0.79
$R = 0.06$			
$F = 0.62, p = 0.45$			

It is recommended that the following future research should be conducted:

- a qualitative study using data collected from remuneration experts working in the education sector;
- a panel study to measure how ROA, ROE, FTE, sales or revenue and student enrolment relate to executive salaries; and
- a cross-sectional study using variables such as transformation, ranking, community engagement and other variables identified by remuneration experts.

## Conclusion

The purpose of this conceptual paper was to provide insight into the relationship between performance indicators and executives' remuneration in the South African higher education sector. We argued that there are financial and non-financial indicators or variables that can be used to determine executive salaries in the higher education. We argued that there are financial and non-financial indicators or variables that can be used to determine executive salaries in the higher education. In conclusion, our position is that executive salaries should consist mainly of fixed pay and should be determined using market data.

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