

EXECUTIVE PERFORMANCE APPRAISAL & COMPENSATION SYSTEM IN KOREAN COMPANIES

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Role of executives and goals of executive human resource management

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The focus of executive human resource management (HRM) is to nurture the entrepreneurial spirit. The goal is to establish an empowered management system by developing executive competence through motivation. Companies need to induce executives to help create corporate value and use their capacity to the fullest. In the present day, with dynamic changes in the environment, securing competitive executives is intimately linked with a company's core competence. So in order to strengthen competitiveness, a company needs to gather talented people from outside, while motivating sitting executives. The most effective motivation is a compensation system that focuses on uplifting corporate achievement.

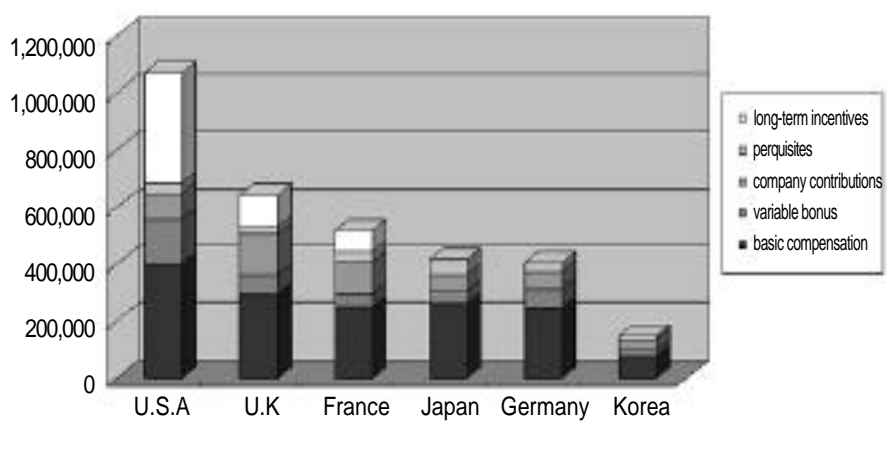
The purpose of executive HRM is to develop competence, and all HRM processes should be set up around the central idea of competence.

Since executives are the principal decisionmakers of a company's strategy and performance, their roles are strategic. Executives propose a strategy that coincides with the company's vision and mission, put it into practice and bear the final responsibility for the company's operation and performance. For executives to accomplish their role effectively, they should demonstrate management competencies in organization, planning, command, control, and coordination. To allow executives to play their strategic roles more effectively, companies should help them actively develop their competence and give it full play. Therefore, the purpose of executive HRM is to develop competence, and all HRM processes should be set up around the central idea of competence.

Actual executive performance appraisal & compensation system

In contrast to Korean companies, international enterprises have a different way of developing executive competence in their compensation systems. The competence of individual executives has a great influence on compensation in international corporations. In Korean companies however, promotions are the main cause of wage increases. With accelerating environmental changes, the relative importance of executive competence and performance is gradually escalating. Keeping up with actual trends, the motivational function of wages should be given more priority.

Figure 1. Comparison of Executive Compensation Levels (US\$)



	U.S.A.	U.K.	France	Japan	Germany	Korea
long-term incentives	390,100	112,687	74,575	0	0	0
perquisites	35,000	24,263	32,780	54,148	34,500	15,050
company contributions	88,700	145,321	114,731	61,156	58,065	35,665
variable bonus	156,400	66,723	47,859	41,771	67,842	21,526
basic compensation	402,220	296,546	250,443	263,779	248,022	78,470
TOTAL	1,072,420	645,540	520,388	420,854	408,429	150,711

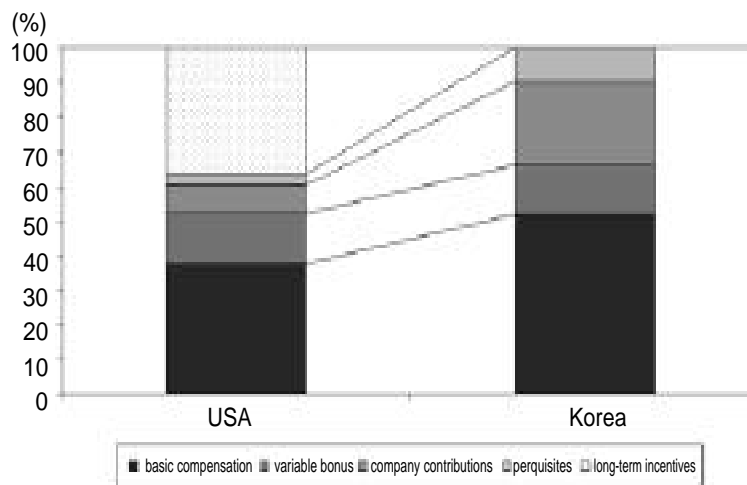
Source: Lance A. Berger & Dorothy R. Berger, The Compensation Handbook, McGraw-Hill, 1999

When wages are standardized by position, the principle of equity (which requires compensation in proportion to contribution) is damaged. Therefore, to increase equity in compensation, compensation levels should vary not only by job and position but also by the executive's competence.

In general, existing HRM systems in Korean companies do not encourage the demonstration and development of core competence. In addition, companies cannot propose a clear vision for HRM because no definition is suggested for executive competence in production, business and administration. If HRM standards and direction are not clear, long-term management strategy is difficult to implement because there is a tendency to concentrate largely on visible short-term results.

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Figure 2. Comparison of compensation structure



Source: Lance A. Berger & Dorothy R. Berger, The Compensation Handbook, McGraw-Hill, 1999

At the operating system on human resource, evaluation is based on short-term financial results rather than long-term vision because there is no performance appraisal system that corresponds with an empowered management system. Also, because of the strong seniority system, the issue of rational performance appraisal is not given the necessary attention. The subjective nature of executive evaluation also hinders compensation based on performance. As a result, executives are compensated without relation to their performance, which decreases motivation.

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In general, the compensation package of executives in Korean companies includes basic compensation, public relations expenses, allowance and bonuses, which are classed as fixed pay. The performance appraisal system for competence which decides variable pay is currently inadequate. Because a fair and balanced appraisal system for non financial aspects does not exist, undue value is given to financial evaluation. Also, there is a lack of incentives for higher performance because the criteria for performance appraisal are not made clear. This is due to lack of connection between performance appraisals and compensation. The usual result is an entrenched management system and excessive executive homogeneity. As the tendency of group think emerges, company organization becomes rigid and it becomes difficult to create a competitive atmosphere for personnel.

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Actual executive compensation in Korean companies is based on the executive's job and duties because these are the main influences on salary level decisions. The merit of this system is that companies can establish rational wage scales based on job evaluation and that compensation management is relatively clear and simple. However, the system does not sufficiently recognize and reward personal

performance. Job position in such a system is more important in compensation than personal performance. As a result, the motivation effect of compensation is enfeebled to some extent. If an executive is not appointed to a certain position, his wages are drastically cut and his living security is threatened. In the average executive compensation system in Korea, basic compensation based on seniority accounts for over 70% of pay, and variable compensation based on performance is under 10%.

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Prospects for the executive performance appraisal and compensation system

To convert the compensation system from a seniority to performance-oriented system, an approach that includes both fixed and variable wages should be established after due consideration of Korean corporate culture. The piecework system should be implemented based on company growth evaluations, including long-term incentives like stock options.

To redesign the executive compensation system, various elements should be considered, including the company's industrial environment, management activity, and the executives themselves. Compensation should vary with the competence of the executives, as well as their characteristics, career path, and age. Likewise, the compensation scale should vary with business diversification, risk management, and personnel pay levels, as well as the characteristics of the industry. In sum, personal, company, and industry factors should be considered in an executive compensation system.

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Entrepreneurial creativity is needed in motivating executives. To stimulate motivation and to actively induce higher competence, a company needs to compensate on a flexible basis with the emphasis on competence. If seniority is the main element of compensation, a company cannot offer many incentives for executive entrepreneurship. In addition, exceptional long-term incentives should be generalized for the active motivation. Contrary to international enterprises that have various long-term incentive programs, there are few Korean companies that have such programs. In spite of the recent introduction of stock option programs in Korean firms, such programs are rather simple. They should form the foundation for various long and short-term incentive programs that foster competitiveness by developing executive competence.

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The most important thing to remember in competence-oriented executive HRM is that empowerment and devolution of responsibility should actually be practiced in a company's organization. In addition, all company members should have a clear understanding about executives' authority and responsibility. **VIP**