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PROCEDURAL FAIRNESS IN PERFORMANCE EVALUATION SYSTEM: EMPIRICAL STUDY AT UNIVERSITY

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ABSTRACT

The performance evaluation system still dominates the research topics in the field of Management Accounting. Performance evaluation system is not only viewed from the metric size, but also how the evaluation process can affect the individuals' behavior to achieve goal alignment with organization. This study aims to investigate whether the process performance evaluations in this case are formality and participation can influence procedural fairness. The research was conducted at one of university in Malang as one of the education institution that prioritizes the quality of education involving all units. Data collection is done by survey method staff and lecturers with the criteria of respondent (1) has served at that position for at least one year for ensure their familiarity with the performance evaluation system, (2) there are superiors who evaluate performance, (3) has been evaluated. Research instrument to measure variable independent and dependent developed from previous research by Hartmann & Slapnicar (2009, 2012). Research is expected to contribute in providing feedback to the individual staff and lecturers of University on performance evaluation systems and how their procedural fairness perceptions improve the quality of evaluation and will have an impact on the quality of education as a whole.

Keywords: performance evaluation system, formality, participation, procedural fairness

1. Introduction

Performance evaluation system is still a dominating topic in management accounting research (Harris & Durden, 2012). Further Harris & Durden (2012) explains that performance evaluation systems are still central to the practice and research of management accounting. Therefore the topic of performance evaluation system is still relevant to be studied more deeply by not only looking at performance measurement aspect but also performance evaluation process, which in this case related to how performance evaluation is done by superiors. Performance evaluation system is developed not only consider financial or accounting information but also nonfinancial information as a measure of performance. It is reviewed by Franco-Santos, *et al.* (2012) by developing conceptual frameworks to understand the consequences of measurement systems contemporary performance comprising measurement of financial and nonfinancial performance and theories underlying these consequences.

Considering the importance and prevalence of performance evaluation procedures in control system, it is likely that fairness of the procedures will have important behavioral implications for organizational members (Lau, Wong, & Eggleton, 2008). Organizational literatures suggest that participants in the organization form a perception of fairness about the organization's procedures against them, then this perception will be able to explain

important work outcomes, such as motivation, commitment, and task performance (Hartmann & Slapnicar, 2012). Hartmann & Slapnicar (2012) also said that the characteristics that lead to performance evaluation perceived fair is still limited.

The normative principle of procedural fairness consists of consistency and accuracy. Therefore, the superior who is consistent and accurate in providing performance evaluation will be considered fairer in the evaluation process. However, Hartmann & Slapnicar (2012) suggests that there is little literature explaining what actual behavior or procedures can improve consistency and accuracy to achieve fairness. The lack of a theoretical basis resulted in earlier studies providing predictions of the effect of fairness on the characteristics of inconsistent performance evaluations. Characteristics of performance evaluation in this case as an example are non-financial measures that are considered more accurate but inconsistent.

This research tries to see performance evaluation not from measurement metrics (Financially and non-financially) but more on the performance evaluation process that is done within the organization. The trade-off that occurs between consistency and accuracy causes fairness to be no longer seen from the measurement of performance evaluation but from the performance evaluation process. Characteristics of the evaluation process include the formalities of performance evaluation and subordinate participation in the evaluation process. This study tries to examine the effect of performance evaluation process on procedural fairness perception.

It is important for organizations to design performance evaluations in accordance with organizational goals and use them to achieve organizational strategic goals. It has been argued that the design of performance evaluation has evolved along

with the development of the organization and is influenced by the culture and behavior of individuals within the organization. This is seen from recent studies that increasingly evaluate the evaluation of performance not only from the aspect of the organization but individuals in it.

Replication is done in this study by testing the generalization level of previous research findings in different contexts. As Leung (2005) points out in Agritansia & Sholihin (2011) that procedural fairness still needs to be tested in various contexts. This suggests that the procedural effect of fairness cannot be generalized in all contexts. Previous research, Hartmann & Slapnicar (2012) examines the impact of the performance evaluation process in the banking industry. The results showed that participation (voice) influences the perception of procedural fairness.

In general, this study aims to assess the perception of procedural fairness in the process of performance evaluation that can provide input to the top management of the organization to build a performance evaluation system framework that can improve the motivation, commitment and individual performance. More specifically, the process of performance evaluation involves formalities and the participation of subordinates in building a performance evaluation system. Furthermore, in relation to the appraisal of employee performance in educational institutions, fairness perceptions in performance appraisal are important to assess the assessment process that promotes quality improvement, which will impact on the quality of education services.

This research contributes in examining the effect of the performance evaluation process on the perception of procedural fairness in the organizational context in the field of education. Desriani & Sholihin (2012) conducted their research in the

aerospace industry, which has different characteristics from this research. Education institutions contribute to the development of quality human resources, which is expected to provide the best education to build not only hard skill but also soft skill. Quality of education cannot be separated from the evaluation for every individual involved in the implementation of education. In this case university, the quality of education is also determined by the quality of educator staff and support staff. An appropriate performance evaluation system can provide feedback for leaders in assessing individual performance for the quality of education maintained.

2. Literature review

2.1 Fairness perception

Organizational justice theory explain about fairness perceptions (Voubem, Kramer, & Schaffer, 2016). Two forms of fairness perceptions distinguished in organisational justice theory are distributive fairness and procedural fairness (Greenberg, 1987). Distributive fairness concerns about achieved outcome, whereas procedural fairness is about fairness in procedure used to determine those outcomes (Greenberg, 1987).

Procedural fairness refers to the social psychological consequences of variations in justice, which focus on the effect of procedures on judgment of justice (Thibaut and Walker, 1975 in Lau and Moser, 2008). It also explains that (1) procedural fairness perceptions will increase satisfaction, (2) procedural fairness is the most important determinant of choice of procedure, and (3) high process control procedures will lead to a high justice assessment as well. With respect to performance measurement, subordinates will assess fair performance evaluations if (1) an accurate and complete information-based performance assessment, (2) reflect long-term interests, (3) contain provisions that reject unfair assessments, (4) reflect on deep performance Control, (5) protect their

interests, and (6) indicate appropriate and appropriate treatment (Lau & Moser, 2008).

Procedures will be perceived fair when consistent over time and between individuals, free of bias, accurate, containing mechanics to correct wrong decisions, stick with the concept of common morality, and represent the opinions of the individuals involved. The management control system has procedural fairness aspects because the management control system is based on the procedure that defines how objectively determined, performance measurement and awarding (Langevin & Mendoza, 2013).

Studies in accounting have acknowledged the need to incorporate fairness considerations in the design of managerial control system because distributive and procedural fairness perceptions have been shown to be important predictors of beneficial work-related behavior and attitudes (Colquitt, *et al.*, 2001). Previous research has examined the effect of procedural fairness on individual behavior that will improve its performance. However, the influence varies both directly and indirectly (Supriyadi, 2010). Procedural fairness on performance evaluation affects job satisfaction through the level of trust in the boss, organizational commitment, and fairness of outcome (Lau, *et al.*, 2008). The models in this study were re-examined using different subjects to assess the generalization of research results by Sholihin & Pike (2009). The results show no difference with previous studies by Lau *et al.* (2008). Nevertheless, there are inconsistent results testing the effect of performance measurement on procedural fairness perceptions. While Lau & Moser (2008) indicate that the perception of procedural fairness of managers is more fair on the measurement of nonfinancial performance because it is considered more complete and accurate. One possible reason for the inconsistency of this study is the

importance of the performance appraisal process.

2.2 Performance Evaluation Formality

Formality performance evaluation construct of the research was first built by Hartmann & Slapnicar (2009) that examined the relationship model associated with the performance evaluation system used by superiors to subordinates confidence. Formalities construct related performance evaluation was developed because the previous studies provide evidence that performance evaluation system has impact on trust, and also raised question about what aspect of the system that affects trust and how they affect. Then, Hartmann & Slapnicar (2009) tested the aspect of performance evaluation process which is how formal evaluation carried out within organization.

Performance evaluation process in this study refers to the process of evaluation in Hartmann & Slapnicar (2009, 2012) research. This performance evaluation is seen by formalities as described as how much objectivity (compared with subjectivity) in the performance evaluation process. A superior that is often informally evaluate performance using qualitative rather than quantitative targets, measuring performance based on qualitative assessment rather than tracked procedures, and often base the award based assessment further than the fact the document (Moers, 2005). Superior that informally evaluate subordinates tend to use qualitative targets such as 'do your best' compared using a well-documented targets (Hartmann & Slapnicar, 2012).

Formality definition in this study followed the proposed definition by Hartmann & Slapnicar (2009). To the different level of performance evaluation process, the formality is defined as follows, (1) related to the determination of the target, which implies the higher the level of formality means that superior explain and set the targets in the form of quantitative and writing, while targeting informal means setting targets implicitly, qualitative and communicated informally, (2) related to performance measurement, the higher

the level of formality that requires more objective and quantitative performance measures rather than subjective and qualitative measurements, which more to the informal performance measurement, and (3), related to reward, the higher the level of formality suggests that there are any provision or formulation in determining bonuses or reward, while the more informal process of using personal judgment in determining bonuses.

2.3 Performance Evaluation

Participation/Voice

Hartmann & Slapnicar (2012) proposed the second characteristics of the performance evaluation process, that is voice which leads subordinate participation in the performance evaluation process. Hartmann & Slapnicar (2012) suggested characteristics of voice in the performance evaluation process in order to improve the consistency and accuracy in the performance evaluation process. Voice is defined by Leventhal (1980) in Libby (1999) as the ability of subordinates involved in the decision-making process by communicating their views to his superiors. Voice used in previous studies to examine the perception of fairness in setting budgeting as did Libby (1999) and Lindquist (1995).

Voice is also associated with the budgeting process which is the participation in the budgeting process. Research on participatory budgeting has been done for over 40 years and provides evidence inconsistent in their effects on satisfaction and performance (Lindquist, 1995; Shield & Shield, 1998). Because of this inconsistency, Lindquist (1995) and Shield & Shield (1998) tried to focus on the antecedents of participative budgeting so that may explain the association with the consequences of participatory budgeting, such as performance and satisfaction. Participation grows not only in the context of the determination of the budget but also the context of financial and nonfinancial performance measurement. Research by Sholihin, *et al.* (2011) developed the participation not only in financial goal setting as Wentzel (2002) did but also in non-financial goal setting. Results showed that participation in goal setting financial and non-financial goals affect commitment that mediated by perceptions of procedural fairness and trust.

2.4 Hypothesis Development

Hopwood (1972) initiated a study of performance evaluation by examining the role of accounting data in performance evaluation. In this case Hopwood (1972) reveals that superiors use accounting information that is considered as a source of formal information in evaluating the performance of subordinates. Performance evaluation system is developed not only consider financial or accounting information but also nonfinancial information as a measure of performance. It is reviewed by Franco-Santos, *et al.* (2012) by developing conceptual frameworks to understand the consequences of contemporary performance measurement systems comprising measurement of financial and nonfinancial performance and theories underlying these consequences.

Several previous studies have examined the effect of performance evaluation on the consequences of individual behavior of the measurement metrics used. Lau & Buckland (2001) examined the effect of performance measurements involving financial measures of employment pressure through trust and participation. The results of Lau & Buckland (2001) suggest that performance measurements that focus on financial measurement indirectly affect job pressures through trust and participation. Lau & Sholihin (2005) examined the effect of nonfinancial measures on job satisfaction through perceptions of justice and trust. An important result in Lau & Sholihin (2005) research is that nonfinancial performance measurement has an effect on job satisfaction which is not unlike the measurement of financial performance. Hall (2008) examines the effect of a comprehensive performance measurement system on performance through role clarity and psychological empowerment. This research underscores the role of cognitive and motivational mechanisms in explaining the effect of management accounting systems on managerial performance.

Hartmann & Slapnicar (2009, 2012) see performance evaluation not from performance measurement metrics but from performance evaluation process which in this case is level of formality of performance evaluation in organization and participation role of subordinate (voice). Hartmann & Slapnicar

(2009) examined the effect of the performance evaluation process, namely the level of formality, on trust through the perception of procedural fairness and quality of feedback. Hartmann & Slapnicar (2012) adds characteristics in the process of performance evaluation that is not only the level of formality, but also the participation of subordinates (voice). Both characteristics of the evaluation process are tested for influence on the perception of procedural fairness. The results of Hartmann & Slapnicar (2012) showed that in uncertain conditions, voice more significantly affect the procedural fairness.

This study suggests that a formal approach in performance evaluation will affect the perception of procedural fairness when subordinates are given the opportunity to participate in the performance evaluation process. Formality will help improve consistency, while voice is expected to improve accuracy in the performance evaluation process because of the belief that subordinates are better able to control the outcome of the process (Hartmann & Slapnicar, 2012). Langevin and Mendoza (2013) also argue that the opportunity to participate is a communication tool between subordinates and superiors that enable subordinates to exchange and seek information from superiors. Sharing of information in participation will improve the accuracy of the data used in the decision-making process. Therefore the hypothesis in this study is put forward as follows.

H1: formality affects procedural fairness perception

H2: participation in performance evaluation affect procedural fairness perception

3. Research Methods

The stages of this study include a preliminary study by conducting observations and focus group discussions with unit leaders to discuss the mechanics of performance evaluation to obtain a comprehensive overview of the performance evaluation process. The next pilot test is testing the research instrument that is in the form of questionnaires distributed to respondents who are not respondents' research. Pilot test is conducted with the purpose of testing the validity of the instrument and level of understanding of respondents related questions posed in the instrument. After the instrument testing process, the next step is

to collect the research data by distributing questionnaires to the respondents in accordance with the selected sampling method. The data obtained is processed and analyzed to obtain results that answer the research question.

This research was conducted by survey method by distributing questionnaires to University staff and lecturers. The reason for choosing survey method is due to two considerations. First, there is no public data archive of the constructs used in this study. Second, the study of fairness is usually regarded as a private secret, which requires that data collection be anonymous, this is easily achieved by survey methods (Hartmann & Slapnicar, 2009).

Research is conducted on a single organization for several reasons. First, focusing on one organization allows us to get very detailed data on both individual information and other qualitative information. In this case, this study may link the detailed data on the performance evaluation formalities of individual employees. Secondly, the university consists of 15 directorates and 10 study programs so as to provide the possibility of meaningful variation of research variables, let alone the research is done at the individual level.

3.1 Research Variables

Independent variables in the research are formality and participation. Variable formality of performance evaluation system is measured by using instrument developed by Hartmann & Slapnicar (2009). This instrument measures the performance evaluation system as a latent construct. The construct is developed into three distinct formalities sub-form as follows: 1) the formality of the target setting is measured using two items of question whether the setting target is made by the superintendent in written and quantitative form or otherwise, 2) the performance measurement formalities using two question items On how the employer performs a performance appraisal whether based on objective and quantitative information (more formal) or otherwise uses personal judgment and is qualitative (less formal), 3) rewarding formalities are measured by 4 items indicating the objectivity of reward determination. All of these instruments are expressed on a 5-point likert scale with

numerical scaling, which in this case is approaching 1 means less formal, and vice versa 5 means more formal.

Participation in performance evaluation is measured using instruments developed by Hartmann & Slapnicar (2012). Participation in this study is the extent to which individuals are allowed to play a role in setting goals, and actively providing feedback in the performance evaluation process. Three question items are developed that (1) ask whether the purpose of work is determined by considering the input of subordinates, (2) whether the supervisor judges the performance, notes the subordinate's explanation, and (3) whether when determining the work objective the supervisor considers factors that cannot be controlled.

Dependent variable in this research is procedural fairness measured by four items of question developed by Hartmann & Slapnicar (2009). Question items include the extent to which respondents believe that subsystems from target setting, performance measurement and rewarding, as well as the system as a whole, lead to the determination of a fair income.

3.2 Hypothesis Testing

Testing of hypotheses 1 and 2 is whether there is influence formalities of performance evaluation and participation to the perception of procedural fairness is done by using multiple regression analysis. To test each hypothesis is done by using t-test to determine whether there is influence linearly between independent variable and dependent variable. The value of t statistic test can be seen from the level of significance, if the level of significance is below the error rate of 0.05 or 5% then declared the independent variable affect the dependent variable.

The coefficient of determination is used to test the goodness-fit of the regression model (Ghozali, 2000). The coefficient of determination is between zero and one. The small value of R^2 means that the ability of independent variables to explain the variation of independent variables is very limited. A value close to one means the independent variables provide almost all the information needed to predict the variation of the dependent variable. The fundamental weakness of the use of the coefficient of determination is the bias

against the number of independent variables entered into the model. Each additional one independent variable, then the value of R^2 must increase regardless of whether the variable significantly affect the dependent variable or not. Therefore, many researchers recommend using an adjusted R^2 value when evaluating a regression model (Ghozali, 2000).

The F statistic test basically shows whether all the independent variables included in the model have a mutual influence on the dependent variable. The null hypothesis (H_0) to be tested is whether all parameters in the model are equal to zero, or: $H_0: \beta_1 = \beta_2 = \dots = \beta_k = 0$, meaning independent variables simultaneously have no significant effect on the dependent variable. $H_a: \beta_1 \beta_2 \dots \beta_k \neq 0$, meaning independent variables simultaneously have a significant influence on the dependent variable (Ghozali, 2000). The way that can be used to determine whether or not Rejected H_0 is to see the level of significance of the results of the F test. If the significance level test $F < (0.05)$, H_0 is rejected and H_a accepted. This means that the independent variable simultaneously has a statistically significant probability to the dependent variable.

4. Conclusion

The topic of performance evaluation system is still relevant to be studied more deeply by not only looking at performance measurement aspect but also performance evaluation process, which in this case related to how performance evaluation is done by superiors. This research aims to assess the perception of procedural fairness in the process of performance evaluation that can provide input to the top management of the organization to build a performance evaluation system framework that can improve the motivation, commitment and individual performance. This study is expected to contribute in performance measurement studies in different context.

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