COMPENSATION STRATEGY AND FINANCIAL PERFORMANCE OF COMMUNITY BANKS: AN EXPLORATORY STUDY

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Abstract

An exploratory study of 52 banks with assets between $100 million and $300 million was conducted to determine the usefulness of incentive compensation systems to this segment of the industry. It was found that incentive compensation plans may be more appropriate when specific circumstances face a bank. Variables most closely linked to the use of compensation plans were: (1) the strategic orientation of the bank, (2) unit or branch bank decision making, (3) the roles played by bank owners, and (4) slightly higher compensation per employee. Implications of the case study findings are discussed. Future directions of research are discussed.

Organizations of all types face the arduous task of developing a culture to achieve their desired goals and outcomes (Appelbaum & Shapiro, 1992; Bowen, 1993; McCormick & Rose, 1994; Rose, 1991). Research suggests that Incentive Compensation Plans (ICP) should improve employee motivation and, subsequently, bank performance in this environment (Bird, 1992; Cates, 1994; Fuehrer, 1994; Heneman, 1984; Heneman, 1992; Lawler, 1990; Marshall, 1993). Unfortunately, the influence of ICPs on financial performance, increased market share, or the motivation and retention of bank employees has been examined, but is largely unknown to date (Lawler, 1981, 1984, 1990).

The purpose of the present paper is to examine ICPs as they are used in organizations. This largely exploratory study of the use of ICPs in community banks addresses a number of issues, including the identification of the types of organizations that should install ICPs, identification of an appropriate business strategy-compensation plan match for organizations, the effects of separation of management from ownership, the effects of stock ownership by the Chair, and the relationship between the ICPs and monitoring costs.

Incentive Compensation

One of the primary approaches to motivating employees is through compensation. While motivating employees may be difficult, the structure of an organization should be congruent with the business strategy of the organization, if it is to meet its goals (Carroll, 1987; Heneman, 1992). Additionally, compensation plans should support and reinforce the business objectives and the behaviors that are needed for the business to be successful (Lawler, 1990).

Support for these statements has been established through a variety of research findings. First, in a summary of studies evaluating merit-pay plans, Heneman (1984) generally found that a positive relationship existed between motivation, performance, and satisfaction relative to the pay-performance relationship, when rewards were contingent upon performance. Taking this idea a step further, given different organizational strategies, the key is to align a compensation plan with the overall strategy of the organization (Lawler, 1990) Given these results and guidelines, the strategies of organizations should influence which compensation plans are adopted. The following section of this paper specifically examines the relationship between the business strategy and characteristics of banks and their use of ICPs. Additionally, the effects of both the business strategy and the use of ICPs will be examined to determine their influence on organizational performance.

Influences on Banking Compensation Methods

A considerable amount of literature focusing on compensation indicates that the environment, strategy, industry structure, management structure, task performance and reward systems pose difficulties to organizations in general (Barkema & Gomez-Mejia, 1998; Conhyon & Peck, 1998; Finkelstein & Boyd, 1998; Gomez-Mejia & Wiseman, 1997). This paper assumes that the banking industry faces these same difficulties. In this section we provide an overview of each of these factors as they relate to banking offering hypotheses.

Banking Environment

The nature, or causal texture (Emery & Trist, 1965) of an organization's environment results from the interaction of two dimensions: (1) environmental change, which ranges from stable to dynamic, and (2) environmental complexity, which ranges from simple to complex (Duncan, 1972). It is not actual uncertainty, but the perception of environmental uncertainty which affects managers' decisions (Milliken, 1987). Environmental uncertainty influences compensation through the costs of sharing risk and gathering information (Eisenhardt, 1988). Finally, environmental conditions have been found to influence managerial activities, leading to higher CEO salaries (Finkelstein & Boyd, 1998). This might also influence the salaries of other employees.

Jobs which are "programmable," that is, simple and repetitious, allow for clear performance standards and easy monitoring. Jobs having relatively low levels of programmability require greater use of performance-contingent compensation due

to the increased monitoring costs needed to evaluate employees. Evidence exists that firms operating in highly volatile, uncertain environments pay higher compensation rates per full-time equivalent employee (FTE) than do other firms to compensate for a perceived increase in discretion and risk (Eisenhardt, 1988, 1989; Gerhart, Minkoff & Olsen, 1995; Kren & Kerr, 1993; Rajagopalan & Finkelstein, 1992). The purpose of increased compensation is to motivate employees to take the risks necessary to successfully perform their jobs (Gerhart, Minkoff & Olsen, 1995). We propose that bank officers would follow a similar pattern. Therefore, the following hypothesis is proposed:

> Hypothesis 1: *Salaries per FTE in banks where officers perceive a high degree of environmental uncertainty are significantly higher than those banks where officers do not perceive a high level of environmental uncertainty.*

Strategy

Miles and Snow (1978) place firms in four strategic categories.

- Prospectors aggressively seek growth opportunities through product and market development and innovation.
- Defenders work to improve operational efficiency and seldom need to adjust their technology, structure, or methods of operation.
- Analyzers normally operate in two product-market domains. One domain is a stable circumstance where analyzers operate routinely and efficiently through the use of formalized structures and processes. The other domain is a rapidly changing environment where managers watch competitors closely, adopting those ideas which appear promising.
- Reactors adjust structure and processes only when environmental pressure forces them to act.

It has been suggested that specific corporate strategies and compensation strategies fit best together (Finkelstein & Boyd, 1998; Gerhart, Minkoff & Olsen, 1995). Building on the work of Miles and Snow (1978), Rajagopalan and Finkelstein (1992) have found that Prospector firms in the electric utility industry paid employees significantly more than Defenders or Reactors and made greater use of outcome-based compensation plans. As the level of environmental uncertainty increased, similar firms adopted outcome-based compensation plans, paid a greater proportion of outcome-based cash compensation, and paid managers more. The aggressive sales and service culture U.S. bank presidents wish to foster in their institutions would suggest those particular banks would be categorized as Prospectors (Miles & Snow, 1978). Prospector banks should exhibit asset growth rates greater than those of Defenders, Analyzers, and Reactors. Finally, the aggressive nature of Prospector banks would suggest higher financial performance, measured by better Return on Assets (ROA) than banks employing other strategic options. Thus, the following hypothesis is proposed:

Hypothesis 2: *Compensation per FTE in banks characterized as Prospectors is significantly higher than compensation per FTE in banks characterized as Defenders, Analyzers, or Reactors.*

Banking Structure

Firms may respond to complexities in the environment, however financial performance and the ability to pay may be influenced by industry level issues (Finkelstein & Boyd, 1998; Gomez-Mejia & Wiseman, 1997). Additionally, evidence exists that firms operating in highly volatile, uncertain environments pay higher compensation rates per FTE than do firms in more stable environments (Kren & Kerr, 1993). To complete successfully in the volatile banking industry, the sales and service culture fostered in branch banking by management, is designed to increase deposits and loans, generate more fee income and provide perceived quality service. Incentive compensation plans developed for branch banks reward employees for those deliverables. The higher salary may be used to compensate for increased discretion and risk assumed in turbulent environments (Eisenhardt, 1988; Kren & Kerr, 1993; Rajagopalan & Finkelstein, 1992). Therefore, it is expected that salaries would be higher in branched banks as opposed to unit banks because of the more unstable environment. Given this circumstance, the following hypothesis is proposed:

Hypothesis 3: *Compensation per FTE in branch banks having ICPs is significantly higher than compensation per FTE in unit banks having such systems.*

Management Structure

The Bank Holding Company Act of 1956, a regulation of the Federal Reserve, defines three categories of ownership when filing regulatory applications: Less than 10% denotes absence of control, 10% to 25% is categorized as a "presumption of control," and over 25% denotes the ability to direct or control the management of an institution. From this perspective, management structure in banks can be defined in terms of the Chair-CEO relationships. Pi and Timme (1993) have found that banks where the Chair was also the CEO performed worse in terms of cost efficiency and profitability than those banks where the Chair was not the CEO. In banks where the Chair was the CEO, there was no relationship between bank performance and percent of stock ownership of the Chair. The level of bank performance in either case was unrelated to the level of stock ownership of the Chair.

Stock options or ownership are a commonly used long-term incentive in compensation of executives (Gomez-Mejia, Paulin, & Grabke, 1995). Rose (1992), from a study involving 6,400 small community banks, determined that as the Chair's stock ownership percentage increases, bank expenses tend to increase

while profits decline. As the Chair's portion decreases, non-interest expenses decline and employee productivity increases. This could be the result of owner-managers selecting financial performance goals that maximize shareholder wealth while banks isolating the Chair from CEO select goals that emphasize growth.

The effects of owner-manager structures on the operation of the bank in terms of efficiency, profitability, and reward system selection also have been analyzed. (Berger, Hunter, & Timme, 1993; Pi & Timme, 1993). Banks where the Chair is also CEO have lower efficiency due to increased operating expenses than do banks where these two roles are separate. Since salaries and benefits can constitute nearly one-half the expenses of a bank, the implications for the effects of owner-managers are twofold. Salaries may be higher because of the expense-preference behavior of the Chair or the Chair's ability to exert social influence on the board in a manner that increases his or her compensation (Belliveau, O'Reilly, & Wade, 1996). Alternatively, as stock ownership increases, other expense preference behaviors may become more important than salaries. Pi and Timme (1993) found that ROA's of banks having owner-managers were less than banks having separation of these roles. As a result of these findings, the following hypothesis is proposed:

> Hypothesis 4: *Overhead efficiency ratios and ROA for owner-manager banks having ICPs are significantly lower than those separate owner-manager banks having ICPs.*

Task Performance

Task performance refers to the manner in which jobs are performed (Katz & Kahn, 1978; Motowidlo & Van Scotter, 1994) and to two classes of behavior (Borman & Motowidlo, 1993). The two behaviors include the execution of the organization's technical processes and the activities which maintain and service the institution's technical requirements. Caruth (1984) studied banking jobs and found they were not amenable to the use of ICPs (Finkelstein & Boyd, 1999; Rajagopalan & Finkelstein, 1992). Jobs in banking were believed to be knowledge intensive, requiring a high degree of individual discretion not amenable to management control. Additionally, Austin & Simoff (1990) found that high performance in a high discretion job requires individual commitment and motivation. They conclude that in banking, tellers actually exercise lower levels of discretion than the officers, which exercise the highest levels of discretion. This might indicate that discretion varies across jobs in banking, and some jobs may be conducive to ICPs. Bettinger (1986), in a study of ICPs in banks, has found customer jobs and knowledge jobs to be the highest in discretion.

Sherwood (1994) has found the measurement of sales and marketing success in the banking industry to be difficult due to the bundled services offered to the consumer. Rewards must be related directly to outcome to achieve the desired performance (Lawler, 1981, 1984, 1990). Therefore, one could assume that bank

managers perceiving a high level of task performance and skill level among their employees would utilize ICPs to link behaviors to outcomes. Thus, the following hypothesis is proposed:

> Hypothesis 5: *Managerial perceptions of the skill level and task performance attributes of employees in cross selling bank products in banks having ICPs is significantly higher than management perceptions of the skill level and task performance of that group of employees in banks not having ICPs.*

Reward Systems

Schuster and Zingheim (1986) studied high-performing banks that utilized goals, budgets, and forecasts to measure the progress of task performance. Certain design elements were found among the best: (1) eligibility — there was an ability to identify yardsticks that measure variations in performance; (2) participation — the plan extended through much of the organization; (3) incentives — the plans were used to achieve competitive pay levels and functioned as tools for recognition of performance; (4) emphasis — the plans tied the employees' financial interest to the organization's success; (5) objectives — forecasts, goals, and budgets were used to judge progress and whether cash compensation should be paid; and (6) timeliness — performance periods coincided with the accomplishment of tasks and attainment of goals. Incentive compensation plans are not only designed to increase organizational performance, but they have been found to increase the performance of employees (Appelbaum & Shapiro, 1992; Finkelstein & Boyd, 1998; Gomez-Mejia & Balkin, 1989; Rajagopalan & Finkelstein, 1992). Since ICPs are intended to motivate employees to higher levels of performance with a corresponding increase in compensation, there should be higher compensation levels per FTEs observed in banks using ICPs.

> Hypothesis 6a: *Financial performance of banks having ICPs is significantly higher than banks not having such plans.*

> Hypothesis 6b: *Total salary expenses per FTE in banks having ICPs is significantly higher than salary expense per FTE in banks not utilizing such plans.*

The purpose of the present paper is to explore if an appropriate match between strategic orientation and compensation strategy might exist in the banking industry. This will be investigated by testing the hypotheses presented in this section of this paper. In the next section of this paper, the methods use to test the hypotheses will be presented.

Method

Sample and Procedures

The FDIC stratifies banks into peer groups for financial analysis purposes. The FDIC uses financial data to analyze banks during examinations to determine how they perform relative to others. Also, would be investors (individuals and other banks/bank holding companies) can access that information through publishing services to analyze the banks as potential investments or acquisitions. One of the peer groups consists of banks having assets between $100 million and $300 million, comprising a small percentage of the total number of U.S. banks, since 80% of those banks are less than $100 million (Rose, 1992). This group represents a specific peer group for analytical comparisons by the Federal Deposit Insurance Corporation, and are not considered "large" banks.

Banks are considered "large" by regulators once they reach an asset level of $500 million (Rose, 1992). Once at this level, these banks have strict internal control and risk management requirements placed on them. Appropriate management structure should be in place when that level is reached.

Several important challenges arise along the growth wave between $100 million and $300 million in assets. An increased reliance on automation and technology occurs as marketing strategies strive to deliver banking products and services in the new sales and service culture being fostered in banks today. Incentive compensation plans are being developed to support this new culture. These banks have the capital structure in place to support increased investments in data processing equipment that the smaller banks lack. Also, new products are needed to attract and retain customers, requiring more professional type employees in the areas of lending, audit and governmental compliance to manage the growth of these banks. Finally, this particular segment of banking faces a unique dilemma compared to banks with fewer or greater assets. Banks with fewer assets may not have the ability to use ICPs, given their lack of resources. Banks with greater assets have the financial resources to pursue this type of compensation plan. However, banks in this range face a more critical question when considering implementing ICPs, making this group of special interest.

Surveys (see Appendix) were mailed to the presidents of 186 banks with assets between $100 million and $300 million. The surveys were mailed to all banks in a Southwestern state meeting this criteria. Of the surveys returned, 52 were usable, representing a response rate of 28 percent. A response rate of 28 percent is slightly higher than the normal rate of 19 percent for research targeting CEOs or Presidents of firms (Barker & Patterson, 1996; Stimpert & Duhaime, 1995). In addition to the surveys, banking structure information was obtained from the Uniform Bank Performance Report (UBPR) data.

The average assets of the responding banks were $163,876,000, with an average compensation per FTE of $32,725. Average overhead efficiency of the sample

was 64 percent. The average ROA was 1.32 percent, while the asset growth rates averaged 6.92 percent.

Measures

This survey was designed to obtain information from each bank president in the areas of perception of environmental uncertainty, strategic orientation, owner-manager data and stock ownership, perceptions of skill level, and reward system selection factors, including whether an incentive compensation plan was used. Each survey question and what measurements of interest were needed for analysis are discussed below.

Perception of environmental uncertainty. Duncan (1972) suggests that there are five components of environmental uncertainty; competitors, customers, suppliers, regulatory groups, and technology requirements of the industry. The bank presidents were asked to rate their perception of their level of uncertainty associated with these 5 factors in predicting the influence of each component on their bank by choosing among six measures with "1" being very unpredictable to "6" being strongly predictable.

Strategic orientation. Determination of strategic orientation was obtained by analyzing the bank president's responses to questions about their bank's competitive strategy, which included 5 areas of bank strategy: market penetration, market innovation, technological innovation, efficiency strategies, and domain expansion strategies. The bank presidents rated each measure by choosing their level of agreement or disagreement with each question. Responses ranged from "1" being strongly disagree to "6" being strongly agree. Following the methodology of Rajagopalan and Finkelstein, (1992) banks were grouped into 1 of 4 strategic orientations. Based on the systematic responses to these questions, strategic orientation was identified as being Prospectors, Defenders, Analyzers, or Reactors.

Effects of owner-managers. Bank presidents were asked to specify if their bank had a majority shareholder who acted as the Chair and CEO or if those two roles were separate. Next, the question asked for the Chair's level of stock ownership. Three choices were given: less than 10% (no control); between 10% and 25% (presumed control); over 25% (controlling shareholder).

Skill level. Bank presidents were asked to indicate agreement or disagreement with questions regarding their perceptions of employee performance and skill level, monitoring information, and the influence of pay practices on employee retention, attraction, and motivation. Perceptions could range from "1" being strongly disagree to "6" being strongly agree.

Reward system selection. A final group of items sought to determine the degree to which bank presidents considered employees' feelings and preferences for reward system selection and if job, skill, or timed based factors entered in the compensation practices. Incentive compensation plan usage was assessed by the last part of the question. Responses ranged from "1" being strongly disagree to "6" being strongly agree.

Analyses

Analysis of variance (ANOVA) was utilized to test for the significant differences in those hypotheses where differences between two or more groups were expected (Hypotheses 1, 2, 3, 4, 5, 6a and 6b). Additionally, T-tests were conducted on Hypotheses 2 to determine which strategic orientations may result in significant differences in levels of compensation per FTE and asset growth rate. The t-tests were conducted assuming that the variances were not equal, which is more conservative than assuming that the variances are equal. This technique was conducted since the number of observations present in each strategic orientation compared were not equal. Multiple regression was used to test the hypotheses in which multiple variables were expected to influence either overall compensation (H1) or ROA (H6b). Financial performance data used to test the hypotheses included: (1) ROA, (2) compensation per FTE, (3) total assets, (4) deposits per FTE, (5) asset growth rates, and (6) overhead efficiency ratios. Banking regulators and investors utilize these measures to compare a subject bank to its peer group and to evaluate the bank from a safety and soundness standard. Finally, because of the exploratory nature of this study, nonparametric analyses will be conducted as an additional test of several of the hypotheses. These analyses further address the small sample size and the ordinal nature of some of the measures associated with this study (Allen & Yen, 1979).

Results

Greater levels of environmental uncertainty were not associated with higher levels of compensation per FTE ($F=.19$, $p=.83$, $DF=51$), thus H1 was not supported. While the ANOVA results clearly did not reach significance, a Mann-Whitney test on the effects of environmental uncertainty on compensation reached significance ($W=1378$, $p=.00$, $DF=51$). Additionally, the regression results approached significance ($F=2.38$, $p=.08$; $DF=51$). These results indicate that a bank's assets, deposits and the uncertainty of the environment facing these institutions could explain a significant portion of the compensation provided at banking institutions, given a larger sample size.

ANOVA results indicated no differences in compensation by strategic orientation ($F=1.95$, $p=.13$, $DF=51$). However, comparisons among mean compensation levels of the different strategic orientations revealed that Analyzers received significantly higher compensation than Prospectors ($T=2.37$, $p=.03$, $DF=14$) and significantly higher than Defenders ($T=2.39$, $p=.01$, $DF=21$). Additionally, Mann-Whitney tests further supported the significant difference between Analyzers and Defenders ($W=215$, $p=.03$, $DF=21$) (Table 1). This provides some support for H2, indicating that strategic orientation of a bank may influence compensation levels of employees.

Table 1
Employee Compensation by Strategic Orientation

Performance Indicator	Prospector n=13	Defender n=20	Analyzer n=3	Reactor n=16
Compensation per FTE p=.13; F=1.95; DF=51	$32,696	$32,675	$39,797	$32,736

H3, that differences in compensation between branched and unit banks existed from the use of an ICP, received mixed support. The results of ANOVA (F=.72, p=.41, DF=25) indicate that banks using ICPs do not significantly vary based upon whether or not the bank is a unit or branched bank. Mann-Whitney test results, however, indicate that compensation at branched banks using ICPs was significantly higher than unit banks using ICPs (W=351, p=.00, DF=25). This provides partial support for Hypothesis 3.

H4, that differences in overhead efficiency and ROA existed due to management structure and the use of an ICP, demonstrated mixed results. Banks managed by owner-managers were significantly less efficient (F= -4.33, p=.05, DF=25) than banks which had separate owner-managers, supporting H4. Additionally, Mann-Whitney tests results further supported this finding, with banks having owner-managers being less efficient than banks having separate owner-managers (W=4082, p=.00, DF=25). Overhead efficiency was 71.83% for the owner-manager group and 61.70% for separate owner-manager banks. However, the ROA measures did not indicate a significant difference (F=2.70, p=.20, DF=25). As a result, Hypothesis 4 received partial support.

H5, that perceptions of the skill level and task performance attributes in banks having ICPs is higher than in banks not having ICPs, failed to receive support (F=.01, p=.90, DF=51). This might indicate that the implementation of ICPs in community banks may not influence the perception of employee skill level. Alternatively, this might indicate that banks in the asset range studied may not consider the perception of employee skill level when implementing ICPS.

ICP presence in banks was not found to significantly influence either the financial performance of the banks or the total salary expenses of the banks, thus hypotheses 6a and 6b were not supported. However, the results of the multiple regression indicated that assets, overhead efficiency, deposits per full time equivalent employee, and the use of an ICP explain a significant amount of the variance of the ROA, with overhead efficiency and deposits per FTE each reaching significance. The regression was run on the sample banks. Overhead efficiency and deposits per FTE were each found to be significant predictors of ROA. Additionally, the independent variables explained 78.3 percent of the variance in ROA, with P-value for the model of 0.000 (Table 2). The correlation between use of ICP and overhead efficiency was .06, ensuring that these items were not measuring the same concept.

Table 2
Regression of ROA for Community Banks

Variable	Regression Weight	T ratio	P value
Assets	-.000000	-0.26	.798
Overhead Efficiency	-.0442	-12.63	.000
Deposits per FTE	-.000458	-5.15	.000
Use of ICP	-.0188	-.22	.831
r2	78.3%		
Adjusted r2	76.5%		
F statistic	42.5		
P value	.000		
N 52			

Discussion

The present case study examined the effects of strategic orientation and ICPs on the financial performance of community banks as well as the conditions under which ICPs were most effective in influencing the financial performance of these same institutions. The results of this study provides insights into the effectiveness of strategic orientation and ICPs as they pertain to banking industry.

While the ANOVA results showed no significant relationship between compensation and level of environmental uncertainty, the Mann-Whitney test results were significant (p=.00), providing some support for Hypothesis 1. Additionally, the multiple regression results approached significance, resulting in a p-value of 0.08 for the model. The combination of assets, deposits and environmental uncertainty could explain a significant portion of the variance in salaries of bank employees, as deposits significantly influenced the salaries. This is a finding which can be considered consistent with previous findings (Eisenhardt, 1988; Kren & Kerr, 1993). In each of these studies, environmental uncertainty was linked to increased compensation. The present results seem to suggest that environmental uncertainty might lead to higher levels of compensation in the banking industry as well.

The results of the exploratory case study are interesting for a variety of reasons. First, while community banks are quite different from the retail sales companies in the Eisenhardt (1988) study, it does appear that compensation may be influenced by a variety of factors beyond the control of the organization. In the retail sales study, programmability of the job, supervisor span of control, uncertainty, type of merchandise, and age of the store chain were strong predictors of compensation policy. Not all these factors may apply to jobs and employees in the banking industry, and those factors which are present may systematically differ from those in the retail industry. Eisenhardt (1988) found that where retail job programmability was low, there was a greater use of salary and commission pay

systems to offset the influence of uncertainty. As programmability of the job increased, variation in uncertainty resulted in greater use of salary plans, having no effect on overall compensation because job programmability was found to increase the organization's monitoring ability. Even though job programmability in banking is high, the bank presidents surveyed indicated that their bank's monitoring information was not timely or available, and this information was not reliable to adequately evaluate their employees. Thus, a lack of monitoring information available to evaluate employees having highly programmable jobs and the decision to use ICPs in situations better suited for straight salary may contribute to the inconsistent results.

Second, a difference between the retail and banking studies is that in the banking study, the "merchandise" is service and the product is fairly uniform throughout the banking industry. Customers can go to virtually any bank and receive similar products or services. Any differences in preferences could be based upon the quality of service and location as opposed to the variety available in retail establishments. Retail establishments encompass a wide variety of stores, ranging from specialty merchandise, to major appliances, to department stores. As a result, depending on the product, a variety of outlets exists.

While compensation per FTE did not systematically vary based on the strategic orientation of the bank, the salaries associated with Analyzer firms were considerably higher than the salaries associated with the other orientations, and reached significance in two of the three cases. Compensation per FTE was consistently about $7,000 higher in banks classified as Analyzers. This might indicate that Analyzers, given the nature of this type of strategic orientation, were more effective at studying the market. This may have led to higher profits, which were then shared with the employees. Given the very small number of degrees of freedom, these results might consistently reach significance if a larger sample were analyzed. The trends found in the results suggest that strategic orientation may influence employee compensation, consistent with the suggestions made previously by Gerhart, Minkoff, and Olsen (1995).

Banking structure might influence the effectiveness of ICPs at increasing compensation levels of employees. The results, while mixed, seem to suggest that employees of branched banks are compensated at higher levels. This might indicate that this type of bank is more profitable, or it could compensate for increased discretion and risk associated with the volatile environments that banks face, as others have suggested (Eisenhardt, 1988; Kren & Kerr, 1993; Rajagopalan & Finkelstein, 1992).

Management structure was found to influence the overhead efficiency of the organization. This may indicate that bank performance is influenced by management structure, providing further support that owner-managers may exert influence on the institution's board in a way that increases his or her compensation (Belliveau, O'Reilly, & Wade, 1996). Additionally, holding the position of owner-manager may influence the individual to maximize shareholder wealth. This strat-

egy could be very different from the strategy selected when the Chair and CEO are separated, where growth is emphasized (Rose, 1992). As a result, it may not only be that overhead efficiency is influenced, but that compensation strategy and strategic orientation of the bank might also be influenced as a result of the management structure.

The final finding, which lends some preliminary support for matching appropriate compensation techniques with the circumstances facing a bank, concerns the multiple regression results associated with testing H6a and H6b. The model predicting ROA was found to be significant. Assets of the bank, overhead efficiency, deposits per FTE and the use of an ICP were the predictor variables, with overhead efficiency and deposits per FTE reaching levels of significance. While in none of these cases was the use of ICP found to be a significant variable, overhead efficiency was found to be significant. Nonetheless, the combination of these variables did explain a significant amount of the variance of the ROA for the banks in this sample. This seems to indicate that the role of ICPs might influence ROA when coupled with overhead efficiency or deposits per FTE.

Given the nature of the case study, the findings do provide some insight and encouraging support concerning the appropriate match of compensation strategy with strategic orientation for organizations. Several steps could be taken to expand on the findings of this case study. First, a larger sample size could further reveal if ideal matches between compensation strategy and strategic orientation exist, enhancing the performance of organizations and their human resources. Many of the results are believed to be diminished because of the small sample size.

A second step which could further provide information about the appropriate match between compensation strategy and strategic orientation would be to gather a more diverse sample of organizations. A more diverse sample would allow for the comparison among types of organizations. It could be the case that matching compensation strategy with the strategic orientation of the firm is more effective in some types of organizations than in others. A more diverse sample would allow for the testing of these differences.

Finally, a closer examination of the interrelationships among management structure, compensation strategy and strategic orientation should be conducted. Understanding these relationships could further reveal information about which circumstances contribute to a more effective match between compensation strategy and strategic orientation. It is very possible that the management structure itself may influence the effectiveness and appropriateness of both the strategic orientation of an organization as well as the proper compensation strategy for the combination of strategic orientation and management structure.

The present case study provides preliminary evidence that appropriate matches between strategic orientation and compensation strategy may lead to increased firm and human resource performance. Scholars and practitioners alike should carefully examine the environment, conditions surrounding an organization and

the strategic orientation before selecting a compensation strategy. When the final decision is made regarding the compensation strategy, the strategy selected should complement the strategic orientation in a way that supports the pursuit of the strategic orientation.

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Appendix
SURVEY QUESTIONS

1. The following environmental factors (customers, suppliers, competitors, regulatory burden, and technological advances) can have dramatic influences on the way you manager your bank. By using the sliding scale below, please circle the numbered response to the right of each environmental factor that best describes your level of uncertainty in predicting the influence of each on your bank:

1= Very Unpredictable 2= Unpredictable 3= Somewhat Unpredictable
4= Somewhat Predictable 5= Predictable 6= Strongly Predictable

a. Customers 1 2 3 4 5 6
b. Suppliers 1 2 3 4 5 6
c. Competitors 1 2 3 4 5 6
d. Regulatory burden 1 2 3 4 5 6
e. Technological Advances 1 2 3 4 5 6

2. Think a moment about your bank's competitive strategy. Please circle the numbered response for each strategy which best describes your agreement with each by using the following scale:

1= Strongly Disagree 2= Disagree 3= Somewhat Disagree
4= Somewhat Agree 5= Agree 6= Strongly Agree

a. Market Penetration Strategies
My bank's strategy emphasizes cautious penetration and development of existing markets through following the lead of my competitors 1 2 3 4 5 6

b. Market Innovation Strategies
My bank's strategy seeks to develop new markets and products through aggressive, innovative marketing and product development 1 2 3 4 5 6

c. Technological Innovation Strategies
My bank's strategy emphasizes improved information and customer service through investment in the most up to date technology 1 2 3 4 5 6

d. Efficiency-orientation Strategies
My bank's strategy seeks to improve the efficiency of existing operations through cost-cutting measures and productivity improvements 1 2 3 4 5 6

e. Domain Expansion Strategies
My bank's strategy seeks to develop new product markets through mergers and acquisition and geographical expansion 1 2 3 4 5 6

3a. The following statements may apply to how your bank's management is organized and how central decision making is handled. Please circle the response which best describes how your bank is organized.

My bank has a separate Chairman and Separate CEO ..... YES NO
At my bank, the Chairman and the CEO are the same individual ..... YES NO

3b. The amount of stock the chairman owns of your bank or your bank's parent holding company is: (please circle the response 1, 2, or 3 below which best describes your chairman's ownership)

1 = Less than 10% 2 = 10% or more but less than 25% 3 = More than 25%

4. The following statements address the availability and reliability of information which can be used to evaluate employees. Also addressed are your perceived performance of employees and the perceived effects of pay on employees. Circle the numbered response factor which best describes your agreement with each by using the following scale:

1= Strongly Disagree 2= Disagree 3= Somewhat Disagree
4= Somewhat Agree 5= Agree 6= Strongly Agree

a. The reliability of informational reports provides enough information for the evaluation of the performance of my bank's tellers and new accounts employees in the areas of cross-selling banking services 1 2 3 4 5 6

b. The availability of informational reports is adequate for the evaluation of the performance of my bank's tellers and new account employees in the area of cross-selling banking services 1 2 3 4 5 6

c. As bank president, the perceived performance of my bank's tellers and new accounts employees in the area of cross-selling bank products and services is high relative to those of my competitors 1 2 3 4 5 6

d. In my bank's experience over the past three years, the pay policies and practices have greatly contributed to retention, attraction, and motivation of employees 1 2 3 4 5 6

5a. My bank has chosen its compensation system to provide the utmost in motivating employees and contributing to their retention. Please rate the following statements for your level of agreement or disagreement with each by circling the number to the right of each statement. Use the following scale for your response:

1= Strongly Disagree 2= Disagree 3= Somewhat Disagree
4= Somewhat Agree 5= Agree 6= Strongly Agree

i) Employee feelings and preferences for various pay forms are taken seriously by management 1 2 3 4 5 6
ii) Factors within the job are key determinants of the amount of pay 1 2 3 4 5 6
iii) Individuals are rewarded in part for their mastery of job skills 1 2 3 4 5 6
iv) Pay is based solely on how long the employee has held the job 1 2 3 4 5 6

5b. My bank uses an incentive type of compensation system:
(please circle your response) ..... YES NO

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