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The Relationship between Perceptions of Due Process and Satisfaction with a Merit Pay System

For the degree of Master of Science

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THE RELATIONSHIP BETWEEN PERCEPTIONS OF DUE PROCESS AND
SATISFACTION WITH A MERIT PAY SYSTEM

A Thesis

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of

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by

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ABSTRACT

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Organizations continuously look to improve the implementation and ultimate success of organizational change. One way to facilitate organizational change is to effectively manage employee reactions to that change. Previous research has examined the use of a due process approach, specifically in relation to the performance appraisal systems. Past results have indicated that meeting the due process criteria for adequate notice, fair hearing and judgment based on evidence positively influences employee perceptions of the performance appraisal system, organizational justice, and other key variables. The current study expands on these findings by applying the due process approach to the implementation of a merit pay system. With the main goals of a merit pay system being to retain and motivate employees, successful implementation is key. The current study measured perceptions of due process over three measurement periods during the implementation of a new merit pay system. Results demonstrated that the due process components are meaningful in the implementation of a merit pay system. Perceptions of due process predicted system satisfaction and organizational justice perceptions both within and across measurement time periods.

INTRODUCTION

Implementing change or setting up a new process within an organization is a challenging endeavor. The overall goal of any organizational change is to ensure that it is supported by employees within the organization, that it is successful, and that ultimately it leads to greater organizational effectiveness and success. When implementing change, organizations need to consider what has brought about the need to change, what type of change is necessary, when is an appropriate time or timeframe to make the change, what process or procedure is needed to implement the change, and perhaps most importantly, how to manage employee reactions to that change. The acceptance of change and resulting benefits are influenced by dissatisfaction with the current practice, the existence of a viable alternative, and a plan to put the alternative into practice (Greenburg, 1999). Jick (1993) concluded, "if the reactions to change are not anticipated--and managed--the change process will be needlessly painful and perhaps be unsuccessful" (p.6). These reactions must be considered during the planning and implementation phase of a change process in order to be anticipated and managed. The current study examines one approach to successfully managing employee reactions, namely due process. The longitudinal relationship between perceptions of due process and employee reactions to the implementation of a new merit pay system are examined.

LITERATURE REVIEW

Merit Pay

There are many different pay systems that an organization can choose to implement. Typically organizations choose to either pay for the job or pay for the performance of the person in the job. Traditional pay systems have focused on the job, paying for the responsibilities associated with the position and seniority therein (Heneman & Gresham, 1998). Even some organizations that claim to offer pay for performance really reward based on seniority (Lawler, 1990). However, by rewarding employees based on position or seniority, organizations could send the wrong message that monetary rewards are not related to performance (Nelson, 1994). A shift in pay strategies has led to more pay systems based on individual performance.

In organizations today, performance-based pay plans receive more attention than traditional job based pay plans and can include piece-rate, standard hour plan or merit pay at an individual or team level(Heneman & Gresham, 1998). One popular pay for performance plan, merit pay, remains the most widely used incentive plan linked to individual performance (Schaubroeck, Shaw, Duffy & Mitra, 2008). The rationale behind pay for performance, and the reason for its popularity, is the notion that it will lead to increased job performance and organizational effectiveness (Lawler & Jenkins,

1992). Merit pay focuses on recognizing individual contributions to an organization, not compensating based on the position alone. Thus, employees performing the same job can be compensated differently based on their performance evaluations. Unlike some pay plans that provide a one-time bonus pay out, merit pay is a percentage increase that is added to base pay as a result of an annual performance appraisal (Lawler, 1990). The intent is to provide a clear link between individual performance and pay in the minds of employees. In a merit pay system, pay allocation is based on individual contribution rather than job position, time with the organization or favoritism.

A goal inherent to the implementation of a merit pay system is motivating employees to do their best work by recognizing and rewarding desired behavior to increase organizational effectiveness. Unfortunately, Rynes, Gerhart and Parks (2005) cite a lack of research demonstrating the relationship between merit pay systems and organizational effectiveness. Although this seems intuitive, some evidence has suggested that merit pay systems do not help companies to position themselves in a competitive marketplace or encourage excellence among employees (Schuster & Zingheim, 1992). Given that the relationship between merit pay and subsequent individual performance does not appear to be consistently strong (Heneman, 1990), a focus must be placed on mechanisms to ensure successful implementation of these systems. In attempting to maximize the influence on organizational success, it is key to implement a pay system that is viewed positively and supported within the organization. It is through better implementation of pay system procedures that organizations can hope to mitigate other factors that may negatively influence success of the system.

One key aspect of successful implementation is positively managing each employee's reactions toward the change (Jick, 1993). As discussed earlier, how a pay system is implemented influences employee perceptions and ultimately system effectiveness. In other words, if employee reactions and responses to this change can be positively managed, there is increased potential for the change to result in positive organizational outcomes. "Perceptions very much influence the ability of a pay plan to reinforce a particular culture, to motivate performance, and to attract and retain individuals" (Lawler, 1990, p. 221). Siegall and Worth (2001) examined employee reactions to merit pay systems and found that negative employee reactions, mainly lack of trust in the administration, could result in the failure of the system. Trust in top management has been found to have a strong positive relationship with establishing the link between pay and performance (Vest, M., Scott, Vest, J. & Markham, 2000). In particular, Siegall and Worth (2001) found a strong relationship between trust and perceived fairness of the system. Individuals who did not trust the merit pay system reported less cooperation, less motivation to work hard, and lower morale (Siegall & Worth, 2001). Research has suggested that ensuring high levels of justice, due process in particular, may contribute positively to such a change effort, in part through helping organizations effectively manage employee reactions (Folger, Konovsky & Cropanzano, 1992; Taylor, Tracy, Renard, Harrison & Carroll, 1995).

Organizational Justice

Organizational justice refers to perceptions regarding the fairness of procedures, outcomes, and treatment that employees have throughout their interaction with their organization. Organizational justice can be broken into three components: distributive, procedural and interactional (Cohen-Charash & Spector, 2001). Organizational justice research began with a focus on distributive justice, achieving fairness of allocation outcomes through Adams' (1965) equity theory. Adams (1965) suggested that fairness perceptions could be measured by assessing the ratio of inputs versus outputs as compared to relevant others. Research then expanded to include procedural justice, the perception of fairness of the process by which outcomes were determined, not just the outcomes themselves (Lind & Tyler, 1988). In 1980, Leventhal presented six criteria that need to be met in order for a process to be perceived as fair: consistent, free of bias, accurate, correctable, representative of relevant stakeholders, and ethically moral. More recently a third form of organizational justice was introduced, interactional justice (Bies & Moag, 1986). This pertains to the fairness of the treatment an individual receives when organizational procedures are implemented and outcomes distributed (Bies & Moag, 1986). Some suggest interactional justice can actually be broken further into interpersonal and informational justice resulting in a four-factor definition of organizational justice (Colquitt, Conlon, Wesson, Porter & Ng, 2001; Greenberg, 1993). However, for the purposes of this study, focus will remain on procedural, distributive and interactional justice components.

Previous research has shown that organizational justice perceptions have a positive relationship with a variety of outcomes in different areas including performance

appraisal (Cawley, Keeping & Levy, 1998; Cropanzano, Bowen & Gilliland, 2007), selection (Bell, Wiechmann & Ryan, 2006; Cropanzano et al., 2007; Truxillo, Steiner & Gilliland, 2004) and compensation systems (Choi & Chen, 2007; Cropanzano et al., 2007). In 2001, Cohen-Charash and Spector and Colquitt et al. published two separate meta-analyses focused on organizational justice. In order to better understand the role of fairness in organizations, both meta-analyses looked at the relationship of procedural, distributive and interactional justice (separated into interpersonal and informational components in Colquitt et al., 2001) measures relationship to each other and organizational measures. There was substantial overlap in the studies included in both meta-analyses. Cohen-Charash and Spector included 190 field and laboratory studies compared to the 183 in Colquitt et al. (2001). Among other results, Cohen-Charash and Spector (2001) found that organizational justice perceptions are highly related to outcomes such as satisfaction with pay, supervisor trust, organizational commitment, and intentions to leave.

Of specific interest to the current study, Cohen-Charash and Spector (2001) found that the mean sample weighted correlations demonstrated that a perceived lack of procedural ($r = -.40$), distributive ($r = -.40$), and to a lesser degree informational justice ($r = -.24$) were all significant predictors of turnover. Similarly procedural and distributive justice were related to pay satisfaction ($r = .48$, $r = .62$) respectively, trust in a supervisor ($r = .65$, $r = .55$) and organizational commitment ($r = .50$, $r = .47$). The meta-analysis presented by Colquitt et al. (2001) found very similar relationships. Emphasizing the importance of organizational justice, Cohen-Charash and Spector (2001) concluded that,

“to maintain employees’ satisfaction, managers should take care that distributions, procedures, and interactions will all be fair” (p.306).

Looking specifically at performance appraisal systems, researchers have suggested that employee perceptions of the fairness of such systems are critical to employee acceptance and response. Heneman, Greenberger and Strasser (1988) suggest that in order to better predict satisfaction with merit pay allocations, perceptions of the procedures used need to be measured, not only the size of the pay adjustment itself. St-Onge (2000) found that perceptions of procedural justice in the decision making process for performance appraisal and merit pay allocations aligned with higher perceptions of the organization’s merit pay system. In fact, Greenberg (1996) found that procedures perceived to be fair could positively influence perceptions of outcomes even if the outcomes were undesirable. In other words, “research has shown that just procedures can mitigate the ill effects of unfavorable outcomes” (Cropanzano et al., 2007, p.38). More recently, Karriker (2007) looked at organizational realignment and found that positive perceptions of procedural justice were significantly related to support of the organizational change, perceived fairness of the realignment outcomes, and perceptions of the overall effectiveness of the organizational change. In fact, the influence of organizational justice, specifically procedural and distributive, can even change over time as employees receive more information and experience (Ambrose & Cropanzano, 2003). In summary, this research suggests that some organizational change efforts need to include careful management of the system’s procedures and employee reactions to those procedures, instead of just managing the resulting outcomes.

Mechanisms to better manage employee reactions benefit the system's effectiveness and ultimately the organization. One set of principles that has been used to guide implementation, the due process approach, is based on the organizational justice literature and provides a framework for bringing perceptions of fairness to the core of organizational systems. "Disagreements and disputes, inevitable within organizations that have multiple constituencies, competing preferences, and differing viewpoints are best handled by methods modeled after the legal system's governing principle of procedural due process" (Folger et al., 1992, p.171). While the due process literature has focused primarily on performance appraisal, the current study will apply this model to the implementation of a merit pay system.

Due Process

The concept of due process originated with the Fifth and Fourteenth Amendments of the Constitution, but at its core refers to using a fair and reasonable process in decision-making (Forkosch, 1958). Under the amendments, the rights of citizens, namely life, liberty and property cannot be taken away without the due process of law. Forkosch (1958) further defined due process in both judicial (criminal and civil law) and non-judicial (administrative) settings, specifying that the essential elements of administrative due process were adequate notice, fair hearing, and judgment based on evidence.

It is through due process that the legal system attempts to resolve conflicts. Working to address conflict resolution issues related to performance appraisal that had not been dealt with in previous frameworks, Folger et al. (1992) presented a due process framework incorporating the due process requirements defined by Forkosch (1958) and

Thibaut and Walker's (1978) theory of dispute resolution. Thibaut and Walker (1975) indicated that it is best to give disputants control over the process such that they have an opportunity to present their relevant information and evidence, which could support perceptions of a fair process. In fact, the authors concluded that, even when disputants ended up with less favorable outcomes they viewed the process as fair if they had a voice in it (Thibaut & Walker, 1975). Performance appraisal usually involves subjective evaluations, creating the need for a system to help fairly distribute organizational outcomes. Building off of procedural and interactional justice issues, the due process metaphor incorporated concepts of conflict resolution, self-appraisal, and employee rights (Folger et al., 1992).

Folger et al. (1992) first described how a due process model could be applied to a performance appraisal system, identifying specific due process characteristics that an organization should demonstrate. Their framework contains three administrative characteristics of due process: adequate notice, fair hearing and judgment based on evidence. *Adequate notice* requires that organizations provide performance standards in advance to employees, explaining how they were determined, how they need to be met, and how employees perform relative to the standards through feedback. *Fair hearing* standards require that employees receive a formal review meeting including a discussion of a tentative performance assessment from a manager with knowledge of the employee's performance. Additionally, the employee should ideally be able to provide his/her own performance evidence through a self-appraisal and also to challenge ratings. Fair hearing also involves training in the performance appraisal process. Finally, in order to ensure *judgment based on evidence*, the organization must uphold performance standards

consistently across all employees, discuss performance ratings and how rewards are allocated, and do so in a fair and honest manner (Taylor et al., 1995, p. 496). When an organization provides adequate notice, fair hearing and judgment based on evidence, it should create a foundation for positive procedural and interactional justice perceptions.

Taylor et al. (1995) tested this due process model on a newly created performance appraisal system in a quasi-experimental setting. By creating a new system, Taylor et al. were able to manipulate the implementation of it by randomly assigning employees and managers to either an experimental group exposed to interventions consistent with due process or a control group who did not experience these interventions. To establish *adequate notice*, the experimental group of employees and managers participated in training to set and communicate performance standards, conducted an expectation meeting, and held a mid-study feedback session. For the experimental groups, *fair hearing* expectations were met by managers undergoing training on how to encourage two-way communication and how to use the evaluation form. Employees were trained on how to conduct a self-assessment and completed one as a part of the process. *Judgment based on evidence* was implemented for the experimental groups through keeping a performance diary, ensuring the appraisal form fit the job, and providing instruction manuals on the appraisal process. Managers also received training on sampling representative performance and soliciting performance information from employees.

Based on these interventions, Taylor et al. (1995) hypothesized that those employees appraised under a due process system would have greater perceptions of fairness, greater satisfaction with the system, greater job satisfaction, higher manager evaluations, and greater motivation to improve. Analyses revealed that in fact,

employees appraised under the due process performance appraisal system reported significantly higher perceptions of fairness, higher satisfaction with the system, higher ratings of managers, and higher intention to stay with the organization. These results were encouraging and suggested that implementing a performance appraisal system with these due process interventions could help organizations reap important benefits such as improvements in behavior and positive employee perceptions.

In 2008, Buehler took due process research on performance appraisal one step further by assessing employee perceptions of due process interventions and empirically testing the factor structure of the three due process factors. Analyses in this study resulted in confirmation of adequate notice, fair hearing and judgment on evidence factors, but it also identified a fourth factor, lack of feedback. Buehler (2008) also looked at the relationship between these due process dimensions and organizational justice, specifically system procedural, rater procedural, and interactional justice. Support was found for the positive relationships between adequate notice and system and rater procedural justice; fair hearing and system procedural justice; judgment based on evidence and system procedural justice, rater procedural justice and interactional justice; and feedback and interactional justice. This research not only helps to validate the concept of due process, but also its relationship with organizational justice.

The Taylor et al. (1995) and Buehler (2008) applications of due process were directed specifically at performance appraisal systems within organizations; however, it appears generalizable to other organizational systems, namely merit pay systems. Given the similar focus that both performance appraisal and merit pay systems have on

performance standards, criteria and evaluation, a due process approach may also lead to positive outcomes associated with the implementation of a merit pay system.

CURRENT STUDY

Building on the Taylor et al. (1995) and Buehler (2008) studies, the current study will do two things. First, it will examine whether due process elements can be generalized to the implementation of a merit pay system. Second, the current study will examine whether due process elements have similar positive relationships with outcomes of interest. Currently there is no published work that examines perceptions of the full due process framework applied to a merit pay system.

In order to establish due process, activities specific to a merit pay system must be aligned with the three due process components. Due process interventions in a merit pay system that contribute to adequate notice would include informing employees of the performance criteria that will be used to determine their merit adjustment, explaining how the merit pay criteria were selected and how they can be met, and communicating current performance in relation to the criteria. All of this should be done in advance of the review period to be evaluated. Establishing a foundation for fair hearing could involve managers having formal review meetings with employees where current performance is discussed, and implementing training on the process for both raters and ratees. In addition to the manager's knowledge of an employee's performance, the employee would be given an opportunity to provide a self-assessment and challenge merit pay ratings. The last component of due process, judgment based on evidence, may

be applied to a merit pay system by disseminating standards related to the system consistently across all employees, and discussing merit pay distributions in a fair and honest manner. While these specific interventions represent some ways to demonstrate due process, there are other ways to align merit pay interventions within the due process framework.

Traditionally, research on employee reactions and effectiveness of work interventions within a due process context has been conducted on performance appraisal systems (Buehler, 2008; Taylor et al., 1995). Measures of employee reactions most prevalent in performance appraisal research include satisfaction, accuracy, procedural justice, and distributive justice (Keeping & Levy, 2000). Those reactions selected for measurement in this study (i.e., satisfaction with the system, procedural, interactional and distributive justice, and intentions to stay) were chosen based on their ability to capture employee perceptions within the context of merit pay. Specifically, this study will examine how perceptions of due process related to a merit pay system predict employee reactions. As noted above, successful management of these reactions should result in a more effective system, in turn helping to better meet organizational goals.

Previous performance appraisal research has studied key aspects of due process and has demonstrated positive relationships with the outcomes selected for this study. Specifically, research has shown that perceptions of participation or voice in the process, a component fair hearing, is positively related to satisfaction with the system (Cawley et al., 1998) and procedural and interactional justice (Buehler, 2008). Taylor et al. (1995) exposed experimental groups to due process interventions such as supervisor training on due process criteria, performance expectation meetings with a voice in the process, self-

assessments and performance reviews. Taylor et al. (1995) was able to show that those exposed to the due process interventions were more satisfied with the system, had higher perceptions of procedural and interactional justice, and were more likely to stay with the organization. The addition of distributive justice in the current study was based on the distinction between performance appraisal and merit pay in regard to the allocation of monetary increases in the merit pay system. Understanding the relationship between due process and perceptions of distributive justice therefore seems relevant.

Whereas Taylor et al. (1995) manipulated due process through actual interventions, the current study used a correlational approach and measured perceptions of due process to examine whether these perceptions related to reactions of a merit pay system. The current study assessed employee perceptions throughout different stages of the implementation of a new pay system in a midsize organization (see Figure 1). The first measurement point assessed employee perceptions of due process (i.e., adequate notice) before the actual merit meeting. The second measurement point occurred after 360° performance feedback was provided and as additional merit pay criteria (objective metrics by position) were being considered. The final measurement point occurred after the merit adjustments were communicated to employees and assessed final perceptions of this organizational event. Perceptions of adequate notice, fair hearing, and judgment based on evidence were expected to be positively related with perceptions of overall satisfaction with the merit pay system, procedural, interactional and distributive justice, and intentions to stay with the organization (see Figure 2).

STATEMENT OF HYPOTHESES

Overall Satisfaction with the Merit Pay System

Overall system satisfaction is typically defined in terms of the level of positive affective response to a company having an excellent *performance appraisal system* (Cawley et al., 1998). In the context of this study, overall system satisfaction is defined as a global positive affective response to the merit pay system, including its ability to accurately capture and recognize employee performance. Given the criticality of employee reactions to the ultimate success of organizational systems (Cardy & Dobbins, 1994), overall satisfaction with the merit pay system is important to examine. Past research supports the link between due process and system satisfaction. Specifically, Taylor et al. (1995) found that perceptions of due process were positively related to satisfaction with a performance appraisal system, and Cawley et al. (1998) further found that having a voice in the performance appraisal process led to higher levels of performance appraisal system satisfaction. Additionally, positive links have been found between adherence to performance standards (i.e., part of judgment based on evidence within due process) and satisfaction with merit pay systems (Miceli, Jung, Near & Greenberger, 1991). Consistent with these findings, the current study hypothesized that perceptions of due process would be positively related to satisfaction with a merit pay system. Therefore, Hypothesis 1 states: Perceptions of due process (adequate notice, fair

hearing, and judgment based on evidence) will be positively related to overall satisfaction with the merit pay system.

H1a: Adequate notice at Time 1 will be positively related to overall satisfaction at Time 2.

H1b: Fair hearing at Time 2 will be positively related to overall satisfaction at Time 2.

H1c: Judgment based on evidence at Time 2 will be positively related to overall satisfaction at Time 2.

H1d: Adequate notice at Time 1 will be positively related to overall satisfaction at Time 3.

H1e: Fair hearing at Time 2 will be positively related to overall satisfaction at Time 3.

H1f: Judgment based on evidence at Time 2 will be positively related to overall satisfaction at Time 3.

Procedural Justice

Procedural justice refers to an employee's evaluation of perceived fairness of the processes and methods used to make decisions (Lind & Tyler, 1988). Taylor et al. (1995) found that those exposed to due process interventions provided higher ratings for the procedural justice components of fairness and accuracy. For example, those who perceive that they are given adequate notice of merit pay criteria and standards, have a voice in the system, and are going to be judged based on relevant criteria should perceive

the process by which the merit pay system was implemented as fair. In addition, the notion that the due process model builds on procedural justice principles (Folger et al., 1992) supports the hypothesized positive relationship between perceptions of due process and procedural justice. Consequently, Hypothesis 2 states: Perceptions of due process will be positively related to perceptions of procedural justice.

H2a: Adequate notice at Time 1 will be positively related to procedural justice at Time 2.

H2b: Fair hearing at Time 2 will be positively related to procedural justice at Time 2.

H2c: Judgment based on evidence at Time 2 will be positively related to procedural justice at Time 2.

Interactional Justice

Interactional justice refers to the interpersonal treatment and communication surrounding the process and distribution of outcomes (Bies & Moag, 1986). As with procedural justice, interactional justice concepts were the foundation for the due process model (Folger et al., 1992). A link between due process and interactional justice suggests that a) those who believe they receive performance feedback relative to merit pay criteria, b) that their supervisor has enough information to rate their performance, and c) their supervisor provides them an opportunity to present evidence of performance should feel as though they received an appropriate amount of communication and were treated with respect through the process. A positive relationship between due process perceptions and

interactional justice perceptions was therefore hypothesized. Consequently, Hypothesis 3 states: Perceptions of due process will be positively related to perceptions of interactional justice.

H3a: Adequate notice at Time 1 will be positively related to interactional justice at Time 3.

H3b: Fair hearing at Time 2 will be positively related to interactional justice at Time 3.

H3c: Judgment based on evidence at Time 2 will be positively related to interactional justice at Time 3.

Distributive Justice

Distributive justice is defined as the perceived fairness of the allocation of outcomes (Adams, 1965). While there have not been any complete studies of the relationship between due process and distributive justice, the framework proposed by Folger et al. (1992) describes due process as a means of achieving distributive justice. For example, those who believe that a) they have enough time to affect their performance relative to the merit pay criteria, b) they will be judged based on relevant criteria, and c) their supervisor has the information to rate them, should see merit ratings and pay adjustments as fair and appropriate. Research has also explored the relationships between procedural justice, interactional justice, and distributive justice. Positive correlations with distributive justice have been found for both procedural ($r=.55$) and interactional justice ($r=.46$) (Cohen-Charash & Spector, 2001). Given that components of due process are key elements leading to procedural and interactional justice, a positive

relationship is also hypothesized between due process and distributive justice. Therefore, Hypothesis 4 states: Perceptions of due process will be positively related to perceptions of distributive justice.

H4a: Adequate notice at Time 1 will be positively related to distributive justice at Time 3.

H4b: Fair hearing at Time 2 will be positively related to distributive justice at Time 3.

H4c: Judgment based on evidence at Time 2 will be positively related to distributive justice at Time 3.

Intention to Stay

Intention to stay with an organization or turnover tends to be defined and measured in a variety of ways in the literature, including the likelihood to look for a new job (Schaubroeck et al., 2008) and the extent to which an employee would prefer to work for another employer (Simons & Roberson, 2003). Intention to stay with the organization in this specific study is defined as an employee's likelihood to remain an employee of the organization for at least 2 years. Taylor et al. (1995) found that those employees under a due process performance appraisal system reported being more likely to remain with the organization than those who were not under a due process system. Additionally, perceptions of fairness (i.e., procedural and interactional) related to due process are significant predictors of turnover (Cohen-Charash & Spector, 2001; Colquitt et al., 2001; Miceli et al., 1991). Colquitt et al. (2001) were also able to show that distributive justice was related to withdrawal behaviors. Positive perceptions of due process measures

should not only influence perceptions of the merit pay system but of the organization as well, resulting in an increased intent to stay with the organization. Therefore, there is a hypothesized positive relationship between due process perceptions and intentions to stay with the organization. Consequently, Hypothesis 5 states: Perceptions of due process will be positively related to intentions to stay with the organization.

H5a: Adequate notice at Time 1 will be positively related to intention to stay at Time 3.

H5b: Fair hearing at Time 2 will be positively related to intention to stay at Time 3.

H5c: Judgment based on evidence at Time 2 will be positively related to intention to stay at Time 3.

METHOD

Research Design

This study was designed as a longitudinal correlational study. Measurement took place at three points in time throughout the implementation of a new merit pay system within an ongoing organization (see Figure 1). This was a field study with no experimental manipulations.

Participants

Employees of a midsize market research firm in the Midwest were solicited for participation. All 166 US employees subject to the merit pay system were included in the invitation. The types of jobs within the organization that were changed to the new merit pay system included: mailroom and printing coordinators, administrative assistants, sample processors, data processors, statisticians, editors, publishers, web programmers, client services (project coordinators), and group managers. Employees who underwent the change to a merit pay system accounted for approximately 88% of the positions within the organization; those excluded consisted mostly of senior management who were not compensated under the new merit pay system. The organization was shifting from an annual cost of living adjustment increase in pay to an annual merit pay adjustment. The merit pay system utilized the existing performance appraisal system and

established objective metrics by position (i.e., percentage of chargeable client time, profitability of projects, etc.). From the 166 employees contacted, an overall response rate of 50% (n = 83) was achieved for all three-time periods, with response rates for individual time periods somewhat higher (Time 1: n = 130, 78%; Time 2: n = 112, 67%; Time 3: n = 103, 62%).

Procedure

Employees were sent survey invitations via e-mail for participation in an on-line survey across three measurement periods. Unique URLs (links) were included in the invitation for each participant at each time period for mapping of responses over time and to ensure that employees did not access the on-line survey more than once during a single survey period. Unique URLs (i.e., 166) were generated for each potential participant. The organization provided the researcher with the 166 email addresses of the sample group. The researcher randomly linked a URL to each email address and maintained this list until the last data collection period ended. In this way, the email the participants received regarding the study came to them independent of the company, and the company did not know which employee was connected to which URL (unique ID). Once a survey was completed using the unique URL, the link was disabled. Additionally, no person within the organization had access to the file linking participant names with URL identification. All identifying information was stripped prior to analysis to ensure respondent anonymity. Identification of respondents was only used to link survey responses across the three measurement periods.

Measurements occurred three times over a 6-month period at various stages of implementation of the merit pay system (see Figure 1). First, employees were assessed in a survey prior to the start of the performance review/merit adjustment process. This was to measure perceptions based on organizational communication prior to the implementation of the merit pay system. This measurement was designed to assess one aspect of the due process model, adequate notice of merit pay criteria.

The second measurement occurred approximately two months later, after the performance evaluation was presented and discussed during a development meeting with the employee's manager/coach. During the discussion, the manager/coach shared actual performance ratings of measures selected from the performance appraisal system as well as ratings achieved for the objective measures selected for that position. It is important to note that final performance and merit ratings could be changed as a result of this meeting. This measurement period was to capture participant perceptions concerning the process of collecting feedback and the use of that information to form merit ratings. This measurement focused on the due process factors of fair hearing and judgment based on evidence. It also included measures of satisfaction with the merit pay system and procedural justice.

A third measurement was taken a month and a half after the second measurement, once the merit pay adjustment had been communicated. This measurement assessed overall satisfaction with the system, perceived fairness of the distribution of pay adjustments, interactional justice, and intentions to stay with the organization. These time periods were separated so that reactions could be captured as the system was

implemented and to ensure the actual monetary adjustment did not influence perceptions of due process measures.

Measures

Constructs measured within this study included due process, procedural, interactional and distributive justice, satisfaction with the merit pay system (after implementation), and intentions to stay with the organization. Coefficient alphas were calculated for each scale and are reported below. Demographic data were collected on employee age, gender, and race. A comprehensive listing of measures is found in Appendix.

Time One Measurement

The definition of due process by Folger et al. (1992) identified the characteristics necessary to demonstrate the components of due process within an organization: adequate notice, fair hearing and judgment based on evidence. As no scale existed to assess perceptions of the characteristics of due process within a merit pay setting, one was developed to measure all three areas of due process for the current study.

Due process: Adequate notice

Adequate notice was defined as providing merit pay criteria and standards to employees beforehand, explaining how these standards were determined, how they needed to be met, and how employees performed relative to them (i.e., feedback). Six items were created to assess adequate notice and were measured on a 7-point Likert scale

ranging from “strongly disagree” (1) to “strongly agree” (7) ($\alpha=.89$). An example item is, “I was notified of performance requirements with adequate time to impact them prior to the merit pay review.”

Time Two Measurement

Due process: Fair hearing

Fair hearing was defined as conducting formal review meetings with a performance assessment from managers, allowing an employee a say in the process through a self-appraisal and challenge of ratings, and providing training on the process. Seven items were created to assess fair hearing on a 7-point Likert scale ranging from “strongly disagree” (1) to “strongly agree” (7). After preliminary factor analysis, three items switched between fair hearing and judgment based on evidence. The final fair hearing scale consisted of eight items with a coefficient alpha of .84. An item on the fair hearing scale is, “During my development meeting, my supervisor/coach discussed my performance relative to the merit pay criteria established for my position.”

Due process: Judgment based on evidence

Judgment based on evidence was defined as upholding standards consistently across all employees, discussing performance ratings and reviewing how rewards were allocated in a fair and honest manner. Six items were created on a 7-point Likert scale ranging from “strongly disagree” (1) to “strongly agree” (7). After preliminary factor analysis, three items switched between fair hearing and judgment based on evidence. The final judgment based on evidence scale consisted of five items with a coefficient

alpha of .86. An example item is, “Performance standards are applied consistently across employees in my position.”

Procedural justice

This measure of procedural justice focused on the process regarding the implementation of the merit pay system and was defined as the perceived fairness of the process and methods used to evaluate employee performance on merit pay criteria. The scale to assess this concept was developed by Keeping and Levy (2000). Five questions were asked using a 7-point Likert scale ranging from “strongly disagree” (1) to “strongly agree” (7) ($\alpha=.94$). An example item from the procedural justice scale is, “The procedures used to evaluate my performance were fair.”

Satisfaction with the merit pay system

Satisfaction with the merit pay system was defined as a positive affective response to the system capturing and recognizing employee performance accurately. All 3system satisfaction scale items by Keeping and Levy (2000) were used. Two additional items from a system satisfaction scale by Williams and Levy (2000) were added to assess satisfaction with the merit pay system after implementation. Originally designed to gauge satisfaction with a performance review system, the item wording was slightly modified to focus on the merit pay system. The five items were asked using a 7-point Likert scale ranging from “strongly disagree” (1) to “strongly agree” (7). Coefficient alphas were calculated for system satisfaction at Time 2 ($\alpha=.94$) and Time 3 ($\alpha = .95$).

An example item from the scale is, “The merit pay system does a good job of indicating how an employee has performed in the period covered by the review.”

Time Three Measurement

Interactional justice

Interactional justice was defined as fair personal interaction and communication between the employee and supervisor regarding the process and outcomes distributed. A portion of the organizational justice scale developed by Moorman (1991) was used. Six of the 10 items from the supervisor justice section were selected and scale points modified to fit with the structure of the questionnaire. All questions were asked using a 7-point Likert scale ranging from “strongly disagree” (1) to “strongly agree” (7) ($\alpha=.92$). An example item from the interactional justice scale is, “My supervisor/coach discussed the merit pay decision in a truthful and straightforward manner.”

Distributive justice

Distributive justice was defined as the perceived fairness of outcome distribution. This concept was assessed using a scale developed by Keeping and Levy (2000). The first and last of the four items were slightly modified to focus on the merit pay adjustment and ratings rather than on a performance review, as the scale was originally designed to do. All questions were asked on a 7-point Likert scale ranging from “strongly disagree” (1) to “strongly agree” (7) ($\alpha=.89$). An example item is, “The merit pay adjustment was fair.”

Satisfaction with the merit pay system

The same measures were used in Time 3 as described in the Time 2 measurement section.

Intentions to stay

Intentions to stay with the organization were defined as the employees' likelihood to remain with the organization in the future. Measures included one question internal to the organization to allow for comparisons over time. In addition, two items were created to enhance reliability. All questions were asked on a 7-point Likert scale ranging from "not at all likely (1) to extremely likely (7) ($\alpha=.96$). An item from the scale is, "Likelihood to be working at [COMPANY NAME] 2 years from now."

Merit scores

The organization provided the actual final merit score for all participants where possible. Eleven merit scores of the 141 unique participants could not be obtained because they were inaccessible or located in off site files. Depending on position, ratings on 2 to 3 items from the 360-feedback system and 2 to 3 objective measures were combined to create a merit adjustment score that ranged from 1 to 5. Merit adjustments were determined based on that score. Merit scores were awarded on a scale of 1.0 to 5.0, with actual scores ranging from 2.3 to 4.8. Higher scores were awarded for higher performance levels on merit pay criteria. Final merit scores were linearly related to pay

adjustments. These data were gathered in order to control for variability in merit scores while conducting the analysis.

Preliminary Analyses

Exploratory factor analyses were conducted to assess the dimensionality of the variables of interest. As the second study to assess perceptions of due process, exploratory factor analysis was used to ensure that items developed to assess the variables of interest did in fact relate as expected. Given that employees were assessed at multiple time periods, factor analyses were conducted only for items collected within the same time period. Thus, for all analyses, principal axis factoring with varimax rotation was used. Initially, factors were retained if their eigenvalues greater were than one. However, as will be noted below a subsequent analysis was used that restricted the number of factors. An exploratory analysis was done for just the six Time 1 adequate notice items. Additional exploratory factor analyses were completed for all items at Time 2 and Time 3.

Results of adequate notice items at Time 1 indicated that all items loaded onto a single factor (loadings ranged from .77 to .87). The single factor accounted for 63.8% of the variance with an eigenvalue of 3.83. Thus, the items were combined into a single scale tapping adequate notice as shown in Table 1.

A second factor analysis was conducted for items measures at Time 2, which included those for system satisfaction, procedural justice, fair hearing and judgment based on evidence. Analysis results supported four factors in total, as was anticipated, accounting for 74% of the variance (eigenvalues = 11.44, 2.68, 1.62 and 1.27,

respectively). Initial analyses indicated that all five system satisfaction and five procedural justice items loaded onto separate factors as anticipated; however, items intended to assess fair hearing and judgment based on evidence cross loaded in some cases, as shown in Table 2.

As a result of the crossloading of items in fair hearing and judgment based on evidence, a subsequent factor analysis was run just with items assessing fair hearing and judgment based on evidence. In this analysis, the number of factors was restricted to two. These two factors accounted for 64.5% with eigenvalues of 6.71 for fair hearing and 1.68 for judgment based on evidence. As shown in Table 3, some of the items from the original scales switched between fair hearing and judgment based on evidence. For instance, the item that read “I feel my supervisor/coach has enough information about my performance to provide accurate merit pay ratings” (item 2 in Table 3) was moved to judgment based on evidence, and the items “My supervisor/coach provided me with an explanation of performance ratings from the PFC feedback process” and “My supervisor explained how my PFC ratings would impact merit pay ratings” (items 9 and 15 respectively, in Table 3) were both moved to fair hearing. However, after reflecting on these items, switching them did make conceptual sense. Thus, the fair hearing and judgment based on evidence scales were constructed consistent with the factor analyses.

A final factor analyses was conducted on items measured at Time 3, which included those for system satisfaction, distributive justice, interactional justice, and intentions to stay. Analysis results supported four factors in total, with items loading on their anticipated factors, accounting for 83% of the variance (eigenvalues = 9.33, 2.07, 2.48 and 1.01, respectively). In two instances measures had high double loadings that

contradicted original expectations. For example, “The merit pay adjustment was fair” originally aligned with distributive justice also loaded strongly on system satisfaction. Additionally, “My supervisor/coach considered my well being in the distribution of merit adjustments” originally included in interactional justice also loaded strongly on distributive justice. In both instances it was determined that the measure would remain within the original factor. The results of the Time 3 factor analysis can be seen in Table 4.

Preliminary analysis of the data also included a review of the descriptive statistics and correlations among the variables of interest as reported in Table 5. While demographic variables showed few significant relationships, strong correlations are seen both within and across measurement time periods for due process, system satisfaction and organizational justice perceptions. These positive correlational relationships provide initial support for some of the hypothesized relationships.

RESULTS

The goal of the current study was to examine the relationship between perceptions of due process and reactions toward the merit pay system, including satisfaction with the system, organizational justice, and intentions to stay with the organization. All hypotheses were tested using correlation and hierarchical regression. Actual merit pay scores were controlled for in all regression analyses to account for the relationship between these scores and employee reactions. In the regressions of fair hearing and judgment based on evidence, measured at Time 2, perceptions of adequate notice were controlled for from Time 1 measurement. A summary of the results is shown in Table 6.

Hypothesis 1

Hypothesis 1 predicted that perceptions of due process (adequate notice, fair hearing, and judgment based on evidence) would be positively related to overall satisfaction with the merit pay system. In all regression analyses, actual merit pay scores were entered into the regression equation in the first step. In the second step, adequate notice from Time 1 was entered. Finally, fair hearing and judgment based on evidence from Time 2 were entered at the third step. These regressions were done twice, first with satisfaction Time 2 as the dependent variable, then with satisfaction Time 3. The results from both analyses are shown in Table 7 and 8, respectively.

As shown in Table 7, when adequate notice was added at step 2 the regression equation it accounted for significant variance in system satisfaction at Time 2 ($\Delta R^2 = .07$, $p < .05$), providing support for Hypothesis 1a. At step 3, fair hearing and judgment based on evidence were entered into the equation. Together they accounted for an additional 62% ($p < .01$) of the variance. However, when the beta weights were examined, only judgment based on evidence ($\beta = .82$, $p < .01$) was found to be a significant predictor of system satisfaction at Time 2, not fair hearing ($\beta = -.02$). Thus, Hypotheses 1b was not supported but Hypothesis 1c did receive support.

The regression analyses for Time 3 system satisfaction revealed somewhat similar findings, as shown in Table 8. Although, adequate notice failed to reach significance in predicting satisfaction at Time 3 in the regression results, it fell just outside the significance threshold ($\beta = .21$, $p = .06$). At step three, as above, fair hearing and judgment based on evidence together accounted for significant additional variance, ($\Delta R^2 = .38$, $p < .01$). However, judgment based on evidence was again the only significant predictor ($\beta = .73$, $p < .01$), not fair hearing ($\beta = -.17$). Thus, there was not support for Hypotheses 1d and e, but was strong support for Hypotheses 1f.

Hypothesis 2

Hypothesis 2 predicted that perceptions of due process (adequate notice, fair hearing, and judgment based on evidence) would be positively related to procedural justice perceptions. At the first step, merit scores were entered into the regression equation. Adequate notice was placed in the regression equation at step 2 and did not

account for significant variance in procedural justice at Time 2. Therefore, Hypothesis 2a was not supported. At step 3, fair hearing and judgment based on evidence were entered into the equation. Together they accounted for an additional 49% of the variance ($p < .01$). However, only judgment based on evidence was found to be a significant predictor of procedural justice at Time 2 ($\beta = .77, p < .01$), not fair hearing ($\beta = -.06$). Thus, as shown in Table 9, Hypotheses 2b was not supported but Hypothesis 2c did receive support.

Hypothesis 3

Hypothesis 3 predicted that perceptions of due process (adequate notice, fair hearing, and judgment based on evidence) would be positively related to perceptions of interactional justice. At the first step, merit scores were entered into the regression equation. Adequate notice was placed in the regression equation at step 2 and did account for significant variance in interactional justice at Time 3 ($\Delta R^2 = .06, p < .05$), providing support for Hypothesis 3a. At step 3, fair hearing and judgment based on evidence were entered into the equation. Together they accounted for an additional 50% of the variance ($p < .01$). However, the beta weights revealed only judgment based on evidence was a significant predictor of interactional justice at Time 3 ($\beta = .67, p < .01$), not fair hearing ($\beta = .10$). Thus, Hypotheses 3b was not supported but Hypothesis 3c did receive support as shown in Table 10.

Hypothesis 4

Hypothesis 4 predicted that perceptions of due process (adequate notice, fair hearing, and judgment based on evidence) would be positively related to perceptions of distributive justice. At the first step, merit scores were entered into the regression equation. Adequate notice was placed in the regression equation at step 2 and did not account for significant variance in distributive justice at Time 3. Thus, support was not found for Hypothesis 4a. At step 3, fair hearing and judgment based on evidence were entered into the equation. Together they accounted for an additional 46% of the variance ($p < .01$). However, as in other results, only judgment based on evidence was found to be a significant predictor of distributive justice at Time 3 ($\beta = .77, p < .01$), not fair hearing ($\beta = -.12$). Thus, Hypothesis 4b was not supported but Hypothesis 4c did receive support. Results are shown in Table 11.

Hypothesis 5

Hypothesis 5 predicted that perceptions of due process (adequate notice, fair hearing, and judgment based on evidence) would be positively related to perceptions of intentions to stay with the organization. At the first step, merit scores were entered into the regression equation. Adequate notice was placed in the regression equation at step 2 and did not account for significant variance in intentions to stay at Time 3. At step 3, fair hearing and judgment based on evidence were entered into the equation. Neither of the variables accounted for a significant amount of variance. Thus, Hypotheses 5a, 5b and 5c were not supported as shown in Table 12.

Overall, these results support the importance of some due process perceptions in organizational change. Although, fair hearing failed to predict the variables of interest, adequate notice and judgment based on evidence were significant predictors in at least some of these hypothesized relationships. In fact, judgment based on evidence significantly predicted all outcome variables at both Time 2 and Time 3 measurements with the exception of intentions to stay. Adequate notice, measured only at Time 1, predicted system satisfaction at Time 2 and fell just below significance for Time 3, but did significantly predict interactional justice perceptions measured at Time 3 (i.e. 3 months later). These results clearly highlight judgment based on evidence as vital due process perceptions in a merit pay context.

Additional Analysis

Although fair hearing had significant bivariate correlations with many of the outcome variables, it did not significantly predict any of the outcomes in regression when entered with judgment based on evidence after merit score and adequate notice were controlled. Fair hearing and judgment based on evidence perceptions were both captured at Time 2, and the measures were significantly correlated ($r = .58; p < .01$). To examine the individual effect of fair hearing in these analyses, additional regressions were run omitting judgment based on evidence for all outcome variables to determine if fair hearing would then significantly predict the outcomes. Results clearly demonstrated that fair hearing was a significant predictor of system satisfaction at Time 2 ($\beta = .44, p < .01$) and Time 3 ($\beta = .29, p < .05$), procedural justice ($\beta = .36, p < .05$), interactional justice ($\beta = .53, p < .01$), and distributive justice ($\beta = .37, p < .05$). However, consistent

with the results reported above for judgment based on evidence, fair hearing failed to predict intentions to stay. These results clearly show that fair hearing and judgment based on evidence are accounting for much of the same variability in the outcomes. When judgment based on evidence is included in the analyses, it accounts for a large portion of the same variance as fair hearing plus unique variance.

DISCUSSION

The goal of implementing a merit pay system is to motivate employees to perform their best in order to enhance organizational success. Researchers suggest that employee reactions such as system satisfaction (Cawley et al., 1998), and organizational justice perceptions (Cohen-Charash & Spector, 2001) are critical elements of such systems. Thus, understanding the factors that may be related to employee reactions to the implementation of a merit pay system is essential. Previous research has suggested and found that the implementation of due process procedures in a performance appraisal setting is effective (Taylor et al., 1995). More recently, Buehler (2008) found that employee perceptions of due process are also important in a performance appraisal context. This study sought to examine if due process perceptions would also be important in understanding employee reactions to other organizational change, specifically the implementation of a merit pay system. As the third empirical study to examine due process, the current study both supports and extends on previous research. This study supports the finding that employee perceptions of process are as critical, if not more, than simply implementing a system. It also demonstrates that due process can be generalized to other systems such as a merit pay system. Additionally, the current study provides insight to the longitudinal relationships between due process perceptions and the outcomes of interest.

The results clearly show that judgment based on evidence was the strongest predictor of outcome variables, well above and beyond adequate notice and fair hearing. One conclusion from these results could be that judgment based on evidence is the only important element of due process. However, when we consider how these perceptions may build on one another, it seems clear that all are important. For instance, it may be that perceiving that the judgment was based on the evidence can only be accomplished by having advanced notice and on going dialog regarding the merit pay criteria, and receiving feedback in relation to the criteria. In other words, employees may not be able to form perceptions of one without the others having also been established. This idea is supported by the modest correlations between the three due process elements. In addition, it may be that the importance of any due process element may depend upon the type of system being implemented. Previous research has only examined performance appraisal and the current study was the first to extend it to a merit pay system. For merit pay systems, reliable criteria, accuracy of ratings, and consistency of standards may be of critical importance because the results are tied to employee pay. It does not mean that providing adequate notice and fair hearing can be overlooked. It is also critical to continue to evaluate all due process components across different organizational systems to better understand the benefits each can bring to system implementation.

Adequate Notice

In a merit pay system, adequate notice refers to the advance communication of merit pay criteria and feedback regarding an employee's performance relative to those criteria. Although Taylor et al. (1995) did not study due process criteria separately; they

did find that a due process system predicted satisfaction with the system and fairness perceptions as was seen with some of the adequate notice results in the current study. The current study found that adequate notice predicted employees' system satisfaction and interactional justice. Adding to previous research, the current study establishes adequate notice as a longitudinal predictor of both satisfaction with the system, 1 month after, and interactional justice, 3 months after. When employees perceived they were given the information needed to both understand merit pay criteria and in enough time to influence their ratings, they were more likely to be satisfied with the system itself and feel as though they were treated in a considerate and honest manner.

Both organizations and individual supervisors play a key role in establishing adequate notice. According to Folger et al. (1992), organizations must first establish performance expectations and subsequent merit pay criteria by position early enough in the merit pay cycle so that employees can impact their final ratings. Supervisors can then establish adequate notice with employees through openly reviewing merit pay criteria and providing performance feedback relative to those criteria. In this way, supervisors provide employees with the critical opportunity to influence their merit pay ratings through enhanced performance. Clearly established communication timelines are essential to ensure that all supervisors are providing employees with the same advance notice of expectations. Given that adequate notice is partially established while interacting with an employee's supervisor, it is not surprising that adequate notice significantly predicted perceptions of interactional justice. However, it is important to note that in the current study, these measurements occurred 3 months apart. Establishing a positive employee experience during the initial merit pay implementation phase of

adequate notice has been shown to continue to be related employee perceptions throughout the implementation all the way to the distribution of ratings and rewards. It appears that the transparency of performance expectations and ongoing feedback is what sets the stage for satisfaction with the system and positive interactional justice perceptions.

Fair Hearing

Fair hearing in the context of a merit pay system involves providing performance feedback relevant to merit pay criteria during a formal review, allowing employees to challenge ratings and provide additional evidence of performance, and training employees on the merit pay process. As reported above, the current study failed to identify fair hearing as a unique significant predictor of any variables of interest, however it was correlated with many of the outcomes of interest. This is inconsistent with Buehler (2008) who found fair hearing be a predictor of system procedural justice. There are two main potential reasons why results from these studies differed. First, Buehler's (2008) research focused on performance appraisal systems, not merit pay. Second, Buehler found that employee training on the appraisal process was the significant predictor of system procedural justice. This differs from the current study where fair hearing perceptions were primarily defined as discussion of merit pay criteria, performance relative to merit pay criteria, and discussion on how performance ratings impact merit pay ratings. It is also important to note that the lack of significance of fair hearing found in the current hypotheses testing was due to the fact that fair hearing and judgment based on evidence were accounting for the much of the same variability in the outcome

measures. As discussed in the additional analysis section, when fair hearing was placed into the regressions without judgment based on evidence, it (i.e., fair hearing) proved to be a significant predictor of all outcomes of interest with the exception of turnover.

Despite fair hearing's inability to stand alone as a significant predictor in the analyses, the criteria associated criteria are still key to merit pay systems. Clearly fairness perceptions are important when it comes to implementing pay systems, and understanding the components of fair hearing provides some additional guidance. Employee's perceptions of fair hearing can be best established through open dialog with supervisors regarding the merit pay criteria for the employee's position, providing ongoing performance feedback relative to the criteria, and discussing how performance ratings impact merit pay ratings. These predictors are very similar to those seen in adequate notice, demonstrating that fair hearing is part of the ongoing dialog regarding performance expectations and feedback.

These results continue to emphasize the role that supervisors play in influencing employee perceptions. Organizations would be smart to ensure that supervisors have the knowledge and skills necessary to effectively communicate with employees, as well as evaluate and share merit pay feedback. Additionally, employee development meetings need to be consistently structured so that there is targeted two-way dialog around the merit pay criteria and employee performance.

Judgment Based on Evidence

In a merit pay system, judgment based on evidence requires that merit pay standards be applied consistently, that merit pay criteria is used in a reliable manner, and

that merit pay criteria provide a fair assessment of performance. Similar to Buehler (2008), the current study found a strong relationship between judgment based on evidence and both procedural and interactional justice perceptions. Expanding on previous research, the current study also found equally strong predictive relationships between judgment based on evidence and system satisfaction as well as distributive justice perceptions. These findings establish judgment based on evidence as an especially strong predictor of employee reactions. When employees perceived that performance standards were consistently applied without prejudice, and performance and merit ratings were discussed honestly, these workers were more likely to be satisfied with the merit pay system itself. They are also more likely to feel that the performance evaluation process was fair, that they were treated with respect, and that the allocation of rewards were done in a just manner. Results demonstrated that judgment based on evidence predicted perceptions of satisfaction and procedural justice at the same time period, while also predicting system satisfaction, interactional justice and distributive justice perceptions 2 months later.

Practically, these results suggest organizations need to establish a training process to ensure supervisors are using performance criteria in a reliable manner, that supervisors have enough information on employee performance to provide accurate ratings, and that performance standards are applied consistently across employees free of bias. The foundation of a successful merit pay system must be based on reliable and valid performance expectations, which are then used to form appropriate merit pay criteria. Once this is established, it is again up to supervisors to demonstrate their ability to apply standards fairly, collect relevant feedback and use it to rate employee performance

appropriately. Organizations must take an active role in training, supporting, and holding supervisors accountable for delivering on these expectations.

Other Findings

In all tests of hypotheses we included merit pay scores as a covariate in the first step of all regression equations. We had anticipated that these scores, like performance appraisal scores, would significantly predict outcomes. Interestingly, they did not. There are two potential reasons this might be the case. First, it is unknown if the pool of money allocated for merit pay adjustments was large enough to influence perceptions. Second, while merit scores could range from 1 to 5, scores within position tended to have limited variability, therefore providing limited variability in the actual merit pay adjustments.

Study Limitations

There are study limitations to be aware of when considering these results. An obvious one is external validity. Conducting data collection within only one organization to assess perceptions of due process, it is questionable if the results can be generalized to other organizations. Another potential threat to accurately interpreting these results would exist if there were a lack of funds available within the merit pay budget to provide what employees would consider meaningful increases.

Other threats exist based on the actual questionnaire and data collection procedures. First, there were no direct manipulations of what could be considered due

process; all participants provided self-reported perceptions. Second, the scales for due process perceptions were new and have unknown construct validity. Third, there was item stem similarity, particularly seen in the procedural and interactional justice portions of the survey. Fourth, consistency of scales existed through the majority of the survey. Last, while longitudinal designs provide many benefits, they also provide limitations due to dropouts, and other factors that may occur during and between data collection periods, and subsequently influence the measures obtained.

Future Research

While the current study provides some insight in terms of the importance of due process perceptions in organizational change, there are clear opportunities to add to this understanding. Given the lack of empirical studies, there is a clear need for additional research on the perceptions of due process regarding systems already studied (performance appraisal and merit pay) to provide more depth of knowledge, and regarding other organizational systems that have yet to be explored (i.e., significant changes to job descriptions or responsibilities, other compensation systems like skill based pay, etc.). Specific to understanding due process in the context of a merit pay system, future research should look to see if findings from this study could be replicated in a different organization. It would also be beneficial to see if judgment based on evidence is consistently the strongest predictor in a merit pay system, and if there is a way to understand what components of due process are the most critical in different organizational systems.

Future research could also assist in the practical understanding of how best to operationalize the components of due process in a merit pay environment. For instance, establishing how much time is needed to be considered 'adequate', how often feedback is required to optimize employee reactions, and how to effectively transform job performance expectations into merit pay criteria would help organizations with the logistics for a successful implementation of a merit pay system.

Summary

The results of the current study provide strong support for the importance of due process perceptions, especially judgment based on evidence, and the effect they may have on the ultimate success of a merit pay system. When implementing a merit pay system, organizations need to put measures in place to positively impact employee perceptions of due process. For instance, organizations should establish clear timing guidelines and the manner in which merit pay criteria and performance expectations are communicated, provide supervisor training on collecting and providing performance feedback, encourage two-way communication about job performance, turn feedback into fair and unbiased merit pay ratings, and effectively communicate final merit ratings and merit pay adjustments. By doing these, organizations can help to influence employee perceptions of organizational justice and resulting merit pay system satisfaction. To leverage the benefits, organizations must ensure that merit pay systems include notification of employees with enough time to impact performance measures influencing merit pay decisions. Supervisors must communicate effectively with employees regarding criteria being used to create their pay adjustments and performance relative to those criteria.

Organizations need to ensure that reliable and appropriate criteria are used to assess performance for each position, and be applied in a consistent manner.

With the implementation of a merit pay system, organizations are looking to motivate employees to behave in ways that support organizational success. In order for that to ever be realized, organizations must first focus on the implementation of the system. Ensuring that measures consistent with due process are followed from the onset provides organizations with a great opportunity to positively affect employee satisfaction with the system and also perceptions that the process, interactions, and subsequent rewards are fair and just.

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TABLES

TABLES

Table 1. Time 1 Factor Analysis

Due process item	Adequate notice
1. Supervisor reviewed merit pay criteria	.87
2. Aware of criteria that would effect merit pay	.81
3. Supervisor provides feedback relative to merit pay	.80
4. Continuously receive feedback related to merit pay	.78
5. Supervisor provided copy of merit pay criteria	.77
6. Notified of criteria with adequate time to impact	.76

Table 2. Time 3 Factor Analysis

	Satisfaction	Procedural Justice	Factor 3	Factor 4
1. Performance Relative to MP	.08	-.06	.82	.25
2. Supervisor Has Enough Info	.69	.28	.25	.34
3. Self Assessment	.36	.19	.33	.58
4. Challenge My Ratings	.14	.14	.26	.85
5. Training on Process	.31	.19	.66	.17
6. Provide Additional Evidence	.21	.19	.51	.47
7. Discussion of MP Criteria	.15	.00	.87	.23
1. Standards Applied Consistently	.70	.21	.26	.14
2. Explanation of Perf Ratings	.20	.34	.62	.04
3. Fair Assessment	.65	.40	.42	-.28
4. Based On Evidence	.40	.49	.26	.29
5. Criteria Used Reliable	.60	.46	.36	.05
6. How Ratings Impact MP	.15	.23	.89	.01
1. Perf Eval Procedures Fair	.43	<u>.79</u>	.06	.14
2. Perf Eval Procedures Appropriate	.41	<u>.81</u>	.13	.11
3. MP Rating Procedures Fair	.43	<u>.67</u>	.24	.03
4. Perf Rating Procedure Fair	.21	<u>.87</u>	.09	.19
5. Process Implemented Fair	.16	<u>.89</u>	.13	.08
1. MPS Indicates Employee Perf	<u>.76</u>	.32	.27	.02
2. MPS Excellent	<u>.83</u>	.17	.21	.20
3. MPS Fair and Unbiased	<u>.85</u>	.32	.10	.09
4. No Change to MPS	<u>.69</u>	.21	.03	.43
5. MPS Recognizes Perf	<u>.84</u>	.30	.07	.19

Note: Underscore (_) notes which measures are included in each factor.

Key: MP = Merit Pay, MPS = Merit Pay System, Perf = Performance, Eval = Evaluation

Table 3. Time 2 Factor Analysis Fair Hearing and Judgment on Evidence

Due process item	Fair Hearing	Judgment Based on Evidence
1. Discussed Performance Relative to Merit Pay	<u>.90</u>	.06
2. Supervisor Has Enough Info for Accurate Ratings	.24	<u>.82</u>
3. Self Assessment Allows Me to Provide Input	<u>.52</u>	.51
4. Able to Challenge My Ratings	<u>.52</u>	.32
5. Received Training/Information on the Process	<u>.71</u>	.41
6. Able to Provide Additional Evidence of Performance	<u>.60</u>	.34
7. Meeting Included Discussion of Merit Pay Criteria	<u>.92</u>	.16
8. Standards Applied Consistently Across Employees	.21	<u>.77</u>
9. Supervisor Explanation of Performance Ratings	<u>.53</u>	.48
10. Criteria Provide Fair Assessment of Performance	.21	<u>.76</u>
11. Performance Ratings Based on Appropriate Evidence	.23	<u>.77</u>
12. Criteria Used Reliable in Reliable Manner	.27	<u>.84</u>
13. Explained How Ratings Impact Merit Pay	<u>.82</u>	.27

Note: Underscore (_) notes which measures are included in each factor.

Table 4. Time 3 Factor Analysis

	Satisfaction	Distributive Justice	Interactional Justice	Intentions to Stay
1. MPS Indicates Employee Perf	<u>.85</u>	.15	.27	.14
2. MPS Excellent	<u>.88</u>	.23	.23	.14
3. MPS Fair and Unbiased	<u>.82</u>	.31	.27	.15
4. No Change to MPS	<u>.81</u>	.13	.15	.04
5. MPS Recognizes Performance	<u>.91</u>	.18	.21	.13
1. Pay Adjustment Fair	.69	<u>.44</u>	.23	.06
2. Merit Pay Rating Fair	.54	<u>.72</u>	.14	.11
3. Manager Rating Appropriate	.30	<u>.75</u>	.30	.15
4. Rating Represents Performance	.55	<u>.66</u>	.23	.12
1. Considered My Well Being	.21	.61	<u>.56</u>	.16
2. Supervisor Showed Kindness	.15	.38	<u>.82</u>	.16
3. Understands MP Means to Me	.25	.32	<u>.81</u>	.14
4. Discussed Truthful Manner	.40	.19	<u>.77</u>	.01
5. Showed Respect	.15	.26	<u>.85</u>	.06
6. Communicated Timely	.24	-.13	<u>.79</u>	-.02
1. Working at COMPANY in 2 yrs	.12	.05	.15	<u>.95</u>
2. Remain an Employee	.05	.18	.08	<u>.95</u>
3. Future Includes COMPANY	.20	.08	-.01	<u>.94</u>

Note: Underscore () notes which measures are included in each factor.

Key: MP = Merit Pay, MPS = Merit Pay System, Perf = Performance

Table 5. Correlation Matrix

	N	M	SD	Correlations														
				1	2	3	4	5	6	7	8	9	10	11	12	13		
1. Gender	127	1.70	.46	-														
2. Race	125	1.09	.52	.11	-													
3. Education	128	3.78	.78	-.18*	-.03	-												
4. Adequate Notice	130	4.61	1.33	-.04	-.03	-.11	.89											
5. Fair Hearing	112	3.81	1.34	-.15	-.03	-.09	.27**	.84										
6. Judgment on Evidence	111	4.25	1.38	-.24*	-.16	-.09	.32**	.58**	.89									
7. Procedural Justice	108	4.61	1.34	-.11	-.07	.04	.16	.37**	.70**	.94								
8. Satisfaction T2	102	3.3	1.31	-.12	-.04	-.20*	.27**	.48**	.82**	.67**	.94							
9. Satisfaction T3	100	3.16	1.38	-.14	-.03	-.17	.22*	.33**	.66**	.62**	.62**	.95						
10. Distributive Justice	99	4.09	1.43	-.31**	-.10	.01	.18	.40**	.67**	.58**	.60**	.75**	.89					
11. Interactional Justice	96	4.73	1.33	-.19	-.04	-.09	.30**	.55**	.73**	.54**	.62**	.57**	.64**	.92				
12. Intentions to Stay	73	3.90	.87	-.02	-.06	-.22*	.02	.13	.20	.17	.20	.25*	.30**	.23*	.96			
13: Merit Score	130	3.51	.53	.01	-.12	.05	.03	.05	.04	-.08	.12	.13	.02	.12	-.10	-		

* Correlation is significant at the 0.05 level (2-tailed).

** Correlation is significant at the 0.01 level (2-tailed).

Note: Cronbach's alpha coefficients are highlighted in the main diagonal.

Table 6. Results Summary

		Adequate Notice T1	Fair Hearing T2	Judgment on Evidence T2
H1	Satisfaction T2	Yes ($\beta=.26^*$)	No	Yes ($\beta=.82^{**}$)
H1	Satisfaction T3	No ($\beta=.21^+$)	No	Yes ($\beta=.73^{**}$)
H2	Procedural justice T2	No	No	Yes ($\beta=.77^{**}$)
H3	Interactional justice T3	Yes ($\beta=.24^*$)	No	Yes ($\beta=.67^{**}$)
H4	Distributive justice T3	No	No	Yes ($\beta=.77^{**}$)
H5	Intentions to stay T3	No	No	No

* $p<.05$, ** $p<.01$, + $p= .06$

Table 7. Regression Summary for Hypothesis 1a-c

Step	Variable	β	R^2	ΔR^2	F Change
1	Merit Score	-.15	.02	.02	1.88
2	Merit Score	-.12			
	Adequate Notice	.26*	.09	.07	6.27*
3	Merit Score	-.12*			
	Adequate Notice	.04			
	Fair Hearing	-.02			
	Judgment on Evidence	.82**	.71	.62	89.37**

Dependent variable: Satisfaction Time 2, * $p < .05$, ** $p < .01$

Table 8. Regression Summary for Hypothesis 1d-f

Step	Variable	β	R^2	ΔR^2	F Change
1	Merit Score	.17	.03	.03	2.31
2	Merit Score	.18			
	Adequate Notice	.21	.07	.04	3.62+
3	Merit Score	.14			
	Adequate Notice	.06			
	Fair Hearing	-.17			
	Judgment on Evidence	.73**	.45	.38	25.40**

Dependent variable: Satisfaction Time 3, * $p < .05$, ** $p < .01$, + $p = .06$

Table 9. Regression Summary for Hypothesis 2a-c

Step	Variable	β	R^2	ΔR^2	F Change
1	Merit Score	-.10	.01	.01	.89
2	Merit Score	-.09			
	Adequate Notice	.15	.03	.02	2.04
3	Merit Score	-.13			
	Adequate Notice	-.07			
	Fair Hearing	-.06			
	Judgment on Evidence	.77**	.52	.49	46.08**

Dependent variable: Procedural Justice Time 2, * $p < .05$, ** $p < .01$

Table 10. Regression Summary for Hypothesis 3a-c

Step	Variable	β	R^2	ΔR^2	F Change
1	Merit Score	.12	.01	.01	1.03
2	Merit Score	.12			
	Adequate Notice	.24*	.07	.06	4.39*
3	Merit Score	.07			
	Adequate Notice	.03			
	Fair Hearing	.10			
	Judgment on Evidence	.67**	.57	.50	41.02**

Dependent variable: Interactional Justice Time 3, * $p < .05$, ** $p < .01$

Table 11. Regression Summary for Hypothesis 4a-c

Step	Variable	β	R^2	ΔR^2	F Change
1	Merit Score	.03	.00	.00	.05
2	Merit Score	.03			
	Adequate Notice	.16	.03	.02	1.93
3	Merit Score	-.01			
	Adequate Notice	-.02			
	Fair Hearing	-.12			
	Judgment on Evidence	.77**	.48	.46	32.91**

Dependent variable: Distributive Justice Time 3, * $p < .05$, ** $p < .01$

Table 12. Regression Summary for Hypothesis 5a-c

Step	Variable	β	R^2	ΔR^2	F Change
1	Merit Score	-.10	.01	.01	.81
2	Merit Score	-.11			
	Adequate Notice	-.10	.02	.01	.76
3	Merit Score	-.12			
	Adequate Notice	-.17			
	Fair Hearing	.02			
	Judgment on Evidence	.24	.08	.06	2.33

Dependent variable: Intentions to Stay Time 3, * $p < .05$, ** $p < .01$

FIGURES

FIGURES

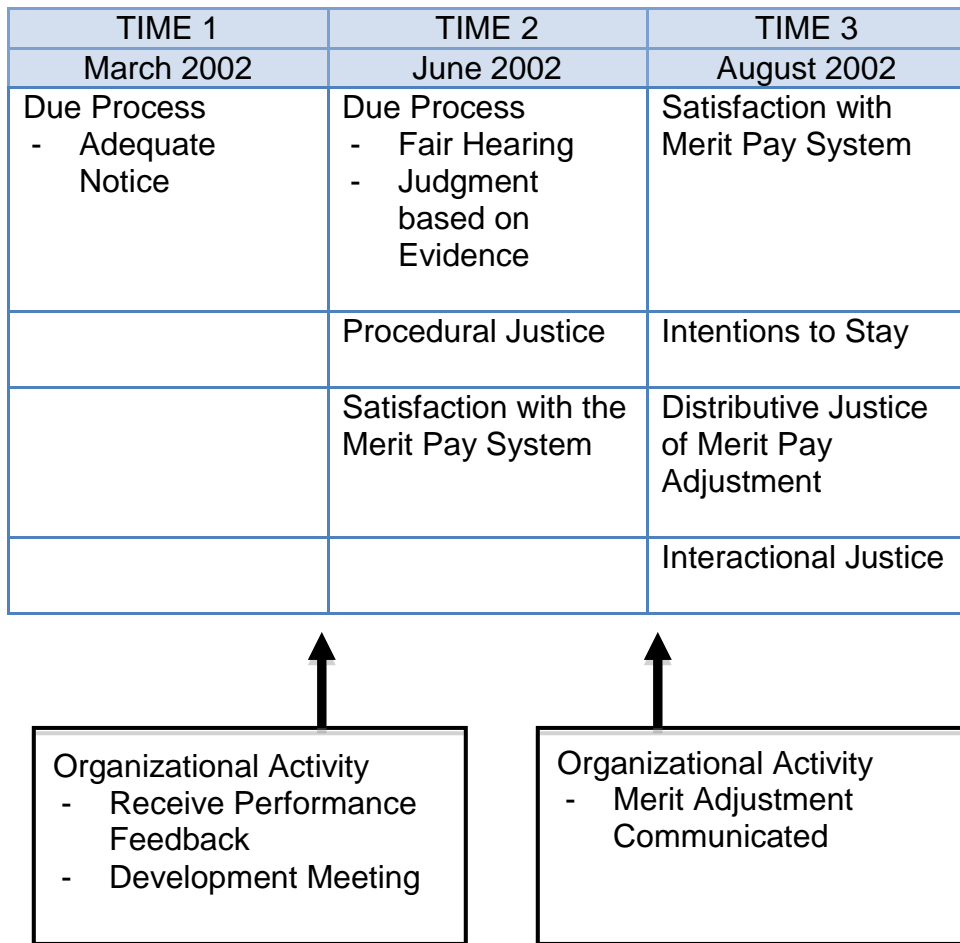


Figure 1. Measurement Timetable

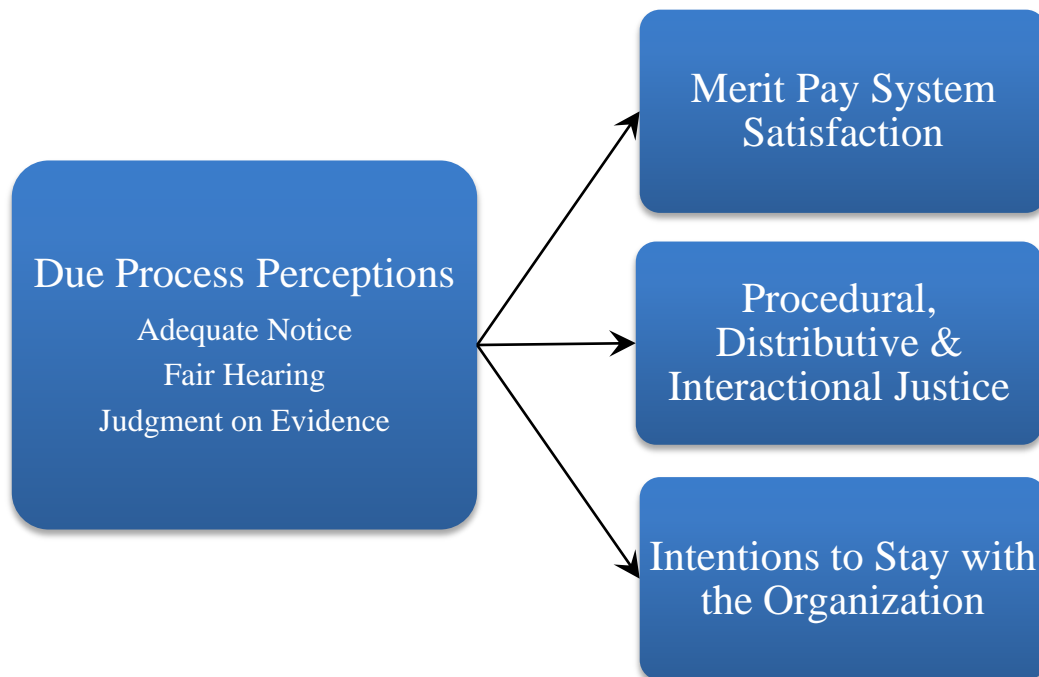


Figure 2. Model

APPENDIX

APPENDIX

1	2	3	4	5	6	7
Strongly Disagree	Disagree	Slightly Disagree	Neither Agree nor Disagree	Slightly Agree	Agree	Strongly Agree

Adequate Notice: Measurement Time 1

1. I was notified of performance criteria with adequate time to impact them prior to the merit pay review.
2. My supervisor/coach has reviewed with me the merit pay criteria that will be used to assess my position.
3. My supervisor/coach provided me with a copy of the merit pay criteria.
4. My supervisor/coach provides me with feedback on my performance relative to the merit pay criteria established for my position.
5. I was made aware of the criteria that would effect my merit pay review.
6. I continuously receive feedback about my performance related to my merit pay criteria.

Fair Hearing: Measurement Time 2

1. During my development meeting, my supervisor/coach discussed my performance relative to the merit pay criteria established for my position.
2. I feel my supervisor/coach has enough information about my performance to provide accurate merit pay ratings.
3. The self-assessment in the 360° process allowed me to provide input on my performance for the merit ratings.
4. I was able to challenge my ratings by presenting my interpretation and an appraisal of my own performance.
5. I received training/information on the process used to determine merit pay ratings.
6. My supervisor/coach gave me the opportunity to provide additional evidence regarding my performance.
7. My developmental meeting included a discussion of my merit pay criteria.

Judgment Based on Evidence: Measurement Time 2

1. Performance standards are applied consistently across employees in my position.
2. My supervisor/coach provided me with an explanation of performance ratings from the [PERFORMANCE APPRAISAL] process.
3. The merit pay criteria selected for my position can provide a fair assessment of my job performance.
4. I feel my [PERFORMANCE APPRAISAL] ratings were based on appropriate evidence.
5. I believe the performance criteria are used in a reliable manner.

6. My supervisor explained how my [PERFORMANCE APPRAISAL] ratings would impact my merit pay ratings.

Procedural Justice: Time 2

1. The procedures used to evaluate my performance were fair.
2. The procedures used to evaluate my performance were appropriate.
3. The procedures used to provide merit pay feedback were fair.
4. The procedures used to determine my performance ratings were fair.
5. The process implemented to gather my performance feedback was fair.

Satisfaction: Time 2 and Time 3

1. The merit pay system does a good job of indicating how an employee has performed in the period covered by the review.
2. In general, I feel the company has an excellent merit pay system.
3. The merit pay system provides a fair and unbiased measure of the level of an employee's performance.
4. I feel that no changes should be made to the merit pay system in this organization.
5. The current merit pay process is a good way to recognize my job performance.

Interactional Justice: Time 3

1. My supervisor/coach considered my well being in the distribution of merit pay adjustments.
2. My supervisor/coach showed kindness and consideration in explaining the merit pay results.
3. My supervisor/coach tried to understand what the merit pay decision means to me on an individual basis.
4. My supervisor/coach discussed the merit pay decision in a truthful and straightforward manner.
5. My supervisor/coach showed respect for my rights as an employee during the merit pay process.
6. My supervisor/coach communicated the merit decision to me in a timely manner.

Distributive Justice: Time 3

1. The merit pay adjustment was fair.
2. I believe my final merit ratings were fair.
3. The way my manager rated my performance on the merit criteria was appropriate.
4. My merit pay ratings fairly represented my past year's performance.

Intentions to Stay: Time 3

1	2	3	4	5	6	7
Not At All Likely	Unlikely	Somewhat Unlikely	Neither likely nor unlikely	Somewhat Unlikely	Likely	Extremely Likely

1. Likelihood to be working at [COMPANY NAME] 2 years from now.
2. Likelihood to remain with [COMPANY NAME] as an employee.
3. Likelihood that future employment plans include [COMPANY NAME].

Demographics: Time 1

1. Age: _____
2. Gender: Male / Female
3. Race: White, African-American, Hispanic, Asian, Other