

Cranfield University

Jonathan Chapman

An examination of the influences on reward mix
determination. Observations from the UK financial
services industry

School of Management

PhD Thesis

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Supervisor: Dr Clare Kelliher

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Abstract

During 2007-2010 significant dislocation occurred in the financial services sector with governments having to come to the aid of a large number of financial institutions. Throughout this crisis much political, media and practitioner interest was given to reward structures within the industry and, in particular, the proportion, or mix, of different rewards provided in overall compensation.

This thesis examines influences on the determination of reward mix in the UK financial services sector. Three theoretical perspectives are examined – agency, institutional and resource dependency – as potential explanations. Semi-structured interviews were conducted with reward executives from 30 financial services firms, alongside perspectives garnered from ten reward consultants.

These interviews identify the strength of institutional pressures on firms to conform to an agreed reward mix norm, largely driven by historical reward patterns and reinforced by strong employee expectations that they will receive this norm. However, firms are still seen to exercise strategic choice, influenced by the extent to which they have the desire and capability to resist institutional pressures. The research also identifies which firms are likely to differentiate their reward mix from that established in the sector.

The findings provide a contribution to an under-researched area in a key sector of the economy. They present both an important account of the pressures facing reward mix determination in the financial services sector at this time, and a theoretically informed approach to understanding those pressures through the presentation of a unified theory of reward mix determination.

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Contents

1	Chapter one: Introduction.....	1
1.1	Preamble – My motives	1
1.2	Introduction.....	1
1.3	The academic context	2
1.4	Research question	4
1.5	Research context	5
1.5.1	Financial services - defined	5
1.5.2	Financial services – significance of the sector	6
1.5.3	Financial services – employment and reward context.....	8
1.6	Theoretical perspectives	9
1.7	Research approach	10
1.8	The research process	11
1.9	Contribution	13
1.10	Outline of the thesis	15
2	Chapter two: Review of the literature	17
2.1	Introduction.....	17
2.2	Conceptualising reward mix	18
2.2.1	Reward defined.....	18
2.2.2	Reward mix defined.....	20
2.3	Theoretical perspectives	28
2.3.1	Agency theory	32
2.3.1.1	Introduction	32
2.3.1.2	Agency problem	33
2.3.1.3	Managing the agency problem - incentives and monitoring	34
2.3.1.4	Agency research	40
2.3.1.5	Criticisms	41
2.3.1.6	Agency and the role of motivation theory.....	46
2.3.1.7	Conclusions	48
2.3.2	Institutional theory.....	49
2.3.2.1	Introduction	49

2.3.2.2	Isomorphic constraints	49
2.3.2.3	Coercive isomorphism.....	50
2.3.2.4	Mimetic isomorphism	55
2.3.2.5	Normative isomorphism.....	59
2.3.2.6	Institutionally contested practices	63
2.3.2.7	Institutionally driven behaviour – empirical evidence.....	67
2.3.2.8	Conclusions	71
2.3.3	Resource dependency theory	72
2.3.3.1	Introduction	72
2.3.3.2	Critical resources.....	73
2.3.3.3	Employee perspective	76
2.3.3.4	Empirical evidence – non reward mix related.....	77
2.3.3.5	Empirical evidence – reward mix.....	80
2.3.3.6	Expectancy and resource dependency theory.....	84
2.4	Combining theoretical insights	87
2.5	The role of benefits	94
2.6	Epistemological approaches.....	99
2.7	Gaps in the literature for further examination.....	102
2.7.1	Conceptual framework and research questions	107
2.8	Conclusion to chapter two	111
3	Chapter three: Research design	112
3.1	Introduction to the chapter	112
3.2	Research strategy	112
3.2.1	An abductive approach	112
3.2.2	Ontological position	115
3.2.3	Epistemology – How we come to know	116
3.2.4	A constructed research approach.....	117
3.2.5	Recognising the role of the researcher	118
3.2.5.1	Behavioural preferences	120
3.2.5.2	Researcher stance	121
3.2.6	Summary.....	122
3.3	Method.....	123

3.3.1	Data sources.....	123
3.3.1.1	Socially derived.....	124
3.3.1.2	Reward consultants (RCs).....	124
3.3.1.3	Reward executives (REs)	125
3.3.2	Levels of analysis	127
3.3.3	Research options.....	127
3.3.4	Semi-structured interviews	129
3.4	Research programme	130
3.4.1	First study - Reward consultants' perspectives	131
3.4.2	Main study - Reward executives' perspectives	132
3.4.2.1	Initial exploratory interviews	132
3.4.2.2	Pilot interviews.....	133
3.4.2.3	Main study.....	134
3.4.2.4	The interview protocol	136
3.4.2.5	Carrying out the interviews	137
3.4.2.6	Interview introduction	137
3.4.2.7	Reward mix conceptualisation	138
3.4.2.8	Interview section 1	138
3.4.2.9	Interview section 2	139
3.4.2.10	Interview closure	139
3.4.2.11	Post interview	140
3.4.3	Interview data analysis	141
3.4.3.1	Data reduction	141
3.4.3.2	Data analysis	144
3.4.4	Saturation.....	144
3.4.5	Sense checking activity	146
3.5	Validity, reliability, generalisability	148
3.6	Conclusion to chapter three	149
4	Chapter four: Reward mix determination: Reward consultants' perspectives.....	151
4.1	Introduction.....	151
4.2	Reward mix conceptualised	152
4.3	Drivers of reward mix	154

4.3.1	Institutional pressures	154
4.3.1.1	Mimetic pressure - The market	154
4.3.1.2	Coercive influences	157
4.3.1.3	Agency interests - Business strategy	159
4.3.1.4	Agency interests - Cost management	160
4.3.2	Resource perspective	161
4.3.2.1	Talent and employee preferences	161
4.3.3	Explanations for inertia	162
4.3.3.1	Quality of HR	163
4.3.3.2	Organisational history	164
4.3.3.3	Breaking down the inertia – The role of events	165
4.4	Implications for main study	166
4.5	Conclusion to chapter four.....	169
5	Chapter five: Reward mix determination: Financial services reward executives’ perspectives	170
5.1	Introduction.....	170
5.2	Reward mix conceptualisation.....	173
5.2.1	Summary.....	177
5.3	Determination process	177
5.3.1	Organisational level and role.....	180
5.3.2	Summary.....	182
5.4	Industry norm.....	183
5.4.1.1	The role of the market	183
5.4.1.2	Benchmarking	184
5.4.1.3	Sources of data	185
5.5	Influences on the industry norm benchmark position.....	188
5.5.1	Employee expectations	189
5.5.2	Union influence	192
5.5.3	Influences on employee expectation – Historical reward patterns	194
5.5.3.1	Control over employees	196
5.5.3.2	Paternalism	198
5.5.3.3	Industry structure and profitability.....	203

5.5.4	Moderating employee expectations	204
5.5.4.1	Regulatory change.....	204
5.5.4.2	Legal pressures	206
5.5.4.3	Taxation.....	208
5.5.5	Summary.....	210
5.6	Diverging from the industry norm	210
5.6.1	Desire to differentiate	213
5.6.1.1	Leadership	213
5.6.1.2	Business strategy	216
5.6.1.3	Political pressure	218
5.6.1.4	Parental influence	219
5.6.1.5	The influence of history	222
5.6.2	Capability to differentiate	222
5.6.2.1	HR capability.....	223
5.6.2.2	Management capability	225
5.6.3	Opportunity to differentiate	225
5.6.3.1	The financial crisis	225
5.6.3.2	Regulatory change.....	226
5.6.3.3	Merger	227
5.6.4	Summary.....	228
5.7	Specific firm propensity to follow the industry norm.....	228
5.7.1.1	Market followers	230
5.7.1.2	Cautious leaders	231
5.7.1.3	Mould breakers.....	232
5.8	Conclusion to chapter five	236
6	Chapter six: Discussion.....	238
6.1	Introduction.....	238
6.2	A descriptive model of industry norm development	238
6.3	A model of firm reward mix determination.....	243
6.4	Overall model of reward mix determination.....	246
6.5	Implications for the theoretical understanding of reward mix determination	249
6.5.1	Theoretical perspectives	249

6.5.1.1	Agency theory	250
6.5.1.2	Institutional theory	258
6.5.1.3	Resource dependency	271
6.5.1.4	Other theoretical perspectives	275
6.5.2	The significance of the context.....	278
6.5.2.1	Sectoral.....	278
6.5.2.2	Firm context	279
6.5.2.3	Individual context.....	280
6.5.3	Combining theoretical perspectives – An integrated theory of RMD....	281
6.5.3.1	Revisiting inputs to RMD	281
6.5.3.2	An integrated theory.....	283
6.6	Conclusion to chapter six.....	285
7	Chapter seven: Conclusions	287
7.1	Introduction.....	287
7.2	Research approach	288
7.3	Addressing the research questions	289
7.4	Contribution	291
7.4.1	Academic – Theoretical, empirical and methodological knowledge	291
7.4.2	Implications for practice and policy	295
7.5	Limitations	296
7.6	Further research	299
7.7	Concluding remarks	302
8	References	304
	Appendix 1 - Outputs and dissemination of research.....	326
	Appendix 2 - Specified activities as defined in part II of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001.....	328
	Appendix 3 - The significance of the research context	329
	Appendix 4 - Review of rejected research methods	333
	Appendix 5 - Reward consultant interview protocol.....	335
	Appendix 6 - Reward executive interviewees	336

Appendix 7 - Reward executive interview protocol.....	337
Appendix 8 - Contact summary sheet	338
Appendix 9 – Coding structure.....	341
Appendix 10 - Assessment of firm’s desire and ability for differentiation	345
Appendix 11 – Table of illustrative quotes from interviewees	348

List of tables

Table 1-1 – Key components of compensation in financial services – Adapted from PwC 2010	9
Table 2-1 - Summary of reward mix measures used in employee reward mix research	23
Table 2-2 - Studies adopting institutional theory to examine employee reward mix determination	69
Table 2-3 – Reward research adopting combinations of agency, institutional and resource dependency theories	90
Table 2-4 – Summary of agency, resource dependence and institutional theories.....	103
Table 2-5 – Potential reward mix determinants.....	105
Table 3-1 – Myers-Briggs preferences and their implications for the research strategy	120
Table 3-2 – Research programme.....	130
Table 3-3 – Interviews completed	145
Table 6-1 - Research contribution to our understanding of RMD from an agency theory perspective	257
Table 6-2 - Research contribution to our understanding of RMD from an institutional theory perspective.....	270
Table 6-3 - Research contribution to our understanding of RMD from an resource dependency theory perspective.....	275
Table 6-4 - Significance of ‘shopping list’ factors in this research.....	283
Table 6-5 - Summary unified theory of reward mix determination	284

List of figures

Figure 1-1 - Research stages.....	12
Figure 2-1 - Conceptual framework	108
Figure 3-1 - Philosophical route map	114
Figure 3-2 – Researcher stances	121

Figure 3-3 - Concept saturation	146
Figure 4-1 – Reward consultants’ model of reward mix determination.....	167
Figure 5-1 – Flow of chapter five.....	172
Figure 5-2 - Typology of firms.....	230
Figure 6-1 – First stage industry norm reward mix model.....	240
Figure 6-2 – Second stage industry norm model.....	240
Figure 6-3 – Third stage industry norm model.....	241
Figure 6-4 – Final model of the development of an industry norm.....	242
Figure 6-5 – First stage firm reward mix model.....	245
Figure 6-6 - Model of firm reward mix determination.....	246
Figure 6-7 – Full model of reward mix determination	248

List of charts

Chart 1 – Financial services sector’s share of UK GDP.....	329
Chart 2 – Financial services’ share of GDP in major economies.....	330
Chart 3 – Tax contribution of UK financial services	331
Chart 4 – Financial services employment by region	332

Abbreviations

CEO – Chief Executive Officer

ESRC – The Economic and Social Research Council

FD – Finance Director

FSA - Financial Services Authority

FSMA – Financial Services and Markets Act

FSSC – Financial Services Skills Council

GDP – Gross Domestic Product

HRD - Human Resources Director

RAO – Regulated Activities Order

RC – Reward Consultant

RDR – Retail Distribution Review

RE – Reward Executive

RMD – Reward Mix Determination

RQ – Research Question

TCF – Treating Customers Fairly

UK – United Kingdom

1 Chapter one: Introduction

1.1 Preamble – My motives

From 2002 to 2007 I was responsible for the development, implementation and communication of reward policy within a large organisation. During that time I led the implementation of a new reward structure which aimed to shift the reward focus from one of base pay management to a wider, more holistic consideration of all types of reward. It was during this time that my interest in the concept of reward mix was formed as we aimed for a balanced deal across all reward elements in order to meet the organisation's need to focus employees on their performance objectives and manage cost, whilst competing with other firms for the talent we needed.

The events in the financial services industry of 2007-2009, described further below, have also allowed me to combine my experience and interest in financial services acquired in various financial services roles with the main research field of reward management. I have relished the opportunity to bring my experience to this area and develop new skills and knowledge through my PhD and have the opportunity to have a series of work published (see Appendix 1 for details of published work).

1.2 Introduction

Since 2007, reward mix determination (RMD) in the financial services sector has been the subject of significant scrutiny and comment by government, regulators, media and the wider public. This thesis examines what influences reward mix, i.e. the combination of elements making up overall reward determination in financial services organisations, and why these influences are significant.

In this introductory chapter, in section 1.3, I provide an initial outline of how reward and reward mix are defined and what academic research tells us about reward mix determination. Next, I outline the specific research question being asked in section 1.4, the context in which this question will be asked in section 1.5 and the theoretical perspectives adopted to address this question in section 1.6. Sections 1.7 and 1.8 briefly outline the approach to the research with section 1.9 summarising the contribution the research makes. The chapter concludes with section 1.10 – an outline of the structure of the thesis.

1.3 The academic context

For the purpose of this thesis, reward is defined as "any direct or indirect payments to employees, such as wages, bonuses, stock and benefits" (Gerhart and Milkovich, 1992: 484). From this we can see that employee reward can come in a variety of forms (Dreher et al., 1988). However, the focus of the reward literature has largely been on pay, both fixed, in the form of salaries and wages, or variable through a range of schemes such as incentives, bonuses and stock related schemes (Gerhart and Rynes, 2003). The interest in pay is unsurprising given the amount that organisations spend on pay as a proportion of their overall costs (Lawler, 1971) and its importance to individuals (Milkovich and Newman, 2008), but it does neglect the wider approach to reward management choices that practitioners are increasingly taking in the area of total reward (Milkovich and Newman, 2008; Armstrong and Murlis, 2007). This has led to a call for academic research to incorporate non-wage compensation elements and look at the determinants of aspects other than pay, such as reward mix (Gomez-Mejia and Welbourne, 1988; Heneman et al., 2000; Milkovich, 1988).

For the purpose of this thesis reward mix is defined as "the combination of the elements making up overall reward" (Balkin and Bannister, 1993). Gerhart and Rynes (2003) suggest that there is potential for variance in how organisations allocate compensation across the various forms of reward and therefore construct their reward mix. This is in contrast to what (i.e. the amount) they pay, where there appears to be less discretion due to the need to stay broadly in line with others for attraction, retention and overall economic competitiveness reasons (Gerhart and Milkovich, 1990). Significant quantitative research has been carried out analysing the relationships between a range of both firm and environmental items to reward decisions including reward mix (e.g. Eisenhardt, 1988; Boyd and Salamin, 2001; Tremblay et al., 2003). However, while the statistical nature of this work may have identified causality, it has only been able to infer why these items might be showing these statistical relationships. Whilst helpful, these lists of variables and their relationships give no insight into the relative importance of factors in the actual organisational reward decisions taken (Perkins and White, 2008).

This presents a potential issue with the research to date, namely that, despite the amount of reward research carried out, we know little about how reward mix is actually determined as there is no single paradigm emerging from the research which adequately explains the process. This may be an accurate reflection of reality, with this area of reward strategy decision making being particularly complex. Alternatively, perhaps the list of factors has muddied the field and after all this research our knowledge remains limited. Convergence around a smaller number of theoretical perspectives might prove helpful in directing future research (Pfeffer, 1993).

1.4 Research question

Gerhart and Rynes identified that although reward strategy is a matter of various choices, “surprisingly little is known empirically about how such choices are made in the first place” (2003: 7). In this context the research question is explored:

What influences reward mix determination in financial services organisations?

This question is intended to explore the elements influencing reward mix determination and deepen our understanding of those elements – the what and the why. This differs from the approach to reward research to date which has been largely explanatory. This difference is articulated by Blaikie when he states that “whereas explanation is concerned with abstract patterns of relationships in deductive arguments or causal sequences, understanding is concerned with the reasons social actors give for their actions.” (2000: 77). Answering this question is important as it allows academics and practitioners to think more consciously about the influences on reward mix, and therefore assess if those influences are genuinely in line with business need, however this may be defined.

The application of the question is not limited to Executives, but extends to all employees. This focus has been selected in the context of criticism of the concentration of research at the reward level of the top executives and in particular the CEO (Gerhart and Rynes, 2003). Hambrick and Mason (Hambrick and Mason, 1984; Hambrick, 2007) showed that the success of an organisation depends on all contributions. This led them to state that reward research should extend its reach to ever-lower levels of the organisation so that reward structures, through better understanding, could be developed and improved.

1.5 Research context

1.5.1 Financial services - defined

The context for the research is the financial services sector. Section K of the Standard Industrial Classification (Office For National Statistics, 2010b) defines ‘Financial and Insurance activities’ as:

- Financial service activities, except insurance and pension funding;
- Insurance, reinsurance and pension funding, except compulsory social security; and,
- Activities auxiliary to financial services and insurance activities.

HM Treasury assists further in defining this group of firms (HM Treasury, 2005), by breaking the sector’s role down into three main functions, with firms operating in this sector carrying out one or more of these functions:

- Matching savers, borrowers and investors through the investment chain – and in doing so, allocating capital to the most efficient investments within the economy and providing mechanisms for saving;
- Risk pooling and management – transferring risk to those better able to absorb it, helping businesses plan and cope with change and facilitating higher levels of economic activity; and,
- Facilitating payments – enabling swift and efficient transactions in the domestic and global economy and reducing the costs of doing business.

The Financial Services Authority (FSA), the UK authority responsible for the authorisation of firms within the sector and their ongoing regulation, defines financial

services firms in relation to the legal definition presented in the Financial Services & Markets Act 2000 (HM Treasury, 2000a) which defines a range of financial services as ‘regulated activities’. Any firm conducting any of these defined activities is deemed to be operating a financial services business and therefore requires authorisation and will be subject to ongoing regulation by the FSA. The activities are detailed in The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (RAO) (HM Treasury, 2000b). Specified activities are defined in part II of the RAO and are shown in Appendix 2. This definition, i.e. firms carrying out an activity detailed in the RAO, is the one used in this research due to its ease of application, as all financial services firms are required to include their regulatory status in their publications.

1.5.2 Financial services – significance of the sector

The financial services context was selected for various reasons. Although the sector has been identified as strategically important, with its contribution to GDP of around 8.5%, it is considered to be under-researched and therefore warrants further attention (Adams et al., 2008). Specifically, the ESRC identifies issues with regard to regulation and policy formulation for the industry, management of human capital, and ensuring that HR approaches are robust enough to deliver the talent that the sector is perceived to require, with remuneration practice a particular concern (Adams et al., 2008).

In addition, during the financial crisis of 2007-2009 a number of commentators, politicians and regulators identified the way reward was structured, and specifically the reward mix within the banking sector of the financial services sector as a contributory factor in what was perceived as excessive risk taking behaviour (McCarthy, 2008; Darling, 2008; Financial Times, 2008; Institute of International Finance, 2009; FSA, 2009b). For example, Callum McCarthy (2008) the Chairman of the FSA stated:

I think it entirely appropriate for supervisors, as part of our general assessment of systems and controls, to be interested in compensation and incentive structures, and – just as we take other aspects of a bank’s control philosophy and practice into account – to adjust our assessment of prudential requirements, including capital, for a bank accordingly. Please note that I am referring to incentive structures. We have no part to play in assessing or influencing individual bonuses or individual remuneration.

This led to changes in the way remuneration risk was considered by financial services regulators across the world as they looked to influence reward mix within financial services firms. This manifested itself in pressure for a reduction in the variable element of the mix, relative to the fixed component and, where large bonuses remain, deferral of those over a period of at least three years (FSA, 2009a, 2009b). The focus of regulatory attention was not limited to the banking sector. Regulatory requirements were extended in 2011 to encompass all banks, building societies and asset managers, plus some firms which engage in corporate finance, venture capital and financial services broking activities, capturing over 2,700 UK financial services firms within the regulatory requirements (FSA, 2010b).

Over the same period, regulatory pressure was also building on the financial advisory sector to reform how it managed its reward mix. In 2006 the FSA announced that it was undertaking a review of the provision of financial advice including how remuneration structures may influence the advice that financial advisors provide to their clients. This came to be known as the Retail Distribution Review (RDR). The aim of the RDR was to identify and address the causes of problems that were perceived in the retail investment market, including the role remuneration structures and reward mix played in

those problems. The FSA proposed that financial advice should only be provided on the basis of fixed charges, not based on commission from product providers for sales as is largely current practice. However, the FSA does not mandate what this means for how firms reward their employees, leaving firms to determine the changes they need to make (FSA, 2010a). Further detail on the sectoral context is provided in Appendix 3.

1.5.3 Financial services – employment and reward context

Over 34,000 firms employing over 900,000 people operate within the financial services sector (FSSC, 2010). Whilst 97% of these firms are small (employing fewer than 250 people), the vast majority of employment comes from a relatively small number of large organisations (FSSC, 2010). The workforce is typically made up of four groupings of employees: first, around 15% of employees carry out managerial duties, which is typically higher than other sectors of the economy; second, professional staff i.e. those holding professional and other qualifications; third, administrative employees who form the largest proportion of the workforce given the large amount of administrative and data handling work that is required; finally, sales and customer service staff which, although a decreasing proportion due to internet use as a distribution channel, still form an important group of the workforce.

Reward mix within the sector is distinctive when compared with other industry sectors (PriceWaterhouse Coopers, 2010). The key components typically making up compensation packages within the sector are shown in Table 1-1 below.

Reward component	Current practice
Fixed pay	Tends to be low in wholesale financial services. Retail business typically 30% of overall package.

Reward component	Current practice
Benefits	<p>Pensions an important component of the benefits package.</p> <p>Typically a wide range of financial benefits (e.g. life insurance, critical illness, medical cover at higher grades) provided.</p>
Bonus	<p>Majority of package in wholesale financial services business.</p> <p>Retail businesses around 30% of reward mix.</p> <p>Typically paid out of profit pools (although commission structures are common where sales roles are in place) with allocation allowing for both financial and non financial factors in distribution decisions.</p>
Long term incentives	<p>Limited application in investment banking.</p> <p>Widespread in retail financial services businesses.</p>

Table 1-1 – Key components of compensation in financial services – Adapted from PwC 2010

As Table 1-1 shows, the reward mix is typically weighted towards variable reward with employee benefits also playing a significant role. Whilst there are notable differences in the reward mix between the retail and wholesale businesses that make up the financial services sector, both sub-sectors are characterised by relatively high levels of variable pay and benefits in the reward mix compared to other sectors of the economy (PriceWaterhouse Coopers, 2010).

It is within the context of the significance of the sector to the UK economy, the employment and reward characteristics highlighted above, and the ongoing scrutiny of reward practices across the sector that this research is framed.

1.6 Theoretical perspectives

A range of theoretical frameworks have been applied to develop understanding of reward determination (Perkins and White, 2008). Review of the literature has led to the use of three for this research – resource dependency (Pfeffer and Davis-Blake, 1987),

neo-institutional theory (DiMaggio and Powell, 1991) and agency theory (Jensen and Meckling, 1976).

Each of these theoretical perspectives offers a different explanation about how reward mix is determined. Agency theory gives us insight into how to align the organisation's objectives to those of the individual and specifically what reward mix will best achieve this alignment (Jensen and Meckling, 1976). Neo-institutional theory helps us to understand the pressures organisations are under to conform and, specifically, to mimic the reward mix of other firms (Eisenhardt, 1988; Conlon and Parks, 1990; Crystal, 1991). Resource dependency theory helps predict who may have most power in influencing the reward mix decision. The theory contends that some jobs in organisations control resources critical to the success of the organisation. Individuals or groups holding those jobs are consequently able to exercise higher levels of power and therefore can use this to influence both the level and mix of the overall reward package (Tremblay et al., 2003; Pfeffer and Davis-Blake, 1987; Balkin and Bannister, 1993).

1.7 Research approach

Review of the literature shows that positivist approaches have directed reward research, with quantitative methods dominating both experimental and field-based work. For example, Werner and Ward's (2004) review of the compensation literature from 1996 to 2002 showed that of the 396 studies identified 1.8% were meta-analytic and 4.5% theoretical, the rest being quantitative analysis of data. This is unsurprising given that pay is monetised.

Whilst the statistical analysis may have established (or falsified) relationships between the variables being examined, the authors could then only speculate on potential reasons

for these relationships (Yanadori and Marler, 2006). Taras concluded that “it is perhaps troubling that while scholars clearly are able to develop strong rational models of wage determination based on inferences derived from large data sets of wage outcomes, they are caught short when exposed to the often intuitive or baffling decisions of actual compensation managers” (1997: 181). Consequently, she proposed that “it is appropriate now to simply ask compensation managers about their decisions, if for nothing else than to posit some plausible explanations for further testing” (1997: 181). In addition, Heneman and Judge noted that “we must enter the field, rather than merely survey it, if we are to fully understand and appreciate its context and changes” (2000: 369). Bloom and Milkovich add to this that “ours is a field of inquiry irrevocably intertwined with the decisions of practical people” (1996: 40). However, reward research remains largely quantitative archival and survey research, rather than field-based, engaging with and interpreting the actions of these “practical people”.

Despite this, an emerging body of work is developing, taking a more constructionist approach, engaging in the field with practising managers. This qualitative research approach, through conversations between an informed researcher and reward professionals from the field, can assist in establishing not only what is influencing reward mix determination in this sector at this time, but also why those influences are significant.

1.8 The research process

As a guide to the research process Figure 1-1 shows the three stages that the research has taken – conceptualisation and identification of research question, data collection and theory building.

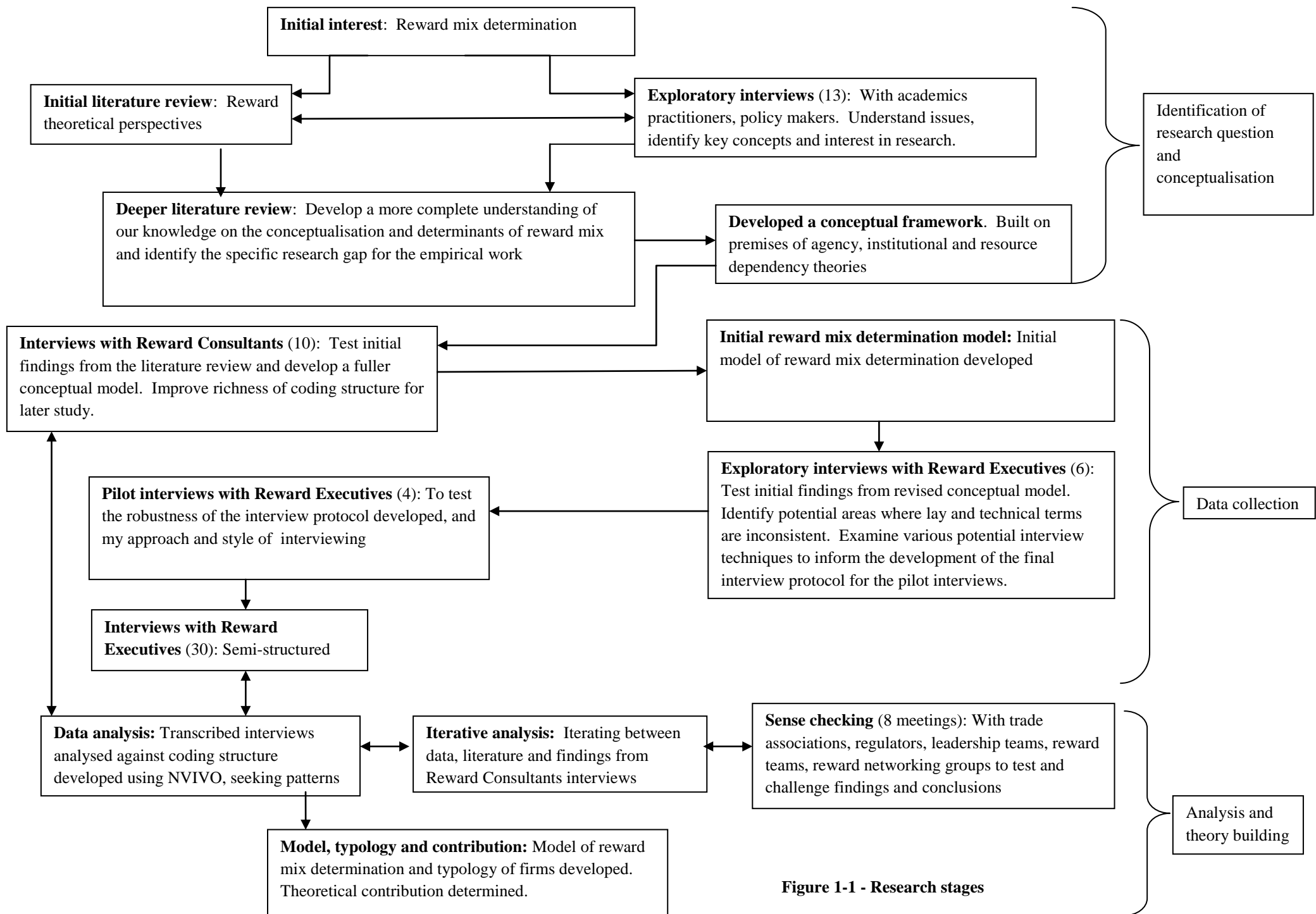


Figure 1-1 - Research stages

As indicated in Figure 1-1, at the beginning of the research I developed a preliminary map of the reward research field and conducted 13 exploratory interviews with academics, practitioners and policy makers to help identify a research gap that existed in the literature that was also relevant to those in the field. This led to a deeper literature review examining what we know about reward mix determination and how we come to know this. From this a conceptual framework was developed which was used as the basic structure for interviews with ten reward consultants (RCs), as acknowledged experts in their field, playing a significant role in reward determination and therefore able to provide a valid insight into the reward mix determination process (Bender, 2011; Clark and Fincham, 2002). Following further exploratory and pilot interviews, 30 interviews with reward executives¹ (REs) were carried out. These were analysed iteratively between the literature and interview data, but also returning to the earlier interviews with the RCs as ideas emerged. Finally, this led to the development of a detailed descriptive model of reward mix determination in the financial services sector and a typology of firms dependent on their propensity to adopt a reward mix position away from the industry norm. This was then tested via various sense-making sessions with a large range of practitioners and representatives from their trade bodies.

1.9 Contribution

The research makes a theoretical, empirical and methodological contribution. Theoretically, the research provides an important contribution by providing an important account of the pressures facing reward mix determination in the financial

¹ The term Reward Executive (RE) will be used throughout this document to represent the individual with overall responsibility for reward strategy and reward mix decisions. This may be the HR Director or Chief Operating Office in smaller firms or Head of Reward, Head of Compensation and Benefits, Reward Vice President and Compensation and Benefits Vice President in larger organisations.

services sector at this time, and a theoretically informed approach to understanding those pressures. It takes a step towards providing us with greater understanding of the strength of reward mix inertia in this sector with its conclusion that adopting institutionally legitimate positions is often, contrary to some other earlier research findings, a rational activity due to the additional, often viewed as unacceptable, risk that moving away from the perceived 'safe harbour' of the market benchmark implies. In addition it provides useful support, refinement and addition to the premises and assumptions of agency, institutional and resource dependency theories in this context, and from this presents a unified theory of reward mix determination.

Empirically, we have developed an understanding of the complexity of RMD in the sector. We have evidence on the practices and responses of financial services firms in the post crises environment and how they are reacting to regulatory and market based pressures at this time. Specifically we now have empirical evidence of how the combination of both a firm's desire and capability to differentiate their reward mix informs their judgement of whether to 'break free' from the established institutional norms.

Methodologically the research adopts a qualitative approach in a largely quantitative field and draws on two pivotal groups in developing understanding – RCs and REs (the former selected due to their access and integration into the process of reward mix determination through their work with clients in this area, the latter able to talk directly about the influences on reward mix determination).

1.10 Outline of the thesis

The thesis comprises seven chapters. After this introductory chapter, chapter two reviews the reward mix determination literature in order, through examining the issue of reward mix determination from multiple perspectives, to develop a series of research questions to be explored in the research. Chapter three provides the link between the research gap identified and resulting research questions, and the empirical work in later chapters. It begins with an outline of the philosophical base for the research. A constructionist approach to the research is presented, given the belief that reward mix decisions are a social activity and that meaning can best be derived on reward mix determination through dialogue with those closely involved in the decision making process. The chapter then outlines the specific research strategy decisions taken to operationalise the research. Specifically, semi-structured interviews are carried out with REs, and those who work closely with them providing reward strategy advice – RCs. The methodology chapter ends with a discussion on how the approach meets established qualitative standards of quality, reliability and validity.

Chapter four presents the findings of the ten interviews with the RCs who provide data on both industry practice in reward mix determination as well as firm-specific practice through discussion of specific consulting assignments they have conducted. Patterns are identified that lead to the development of a model of reward mix determination, which is then built on and refined, in the context of the financial services sector, through the interviews with REs presented in the next chapter.

Chapter five presents the findings of the interviews with REs working in 30 different financial services firms. Personal and purposeful recruitment of the interviewees leads

to their being able to speak of, rather than for, their organisation. The findings are presented in four sections: the determination process with respect to the formality of the reward mix decision and the extent to which the process is a coherent one; reward mix conceptualisation and the factors that are found to be an influence on this: the factors determining reward mix and the extent to which they are consistent with the findings of the literature review; the review of the dimensions identified as catalysts for change in reward mix.

Chapter six presents a discussion of the findings through the development of a reward mix determination model in the financial services sector. The findings are then discussed in the context of the literature and considerations of agency, institutional and resource dependency theories and what they say about reward mix determination. A revised integrated theory of reward mix determination is then presented, drawing on the range of perspectives discussed in the literature and the empirical data gathered in this research.

Finally, in chapter seven I review the analysis discussed in chapter six and provide a summary of my answers to the research questions established in chapter two. The chapter then goes on to summarise the contribution of this thesis to knowledge, practice and policy makers. The limitations of the research are then acknowledged before avenues for further research are suggested. The thesis concludes with some reflective remarks on the research process and its findings.

2 Chapter two: Review of the literature

2.1 Introduction

The purpose of this chapter is to present the results of a review of the literature relating to reward mix determination (RMD). This review has two objectives. First, it will examine the issue of RMD from multiple perspectives, in order to develop a more complete understanding of both our current knowledge on the determinants of RMD and how we acquire this. Second, building on this understanding, it will clarify the specific research gap in the context of the research question introduced in chapter one – What influences reward mix determination in financial services organisations? – and develop supplementary research questions to be examined through further empirical work.

This chapter has seven sections. After outlining the method used to conduct the literature review, section 2.2 defines key reward mix terms and examines how reward mix has been conceptualised in the literature to date. Following this, section 2.3 presents three explanations of RMD. First, agency theory is discussed as the base for understanding what is driving reward mix decisions in organisations. This base view is then critiqued and accompanied by alternative explanations of reward mix decisions. Resource dependency and institutional theory² are offered as both competing and complementary explanations for RMD. Section 2.4 draws these three explanations together in a review of research which has combined their insights to examine RMD.

² Although the term institutional theory is used in this review, the literature is based on neo-institutional theory which took initial theorising on the influence external factors have on organisations and extended it through describing the processes by which external factors influence organisations (Hatch and Cunliffe, 2006).

Section 2.5 examines separately the role of benefits in reward mix, given that this is an area often excluded from reward research. Section 2.6 examines and critiques the epistemological positions taken by researchers into RMD. In section 2.7, the gaps in our knowledge that emerge from the review of the literature are summarised, and the conceptual framework and research questions for the empirical work to follow are presented. Finally section 2.8 summarises the chapter.

2.2 Conceptualising reward mix

2.2.1 Reward defined

Milkovich and Newman (2008) draw together much of the thinking on reward definition. They outline the various returns that could be said to accrue to employees in exchange for their labour and therefore the range of choices employers have about the mix between these returns that they look to provide. These returns cover three main areas – cash compensation, benefits and relational returns.

Cash compensation is made up of base pay and incentives. Base pay is the fixed cash element of overall reward and generally reflects either the value the employer puts on the role being performed or the skills the employee brings to the role. Changes to base pay are made due to a change in the wider market valuation for the role, employers' perception that employee skills have improved, or a more general shift to reflect changes in inflation. Incentives, which can be long- or short-term, are elements of the overall mix that change with respect to either individual or organisational performance, but are not consolidated into base pay. Generally, they take two forms –cash, for example bonuses and profit sharing, or equity through either direct equity grants or equity options.

Benefits are non cash elements of reward and take a number of forms. Income protection benefits are designed to “help protect employees from the financial risks inherent in daily life” (Milkovich and Newman, 2008: 12). Pensions, health insurance and life insurance are examples of benefits that are common in the UK (CIPD, 2008c). Work-life benefits are those “which help employees better integrate their work and life responsibilities” (Milkovich and Newman, 2008: p12). Examples include flexible working arrangements and child care provision (CIPD, 2008c). Finally, allowances are extras that enhance the attractiveness of the package. These are more common in areas where certain goods are in short supply or the employer can provide them at a lower cost than the employee would be able to obtain them for themselves, e.g. the provision of employee housing.

Relational returns explain wider reasons why employees are felt to work for a particular employer. Milkovich and Newman (2008) categorised these as recognition and status, job security, the challenge of the work and the learning experience it brings. Although some of these may not be fully within the organisation’s control, such as employment security which will be influenced by wider economic trends, these are still considered to be an important part of the overall reward mix (Gélinas, 2005). Further, the importance of relational returns can be seen through the increasing focus that organisations are placing, at least in their rhetoric, on them as part of their overall total reward packages (Armstrong and Murlis, 2007).

Whilst a helpful categorisation of the elements making up overall reward, the definition outlined above does not capture the interplay between the elements making up total return, nor even the interplay in the sub-categorisation of total compensation. For

example how, if at all, is cash compensation related to benefits or within benefits what determines whether firms provide, say, income protection type benefits, and if so how does this influence other elements of the total compensation mix? This interplay is an area where the review of the reward mix literature will provide further insight through exploring the theoretical drivers of choices organisations make with respect to the combination, or mix, of all the elements discussed.

2.2.2 Reward mix defined

Whilst there is a general consensus around the definition of reward (Milkovich and Newman, 2008), there is no such consensus around how reward mix should be conceptualised (Yanadori et al., 2002). Definitions are both broad, covering a wide range of the reward elements discussed, and narrow, focussing on the mix of just two, typically base salary and incentives. Measures vary across different studies. A narrow definition of reward mix has been conceptualised through the use of the ratio of base salary to short-term bonus payments as this was perceived as the most common form of incentive pay (e.g. Gerhart and Milkovich, 1990; Eisenhardt, 1988; Boyd and Salamin, 2001; Werner and Tosi, 1995; Gerhart and Trevor, 1996; Bloom and Milkovich, 1998). Alternatively, others have widened this simple ratio to examine the proportion of base pay to cash compensation, i.e. including both short- and long-term incentives (e.g. Tremblay et al., 2003; Roth and O'Donnell, 1996; Tremblay and Chenevert, 2005; Burke and Hsieh, 2006) or the closely related area of bonus to cash compensation (e.g. Pappas and Flaherty, 2006; Tosi and Greckhamer, 2004; Anderson et al., 2000; Elvira, 2001; Gomez-Mejia et al., 1987). A number of studies have also used multiple measures, arguing that this best captures the range of variability which has generally

been the area of study (e.g. Gerhart and Milkovich, 1990; Gomez-Mejia and Balkin, 1989).

A summary of measures used in employee level (as opposed to solely executive level) reward research is given in Table 2-1 alongside my interpretation of the theoretical perspective that each study has taken³.

³ A number of the studies explicitly state the theoretical perspective. Where this is not the case I have allotted a perspective based on my reading of the paper and the conclusions it draws.

<u>Study</u>	<u>Reward mix conceptualisation</u>	<u>Theoretical perspective</u>
Darmon 1982	Relative proportion of salary, commission and bonus	n/a
Ippolito 1987	Proportion of reward in pension as measured by capital loss	n/a
Balkin and Gomez-Mejia 1987	Relative importance of fixed (salary and fringe benefits) and variable (incentive) components of reward.	Contingency
Eisenhardt 1988	Proportion of salary relative to sales commission payments	Agency, institutional
Gomez-Mejia and Balkin 1989	Merit pay as a percentage of base salary. Bonus as a percentage of base salary. Aggregate incentive pay as a percentage of base salary.	Strategic compensation
Gerhart and Milkovich 1990	Extent of variable pay, in terms of relative amounts of short-term bonuses, long-term incentives and base salary in individuals' pay	Agency, expectancy
Conlon and Parks 1990	Proportion of contingent versus non contingent pay	Agency, institutional
Gomez-Mejia 1992	Proportion of incentives relative to fixed pay	Strategic compensation
Balkin and Bannister 1993	Proportion of earnings coming from each pay form	Resource dependency
Werner and Tosi 1995	Bonus to bonus and base ratio	Agency
Umanath et al. 1996	Proportion of salary in total compensation	Agency
Gerhart and Trevor 1996	Average ratio of bonus pay to base pay	Agency
Roth and O'Donnell 1996	Proportion of compensation as incentives (short-term bonus, long-term bonus, short-term equity plan, long-term equity plan)	Agency
Stroh et al. 1996	Bonus divided by total cash	Agency

<u>Study</u>	<u>Reward mix conceptualisation</u>	<u>Theoretical perspective</u>
Bloom and Milkovich 1998	Ratio of base pay to bonus	Agency
Demougin and Fluet 2001	Strength of incentives in mix relative	Agency
Boyd and Salamin 2001	Ratio of bonus to base pay	Strategic compensation
Miller et al. 2001	Weighted mean of productivity bonus	National culture
Tremblay et al. 2003	Proportion of salary component as a percentage of total average sales compensation	Agency, resource dependency, transaction cost
Kuhn and Yockey 2003	Salary component relative to bonus	
Van der Stede 2003	Percentage of compensation that is performance dependent	Institutional, Hofstede, contingency
Datta et al. 2004	Mix of wage payment between cash and kind payments	
Yanadori and Marler 2006	Ratio of long-term pay to short-term pay	Strategic compensation, agency, resource dependency
Burke and Hseih 2006	Balance of fixed and variable compensation	n/a
Pappas and Flaherty 2006	Percentage of total pay in incentives	Expectancy
Segalla et al. 2006	Fixed versus incentive compensation	Agency, expectancy, Hofstede
Ittner et al. 2007	Salary to cash bonus ratio	Agency
Festing et al. 2007	Fixed pay compared to variable pay	Resource dependency, institutional, Hofstede.
Abbot and De Cieri 2008	Extent to which work-life benefits are included in reward mix	Strategic choice, stakeholder, resource based view

Table 2-1 - Summary of reward mix measures used in employee reward mix research

This shows that the dominant area of interest for employee level research on reward mix is the relationship between fixed and variable elements in the mix, generally defined with regard to base salary and incentive payments both short- and long-term. Festing et al. justified this focus as “the decision about variable and/or fixed pay is the starting point which guides all the other decisions” (2007: 122). Further examination shows that conceptualisation of reward mix is dominated by an examination of cash compensation not total compensation, nor wider total reward. Benefits and relational returns are generally excluded. Some studies have extended the definition to include some benefits and even relational elements in theoretical discussions of reward mix, but the use of these definitions in empirical research designs is limited. For example, Werner and Tosi defined reward mix as “the way that firms orchestrate different components of pay, such as base pay, bonuses and incentives, and benefits, so that they are effective, motivational and control mechanisms with which to achieve different organisational performance objectives” (1995: 1672). However, they then measured mix as the ratio of bonus to total cash compensation in their empirical research on the effects of ownership on reward mix. Balkin and Bannister, in their examination of how pay mix is influenced by different employee groups who are deemed to hold critical positions, defined mix as “the various forms an employee’s earnings may take as well as the proportion of earnings that come from each pay form” (1993: 139). They went on to define pay in three ways. First, salary or payment for time spent working, second, pay incentives or pay contingent on performance, and finally benefits, defined as rewards pertaining to membership of the organisational group. Despite this more holistic definition encapsulating more elements of reward, their work only goes on to examine

the cash-based elements of compensation, i.e. salary and pay incentives, thus missing out a significant element of their definition.

Others note the weakness of excluding benefits from research on reward mix. For example, Ittner et al. (2007), in their study of agency influences on the base salary to cash bonus mix in member-owned medical practices, noted how their exclusion of other direct and indirect rewards such as pensions and insurances limited the usefulness of their results. Miller et al. (2001) did examine fixed, variable and benefit components of reward mix, but the focus of this work was on one specific outcome (turnover) of the levels of each of these reward components, not determinants of their mix, and was also set in a very specific situation – the study of American-owned manufacturing plants operating in Mexico.

Studies of the cash compensation to benefits mix in the form of ‘kind’ payments have been carried out in the agrarian sector. Kind payments are in line with Milkovich and Newman’s (2008) definition of allowances, as they include the provision of goods in return for labour as opposed to cash payment and include shelter, insurance, water, meals and outputs of whatever is being produced, such as food (Datta et al., 2004). However, given the specificity of the research scenario, subsistence reward and developing economies, the wider applicability of their results to developed economies could be questioned. Ippolito (1987) also examined a wider definition – the proportion of pensions in the overall mix measured through assessment of the capital loss that would occur if an employee quit an organisation – in his investigation of why US federal workers’ turnover was lower than in other sectors. However, this study is also focused on the very specific element of cash compensation to benefits mix in the form

of defined benefit pensions, rather than the overall reward mix decision and the range of components that we have defined in this mix, so again its wider applicability may be limited.

Others have called for reward mix to be defined even more widely to encompass more relational elements of reward (Milkovich and Newman, 2008). Gerhart and Milkovich, in their review of the state of employee compensation research, stated that

In structuring monetary compensation, decisions concerning the mix between direct pay and benefits are important. But, at an even more general level, organizations face a choice between allocating resources to pay versus other potential rewards / returns, such as improved supervision, participation, working conditions, advancement opportunities, job design, training and so forth (1992: 551).

They add that, given the increase in the proportion of compensation provided through benefits, “it is less and less correct to equate direct pay with total monetary compensation” (1992: 484). Further, Bloom and Milkovich (1996) suggest that research needs to shift its focus away from examination of the single one-for-one exchange, to examination of the wider return as a whole, given that meaning is derived from the whole and interactions with it. With respect to benefits, even the terminology often used by researchers gives us some perspective on the significance they give to benefits in total compensation constructs, often referring to them as ‘fringe benefits’ (e.g. Tremblay et al., 2003). Given the proportion of overall reward coming from benefit items and the significant interest practitioners have in this area (Deadrick and Gibson, 2007) defining benefits as ‘fringe’ appears inappropriate.

The wider definition of reward, although not really applied in academic research, is in line with recent practitioner interest in an extended reward definition often termed ‘total reward’ (Perkins and White, 2008; Medcof and Rumpel, 2007; World at Work, 2007; Gross and Friedman, 2004; Poster and Scannella, 2001).

The need to shift research from solely focussing on pay to other components making up the overall reward mix led Gerhart and Rynes to conclude that

Simultaneous consideration of direct pay, benefits, non monetary rewards and sanctions was required when considering reward rather than the focus on the much tighter area of pay or the single program approach (e.g. review of employee share ownership) which had been adopted to date. (2003: 259).

The way in which the phenomenon under study is conceptualised will influence the overall results and any conclusions that are drawn as a result (Kuhn, 1962). It is therefore important in using the results in practice that the definition applied reflects reality and practitioner understanding of the term.

Table 2-1 also shows that a consensus on definition is not present even when the studies are using the same theoretical perspective. This is most apparent for agency theory, the most prevalent perspective for examining reward mix (Eisenhardt, 1988; Shaw et al., 2000; Gomez-Mejia and Balkin, 1992), which has seen mix conceptualised in relation to short- and long-term bonuses, base pay, total cash and total compensation. None of the employee agency theory studies record in their papers having spent significant time with practitioners to understand what reward mix means to them and how this translates into RMD ahead of their generally quantitative assessment of the relationships between

elements of the mix and other variables. One notable exception to this was Eisenhardt's (1988) study of retail sales operations which included some interviews of store owners, albeit the focus being on RMD rather than conceptualisation. It may be that there is a range of classifications used by practitioners and examination of a range of conceptualisations is therefore appropriate, or it may be that there is a dominant paradigm and future studies should focus on that definition.

To conclude, there is limited agreement between studies as to a single definition of reward mix, even when using the same theoretical perspective to examine the issue. Research on reward focuses largely on monetary rewards, particularly the cash compensation elements and, with respect to reward mix, has a significant emphasis on base pay and incentives. Few studies combine all elements of reward mix, despite calls for compensation researchers to look at reward more holistically and human resource management research stressing the importance of grouping HR practices to reflect the organisation's overall employment philosophy (Storey, 2007).

2.3 Theoretical perspectives

Whetten (2002) identified that scholarly theory (as opposed to ordinary explanatory theory) should be developed to improve enquiry. In relation to compensation theory, Gerhart and Rynes supported this when they concluded that there was the need for a "broader process of developing careful and well-reasoned theory" (2003: 263). A wide range of theoretical frameworks has been applied to gain understanding of various aspects of reward management (Perkins and White, 2008). Given this, understanding which theories are relevant to actual practice is important from the perspective of both academics and practitioners in directing organisational policy and future research.

Kessler (2001) noted that reward research has been influenced by theoretical development from a range of disciplines. However, over 30 years ago Mahoney stated that no “comprehensive theory of employee compensation exists at present. Rather, there exists a number of segmented theories or models of compensation” (1979). In the last 30 years, we have added further to this collection of ‘segmented’ theories. Bloom and Milkovich (1996) identified 14 different theoretical perspectives that had been used to assess reward determination, with a further eleven theories focussing on the effects of compensation on outcomes. A more recent review of the theoretical foundations of studies of executive compensation identified an additional nine theoretical approaches taking the total to 34 (Baeten, 2008). Therefore, although significant reward determination research has been carried out, we know little about why reward strategy decisions are taken as there is no consensus emerging from all the work (Gerhart and Rynes, 2003). This may be an accurate reflection of reality with the area of reward mix decision making being particularly complex, and as a result each theory adding insight to this complex issue. Alternatively, it may be that after all this research, we actually know very little. Convergence around a smaller number of theoretical perspectives might therefore prove helpful in directing future research (Pfeffer, 1993). Gerhart and Milkovich (1992) noted that we should be looking to adapt the range of theories that have emerged to improve our knowledge of reward systems. Clearly, some simplification is required and categorising reward theories may help.

Bloom and Milkovich (1996) identified that there are two types of reward theories. First, those that treat reward as the dependent variable. These studies aim to help us understand the determinants of reward. For example, studies applying institutional

theory are looking at the influence isomorphic pressures have on the final reward approach that organisations adopt. Second, those that are interested in the effect that different reward policies have on individual and organisational outcomes. These treat reward as the independent variable. For example, theories that would fall into this area include the range of motivation theories (e.g. expectancy, goal setting, equity), pay satisfaction theory and contingency theory, all of which examine the transmission mechanism between elements of reward strategies and specific outcomes (Bloom and Milkovich, 1996).

Reward theories can be categorised further into those that are looking at organisational policy level decisions on reward that apply across the whole organisation and those that consider the individual level reward decision⁴ (Werner and Ward, 2004). Given that reward policy decisions are organisational processes, the correct unit of analysis for this review would appear to be the organisation (Barringer and Milkovich, 1996), excluding any theoretical perspectives where the unit of analysis is not organisational. Therefore, theories focussing on individual level reward determination can be excluded from this review. Within these bounds, a review of the literature indicates four theoretical perspectives have been used to understand RMD at an organisational level – agency theory, transaction cost theory, institutional theory and resource dependency theory⁵.

However, evidence for the transaction cost perspective is relatively weak (John and Weitz, 1989). Anderson (1985) applied a transaction cost approach to gain insight into

⁴ Individual level theories include human capital theory and justice based theories.

⁵ A number of other theoretical perspectives have been used to examine reward policy decisions, e.g. efficiency wage theory or labour market theories. However, these other perspectives were not selected for review as they typically focus on what level to reward employees rather than RMD.

when salary or incentives might be optimal in the reward package. The research concluded that there was limited explanatory power in the framework for explaining mix decisions (with the results replicated by John and Weitz (1989)). Tremblay et al. (2003) in their investigation of sales reward strategy, used agency, resource dependency and transaction cost theories to examine the proportion of salary in sales compensation. They also found that the transaction cost approach provided little explanatory power. For example, they discovered that the relationship between career planning, level of education and training, and compensation strategy was very weak. All the authors suggested agency theory as a more effective explanatory framework, with its emphasis on matters of both control and motivation. Therefore the transaction cost approach is not adopted in this review.

A range of motivation theories have also been used to provide insights into what elements of reward cause changes in the behaviour of individuals and, from this, the effect different elements of the mix choice may have. Although motivation theories are not the focus of the literature review, due to their emphasis on both compensation as the independent variable and the individual, they will be discussed in the context of the other theoretical perspectives examined and the influence beliefs about motivation may have on organisational policy making.

What follows is an outline and assessment of the three theoretical perspectives chosen. In outlining each theoretical perspective, a review is carried out of the basic theory and the key assumptions which underlie it. Following this, empirical research is examined to identify what this tells us about its explanatory power in the area of RMD and any

criticisms that can be made. This then leads to conclusions on the theoretical perspectives usefulness in understanding how reward mix decisions are taken.

2.3.1 Agency theory

2.3.1.1 Introduction

Agency theory examines the relationship between owners of businesses, or principals, and employees, or agents. It proposes that both parties to the employment exchange look to achieve the most favourable exchange possible for their interests and will act accordingly. According to the theory reward mix, the form of the extent to which reward is variable and therefore at risk, is a significant control mechanism used by principals to ensure that agents act in the owners' best interests. Agency theory has been used to explain phenomena across a wide range of disciplines such as accounting, economics, sociology, organisation behaviour, marketing and political science (Eisenhardt, 1989a). A significant part of this work has been focused on the employment context including the reward mix relationship between fixed and variable pay (Gerhart and Milkovich, 1990; Bloom and Milkovich, 1998; Segalla et al., 2006; Fernandez-Alles et al., 2006).

Underpinning much of the agency theory research is the assumption that work is delegated within organisations from one party, the principal, to another, the agent (Jensen and Meckling, 1976). This led Jensen and Meckling to define the agency relationship as “a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent” (1976: 308). The issue is not solely about owners of organisations and executives who run organisations, but applies

throughout organisations as management delegates to subordinates. This separation of work and the resulting delegation continues throughout the hierarchy of the organisation. Despite this, most of the reward research, using agency theory as its theoretical base, has been done on the compensation of top executives in organisations, usually the CEO, with employee reward mix less well studied (Bloom and Milkovich, 1998; Stroh et al., 1996; Trevor, 2008). Fama and Jensen (1983) and Stiglitz (1975) outlined how the agency approach can be applied below the top level of management. However, Baker et al. (1988) and Tosi and Werner (1995) showed that this was not a straightforward relationship down the hierarchy. They concluded that when agency theory prescriptions around alignment of reward were strong at the top of the organisation, it weakened at each level of hierarchy examined. However, despite this concern, studies where the extension of agency theory beyond executive reward have been made include sales clerks (Eisenhardt, 1988), gain sharing (Welbourne and Meija, 1995), national culture (Segalla et al., 2006) and faculty pay (Gomez-Mejia and Balkin, 1992).

2.3.1.2 Agency problem

At the heart of agency theory is the core assumption that the parties to the employment exchange, employees or agents, and owners or principals, have different goals and that these goals conflict with each other (Jensen and Meckling, 1976). Owners are assumed to be looking to maximise profit through their investment in the organisation, whilst employees are assumed to wish to minimise their effort for a given return. Therefore, it is proposed that the agent will not always act in the best interests of the principal and vice versa (Jensen and Meckling, 1976).

Alongside these different interests, the theory assumes that the principal and agent will have different risk preferences reflecting their particular circumstances. The overall level of risk aversion of the agent will be higher than that of the principal. By the nature of the employment they have with the organisation, agents are not able to diversify their risk as either all or a significant part of their income comes from this employment. This directly contrasts with the principals' position and the ability this gives them to diversify their investments across a range of assets and thus manage risk more effectively. These differences in risk preference influence both the principal's and agent's behaviour (Eisenhardt, 1989a).

Finally, principals are also assumed to face the problem of information asymmetry. As they are inevitably removed from the day-to-day operation and knowledge of the business operation, it is difficult and expensive for them to gain complete knowledge of what the agent is doing. They will have limited information about the ability of, and decisions made by, the agent (Eisenhardt, 1989a). This presents the problem of ensuring, from the principals' perspective, that employees are aligned with the principals' interests. The principals can manage this through two means: through developing appropriate incentives for the employee to act in the principals' interests and by incurring monitoring costs designed to manage the shirking and self-interested behaviour of the employee (Jensen and Meckling, 1976).

2.3.1.3 Managing the agency problem - incentives and monitoring

Agency theory provides significant insight into how goal incongruence, differing risk preferences and information asymmetry can be managed. At the centre of managing these issues is the organisation's reward mix, particularly around the balance of fixed

and variable reward making up total compensation, laid out in the contract between the principal and employee. Wiseman et al. outlined the importance of aligning agents' reward to outcomes that the principal values to "create a common fate" (2000: 312). A higher proportion of variable pay in the overall reward mix is intended to achieve this common fate by tying employees' interests more tightly to that of the firm (Gomez-Mejia and Balkin, 1992; Delvey, 1999).

How organisations achieve the 'common fate' will depend on the type of contracting arrangement they put in place and the reward mix arrangements that flow from this. There are outcome based contracts, linking agents' reward to an outcome desired by the owner of the organisation, e.g. profits or total shareholder return. This is clearly desirable from the principal's point of view as it aligns reward between principal and agent. Burke and Hsieh (2006) noted the importance, from a financial management point of view, of reward costs varying with revenues which outcome-based contracts supported. Burke and Terry (2004) illustrated conceptually how outcome-based contracts, with their emphasis on variable reward, reduce fixed costs and therefore the firm's breakeven point which, in turn, they argued translated into increased profit.

However, the use of outcome-based contracts may be less appealing to the agent as outcome measures of this type are not fully in the agent's control (Eisenhardt, 1989a). For example, an organisation's share price, a key component of total shareholder return, will move, not only due to the individual performance of the organisation, but also due to wider general market risk arising from moves in the whole market independent of the individual organisation's performance (Hull, 2009). This broader, general market risk can come from numerous sources, such as changes in government policy and wider

economic conditions influencing general investor sentiment (Hull, 2009). Burke and Hsieh (2006) also note that this approach to determining the reward mix does not account for attraction and retention issues which are likely to occur with a shift to a more outcome-based and variable-orientated reward contract. The transferring of risk, through outcome-based contracts to agents, has a cost as it is likely that the agent will require some form of risk premium, such as a higher level of total reward, to compensate for the increased risk that they are bearing (Eisenhardt, 1989a). The level of risk premium will reflect the increased uncertainty of result which comes from outcome-based contracts, given that the agent cannot solely influence the outcome (Eisenhardt, 1989a).

This risk premium was examined by Tremblay et al. (2003) who showed, in the context of sales commission policies, that the level of business uncertainty which an organisation faces, and therefore the extent to which the ultimate outcome is outside the direct control of the agent, will influence the level of risk premium required to compensate the agent. Where there is high business uncertainty, and therefore a higher risk of agent effort not translating to sales, then higher commissions when sales do result will be required to compensate the agent.

The level of uncertainty has also been theorised as being related to not only reward level (Tremblay et al., 2003), but also reward mix (Gerhart and Trevor, 1996; Balkin and Gomez-Mejia, 1987; Gomez-Mejia and Balkin, 1992). Agency theory predicts that high levels of business uncertainty lead to higher proportions of fixed pay. This is attributed to the fact that the risk premium, required to compensate employees for uncertainty about future compensation flows and lowered employment security,

becomes prohibitively expensive (Bloom and Milkovich, 1998). However, empirical research has not shown this to be the case, with organisations in fast-paced uncertain markets looking for and adopting more flexible approaches to compensation to manage cash flow and attract required skills (Balkin and Gomez-Mejia, 1987; Stroh et al., 1996; Balkin and Gomez-Mejia, 1990). For example, Gomez Mejia carried out a series of studies (Balkin and Gomez-Mejia, 1987; Gomez-Mejia, 1992; Balkin and Gomez-Mejia, 1990) and concluded that reward mix was weighted more towards variable elements in industries with high levels of technology intensity and where there were higher levels of environmental uncertainty as firms look to ‘share’ the risk with employees by aligning payouts to firm profitability, i.e. the propensity of a firm to risk share is contingent on certain contextual factors such as technological intensity and economic uncertainty.

Another form of contract that is available to organisations is a behaviour-based contract which links agent’s reward to specific behaviours or actions delivered by the agent regardless of their ultimate effect on the return accruing to the principal. This may be more appealing to the agent as it is solely within his/her control, but may have less appeal to the principal given the monitoring costs associated with the more subjective-based measurement and the fact that these behaviours are not guaranteed to deliver the principals’ goal – profit maximisation and total shareholder return (Eisenhardt, 1989a). The decision around which form of contract to adopt is a key one for an organisation, given the implications that it appears to have for how reward is distributed between fixed and variable reward elements.

The extent to which outcome-based contracts are used and the implications this has for the decision on fixed versus variable reward, may also be related to how easily employees can be monitored in their roles. In environments where monitoring is relatively low cost, behaviourally-based contracts would be applied, as they eliminate the need for risk premium payments (Conlon and Parks, 1990). Consequently, compensation can be delivered in the form of fixed rewards, such as salary, and also other forms of fixed reward such as those contained in the benefits package. Moreover, employees have been shown to prefer fixed returns, given the certainty and security these bring; this will generally increase overall employee satisfaction with their reward mix (Eisenhardt, 1989a; Baiman, 1990). However, where there are relatively high costs associated with monitoring employee behaviour, due say to remote working or the relative complexity of the role, an outcome-based contract is more likely to be employed. Incentive payments would then tend to form a higher proportion of the overall reward mix (Gerhart and Rynes, 2003; Eisenhardt, 1989a). The cost of monitoring employees will be a function of the complexity of the activity being performed and the resulting span of control that management require to monitor the behaviour. Where larger spans of control are possible, whilst still allowing appropriate monitoring of behaviour, costs will be lower.

Where the task is highly programmable, monitoring costs will be lower as larger spans of control will be manageable and therefore higher proportions of fixed reward can be offered. However, where significant amount of initiative and discretion are employed then behaviour monitoring will be more problematic and it is likely that outcome-based contracts will be more dominant to manage this (Tremblay et al., 2003; Eisenhardt,

1989a; Stroh et al., 1996; Gerhart and Milkovich, 1990). For example, Eisenhardt (1988) showed that the relationship between span of control and the proportion of fixed pay in the overall reward mix was related. The higher the span of control and therefore, by inference, the harder it is for the manager to monitor behaviour, then the larger the variable outcome-based component of the mix. Examination of sales teams has shown that, given that they operate autonomously in the field away from direct management observation, direct monitoring of their performance can be problematic (Tremblay et al., 2003; John and Weitz, 1989). This is often cited as the reason why outcome-based contracts are more suitable for this group and reward mix proportions tend to be weighted towards a higher percentage of variable pay.

Consequently, when assessing which type of contract to use, the principal will need to weigh up the cost of acquiring more information on the agent's action which would allow a more behaviour-based approach at lower cost (given it eliminates the need for a risk premium to be paid) and compare this to the lower information costs built into an outcome-based contract approach, but the higher employment cost due to the risk premium. Conlon and Parks (1990) found, in their experiment on the effects of reward traditions and employee monitoring on reward mix, that "when the costs of directly monitoring an individual's actions exceed the costs of administering incentives based on performance outcomes, performance contingent incentives are a preferred method of control" (1990: 604). They added that "the trend towards contingent pay suggests that some organizations are discovering that incentives may be more efficient than hierarchy" (1990: 604).

In summary, under agency theory, incentives are provided to try and align employee and employers interests. “Paying individuals to do X causes them to do X.” (Prendergast, 1999: 11). The main barrier to establishing contracts in this way is the additional cost employers will incur as employees require compensating for the higher risk that contracts of this type imply. The extent to which it is rational to pay this premium will depend on the ease with which the roles can be monitored by management and how the cost of monitoring compares with the risk premium that will be payable.

2.3.1.4 Agency research

Reviews by Eisenhardt (1989a), Zajac and Westphal (1995), Prendergast (1999) and Miller and Whitford (2007) have indicated that the large body of research on agency theory generally supports its predictions that organisations should use both incentives and monitoring activity to control managers and employees, and that incentives and monitoring are considered as substitutes under various scenarios.

A range of studies has examined whether higher proportions of incentives in the reward mix improve performance. Lazear (1986) showed a 36% increase in worker productivity in the auto windshield installation sector when they shifted from fixed reward to piece rates. Reflecting agency theory prediction that a risk premium would also have to be paid, overall wages increased by 12%. In the same study he showed that payment can have both incentive and attraction effects, with better workers attracted to contracts that have higher levels of pay for performance. Consequently, from this economic perspective, contracts should be designed not just to induce increased effort, as agency theory contends, but also to attract a higher quality of worker to the

organisation. Paarsch and Shearer (2000) carried out a similar study in the British Columbian tree planting industry. They found increases in productivity of up to 22%. Both studies collected individual, as opposed to organisational, performance data, which are more likely to be influenced by other uncontrollable factors, and therefore make their results more convincing. Other studies have examined aggregate performance effects arising from the introduction of variable reward schemes. For example, in the retail sales sector, Banker et al. (1996) examined piece rate effects and found store changes in productivity of 9-14%. Clearly, a number of studies have found evidence of incentive effects.

2.3.1.5 Criticisms

Agency research offers only a partial insight and can be criticised on a number of fronts. Studies have typically focused on sectors and roles where measurement of performance is relatively straightforward on an outcome-based basis (e.g. piece rates, sales performance and overall profitability when using CEOs as the target role). That limits the usefulness of the approach in understanding roles and sectors where behavioural contracts are much more common due to outcome measurement difficulties. Prendergast (1999) notes that a cautious interpretation of the results would also take into account whether the activities performed in their own right carry any intrinsic motivation which, according to Deci and Ryan (1985) would be diminished by explicit monetary payment. Tosi et al. (1997) criticised the firm-level econometric approach to testing agency theory which required proxy variables to be developed based on the availability of data. They contended that the usefulness of these studies is limited by concerns over construct validity, i.e. Does the variable actually measure what it claims to measure?, and the correlation techniques applied could result in reverse causality.

Prendergast also notes the problem with “identification difficulties” (1999: 11), i.e. although the theory often provides a good explanation, the outcomes observed could also be explained by other theories. Given a number of these concerns, Tosi et al. (1997) applied a laboratory approach in their research. They found that incentive alignment was more effective than increased monitoring in aligning the agents’ behaviour to that of the principal, i.e. substituting monitoring for incentives could lead to a less optimal position from the principals’ perspective.

Miller and Whitford asked the question that in the light of this support for the use of incentives to align outcomes “Why are incentives not used more often than they are?”, noting that “even in those cases where the agent’s performance can be directly linked to compensation, corporations often still choose to use contingency-free compensation schemes” (2007: 214). They concluded, through theoretical review, that this is driven by self-interested principals accepting lower efficiency “out of a concern for the principal’s own profit” (2007: 215). They outline that there are a number of theoretical cases where the incentive levels required to induce effort are more costly due to the risk premium required being significantly higher than the resulting increase in profitability. A degree of inefficiency is profit maximising. Consequently, “most organisations, and in particular public agencies, rely very little on pure incentive contracts and instead use coercive mechanisms of monitoring and sanctioning” (Miller and Whitford, 2007: 213).

Alternative views have been offered to explain the reward mix relationship based on perceived problems with a number of the assumptions underpinning agency theory. The agency model has been criticised for its focus on the contract as the pivotal mechanism for control which ignores political and environmental elements of the agency

relationship (Eisenhardt, 1989a; Fernandez-Alles et al., 2006). The contract specification cannot capture all relevant dimensions such as uncertainty, information shortages, and the dynamic and political nature of the relationship (Tosi et al., 1997). Also, the balance of relationships may not be as assumed in agency theory. O'Reilly et al. (1988) contend that contracts are influenced more by the manager-subordinate relationship than by an overarching and dominant responsibility to the organisation's owners. The information asymmetry may also influence the contract, with employees able to use their information advantage to negotiate a contractual position that better manages risk from their personal perspective.

These problems have led scholars to suggest that research should look to extend its investigation of reward mix beyond an agency perspective. For example, strategic compensation research has shown that organisational strategies around how to reward employees have revolved around two areas: first, industry characteristics such as product demand and technological focus (Gerhart and Milkovich, 1990; Baker et al., 1988) and second the characteristics of the specific organisation, in particular the business strategy (Gomez-Mejia and Balkin, 1992; Rajagopalan, 1996), such as diversification (Gomez-Mejia, 1992; Kerr, 1985) and life cycle stage (Chen and Hsieh, 2005). However, Stroh et al. (1996), in their application of agency theory, noted that middle managers were removed from these industry and organisational factors and therefore those factors may not be relevant. They concluded that the level of turbulence an organisation is facing, perhaps brought about by restructuring or downsizing, would also influence reward mix. Turbulent environments require dynamism and flexibility in employees. Consequently, it is more difficult to lay down the exact behaviours required

of employees, leading to more outcome-orientated contracts and therefore higher proportions of variable pay in the mix (Stroh et al., 1996). Further, they speculate that this transfer of risk was also due to organisations using variable reward strategies to manage the additional variability in revenue and profitability that they are facing at this point in their history.

Eisenhardt (1988) also showed that organisational tenure was related to the proportion of reward which was variable, with longer tenure leading to lower proportions of variable reward. This was inferred to be down to the socialisation that occurs in longer term relationships and the resulting tendency for the basis of a contract between employee and manager to be behavioural. This socialisation view was supported by O'Reilly et al. (1988), Jensen and Murphy (1990), Bruce et al. (2005) and Aguilera and Jackson (2003), albeit through executive level research, who identified that the weak relationship between CEO pay and organisational performance was attributable to norms in place created by external groups, e.g. regulators, consumer groups and unions.

Eisenhardt (1988) therefore concludes that agency theory, with its basis in operational efficiency, suggests a range of possible efficient positions around combinations of job programmability, managerial spans of control and fixed to variable rewards, e.g. high programmed jobs leading to a higher proportion of fixed reward and less programmed jobs with higher spans of control leading to a higher proportion of commission payment in the overall mix. All outcomes are efficient according to theory. She then notes that which choice an organisation will make could be influenced by strategic considerations or by dominant institutional factors, as suggested by institutional theory. Her research leads her to conclude that an institutional determination of final reward mix choice was

most prominent (Eisenhardt, 1988). This was supported by Roth and O'Donnell (1996) who, in the context of foreign subsidiaries reward mix, found that agency theory could not explain all reward mix elements. They noted that the interactions between home country or firm-specific practices and host and local market norms were complex, and could perhaps be better explained by introducing an institutional theory perspective to the problem. Werner and Tosi (1995) found that manager-controlled firms put more employees' pay at risk than owner-controlled firms. This was contrary to their hypothesis which, they argued, was possibly down to political processes in play in these firms with manager-controlled firms having bonus schemes with terms more advantageous to internal managers with respect to performance targets set. However, they noted that their use of one consulting firm's data set may have led to conformity in the data around the consulting practices of that particular firm.

One weakness with agency theory is its inability to take into account political forces both within and outside the organisation. These forces are not responsive to evaluation by the economic methodology underpinning agency theory and the statistical testing that has been used to assess its applicability (Jensen and Murphy, 1990; Barringer and Milkovich, 1998).

A further criticism questions the agency theory assumption of a conflict of interest between principal and agent and consequently whether there is a need for the control mechanism of incentive pay (Deckop et al., 1999). Whilst widely adopted, not everyone subscribes to this assumption. For example Ouchi (1980) contended that goal incongruence actually varied across the workforce. Where alignment was strong, Deckop et al. (1999) believed there was little need for incentive pay as the "clan-form"

(1999: 421) would ensure behaviour consistent with organisational goals. They showed how employees with low organisational commitment were even less likely to carry out extra-role activities when the performance-related pay link was significant. However, they also found in employees where commitment was higher, the extent of performance-related pay was not an influence on their likelihood to carry out organisational citizenship behaviour. Blau (1964) also argued that the social exchange as well as the economic exchange was significant, with trust allowing temporary misalignments of pure self-interest between the parties to be accommodated.

A final criticism comes from the fact that agency theory has generally been applied solely to consideration of elements of cash compensation (Barringer and Milkovich, 1998). However, it could be extended to include other elements of reward with benefits considered as a fixed element. This approach has its drawbacks, given the deferred nature of certain benefits such as defined benefit pension payments and the rising value (i.e. variability) of this benefit as retirement approaches. Shepard et al. (1996) also showed the incentive effects that flexible work has where workers would work hard enough not to lose this valued part of the mix for fear of losing it through being dismissed.

2.3.1.6 Agency and the role of motivation theory

Underpinning agency theory is the premise that financially-based rewards in different forms and combinations will influence employee behaviour. Research suggests that how firms choose to reward their employees may influence performance in two distinctive ways – sorting effects (Schneider, 1987) and incentive effects (Lazear, 1986; 1999). Sorting effects work through the influence the reward mix has on those that join

(Cable and Judge, 1994) and stay (Harrison et al., 1996; Trevor et al., 1997) with the organisation, through a relationship between the attributes of those that apply and stay and work in an organisation, and the reward system and mix in place. Whereas incentive effects work solely on those that are currently employed by the organisation and are felt to influence how hard someone works towards achieving the rewards based on the attractiveness of the reward and the likelihood of this reward being achieved (Vroom, 1964).

Looking through the two different perspectives of psychology and economics, we can see that economists generally tend to assume that pay has stronger motivational effects than psychologists (hence the importance of incentives in agency theory). Rottenberg (1956) outlines that the main reasons for this are largely pragmatic, involving the fact that money is much more easily quantifiable than other less tangible elements which have been claimed to be motivating, such as security and management. Rottenberg also contends that people will always prefer more money to less, which is not the case for other job attributes such as, say, responsibility or travel. Finally, although economists do not strictly believe that money is the only motivator (Lazear, 1999), models based on money continue to dominate because they give “tolerably good results.....Everywhere there is massive aggregate evidence that people move from low income areas to high.... not in the opposite direction” (Rottenberg, 1956: 188).

Psychologists are less clear. Lawler (1971) concludes that as money plays such a significant role in meeting a large number of other needs such as security and status type needs, then it must be significant. Three traditional, and often quoted, psychological theories question the dominance of money as a motivator: Maslow’s

hierarchy of needs theory (Maslow, 1943), Herzberg's hygiene theory (Herzberg, 1968) and Deci and Ryan's cognitive evaluation theory (Deci and Ryan, 1985). These theories, despite gaining widespread acceptance in practitioner textbooks, have been criticised by other academics. They contend that, although intuitively appealing, the findings have not been backed up by sufficiently robust research findings with the original experiments not being designed for the wider significance for which they have been taken and as a result were methodologically flawed (Lawler, 1971; Bowey and Thorpe, 2000). Given this debate, the effect the use of variable pay in the reward mix has on agent behaviour, a key tenet of agency theory, may be questioned.

2.3.1.7 Conclusions

Agency theory has emerged as an important theoretical explanation of RMD. The theory aims to "explain the choices principals make about the form and structure of compensation systems and how those choices are related to the principal's outcomes" (Bloom and Milkovich, 1998). The theory tells us about the fixed to variable reward relationship, but does not tell us about wider total compensation, or total reward. For this we need to look at other theories for insight. It has also been suggested that the approach overemphasises the efficiency and rational drivers of decision making in reward mix choice and underestimates the institutional and political power-related pressures that may be relevant to organisations (Barringer and Milkovich, 1998; Bartol and Locke, 2000). Eisenhardt concluded that agency theory "is an empirically valid perspective, particularly when coupled with complementary perspectives" (1989a: 57), and Barringer and Milkovich stated that "agency theory presents a partial view of the world thatignores a good bit of complexity of organizations" (1998: 71). Further

examination of these “complementary perspectives” is important to understand the role they may play in RMD.

2.3.2 Institutional theory

2.3.2.1 Introduction

The management literature has recognised the significance of institutional factors on reward strategy decision making and specifically the decision of reward mix (Gerhart and Rynes, 2003). This theoretical perspective proposes that coercive, mimetic and normative institutional forces create significant pressures on firms to be similar in how they operate in their search for legitimacy (DiMaggio and Powell, 1991). The extent to which these constraints operate for each firm will influence how much freedom of choice the firm actually has in its operation (Carpenter and Wade, 2002).

Institutional theory helps us to understand the constraints organisations are under to conform and specifically to mimic the reward mix of other firms (Eisenhardt, 1988; Conlon and Parks, 1990; Crystal, 1991). This theoretical approach explicitly recognises the importance of context and external environment and their role in shaping this behaviour (Marsden and Belfield, 2010). These isomorphic pressures will now be examined and empirical evidence of their existence in the reward mix area discussed.

2.3.2.2 Isomorphic constraints

Isomorphism is the constraining pressure that forces one element in the population facing similar environmental characteristics to behave like the others. In their seminal work on institutional pressures, which they proposed acted like an “Iron Cage” (DiMaggio and Powell, 1991: 64) on organisations, Di Maggio and Powell note that the traditional strategic view of organisations competing for resources and customers is

incomplete. They are also competing for both social and economic legitimacy in the activities they perform. Suchman defined legitimacy as “a generalised perception or assumption that the actions of an entity are desirable, proper or appropriate within some socially constructed system of norms, values, beliefs and definitions” (1995: 574). DiMaggio and Powell (1991) identify three mechanisms by which the isomorphism pervades organisational decisions – coercive, mimetic and normative pressures – each of which will be discussed, in turn, in the context of reward mix decisions.

2.3.2.3 Coercive isomorphism

Coercive isomorphism “results from both formal and informal pressures exerted on organizations by other organizations upon which they are dependent” (DiMaggio and Powell, 1991: 67). These coercive pressures can take a number of forms. The pressure could be legal, through laws and regulations set by government or bodies acting on their behalf, such as tax authorities. The volume of employment legislation in the UK has significantly increased since 1970 with, for example, equal pay rights between men and women, compensation for loss of job, minimum wage rights, maternity and paternity rights, hours of work and holiday entitlements, share ownership and pension legislation having been introduced (Perkins and White, 2008). Given that a number of these are components of our wider definition of reward mix, then constraints on how they are managed are likely to influence the overall mix provided to employees. Perkins and White felt that the legal context was so significant that “while employers may wish as far as possible to create reward strategies for their own particular circumstances, the starting point will always be what the law allows or requires.” (2008: 67), and given this “a major skill for reward specialists is being able to implement strategy within the constraints of the law” (2008: 94).

Social goals of government, e.g. the family and retirement, may be an institutional influence, shifting the balance to higher proportions of benefits in the overall reward mix if organisations look to hold costs stable while meeting these social pressures. Smith (2000) noted that two government policy changes were the big drivers of benefit provision in the UK. First, was the change in pension legislation in 1975, which allowed employers and employees to contract out of certain elements of the State pension and establish work-based pensions on more favourable terms than had historically been the case. Second, was the repeal of the Truck Act in 1986 which removed the requirement to pay manual workers in cash, paving the way for harmonisation of their packages with that of non-manual staff. More recently, the introduction of pension reforms has looked to influence organisations' behaviour towards employee pension provision through tax breaks which reward the company for providing this element of the reward mix. Politically driven influences on reward mix, through the effect on benefit provision, may mean specific benefits are provided even though they are considered expensive (Festing et al., 2007).

A major role for reward managers during the 1980s and 1990s, as the tax system regarding pay and benefits changed, was the goal of tax efficiency in their reward design, especially benefits scheme choices and the balance between benefits and cash wage payments (Perkins and White, 2008). The significance of tax was emphasised by Long and Scott who concluded that "taxation is a major determinant of the compensation mix" (1982: 218).

Abbot and De Cieri (2008) note a political agenda driving the introduction of work-life provision benefits into the reward mix, operating alongside the business rationale of

improving organisational performance. However, studies have shown significant variation in work-life provision, which may point to a lack of robust social and political institutional pressure in this area (Hyman and Summers, 2004; De Cieri et al., 2005). Abbot and De Cieri (2008), in their examination of the influences on work-life benefit provision, conclude that work-life balance provision is attributable to conscious managerial decision taking. However, they add that this decision is made more difficult by the complex interaction of stakeholders, including government, and the pressure they put on firms.

Oliver (1991) identifies that organisations will look to actively manage these regulatory and government pressures. This will mean organisations may take a conscious decision to ignore the requirement through a rational assessment of the consequences of such action. However, this is a relatively extreme position. The extent of the coercive power that organisations face is likely to depend on the power they have over others by the nature of their control of critical resources. For example, in a financial services context, any requirements laid down by the FSA on how firms should manage their compensation structures, such as that laid out in their 'Dear CEO' letter (Sants, 2008), is likely to coerce change across the sector as the FSA controls a critical resource to all financial services organisations – their authorisation to transact in that market.

In the context of their work on resource dependency, Pfeffer and Salancik (2003) noted how typically politically driven coercive forces will be applied across the board and consequently are likely to restrict adaptability and flexibility, as is the case with the introduction of personal accounts in the UK which applies to all organisations equally. This will automatically influence reward mix in those institutions where pensions are

not currently provided, or more significantly, there is concern that organisations currently offering more than the minimum contribution level will lower their contribution to this coerced level (Department for Work and Pensions, 2006). This change will occur irrespective of other characteristics of these organisations which is inconsistent with the contentions of strategic compensation research that organisations should align the overall reward approach to organisational strategic drivers such as organisation life stage, ability to pay and desired workforce characteristics.

However, coercion is not just politically driven (DiMaggio and Powell, 1991). With the increase in the global operation of large conglomerates, it may also come from head office operations setting out restrictive requirements for their subsidiary and branch operations (Van der Stede, 2003). Whilst these policies, HR and otherwise, may be compatible with the parent group's needs and their operation in the home market, they may not be 'efficient' for the subsidiary, given local market conditions, and specifically in relation to reward mix, local labour market conditions. These restrictions could take many forms (Van der Stede, 2003). They may be requirements on budgets available for distribution to employees or restrictions on how payment should be made, i.e. the overall reward mix. For example, group benefit plans are commonplace, given that they are often seen as an element of the reward mix supplied for organisational membership rather than performance related reasons (Perkins and White, 2008).

One such source that may have significant coercive strength is trade unions. Organisations often have no choice over whether to participate in collective bargaining with unions as this is predetermined by a number of factors. Unions (and by default their members) have certain rights in the UK under the Employment Relations Act 1999

to represent the workforce when 40% of employees are union members in the area under consideration (Crown, 1999). Almost two thirds of workforces of more than 500 employees set some pay through collective bargaining (Kersley et al., 2006). However, in the full workforce the number is on the decline down from 70% of workforces employing 25 workers or more in 1984 to 40% in 2004 (Kersley et al., 2006). This masks an increasing trend in the public sector and a significant decline in private sector employees (significantly financial services is down from 49% in 1998 to 35% in 2004 (Kersley et al., 2006)).

With respect to the wider reward mix, unions appear to have a particularly strong effect on certain elements of the reward mix such as holiday entitlement, pensions and sick pay (Forth and Millward, 2000). Budd and Mumford (2004) showed how union representation was related to the extent to which family-friendly policies were in place, such as paid parental leave, job-sharing and childcare provision. Whilst Arrowsmith and Marginson (2011) identified how within the retail banking sector at least the strength of collective bargaining had had some success in limiting variations in base pay and created greater standardisation of variable pay than would have been the case had the union influence not been present. However Arrowsmith et al. (2010) also note in a further paper that bonuses (as opposed to merit pay) are increasingly significant in employee pay and these are beyond the reach of collective bargaining.

Alongside this, the Information and Consultation of Employees Regulations 2004 put in place the requirement for employee consultative bodies to be established when organisations have more than 50 employees (Crown, 2004). The regulations do not give formal rights to employees to be consulted on reward and reward mix, rather a

more general requirement to keep employees informed about the company's activities and decisions likely to lead to substantial changes in employees' contractual relations which could include changes to reward mix. In practice, employers are often willing to allow input on the mix rather than the level of the pay package (Perkins and White, 2008).

As institutional theory has developed, a definition for what constitutes an institution has developed. This has meant institutions being taken as not just explicit and direct pressures such as the coercive constraints just discussed, but less direct pressures on organisations from their surroundings (Marsden and Belfield, 2010; Scott, 2008). This has led to the evolution of theory and research around mimetic and normative isomorphic pressures organisations face. These are now discussed.

2.3.2.4 Mimetic isomorphism

Mimetic behaviour takes the form of organisations adopting approaches and policies that others have adopted (DiMaggio and Powell, 1991). Mimetic behaviour is largely caused by the security that conformity brings – that your policies are at least in line with others (DiMaggio and Powell, 1991). Organisations look to avoid uncertainty and diverging from standard practice introduces a level of uncertainty in comparison to other organisations (Norman et al., 2007). Where there is no clarity around the process by which goals will be achieved and/or goals are ambitious, then it is more likely that organisations will mimic the behaviour of other organisations they perceive to be successful (Norman et al., 2007). The legitimacy this conformity bestows can enhance survival chances in contrast to ecologists' views that mimetic behaviour gives no competitive advantage (DiMaggio and Powell, 1991).

Arrowsmith and Sisson (1999) showed that sectoral mimetic effects were present. They examined reward decision taking following the decline in numbers of collective agreements in the UK in the 1980s. In this context their research investigated whether this decentralisation had led to changes in reward practices in specific sectors, or whether sector influences were still strong and influencing decisions. They showed across the four sectors studied (engineering, printing, health, retail) that differences in institutional arrangements for pay setting (i.e. different degrees of collective versus independent pay setting) did not lead to significantly different outcomes. Where centralised arrangements were no longer in place (engineering and retail) there were still strong sector effects, even after coercive restrictions had been removed. They attributed this to the widespread availability of benchmarking data and its influence on the practices of organisations, which meant the tie provided by centralised collective sectoral bargaining was unnecessary as organisations effectively, through their benchmarking activities, carried out this process of their own free will. This led them to conclude that “employers continue to move like ships in a convoy..... There is an apparent reluctance to embark upon more radical change initiatives which might break the pattern.” (1999: 63). So, although collective bargaining remains significant, with around one third of employees still covered by collective bargaining arrangements, its effect may be less pronounced than might be expected given that, when it is removed, organisational behaviour appears to continue to operate in a collective way. This suggests that organisations may, under certain conditions and without coercive pressure, mimic each other’s approach to RMD leading to similar outcomes. DiMaggio and Powell concluded that “organizations tend to model themselves after similar

organizations in their field that they perceive to be more legitimate or successful” (1991: 70), but it may also be behaviour that has become habitual.

Mimetic pressures would appear to be commonplace in the reward field. The diffusion of policies and approaches may come from a number of sources (DiMaggio and Powell, 1991). First, organisational knowledge may be held by particular individuals and, through turnover, this knowledge may be spread across other organisations. Specifically, employees may be hired because they are valued for this knowledge of wider practice. Reward knowledge is likely to be held by REs. Specific reward specialist recruitment agencies are established (such as TotalRewardCareers and Portfolio CBR) potentially indicating a specialist market in REs and a flow of their expertise across organisations.

Diffusion of standard practice may also occur through the activities of consulting firms and trade associations (DiMaggio and Powell, 1991). Both of these routes for spreading practice would appear likely in the reward field. The use of consultants has been shown to have a legitimising effect (Barkema and Gomez-Mejia, 1998; Main et al., 2008). The reward consulting profession is well established in the UK. Reward consultancy firms (e.g. Towers Watson, Hay Group, Mercer) offer specific reward services including benchmark data provision and reward strategy advice built on their current view of best practice in the profession drawn from their exposure to practice across the organisations which they serve. In their 2008 reward survey, the Chartered Institute of Personnel Development (2008c) found that of those surveyed 32% had used a consultancy service to provide benchmarking data, 47% were supported in job evaluation work and 26% received advice on reward structures. Benchmarking support of this type has been

identified as a key factor assisting the spread of isomorphism (Eisenhardt, 1988; Crystal, 1991).

Specific reward trade and professional bodies are also in place. In the UK, the largest is the Chartered Institute of Personnel Development (CIPD) which operates as the HR profession's overarching professional body. In 2008 the CIPD's annual report indicated that it had 133,000 individual members (CIPD, 2008a). Within its operation it has a specific reward forum for reward professionals. The forum's role is to "engage HR professionals in discussion on recent reward management and planning issues" (CIPD, 2008b). It carries out this role by holding dedicated reward meetings to discuss current issues, facilitating networking among reward professionals, and publishing factsheets and newsletters raising issues of best practice. Alongside this formal professional association other bodies also exist, such as E-Reward⁶ in the UK, or internationally WorldatWork⁷. These have as their remit the provision of information and guidance, training and conferences to spread best practice. Practitioners have also taken it upon themselves to develop semi formal gatherings of those from similar sectors through the establishment of groups, such as the Financial Services Reward Networking Group, with the intention of sharing examples of their practice and benchmarking data⁸.

⁶ E-Reward aims to deliver reward advice and support through its website, electronic newsletters, journals and reports, and conferences.

⁷ Formerly known as the American Compensation Association, WorldatWork is a global human resources association focused on compensation, benefits, work-life and integrated total rewards. It was established in 1955 and now provides a network of more than 30,000 members and professionals in 75 countries.

⁸ The author became aware of such a group when various interviewees in the research indicated that they were members, and subsequently presented the findings of this research to that group.

In the context of these mimetic influences DiMaggio and Powell concluded that “the ubiquity of certain kinds of structural arrangements can more likely be credited to the universality of mimetic processes than to any concrete evidence that the adopted models enhance efficiency” (1991: 70).

2.3.2.5 Normative isomorphism

Finally DiMaggio and Powell raised the existence of normative pressures stemming from “the collective struggle of members of an occupation to define the conditions and methods of their work.....and legitimation for their occupational autonomy” (1991: 70).

The reward profession, like any organisation, is subject to the coercive and mimetic pressures already discussed. Di Maggio and Powell (1991) note isomorphism being driven in professions through the arrangement of practice into codified principles and accepted standards, e.g. the ‘New Pay’ prescriptions that pay should be linked to performance (Lawler, 1995; Schuster and Zingheim, 1996) which have been widely adopted and promoted by the professional bodies, despite concern that they may not be appropriate prescriptions for all types of organisation (White, 1996).

Barringer and Milkovich, through their research into the adoption of flexible benefit systems in the US, noted the significance of “diffused” (1998: 312), practice which becomes seen as best practice and thus increases the pressure on those not following this practice to conform. They outlined how the proportion of competitors which are following certain practices, in their case the operation of flexible benefits, will increase the pressure on others to conform. This conclusion is supported by Eisenhardt (1988). Eisenhardt found, in her study of retail stores and the extent to which they use salary or

performance related bonuses in rewarding sales staff, that the key driver in determining the salary and commission mix was acceptance of the practice within the retail stores sector, rather than alignment with strategic goals. Significantly, Eisenhardt identified that the age of the department store influenced the choice of whether to use commission-based reward structures, with accepted practice at the time of opening driving the decision. This result was in line with earlier theoretical work by Wright and McMahan, in the context of all HR practices, which noted the possible influence of history, suggesting that “organisation practices can be institutionalised through an imprinting process whereby the practices adopted at the beginning of the organisation’s history remain embedded in an organisation” (1992: 314).

Tolbert and Zucker (1983) note that the influence of institutional pressures will be much lower, and other elements will drive decisions (i.e. efficiency/strategic considerations), in what they described as the pre-institutionalised phase, i.e. early in the institution’s life, where institutional norms have not been established. Thus decisions could be proposed as being more strategic in this early stage. Hence, reward decisions including mix decisions will be based on reward goals which in turn will be based on strategic organisational goals.

Support is also evident from research on executive reward. Bender, in her research on why companies use performance-related pay for executive directors, concluded that “companies used performance-related pay because their peers did, and because that legitimised them in the eyes of the establishment” (2004: 521). Ogden and Watson (2004; 2007; 2008), in their interviews with remuneration committees of water companies, found that the committees felt under significant political pressure, which has

led to policies shaped by comparisons with other companies rather than analysis of the performance consequences of reward decisions. This conclusion was supported by Main et al. (2008) who noted the significance remuneration committees place on the market in determining which measure of performance was used in long-term incentive schemes. Perkins and Hendry also concluded that “what matters is how rewards appear” (2005: 1464). Jensen and Murphy supported this finding noting how “uninvited but influential guests at the managerial bargaining table (the business press, labour unions, political figures) intimidate board members and constrain the types of contracts that are written between managers and shareholders” (1990: 139). This is unsurprising given that executive pay decisions are a matter of public record through annual reports and have come under significant public and institutional investor scrutiny (Main et al., 2008). However, as lower level reward structures are not generally public then perhaps the institutional pressure to conform may be lower at this level.

Normative practice may also be established through the programmes in place to educate reward practitioners. Formal reward qualifications are well established in the UK. CIPD offers direct postgraduate training in reward management leading to a recognised qualification – Advanced Certificate in Reward Management. Alongside this formal codification, reward consultancies also offer training programmes, and although not leading to recognised qualifications it could be argued still offer some normative status.

Social networks have also been highlighted as a potential route to spreading practices (DiMaggio and Powell, 1991; Palmer et al., 1993). Reward practitioner networks are in place, through the range of conferences arranged by CIPD, other professional bodies and the reward consultancies.

DiMaggio and Powell (1991) believed that these normative pressures led to what they termed ‘the creation of an organisation field’. Has such a field emerged in the reward arena? To ascertain this, they felt four conditions needed to be met. First, a trend of increasing interaction. In reward, the proliferation of written materials, conferences, professional groups and forums discussed above would tend to indicate high levels of interaction between REs. Second, the emergence of dominant paradigms. Best practice guides are provided through CIPD ‘reward factsheets’, and practitioner textbooks and often extol the virtues of certain reward mix approaches such as the ‘New Pay’ call for higher proportions of performance-related pay (Lawler, 1995). Third, an increase in the information load which must be dealt with in the field. The aforementioned development and circulation of literature through professional bodies and conferences may provide some indication of this occurring. Finally, they noted how “mutual awareness”, among participants in the field, that they are involved in a “common enterprise” (DiMaggio and Powell, 1991: 65) was required. The willingness of practitioners, despite coming from often competing organisations, to share examples of practice at conferences, through practitioner literature and in case studies prepared by reward groups (e.g. Information Data Services and E-Reward) may be an indication of this commonality in action.

The consequence of the existence of organisational fields, such as appears to exist in the reward area, creates “a pool of almost interchangeable individuals who occupy similar positions across a range of organizations and possess a similarity of orientation and disposition that may override variations in tradition and control that might otherwise shape organizational behaviour” (DiMaggio and Powell, 1991: 71). The consequence

of this is that it provides “a context in which individual efforts to deal rationally with uncertainty and constraint often lead, in the aggregate, to homogeneity in structure, culture and output” (DiMaggio and Powell, 1991: 71).

2.3.2.6 Institutionally contested practices

A key element of institutional theory is the legitimacy that isomorphic behaviour is expected to provide. Scott (2008) identified that the legitimacy of organisations' practices is determined by three areas. Normative legitimacy comes when the practice is consistent with current values in society. Legitimacy can also be conferred when the activity is compatible with regulatory principles and more detailed rules. Finally, legitimacy can also be gained when the practice is in line with institutional culture, and the members' of the organisations understanding and knowledge of this culture. Consequently, when practices, such as specific reward mix combinations, are in line with these three elements it will be deemed legitimate and may further legitimise the activities of the organisation adopting the practice. These legitimising pressures are strong and, therefore, adoption of practices that break one or more of the three elements can reduce legitimacy (Sanders and Tuschke, 2007).

Scott (2008) identified that the adoption of 'non-legitimate' practices required organisational courage which, if successful, begins a process of legitimisation for the new practice. Sanders and Tuschke termed these “institutionally contested practices”, and defined them specifically as “new organizational practices that face stiff opposition from key constituents in potential adopters primary institutional environment” (2007: 34). They identified four processes that facilitate the spread of institutionally contested practices: exposure to other institutional contexts where the practice is considered

legitimate, CEO education, organisational learning and regulatory/legislative change. Each of these processes will now be considered.

First, is organisational exposure to other institutional contexts, for which the organisation has a high regard, where the disputed practice is considered legitimate, i.e. learning from other respected institutional contexts. This could be, for example, practices of a different sector or country setting. Sanders and Tuschke's (2007) research into the reward mix, and specifically the role of stock options in this mix, in German executives found that those adopting a form of mix with a higher proportion of stock options are likely to have exposure to both perceived high status institutional environments in which the practices are legitimate (e.g. UK or US markets) and experience introducing other contested practices, not necessarily from the reward area.

Second, organisational learning can be significant in influencing the propensity to adopt institutionally contested practices. Previous success in adopting contested practices increases the probability of adoption of further such practices (DiMaggio and Powell, 1991; Hambrick et al., 2005). Related to this, the educational breadth of the CEO has also been shown to influence the extent to which learning from wider environments was encouraged and acceptable. Scott (2008) noted how much institutional theory application had neglected the significance of key organisational actors, such as the CEO, in bringing about change in institutionalised practices. This is consistent with upper echelon theory outlined by Hambrick and Mason (Hambrick and Mason, 1984; Hambrick, 2007) and the significance this perspective puts on executive values and beliefs, and how these are shaped by their experience and education. For example,

CEOs with a formal business education are more likely to scan the environment and adopt practices from other institutional settings (Sanders and Tuschke, 2007).

Third, the degree of cohesion and networks between organisations in an institutional setting will influence information exchange and practice adoption (Scott, 2008). Where cohesion is strong, practice is more likely to spread, with particular significance on the extent to which board membership interlocks organisations and brings different institutional experiences (Sanders and Tuschke, 2007). Alongside these network ties comes the extent to which others in the industry have adopted the contested practice and thus begun to provide some form of safety in numbers (Galaskiewicz and Burt, 1991).

Finally, regulatory legitimisation influences the adoption of contested practices. As discussed above, legal barriers can be significant, with organisations, short of doing something illegal, having to find suitable interpretations of legislation or regulatory rules in order to proceed. However, when regulatory and legal change occurs it can “open the floodgates” (Sanders and Tuschke, 2007: 207) to what were previously seen as contested practices.

Whilst the four factors identified will facilitate the spread of practice, and through this potentially increase the level of adoption of contested practices, final decisions about whether to adopt practices that are institutionally contested will need to be weighed between the benefits expected to accrue from the adoption of the practices (e.g. productivity increases or attraction benefits from a new reward mix) against the cost accruing from the potential accompanying loss of legitimacy (Meyer and Rowan, 1991). A sustained competitive advantage by differentiation of this nature will be dependent on this ratio of benefit to cost (Sanders and Tuschke, 2007).

Strategy researches have for a long period proposed that benefits can accrue to organisations through differentiation relative to their rivals (Johnson et al., 2008). According to the resource-based view of strategy, differentiation can come through specific people policies where people resources are a key resource in business success (Barney, 1986; Barney and Wright, 1998). In the context of reward strategy decision taking, Lawler noted that organisational reward strategy should be built with regard to specific organisational circumstances not a “vanilla, me too flavour that provides no competitive advantage” (1990: 5). The extent to which the reward mix is aligned to the organisational strategy, and through this differentiated from the competition, will dictate its effectiveness in supporting the delivery of this strategy. However, institutional theory warns that extreme divergences from established norms can cause a deterioration in firm performance (Norman et al., 2007; Miller and Chen, 1994; Chen and Hambrick, 1995).

A number of studies have examined, in a non reward context, the costs and benefits of non-conformity (Miller and Chen, 1994; Chen and Hambrick, 1995). Deephouse (1999), in research on airline deregulation, showed performance falling when deviation from norms occurred. A more refined analysis, considering the conformity/non conformity choice as a continuum of options rather than a conform/do not conform choice, came from Norman et al. (2007). They showed, again in the context of the airline industry, that small levels of divergence from the institutionally established norm would actually increase organisational performance as this allowed some differentiation whilst maintaining legitimacy. However, larger deviations from established norms had negative performance consequences as the cost of loss of legitimacy outweighed any

differentiation benefits. This may indicate that although organisations may have some flexibility and therefore be able to differentiate their overall reward package this choice will at some point be constrained by the institutional pressures that have been discussed.

2.3.2.7 Institutionally driven behaviour – empirical evidence

The main application of institutional theory has been the examination of the legitimising effect of different organisational structures (Barringer and Milkovich, 1998). Relatively little has been done to examine institutional pressures on reward decision taking (Kessler, 2001). However, drawing from wider studies of institutional theory, it seems reasonable, given the effects on organisational form that institutional pressures appear to exert, that they might influence reward strategy (Kessler, 2001). We have seen that these pressures can come from both within and outside an organisation. The former occurs as the practice becomes so embedded within the organisation over time that it becomes difficult to change, and the latter through the pressure to mimic other organisations to lower risk to the organisation and establish legitimacy.

Institutional theory suggests that the adoption of a new reward practice, driven by a desire to improve performance in some way will, if successful, soon spread to other organisations through normative pressure. This momentum will take the innovation to a point where introducing the practice provides legitimacy, but does not necessarily improve organisational performance, as was originally the case (Meyer and Rowan, 1991). This led DiMaggio and Powell to conclude that “strategies that are rational for individual organizations may not be rational if adopted by large numbers. Yet the very fact that they are normatively sanctioned increases the likelihood of their adoption” (1991: 65). Conlon and Parks add “that the existence of a pay tradition can inhibit the

economically rational thinking agency theorists assume” (1990: 619). This will have implications for the effectiveness of the reward mix strategy, as it will not be in line with organisational goals, but rather wider environmental trends (Gomez-Mejia, 1992).

This passive description of institutionally motivated behaviour has been challenged (Suchman, 1995; Oliver, 1991; Goodrick and Salancik, 1996). For an organisation’s action to be considered strategic, as opposed to simply a passive reaction to its environment, it needs to be managed through “a pattern of planned action” (Wright and McMahan, 1992: 298). Strategic action implies a rational, proactive decision making process. Although mimicking other organisations may not be wholly rational from a purely economic assessment of the efficiency of a certain action it may, through the legitimacy it is perceived to confer, increase organisation effectiveness in other ways. For example, Hillebrink et al. (2008) found no evidence of either efficiency or cost being a driver of the introduction of flexible benefits. However, this may have been due to the way they operationalised the reasons for introducing a flexible approach to benefit management, which did not include any labour market factors. They concluded that institutional factors were significant but added that "there is no reason to believe that the way these factors are responded to is not rational or economic." (2008: 320). What evidence do we have of this type of behaviour in reward mix situations? Table 2-2 summarises a number of studies that have used institutional theory to specifically examine reward mix decisions for employees⁹ of different types.

⁹ A number of studies have been carried out on the executive reward mix and the influence of institutional factors on the determination of this mix. However, whilst this literature review has drawn on insights from these studies in the main discussion of institutional theory, this section on empirical studies will focus solely on levels of employees below the executive.

Study	Objective	Reward mix	Theoretical perspectives	Setting	Findings
Eisenhardt 1988	Evaluation of when organisations use salary compensation as opposed to compensation based on performance	Salary: Commission	Agency / Institutional	Retail sales	The store age is negatively related to the use of salaries and positively related to the use of commissions. Commissions are more common in shoe sales than in other types of retailing
Conlon and Parks 1990	How behaviour monitoring, and the presence of tradition of non contingent pay, interact to affect compensation arrangements	Fixed: variable	Agency / Institutional	Experiment on MBA / Graduate students	Pay traditions can inhibit the economically rational thinking predicted by agency theory
Taras 1997	Assessment of the impact of managerial objectives on wage policies	Significance of wage	Institutional	Canadian petroleum industry	Managerial Objectives - in particular, a tendency toward imitative behaviour and a strategy of union avoidance - influence wage mix.
Milne 2001	Investigation of the pattern of adoption of an HMO option as a component of a multiple choice health insurance plan	Adoption of HMO medical plans	Institutional / Resource dependency theory	US	Several factors both internal and external affect the responses of management
Van der Stede 2003	Examining the influence of variations in national culture on incentive mix	Percentage of compensation that is performance dependent	Institutional / Hofstede's cultural dimensions / Contingency	Belgian multinational enterprises	Corporate effects are dominant over national cultural effects with respect to incentive pay systems. Incentive systems tend to be uniformly implemented within firms
Fernandez-Alles et al. 2006	Analysis of whether compensation design is an economically rational incentive to increase performance or whether it responds to other factors such as the search for legitimacy	Extent of variable compensation	Agency / Institutional	Middle managers in Spanish banking	Compensation design considers the company's adoption of popular management practices that increase its legitimacy but not its performance.

Table 2-2 - Studies adopting institutional theory to examine employee reward mix determination

As can be seen in table 2-2, institutional theory has been used to understand organisations' approach to RMD in a variety of ways. The first significant application of an institutional theory perspective to RMD for employees was by Eisenhardt (1988). Her study evaluated when organisations use salary compensation, as opposed to compensation based on performance, for US retail sales staff. The work concluded that contextual conditions at the time of the organisation being established were particularly significant on reward mix choice and, once chosen, the reward mix had longevity.

Van der Stede identified the presence of “intracorporate isomorphism” (2003: 268), reflecting the strong influence of parent companies on business unit policies including reward (in this case incentive) design. In line with DiMaggio and Powell's (1991) framework this pressure may be coercive: with head office dictating policy, mimetic: with the business unit mimicking a successful business unit or head office practice, or normative: adoption of a corporate template already available in the organisation. These isomorphic pressures are in direct contrast to “business-unit idiosyncrasy” (Van der Stede, 2003: 268), which pressures business unit subsidiaries to diverge from the remainder of the organisation.

Whilst relatively little is known about cross-national reward mix practices (Werner and Ward, 2004), Segalla et al.'s (2006) examination of cross-national sales compensation practices concluded that culture influences reward mix decisions through the effect it has on managers. They showed that Germanic managers were less likely than Anglo-Saxon managers to favour incentive-heavy reward mixes. This led them to question the applicability of institutional theories prescriptions for effective reward mix decisions in all scenarios, particularly where national and cultural boundaries are concerned.

Fernandez-Alles et al. (2006) found, in their research on variable compensation for middle managers in the Spanish banking industry, that reward strategy formation incorporates popular reward trends and practices that will not necessarily increase organisational performance but will increase legitimacy. Social objectives are as important as financial and efficiency objectives. “[V]ariable compensation is sometimes designed to reward not those particular practices and procedures that rationally should enhance the performance of the company but those that enhance its social standing and reputation in its institutional context” (Fernandez-Alles et al., 2006: 963).

This perspective was contested by Milne (2001) in his investigation into the introduction of health care programmes into the overall reward mix in the US. He found that organisational behaviour varied, being neither always passive nor uniform, with employers seen to be acting differently when presented with the same pressure. Organisations varied in their choices, despite pressures to conform to one approach, often due to their assessment of the power of the bodies imposing the pressure, which was driven by the organisations’ own unique and specific resource dependence. This was in line with Tremblay et al.’s (2003) warning of the dangers of determining reward mix strategy simply by mimicking other organisations. Their research into sales teams in French-Canada found that organisations led by institutional factors are likely to have a less effective salary and variable reward mix and, because of this, may be at a competitive disadvantage.

2.3.2.8 Conclusions

The review of empirical research appears to show that institutional pressures do exist, and that they are often influential. However, the research is not categorical with a number

of studies showing that the pressure is not automatically and uniformly followed. Whilst insightful, the theory does not appear to fully explain behaviour and differences in practices between organisations. For example Gerhart and Rynes (2003) note significant differences in reward mix policy in Microsoft and SAS when both are operating in the same industry and competing for the same talent. As differences do exist, critics argue that institutional theory fails to fully incorporate individual organisational strategic and leadership goals (Hambrick, 2007; Oliver, 1991). Examples of changes in reward mix policies are occurring, such as the introduction of different types of performance-related pay, closing of defined benefit pension schemes and introduction of work-life balance initiatives (Armstrong and Brown, 2005). Innovation is occurring but does, as predicted by institutional theory, also tend to spread across the field.

This has led to calls from researchers to integrate the exploratory appeal of the institutional theory approach with other relevant theoretical perspectives. This combination of approaches is discussed further below.

2.3.3 Resource dependency theory

2.3.3.1 Introduction

Resource dependency theory came to the fore with the publication of 'The External Control of Organizations' by Pfeffer and Salancik (2003). In developing resource dependency theory they drew heavily on exchange theory (Jacobs, 1974) and power dependency theory (Emerson, 1962). Broadly speaking these approaches propose that individuals and organisations have an innate desire to reduce their dependency on others in order to increase the power they have over their own future. The central theme of

resource dependency theory is that to “understand the behaviour of an organisation you must understand the context of that behaviour – that is, the ecology of the organisation” (Pfeffer and Salancik, 2003: 1).

2.3.3.2 Critical resources

Whether an organisation is dependent on particular resources will depend on the extent to which the resource is deemed critical to its operation and the availability of substitutes for the critical resource. All decisions that organisations take are heavily influenced by both external and internal agents who have control over what are termed ‘critical resources’ (Pfeffer and Salancik, 2003). The agents may be organisations, government or government agencies, or individuals. Resources are critical if their removal from the organisation would cause the organisation to cease operation or, at the very least, materially disrupt this operation to the point where it threatens the organisation’s survival (Pfeffer and Salancik, 2003). Criticality does not necessarily come from the level of resource that is controlled by the agents (although it may do if control over the scale of resource would allow significant business disruption) but the overall impact its withdrawal or rationing would have on business operation. Consequently employee positions in organisations are likely to be more critical when other organisational functions are highly dependent on them to carry out their own activities (Balkin and Bannister, 1993).

The extent to which a resource is deemed critical is also influenced by the availability of substitutes for the resource, should it be withdrawn. A position or resource will be more difficult to replace where substitutes are not easily available (Nienhüser, 2008). Low numbers of available substitutes, say of a particular skill that an individual or group of

individuals bring to the organisation, increases the dependence the organisation will have on the individuals' possessing the critical skill (Balkin and Bannister, 1993).

The existence of critical resources, and the power that these provide to those who control them, can present a number of problems for organisations. The very existence of critical resource dependencies creates uncertainty for organisations, defined as “the degree to which future states of the world cannot be anticipated and accurately predicted” (Pfeffer and Salancik, 2003: 67). Organisations will look to try and reduce these uncertainties through planned action. The extent to which the uncertainty will materially influence organisation behaviour will be dependent on how the critical resources are distributed within the environment. It is the concentration of these critical resources that leads to concentration of power and associated influence on organisational decisions (Nienhüser, 2008). Individuals who control critical resources, but do not call on any resources from the organisation or are not dependent on the organisation, have high power which in turn gives them the ability to make demands, e.g. their preferred reward mix, and expect them to be fulfilled. This may suggest, with regard to reward decisions for individuals or groups of individuals that are deemed to be critical, that the organisation should aim to create a situation whereby the individual is also dependent on the organisation for something which they value, e.g. a particularly satisfying reward mix that is unavailable elsewhere.

Decisions on how dependent an organisation is on an individual or group of individuals are likely to influence reward mix decisions for this individual or group (Tremblay et al., 2003; Pfeffer and Davis-Blake, 1987). Talent shortages and the resulting dependency this can create for organisations that need certain skills to be successful are

widely reported (e.g. Michaels et al., 2001). To assess these shortages REs are provided with a range of information which they need to interpret to form a view about the appropriate reward mix decision given these dependencies. The information includes RCs' reports, both with respect to reward levels in the market through benchmarking and recruitment data on hard-to-fill posts. The RE may also be involved in networking groups and be part of professional associations which will also provide intelligence on skill issues and potential dependency building as a result of these skill shortages.

If, as resource dependency theory suggests, organisations are influenced by those who control critical resources, particularly when substitutes for these resources are not readily available, then the extent to which managers control outcomes may also be limited. This may mean we assume generally that managers have more influence on decisions than they have in reality and can, as a result, be made scapegoats when organisational outcomes are not as intended when the critical resources for success were not under their control (Pfeffer and Salancik, 2003). Any individual or organisation controlling critical resources can exert pressure (Balkin and Bannister, 1993), e.g. investors who control capital, particularly if capital is scarce, or suppliers where suppliers are critical, or unions who may control the supply of a particular type of labour. Where these individuals or organisations have a personal interest in reward design, as is likely when employees or unions control critical resources, then we may expect them to exert influence on this design. There are clear parallels with the external forces of institutional theory and the effect they have on management choice (Barringer and Milkovich, 1998). A number of scholars have noted this similarity. Tolbert and

Zucker (1996) criticised this as evidence that resource dependence was in fact one element of institutional theory rather than a new theory in its own right. However, Oliver (1991) noted that the crucial difference between the theories was in how organisations respond to the coercive pressures with a resource dependency perspective being seen as a more autonomous or strategically conscious response compared to the more automatic and unconscious response of institutional theory. Organisational characteristics will, under resource dependency, determine the reaction to the pressure. For example, the proportion of variable reward available to sales teams (a potentially critical internal resource) will vary according to their autonomy and complexity of sales process rather than simply getting a high proportion of reward in an incentive purely because that is the industry convention (Eisenhardt, 1988).

2.3.3.3 Employee perspective

Bartol and Martin (1988) raise seven factors that influence the level of dependence an organisation has on an employee, or a group of employees, and consequently the power those employees may have over the reward mix design. First, task uncertainty around the input/output process carried out by the employee where, due to the complexity of the task, the manager is unable to direct the activity. This is often the case for specialist research jobs (Balkin and Bannister, 1993). Second, the extent to which the manager can monitor performance or alternatively, as outlined in agency theory, is reliant on outcome-based monitoring. Next, performance visibility, defined as whether failures and successes are visible to both management and significant external parties to the organisation. Specialised skills are also felt to increase dependency. Management is more dependent when employees have skills that are difficult to replicate in the short run. Replicability is also related to the fifth of Bartol and Martin's factors – replace

ability. Where skills are difficult to replace then organisations will be more dependent on those performing those skills. Next, task centrality will have a dependency effect. The more important the task is to the organisation's success, the more likely the organisation is to be dependent on the individual's performing the task. Finally, organisational connections are significant. Individuals with connections with powerful others outside the immediate work group, such as internal senior level sponsors or others who are powerful within the organisation due to the dependency they have created, potentially provide increased power for those individuals.

2.3.3.4 Empirical evidence – non reward mix related

The theory has been well tested, both by Pfeffer and Salancik and those who have worked closely with them, and others who have applied the approach to different organisational issues e.g. Festing et al. (2007); Pfeffer and Davis-Blake (1987); Carpenter and Wade (2002). A number of the studies have been performed in the area of reward decision making and, to a more limited extent, reward mix decisions. The results, which are not clear-cut, will now be discussed.

Morgan and Milliken (1992) aimed to show how the proportion of women in an organisation, through resource dependency, influenced the extent to which the organisation applied family-friendly policies as part of the overall reward mix. They found a positive relationship. However, the work can be criticised on two fronts. First, the statistical correlation was weak and did not meet tests of statistical significance. Second, there was no indication as to whether the proportion of women controlled what were deemed to be critical resources for organisational success, and therefore had power to dictate terms more aggressively. Therefore, it would be difficult to conclude from

this work that it was dependency on these women that caused family-friendly elements to be a greater proportion of the mix, as opposed to other factors such as organisational paternalism, or wider motivational beliefs that this type of policy increased productivity.

In the context of the pay level decision, Pfeffer and Davis-Blake (1987) examined how position and the criticality of that position would influence pay level. They showed that differences in wage levels could not solely be explained by “market, economic or technical forces” (Pfeffer and Davis-Blake, 1987: 452), rather that other firm-specific factors, such as criticality of the position to that firm at that time, and wider institutional and environmental factors, were significant influences. The test results were significant. It does not appear unreasonable to believe that this result may also apply to reward mix decisions, given these wider institutional and environmental factors are also present to influence the reward mix decision.

Resource dependency principles have been applied to the determination of CEO reward mix (Elvira, 2001). Studies in this area include Hambrick and Finkelstein’s (1995) examination of the effect of ownership structure on CEO reward and Crystal’s (1991) work on CEO and compensation consultant’s roles in executive pay determination. Elvira (2001) focused her work on one institution in the financial services sector, given the widespread use of incentives in that sector, and noted that most incentives are paid, at managerial and professional levels, due to attraction and retention considerations driven from higher levels of resource dependence for these types of role. These studies suggest reward determination, including mix, is significantly influenced by relative power and through this power the ability to negotiate reward mix in line with personal preferences, not organisational alignment. Fiss (2006) challenged this perspective, at

least with regard to executive reward. In his study of the social influence of the CEO on company boards, and through that the remuneration decisions taken, he argued that the strength of this social relationship was a significant driver of top management team's compensation with, as resource dependency predicts, human capital aspects, and in particular scarcity of key human resource skills, being less significant. What seems to be agreed is that the CEO has an influence over the overall reward mix he/she receives. However, what is in dispute is the relative effects of social interaction and organisational resource dependence in influencing this mix. Better understanding of this dynamic is important below executive levels as social interaction is likely to be less of a factor on organisational policy decisions of reward mix, given that the decision is at an organisation not an individual level. However, resource dependencies on groups of employees may exist, making this factor relevant to RMD.

Nienhüser (2008) found two reactions to this form of dependency. First, organisations look to the market to recruit others with the required skills and thus reduce their dependency on existing staff. Next, he noted this dependency makes these staff more powerful. Consequently organisations look to tie them into the organisation by making them more dependent on the organisation through more attractive benefits and other forms of financial tie-ins. This supports the earlier conclusions of Bannister and Balkin (1993), in their study of sales representatives, that organisations will look to reduce uncertainty of operation by using means to reduce their dependency, or at least create mutual dependency through reward structures, between the organisation and the critical individuals.

Union representation, and the power that collective organisation may give employees over the employer, may create a form of dependency and consequently influence reward mix for the workforce (Budd, 2004). Freeman and Medoff (1981) showed how unionised environments typically have a positive effect on benefit provision. This influence is attributed to the monopoly power they have in organisation sectors where unions are strong, increasing their bargaining power. Second, they provide a collective voice to employees. This may mean that benefits are increased as democratic preferences of employees (Freeman and Medoff, 1981). Kaufman (2002) showed how the collective voice provided by unions was likely to lead to increased fixed wages and lower contingent compensation, even if that was at the expense of a higher overall level of unemployment. Other research has supported these conclusions showing, in particular, that declines in benefit provision as part of the overall package have occurred when union density has declined (Budd, 2004; Bloom and Freeman, 1992).

2.3.3.5 Empirical evidence – reward mix

As the discussion above shows, resource dependency theory has provided insights into a number of reward-related areas. However, only a small number of the empirical research papers relate to human resource dependence at an employee level and explicitly the effect this may have on reward mix decisions organisations take. These are now discussed.

Balkin and Bannister (1993) examined how reward mix may be influenced by the relative power of certain types of employee groups, namely executives, sales representatives, and scientists and engineers. These groups were deemed to hold critical positions by the specialist nature of the roles, the autonomy they have in how they

operate and the overall effect they have on organisational performance (Milkovich and Newman, 2008; Bartol and Martin, 1988). They found that the relative power these groups have over other employee groups should have an influence on the reward mix they receive in respect of the balance between fixed and variable reward. They conclude that the determining factor for the mix for key groups such as these, is the relative preference they have for the employees' desire to participate personally in higher returns relative to their risk tolerance. Given the risk aversion of agents they should generally prefer secure and therefore fixed forms of income (Conlon and Parks, 1990). They concluded that the more powerful the individual or group is, the more the organisation will do to meet their reward mix preferences. Managers may also be willing to overlook other reward issues, such as equity with other groups of staff on whom the organisation is less dependent, due to the specific dependency the organisation has on the individual(s). Consistent with resource dependence theory, this suggests that management will have greater control over reward mix for non critical groups of employees on whom they are less dependent. Consequently, for these groups, the prescriptions of strategic compensation and agency theory are more likely to apply in the determination of reward mix. However, the power of these strategic groups of employees is not unfettered and the degree of dependence will be moderated by a range of factors (Balkin and Bannister, 1993), e.g. for executives, the existence of a dominant shareholder, for the sales representative the extent to which the representative controls the relationship with the customer, and for the scientist and engineer the proportion of total revenues which are spent on research and development.

One weakness of the study is the exclusion of the benefit component of the overall reward mix. Balkin and Bannister (1993) justify focussing solely on total cash compensation as they felt resource dependency has limited exploratory power with respect to benefits, as, in their view, benefits are generally group membership rewards. They speculate, but provide no theoretical or empirical evidence, that internal pay equity and local employment regulations will be the main drivers of benefits in the overall mix. However, like many reward studies, the focus on cash compensation is likely to have been driven by more pragmatic considerations of the difficulty in measuring benefits and more relational returns in the mix.

Gomez -Mejia and Balkin also examined what they termed “strategic employee groups” (1992: 101). They also concluded that the reward packages of these critical groups should be tailored to better align to their preferences. They define these groups as those contributing more to organisational performance which, although not the same as the critical resource definition of resource dependency, has similarities around the importance of the individual to the organisation. For research and development employees they found that the firms’ overall research and development leaning led to different designs around compensation time horizons (i.e. vesting period of reward elements) and the relative balance of short- to long-term incentives. In addition, they also noted a knock-on effect on the reward mix of other ‘non strategic groups’. They speculated, in contrast to Balkin and Bannister’s (1993) conclusions, that this was down to firms not wanting to totally separate reward systems for these critical groups of employees from other employee groups for internal equity reasons. However, as this was not tested, it is also possible that this was not a conscious process and different job

families simply mirror each other for more passive convenience reasons. Gustman et al. (1994) lent support to this view, finding that pension plans, whilst having a cross-organisational structure, are sometimes built with particular employee groups in mind, consistent with a resource dependency view of critical employee groups shaping the reward mix in their favour. This argument could easily be applied to other benefits that are provided collectively.

Abbott and De Cieri (2008), in their examination of the influences on the provision of work-life benefits in organisations, found that different environmental conditions were seen to influence the respective power of employee stakeholders and consequently the extent of work-life benefits. In company A, which was growing and therefore had a real need to retain current employees and attract more from the market, employees were perceived as key stakeholders and this exerted significant influence over the benefits provided. However, in company B, which was contracting, it was noted employee influence was much lower and was therefore reported to have resulted in the removal of certain work-life benefits. Overall, they concluded that specific work-life balance provision is organisationally context-specific and the effect of employee stakeholder power is relevant. This, although not the focus of the study, provides some support for a resource dependency perspective on benefit provision, but, given the communal nature of the benefits, one which applies across the workforce when there is a general shortage of talent and thus all employees are deemed somewhat critical. However, we need to exercise care in drawing too strong a conclusion from this work as its focus is only on two companies, and only captures one element of the reward mix, i.e. work-life benefit,.

From the above discussion, we can see that we have only a limited understanding of the influence resource dependence may have on reward mix, and the impact its provisions may be having on organisational decision makers, when we may expect the approach to have reasonably powerful predictive capabilities. The literature examined, although identifying the link between resource dependency and reward mix decisions, is relatively limited in volume and consequently it could be argued that further testing of the relationship would be helpful. Neinhüser (2008) concludes that, although there is much confirming empirical evidence for resource dependency theory, it is not always strong and does not always explain a high proportion of variance in the situations reviewed. This led him to conclude that it may need combining with other theories to improve our understanding of the situation being examined. This will be examined further in the section below on combinations of theories to explain reward mix decisions.

2.3.3.6 Expectancy and resource dependency theory

Vroom (1964) identified that performance is a joint function of both the ability of an individual and the motivational force that drives them. Motivational force was defined as a multiplicative function of expectancy, i.e. the expectation that effort will lead to the desired behaviour, instrumentality or the perceived link between exhibiting the behaviour and the outcomes received, such as monetary reward and finally the valence or the perceived value of the reward to be received to the individual concerned. This theory provides two particularly significant insights when examining reward mix choice and the effect that this reward choice may have on overall organisational performance. First, in order for an individual to be motivated, and therefore perform effectively, they need to see the link between their effort and behaviour and receipt of a reward. With

respect to agency theory this may question the effectiveness of subjective behaviour-based contracts on the motivation of the employee. Second, for the individual to be willing to expend the effort required they must value the reward on offer. This is clearly relevant for the reward mix in ensuring that the forms of reward offered are to the liking of the employee receiving them. For example, Darmon et al. noted that “sales forces are likely to display heterogeneous preference patterns for compensation formulae” (2003: 151), and, given this, he called for programmes to be designed by seeking and analysing sales force reactions to proposed compensation, and in particular incentive mix design. In addition Medcof and Rumpel (2007) demonstrated that the preferences of high technology workers would be different from other employee groups and thus if they are considered critical to the organisation the package should be designed around their, rather than other employee, preferences. This is particularly significant where group-wide benefits are concerned, as opposed to fixed and variable reward where differences may be easier to accommodate.

Expectancy theory outlines how consideration of employee preferences for different types of reward and reward systems should be significant in reward mix determination, given the importance that the reward is actually valued by the critical employee group. Why extend effort if the payment at the end is not valued? There is some research on what these preferences might be. In studies of job applicants it was seen that they prefer merit-based to tenure-based reward systems (Turban and Keon, 1993), individual-based incentives as opposed to group or organisationally determined ones (Bretz and Judge, 1994), fixed rather than contingent pay (Cable and Judge, 1994) and flexible over fixed benefits (Cable and Judge, 1994). Examination of incumbent employees found similar

preferences to those of job applicants, namely individual not team/group reward increases in pay to be fixed not variable (LeBlanc and Mulvey, 1998); specifically, Slade (2002) showed that high potentials had a preferences for stock options, incentive opportunities and sabbaticals. A resource dependency perspective may lead to reward structures being designed around critical employees, or employee groups which may include high potentials.

Where organisations hold a belief that reward mix is key in incentivising employees one would expect them to focus on the expectancy, instrumentality and valence of the rewards on offer (Pappas and Flaherty, 2006). Pappas and Flaherty (2006), in their research on salespersons, found that this relationship is affected by individual difference variables. They suggest from this, that REs need to see beyond traditional agency-based theories when deciding reward mix and consider matching mix with individual characteristics. This clearly presents a problem for organisational level analysis of reward mix and perhaps indicates that policy level decisions should be for flexibility at local manager level so these different preferences can be taken into account, especially for those employees on whom the organisation is particularly dependent. The risks and difficulties of this led Pappas and Flaherty(2006) to suggest that greater effort should be made at the recruitment stage to better understand potential employees and the resulting fit with the organisation and in this case its reward mix approach. They also suggest that the relationship between reward structure and reward mix needs to be considered as they expect preferences of mix to change as an individual advances up the organisational hierarchy.

Designing reward mix around the preferences of critical employees or employee groups may present other difficulties with regard to employee equity which may have to be compromised as reward mix is designed to better meet the preferences and needs of critical employees (Gomez-Mejia and Balkin, 1992). This may have implications for wider employee motivation, as research has shown that perceptions of fairness of overall reward have an influence on overall levels of motivation (Adams, 1965).

2.4 Combining theoretical insights

This literature review has attempted to draw together our current knowledge on reward mix determination through examination of three theoretical perspectives – agency, institutional and resource dependence. Whilst most research has adopted agency theory through which the mix decision has been explained, the other theoretical viewpoints have been shown to potentially have further explanatory power. Miller et al. (2001) and Festing and Sahakians (2010) noted the weakness of single approaches to examining reward mix following an earlier conclusion by Eisenhardt that “multiple perspectives contribute to robustness in exploring a phenomenon by emphasizing complementary facets” (1988: 490). Given this, a range of scholars have suggested that increased understanding may result from analysing the reward determination question from more than one theoretical perspective (Baker et al., 1988; Jensen and Murphy, 1990; Barkema and Gomez-Mejia, 1998; Berrone and Gomez-Mejia, 2009). The trend appears to be towards using complementary theoretical perspectives to deepen our knowledge of reward mix, particularly to counter some of the criticisms that have been made of agency theory alone in explaining the phenomenon (Eisenhardt, 1989a; Fernandez-Alles et al., 2006; Berrone and Gomez-Mejia, 2009).

Eisenhardt (1989a) suggests that agency theory should be expanded alongside other theories to gain greater insight into organisational behaviour. She contends that although agency theory has a valid view of organisational behaviour it was only a partial view supporting Hatch and Cunliffe's (2006) view that the use of multiple perspectives in organisational theory was one of its many strengths.

In this context, Fiss identified that "approaches drawing on several theories and disciplines offer the greatest promise for future research on compensation" (2006: 1028). Barringer and Milkovich added that we could obtain "richer explanations of organizational structures by integrating complementary explanations of organizations into a single model" (1998: 311). Whether combining the theoretical perspectives reviewed will provide a deeper insight into RMD making will depend first on whether they are complementary, and second, whether they can be integrated into one framework to explain reward mix decisions. These two issues will now be discussed.

The approaches would appear similar in that they all examine managerial decisions from a perspective of those decisions being influenced by external factors, i.e. ownership structure, critical resource holders, institutional norms. Each of the approaches also operates with similar dependent and independent variables. Where the differences lie is in the assumptions they make and how they are moderated in their effect on RMD. With respect to moderation, agency stresses the ability to monitor performance, resource dependency emphasises the importance of relative power on decision making, and institutional theory the significance of norms and values as moderating influences. Alongside these moderating influences is the significance of the assumptions each theory makes about how organisations react to pressures. Agency and

resource dependency theories assume that the interests of the organisation will prevail. Barringer and Milkovich termed this a “rational response”, noting that underpinning the rationality was the assumption “that organizations actively manage environmental constraints, adopting structures that ensure the flow of resources, or minimize agency or transaction costs.” (1998: 312). This can be contrasted with an institutional theory perspective which they stated “assumes that organizations do not exercise active choice; rather they more passively conform to their environments” (1998: 312). Enhanced legitimacy was a separate objective from considerations of efficiency.

Chizema and Buck, in their study of CEO governance and the use of executive share options in German companies, identified that “the pure agency or economics-derived views of shareholder-based corporate governance are seen to be under socialised” (2006: 489). They added more generally that “to survive, organizations must accommodate institutional expectations, even though these expectations may have little to do with short run, technical notions of efficiency or performance accomplishment” (2006: 492). But does this apply to other levels of the hierarchy?

Table 2-3 summarises a number of research papers that have explicitly adopted combinations of agency, institutional and resource dependency theories in their study of reward mix strategy for employees.

<u>Study</u>	<u>Perspectives</u>	<u>Purpose</u>
Eisenhardt 1988	Agency, institutional	Evaluation of when organisations use salary compensation and when they use compensation based on performance
Barringer and Milkovich 1998	Agency, institutional, resource dependency, transaction cost	Theoretical examination of the adoption and design of flexible benefit systems
Conlon and Parks 1990	Agency, institutional	How behaviour monitoring and the presence of tradition of non contingent pay, interact to affect compensation arrangements
Milne 2001	Institutional, resource dependency	Investigation of the pattern of adoption of an HMO Option as a component of a multiple choice health insurance plan
Elvira 2001	Agency, resource dependency, power	Examination of the relationship between bonuses and promotions and whether these incentives are traded off
Tremblay et al. 2003	Agency, resource dependency, transaction cost	Investigation of the influence of the theoretical perspectives on the proportion of salary in sales compensation
Yanadori and Marler 2006	Agency, resource dependency	Examining whether innovation strategy affects compensation decisions in the high technology sector
Fernandez-Alles et al. 2006	Agency, institutional	Analysis of whether compensation is designed as an economically rational incentive to increase organisational performance or whether it responds to other factors such as the search for legitimacy
Festing et al. 2007	Resource dependency, institutional, cultural dimensions	Analysis of power relations in multinational enterprises and their influence on compensation strategies
Trevor 2008	Agency, institutional	Exploration of the contemporary realities of compensation strategy – what, how and significantly why organisations are structuring reward as they are

Table 2-3 – Reward research adopting combinations of agency, institutional and resource dependency theories

With the exception of Festing et al. (2007) and Milne (2001), all of the studies examined have adopted agency theory as one of the components of their study. The range of studies employing both agency and institutional theory have generally concluded the addition of institutional factors have enhanced results given the partial understanding that agency research has brought (Eisenhardt, 1988; Conlon and Parks, 1990; Fernandez-Alles et al., 2006; Trevor, 2008; Barringer and Milkovich, 1998).

Eisenhardt concluded that agency theory was too narrow a focus, presenting only a “partial view of the world” as it “ignores a good bit of the complexity of organizations” (1988: 71). She added that “the institutional emphasis on tradition complements the efficiency emphasis of agency theory, and the result is a better understanding of compensation” (1988: 72). Barringer and Milkovich (1998) considered two overarching themes in their review of flexible benefits adoption and design. They grouped resource dependency, agency and transaction cost theories into the category of expected efficiency gains as they felt each took a different approach to efficiency. This is in contrast to the institutional theory approach which emphasises external pressures exerting influence which is conformed to rather than strategically chosen. Earlier Eisenhardt (1989a) had noted how institutional and resource dependency are stronger when efficiency is not a pressing concern, citing large public bureaucracies as examples.

Conlon and Parks (1990) found that the institutionalisation of practices may come due to the influence of particularly powerful bodies. Resource dependency suggests these members would be those controlling critical resources. Their study, which examined how a tradition of fixed or non contingent reward interacts with the classic agency area of study, or ability to monitor employees’ behaviour, used a laboratory experiment with

MBA and undergraduates carrying out the role of principal and agents respectively. Through this work they found support for their hypothesis that the ability to monitor employees would reduce the extent to which variable pay is used, but only when institutional traditions were not present. This led them to conclude that pay traditions, which may not be economically efficient, play a significant role in influencing reward mix. This effect can overrule the economically rational position assumed by agency theory. Whilst the results appear robust in the laboratory setting, the experimental aspect does raise questions about how much confidence we can take from the results in a wider organisational setting. Conlon and Parks (1990) acknowledge this and other limitations arising from the fact that it was experimental. Their operationalisation of pay traditions in the fictional industry, i.e. telling the actors that a certain tradition did/did not exist, is also particularly questionable given the complexity with which institutional factors are formed and manifested in organisational life (DiMaggio and Powell, 1991). However, despite these limitations, they conclude that as the results support and build on Eisenhardt's (1988) work, "efficiency and tradition are both critical for understanding control and compensation in organisations" and "the presence of traditions may interfere with the careful consideration of economic outcomes the agency theory perspective assumes" (Conlon and Parks, 1990: 621).

Festing et al. (2007) found, in their study of analysis of power relations in multinational enterprises and the influence of this power on compensation strategies, that whilst institutional theory has given particular insight into reward decisions it does not fully explain the pressures REs face. They added that an understanding of relative power is also needed, as discussed in resource dependency theory. This followed Segalla et al.'s

thoughts that reward strategies are determined by managers using insights from the human resource management, general management and marketing literature but alongside “idiosyncratic factors related to their personal and cultural characteristics” (2006: 420).

Fernandez-Alles et al. (2006) also discovered that reward mix design is heavily influenced by the company’s adoption of popular practices that increase legitimacy, but not necessarily performance. Financial objectives, as agency theory contends, are not always the final goal but other social objectives, such as the search for legitimacy, are important.

Approaches that have combined agency with resource dependency also conclude that the explanatory power of the combination is stronger than when agency is applied on its own (Tremblay et al., 2003; Yanadori and Marler, 2006; Elvira, 2001; Carpenter and Wade, 2002). Yanadori and Marler (2006) showed that the increased compensation risk that comes with longer term incentives, which they show are payable to strategic groups of employees, may be counterbalanced by increased job security that these groups enjoy due to their criticality.

The combination of resource dependence with institutional theory has also been shown to enhance insight into reward mix decisions, albeit with fewer studies solely taking these two perspectives (Festing et al., 2007; Milne, 2001). Both resource dependence and institutional theory share the drivers of their actions as internal and external forces, with legitimacy as an important factor. Whilst the reactions to these pressures are often deemed strategic (resource dependency) and passive (institutional), based on the extent to which legitimacy can be pursued (resource dependency) or the extent to which it is

just imposed (institutional). However, the assumption of passiveness underpinning institutional theory has been questioned as conformity of this type may be a conscious strategic choice given the significance of legitimacy for the business model (Norman et al., 2007).

In Barringer and Milkovich's (1998) model, all three perspectives plus transaction costs theory were used to derive pertinent determinants of managerial reward decisions. This integration of theoretical perspectives was a major contribution provided by this work. Although others have integrated combinations of the theories, this was the first (and as far as I am aware only) detailed explanation of more than two perspectives, which is more typical. Again, they concluded that in this situation the explanatory power of flexible benefit system adoption would be improved by this multi-theoretical perspective.

2.5 The role of benefits

As the benefit component of reward mix is largely excluded from reward mix research discussed above, a separate review of what we know about the determinants of benefits provision is required to close this gap. As far back as 1994, Williams and MacDermid (1994) note that benefits, although an increasing proportion of the overall compensation spend, had been subjected to limited research to understand the drivers of this expenditure. Perkins and White (2008), note that little has since changed, with no clear theoretical approach emerging to understand the role of benefits in the overall reward mix.

As discussed above in the context of institutional theory, changes in tax regulations have been shown to be influential (Tremblay et al., 2003; Gustman et al., 1994).

Gustman et al. (1994), in line with Long and Scott (1982), identify tax savings for both the employee and employer as a significant driver to the provision of reward through pension contributions rather than cash salaries. Abbot and De Cieri (2008), in their case studies of work-life benefit provision in two companies, found that both companies noted the significance of tax legislation on decisions to implement certain benefits and, significantly, how the tax regime was leading to lower provision of certain benefits.

Other influences have been suggested: First, employers' ability to negotiate group discounts for certain benefits relative to that which the individual employee would be able to get in the market and, consequently, increase the value of the reward mix to the employee at no extra cost to the employer (Gustman et al., 1994; Lucero and Allen, 1994). Next, scholars have identified that the proportion of benefit to cash compensation had increased as demand for this form of reward was influenced by demographic factors such as increases in life expectancy, retirement trends and changing employee preferences for leisure. They outline that as life expectancy increases employees will want to defer a greater proportion of their lifetime income beyond retirement and thus will demand more deferred compensation (Gustman et al., 1994). Accompanying this we have seen a shift in employee preference for increased leisure (Lucero and Allen, 1994). Perkins (1998) noted that this was in line with expectancy theory predictions, with the provision of benefits only leading to increased performance if the workforce actually values them. This has been given as a significant driver for the introduction of flexible benefits schemes that allow employees choice over benefits they receive within a defined budget¹⁰.

¹⁰ Flexible benefit plans, which hand control of some of the reward mix decisions to employees, came into being in the early 1970s in the US and gained prominence in the 1980s (Perkins and White, 2008) .

The Employee Benefit Research Institute (Employee Benefit Research Institute, 1991) identified two main drivers for the adoption of flexible benefits schemes. First, the belief that increased employee choice will increase employee benefit satisfaction, and second costs will be better controlled by moving from defined benefit provision to defined contribution benefit provision. Limited scholarly work has supported these claims (Barringer and Milkovich, 1998; Beam and McFadden, 1996). Hillebrink et al. concluded that “the more diverse an employee population, the more incentive there is for an organisation to let employees choose the benefits they prefer, instead of attempting to find a standard package that is of greatest value to most employees.” (2008: 307). However, research by Slade et al. (2002) found that employees expressed surprisingly similar reward preferences across job groups, salary levels and tenure, suggesting that the benefits of employee choice may be overstated.

Next, union power has been shown to influence the proportion of non-wage compensation, through increased understanding of the tax and group saving discounts that are generally available in unionised environments due to union communication (Medoff, 1979). Medoff also notes the role of collective bargaining in ensuring management is aware of employees’ preferences for these non-wage components. In addition, and more cynically, Mabry (1973) suggests that unions themselves may prefer this form of compensation due to the bureaucracy and increased complexity it brings, potentially strengthening the reason for the unions’ existence. There is some evidence to support the claim that unions are having an effect, e.g. pension benefits have been found to be generally higher in unionised firms (Gustman et al., 1994). Gustman et al. (1994) attributed this to the unions’ desire to meet the preferences of the average

worker, who is typically older than newly hired workers and therefore places a higher value on pension provision.

Others have contended that benefits, especially defined benefit pensions, may be instituted to develop long-term loyalty as workers are accepting lower wages in return for a future return (Long and Scott, 1982; Gustman et al., 1994; Lazear, 1998). Lazear (1998) contends that long-term deferred compensation through defined benefit pension provision provides an incentive for workers not to shirk, especially as they approach retirement. Due to difficulties obtaining data, this long-term deferred effect of defined benefit pension schemes does not appear to have been tested. However, we do know that turnover is typically lower in organisations that offer pensions compared to organisations that do not (Ippolito, 1987) although this may be down to employees taking a lifetime view of earnings, as Lazear suggests.

A further justification for benefit provision has been made on historical and philanthropic grounds (Perkins and White, 2008). The first benefit packages (e.g. Rowntree, Lever Brothers and Cadbury) were largely provided on philanthropic grounds by these family businesses, but also the belief that the health of the workforce would be improved and therefore productivity would increase. This is in line with Flannery et al.'s (1996) assessment that benefits should be categorised not with respect to the objective they are looking to achieve, but contingently on the type of organisation that is providing them and the organisational culture they have.

Finally, the extent to which benefit provision is part of the reward mix has been put down to concerns over the burden administering such schemes can present (Conlon and Parks, 1990; Barringer and Milkovich, 1998; Beam and McFadden, 1996). Conlon and

Parks conclude that fixed forms of reward were more likely, simply because they are easier to implement, “a ready solution” (1990: 606). Barringer and Milkovich (1998) propose that organisational size will impact on the extent to which organisations implement flexible benefit plans, given the cost of doing so and the higher cost per employee of implementing such schemes. This conclusion may be extendable to standard benefit schemes which will also have administrative running costs (although, as discussed, tax savings may distort this).

The extent to which benefits are provided as part of the reward mix has been summarised by various scholars into benefit typologies. Perkins and White (2008) conclude that benefits are given for four different organisational objectives. First, some benefits are required by law, such as minimum holiday entitlement and statutory sick pay. Second, some are to compensate employees for expenses incurred in the normal course of their duties, such as travel expenses and company car use. Third, some are ‘welfare’ benefits designed to elicit loyalty through the impression of a caring employer. Finally, some are status benefits meant to reflect the level at which someone works and reward them for the extra responsibility this entails. Other typologies have been proposed which are similar to this, e.g. Hume (1995) (financial security, financial assistance and employee personal needs), Smith (1983) (security, goodwill and performance) and Wright (2004) (security and health, job status and seniority, family friendly, and social, goodwill or lifestyle benefits), but broadly they agree on the main drivers. However, there is limited empirical testing of these conjectures; what testing has been done is dominated by examination of pensions and health care benefits (Perkins and White, 2008).

2.6 Epistemological approaches

Having reviewed what we know about RMD we will now examine how we come to know it.

Review of the literature shows that a positivist approach has directed the area of reward research, with quantitative methods dominating both experimental and field-based work. For example, Werner and Ward's (2004) review of the compensation literature in 20 top management journals over a seven year period from 1996 to 2002 showed that of the 396 studies identified 4.5% were theoretical, with the rest being quantitative (either direct or meta analytic) analysis of data.

Has the dominance of research under one epistemological approach created potential shortcomings in our knowledge in reward determination? The statistical approach has led to a large number of determinants being identified but has told us little about why the relationships may exist. Whilst the statistical analysis may have established relationships between the variables being examined, authors could then only speculate and propose potential reasons why these relationships might be the case (Yanadori and Marler, 2006). This led Taras to conclude that "it is perhaps troubling that while scholars clearly are able to develop strong rational models of wage determination based on inferences derived from large data sets of wage outcomes, they are caught short when exposed to the often intuitive or baffling decisions of actual compensation managers" (1997: 181). Consequently she proposed that "it is appropriate now to simply ask compensation managers about their decisions, if for nothing else than to posit some plausible explanations for further testing" (1997: 181). Heneman and Judge, albeit in the context of research on employee pay satisfaction, noted that "we must enter

the field, rather than merely survey it, if we are to fully understand and appreciate its context and changes” (2000: 369). Bloom and Milkovich add to this that “ours is a field of inquiry irrevocably intertwined with the decisions of practical people” (1996: 40). However, in the time since that was written reward research remains largely one step removed through archival and survey research rather than field-based as suggested.

In the context of executive pay, Bender and Moir note that the research has been overwhelmingly dominated by a positivist approach, stating that “these are to some extent static analyses: they use archival data to examine the outcomes of the remuneration setting process, but not the processes themselves” (2006: 76). They therefore suggest that a qualitative approach is the most effective way of understanding not just *what* firms are doing, but also *how* and *why* they are doing it.

Work on remuneration committees in the UK has taken a different approach to “look inside the black box” (Main et al., 2008: 226), of the decision making process through qualitative interviews and analysis rather than using archival or quantitative survey data (Bender, 2004; 2004; Ogden and Watson, 2008; Main et al., 2008; Perkins and Hendry, 2005; Bender and Moir, 2006). Given this developing qualitative base at executive level, it is surprising that little qualitative work has been done below executive level.

However, although infrequent, interview-based studies of employee organisational reward issues have been carried out, despite reservations that the social element of the reward decision may influence what is said (Bartol and Martin, 1988). Eisenhardt predominately used survey data in forming her conclusions on agency and institutional influences on compensation in the retail industry but did “enrich insights” through qualitative questions which she asked of store managers. She noted that this approach

supplemented the quantitative data to “develop a better understanding of how retailers think about managing and pay” (1988: 498).

A similar approach was taken by Elvira (2001) in her case study of a financial services firm and how agency theory relates to issues of employee promotion. Whilst predominantly statistically driven, the research did follow up the results with interviews with human resource executives and a number of employees. This was considered justifiable to help counter the criticism that economic-based theories do not take into account the social structures which will influence behaviour and through this treat the organisation as a ‘black box’ not a system of social relations (Elvira, 2001). This led her to conclude that “research progress depends on integrative approaches to how economic and social forces interact and the conditions that determine their balance” (2001: 367).

Segalla et al. (2006) also go against the trend for a solely quantitative-based approach, sending out a specific scenario to managers to help elicit their objectives, combining the scenario with an open-ended question to understand why the choice was made. They justified this choice in two ways. First, they argued that simply providing managers with a list of potential objectives (which, from the review of the literature, are numerous) might influence the true reasons. Second, they note that given they are looking to examine why actual choices are taken it supported an open-ended exploratory approach. This approach helped them discover that the espoused rationale for the decision to use incentives was to motivate employees and fixed pay to manage equity issues. Taras (1997) takes a more inductive approach, to explore in more depth the reward mix issues in the Canadian petroleum industry. She uses a combination of

qualitative and quantitative methods and, with respect to the interviews she carries out, notes that she “found that managers were startlingly open about themes that rarely appear in existing wage-determination literature” (1997: 184). A further exception is Fernandez-Alles et al. (2006) who use a case study approach to examine why efficiency is not always the driver of reward mix decisions. The approach was justified as it was felt a case study approach was particularly suited to exploratory research in an area that lacked clarity or was subject to a number of different explanations (Eisenhardt, 1989b).

To conclude, much of what we know about RMD is known through a positivist epistemology. An emerging body of work is developing taking a social constructionist approach to reward determination. This has developed in the light of findings that institutional pressures exist and influence reward decisions as a potential means to establish not only what is driving reward decisions but significantly why those factors are driving decisions. This is an attempt to move beyond deducing reasons why, to explore with decision takers the actual situational pressures they are under when they determine reward strategy.

2.7 Gaps in the literature for further examination

The literature review has examined what is already known about RMD for employees and also assessed how we come to know this with a view to determining what gaps remain in our knowledge. A summary of the three theoretical perspectives examined, based on the findings of the literature review, is given in Table 2-4.

	Agency	Resource Dependence	Institutional
Purpose of reward mix decisions	To control and direct behaviour towards the objectives of the principal especially when monitoring is difficult/costly	Acquisition of business critical resources	Conformity with other organisations and market practice to gain legitimacy
Main Assumptions	<p>Rational decisions</p> <p>People are self-interested, risk averse</p> <p>Goal conflict exists between owners and employees</p> <p>Information asymmetry</p>	<p>Rational decision</p> <p>Control of critical resources leads to power</p>	<p>Organisations seek legitimacy</p> <p>Organisations conform to norms</p> <p>Process of satisficing behaviour</p>
Organisational reaction	Rational active management	Rational active management	Passive conformity or rational legitimacy seeking
Implications for reward mix	Relative weight of incentives versus fixed reward will be managed to optimise the alignment of agents' and principals' interests	Reward mix will be influenced by the relative strength of employee groups determined by their criticality to organisation success	Reward mix will be influenced by institutional norms and the extent to which operating within them confers legitimacy

Table 2-4 – Summary of agency, resource dependence and institutional theories

Each of the theoretical perspectives has offered a slightly different explanation about what factors influence RMD in organisations.

If agency theory is to be accepted, then we might expect RCs and REs to discuss how monitoring of employees, efficiency considerations around this monitoring and the span of controls of managers has determined the mix of at least fixed and variable pay. However, it has little to say about the benefits or relational elements of the reward mix. Resource dependency meanwhile focuses on the relative power between the actors involved in the employment exchange. Organisational success will be controlled by those individuals, groups of individuals or influential organisations, who control access to critical resources needed for that success. Consequently, reward mix, including the benefit component, will be developed with the acquisition and retention of those critical resources in mind. Institutional theory questions these more economic and resource efficiency-based approaches, identifying a societal dimension to RMD as organisations seek to gain wider ranging legitimacy. Reward mix is therefore largely driven by fixed constraints, both legal and tax regulations, alongside pressure to conform to the practice of other successful organisations or prescribed best practice.

The factors that have been identified, through the literature review, as potentially having an influence in reward mix decisions are summarised in Table 2-5.

Theoretical Perspective	Decision driver
Agency	<ul style="list-style-type: none"> • Alignment of employee effort • Managing monitoring costs (spans of control and contract type) • Business risk
Resource Dependency	<ul style="list-style-type: none"> • Attraction and retention of critical employees/employee groups • Task complexity and the need for specialist skills • Ease of employee monitoring and performance visibility • Substitutability of skills • Task centrality • Organisational connections • Union dominance
Institutional	<ul style="list-style-type: none"> • Legal requirements • Political and societal pressure • Taxation and other regulations • For subsidiaries of multinationals, parent group policies • Union pressures • Historical precedents • Benchmarking others' practice • Consultants' advice • Professional networks • Codification of practice in reward qualifications • Organisational exposure to other institutional settings • CEO and board members' business education and experience • Cost of loss of legitimacy against benefit of differentiation

Table 2-5 – Potential reward mix determinants

With what we know, what must be asked next? The review has highlighted four areas where further investigation is required.

First, we need to examine RMD for all employees, not just executive management. Although a range of studies have examined RMD they have been dominated by research at the executive level and in particular the Chief Executive level. This is unsurprising given the significant decision making authority that individual has and also the availability of data on executive reward. However, it may also be misguided, given the

significance of employee compensation relative to organisational cost. Focusing solely on the CEO attributes all the success of the organisation on that one compensation decision and the effect it has on one individual. This creates the impression that the remainder of employees make little contribution to the organisation's success. Hambrick and Mason (1984; 2007) showed that the success of an organisation depends on all contributions. This led them to "encourage 'pay strategy' researchers to extend their examination of pay practices to include ever-lower levels of the organization" (1984: 375). Further review of RMD at employee level is needed.

Second, we need to broaden the conceptualisation of reward mix used in research on RMD. The review highlighted that reward mix has been conceptualised in numerous ways in the academic literature. For example, a narrow definition of reward mix has been conceptualised through the use of the ratio of base salary to short-term bonus payments as this was perceived to be the most common form of incentive pay (Gerhart and Milkovich, 1990; Eisenhardt, 1988; Boyd and Salamin, 2001; Werner and Tosi, 1995; Gerhart and Trevor, 1996; Bloom and Milkovich, 1998). Alternatively, others have widened this simple ratio to examine the proportion of base pay to cash compensation i.e. including both short- and long-term incentives (Tremblay et al., 2003; Roth and O'Donnell, 1996; Tremblay and Chenevert, 2005; Burke and Hsieh, 2006). This, of course, misses a proportion of reward mix with respect to the benefits that employees receive and the relational returns that also accrue from employment around the job and the work environment. Investigations should therefore include all elements of reward, not just those that can be easily statistically measured.

Next, we need to provide greater order and develop deeper understanding through explanation of the influences on RMD. The literature review established a long list of factors that have been shown to have statistical relationships to reward mix – ‘The shopping list’. Within this ‘list’ agency theory has emerged as the most prevalent explanation for the reward mix decision. However, there is some more limited evidence that reward decisions are taken that are not always in line with the expectations of agency theory but, additionally, social interactions appear to have an influence. Further examination of RMD is needed to understand and explain these influences and, through this, provide greater structure and clarity to our understanding of RMD.

Finally, we need to examine RMD from an alternative research paradigm in order to develop our explanations of the approach firms are taking. Much of what we know about RMD is known through a positivist research approach. However, an emerging body of work has developed taking a more constructionist approach to reward determination as a potential means to establish not only what is driving reward decisions but significantly why, albeit at executive level (e.g. Bender, 2004; Ogden and Watson, 2008; Main et al., 2008; Perkins and Hendry, 2005; Bender and Moir, 2006). Building theory from a different research paradigm will add insight to the area through revised theory generation and potentially contribute to simplifying the field.

2.7.1 Conceptual framework and research questions

Whilst agency theory has emerged as the most voluminous perspective through which reward mix has been examined, the other theoretical viewpoints have been shown to potentially have further explanatory power. A theoretical conceptual framework derived from these theoretical standpoints is presented in Figure 2-1.

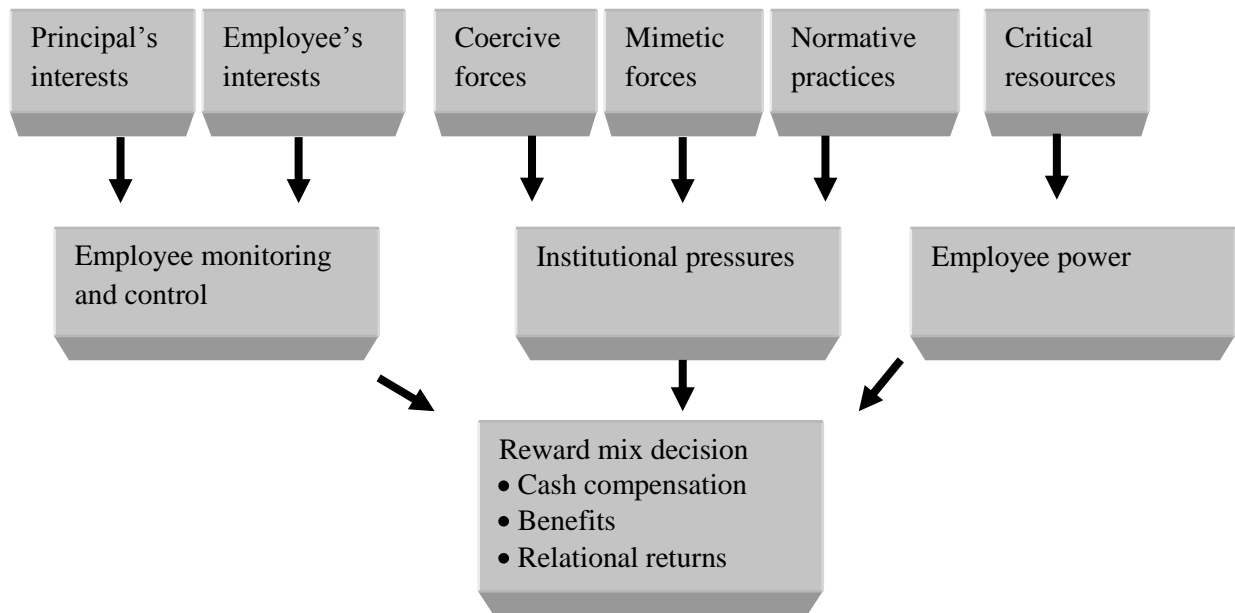


Figure 2-1 - Conceptual framework

This conceptual framework presents interests, forces, practices and resources as theoretical drivers of reward mix decisions. It forms both the base for the examination of RMD and the main research question.

Research question (RQ) – What influences RMD in financial services organisations?

Gerhart and Rynes identified that although reward strategy is a matter of various choices, “surprisingly little is known empirically about how such choices are made in the first place” (2003: 7). Theory suggests that there is potential for significant variance in how organisations design their pay systems including choice over what reward mix to offer (Rynes and Bono, 2000). This is in contrast to the choice over the amount they pay where there appears to be less discretion due to the need to stay broadly in line with others for attraction, retention and overall economic competitiveness reasons (Gerhart and Rynes, 2003). However, it is not clear from the research what factors reward specialists consider when determining reward mix, why these factors are influential and how this explanation compares with what theory might suggest.

Through the literature review a number of sub questions are also suggested. Each of these questions is now presented and briefly discussed.

RQ2a To what extent is the alignment of principal and agents' interests and the issues of monitoring and control an influence in RMD?

RQ2b Why are they / Why are they not an influence?

As has been outlined in this chapter, agency theory provides significant insight into how goal incongruence, differing risk preferences and information asymmetry can be managed. At the centre of managing these issues is the organisation's reward mix policy, particularly around the balance of fixed and variable reward. Wiseman et al. outlined the importance of aligning agents' reward to outcomes that the principal values to "create a common fate" (2000: 312). A higher proportion of variable pay in the overall reward mix is intended to achieve this common fate by tying employees' interests to those of the firm (Gomez-Mejia and Balkin, 1992; Delvey, 1999).

Under agency theory, the literature suggests that incentives are provided to try and align employee and employers' interests. "Paying individuals to do X causes them to do X." (Prendergast, 1999: 11). The main barrier to establishing contracts in this way is the additional cost employers will incur as employees require compensating for the higher risk that contracts of this type imply (Gerhart and Trevor, 1996; Balkin and Gomez-Mejia, 1987; Gomez-Mejia and Balkin, 1992). The extent to which it is rational to pay this premium will depend on the ease with which the roles can be monitored by management and how the cost of monitoring compares with the risk premium that will be payable (Conlon and Parks, 1990; Eisenhardt, 1989a).

As shown in the conceptual framework, alternative views have been offered to explain the reward mix relationship. The next two research questions attempt to explore two of these perspectives by introducing institutional and resource dependency theories as potential complementary explanations.

RQ3a To what extent are coercive, mimetic and normative institutional pressures an influence on RMD?

RQ3b Why are they / Why are they not an influence?

We have seen that a range of institutional pressures are likely to exist. Coercive pressures can take a number of forms such as employment legislation, social goals of government, taxation policies and restrictive head office controls. Mimetic pressures would appear to be commonplace in the reward field. The diffusion of policies and approaches may come from a number of sources (DiMaggio and Powell, 1991) including the movement of reward professionals, the activities of reward consultancies, and professional trade and professional bodies, and through this the arrangement of practice into codified principles and accepted standards. Normative practice may also be established through training and education programmes.

RQ4a To what extent do the reward mix preferences of critical groups of employees influence RMD?

RQ4b Why are they / Why are they not an influence?

Decisions on how dependent an organisation is on an individual or group of individuals are likely to influence reward mix decisions for this individual or group (Tremblay et

al., 2003; Pfeffer and Davis-Blake, 1987). Talent shortages and the resulting dependency this can create for organisations are widely reported (Michaels et al., 2001). Any individual or organisation controlling critical resources can exert pressure, including the design of reward practices and specifically organisational reward mix (Balkin and Bannister, 1993).

Addressing these questions begins to answer the call made by Gerhart and Rynes for research to “uncover the mental models used by real executives and compensation specialists in designing pay programs” (2003: 78).

2.8 Conclusion to chapter two

This chapter has positioned the research question of what influences RMD within the reward literature and from this developed a series of supplementary research questions. The literature points to a number of influences which I have explored. However, from this it is still not clear what the influences are and how they apply to the financial services sector at this time. This thesis develops and assesses empirically a conceptual model in order to better understand those influences. The framework is built around the theoretical explanations of agency, institutional and resource dependency theories.

Having established the research question to be addressed, the next chapter presents the approach taken to examine it.

3 Chapter three: Research design

3.1 Introduction to the chapter

The purpose of this chapter is to provide the link between the research gap, conceptual model and resulting research question identified through the literature review in chapter two with the empirical work to follow in the later chapters by setting out and justifying the methodology and methods pursued in this research.

First, in section 3.2, I outline the philosophical position the research takes, the assumptions this means have been made about the nature of social reality and, from this, the way it is proposed that knowledge can be created. Section 3.3 outlines the qualitative approach taken in the research as the best means of generating theory from the accounts of those closely involved in RMD. Section 3.4 describes the research programme. The methodology chapter ends in section 3.5 with a discussion of how the approach meets established qualitative standards of quality, reliability and validity.

3.2 Research strategy

3.2.1 An abductive approach

The choice of research strategy has significant implications for later research choices, both philosophical, with respect to ontological and epistemological positions, and methodological with regard to the use of concepts and theory, styles of explanation and the status of the understanding developed (Blaikie, 2007). A coherent approach is required to ensure that the ontological, epistemological and from this the methodology are all consistent (Burrell and Morgan, 1979).

As outlined in chapter 2 a largely deductive approach has been taken to reward research to date. This research takes an alternative research strategy to the dominant deductive

route, abduction, to answer the research questions. Abduction explores the everyday language used by social actors and then seeks to re-describe this language in the form of a social scientific account. It goes beyond observation of actors and explores the understanding and meaning put on process and events by the actors themselves. Blaikie summarised this when he stated that “the aim is to discover why people do what they do by uncovering the largely tacit, mutual knowledge, the symbolic meanings, intentions and rules, which provide the orientations for their actions” (2007: 90). He added that abductive research was “the process of moving from lay descriptions of social life, to technical descriptions of that social life” (2007).

This research strategy does present a range of challenges. Everyday social activities are often carried out without conscious recognition of their motives as much of what we do is taken for granted (Blaikie, 2000; Easterby-Smith et al., 2008). Therefore, discovering this meaning will take both time and skill. Blaikie noted that “it is only when enquiries are made about their behaviour by others (such as social scientists) or when social life is disrupted, and/or ceases to be predictable, that social actors are forced to consciously search for or construct meanings and interpretations” (2000: 116). Eliciting the “taken-for-granted” (2000: 116) assumptions will require developing understanding of the language of those involved in RMD and facilitating their thought processes so that they are able to articulate the assumptions that are not openly apparent. Further, managing the relationship with the social actors will be significant. In the abductive approach, researchers need to ensure that they are sufficiently close to the individuals concerned to be able to re-describe the phenomenon outlined and, through this, ensure that they stay true to the phenomenon being explained. This is particularly significant as traditional methods of triangulation often adopted in research are not appropriate for this approach,

given that reality being examined is constructed and consequently does not have an independent existence of its own (Blaikie, 2000). These challenges are addressed in the method followed to gather data.

The overall philosophical paradigm needs to be consistent with the research strategy to be pursued (Easterby-Smith et al., 2008). Consistency is required in the choices taken throughout (Burrell and Morgan, 1979). A schematic of the choices taken in this research is shown in Figure 3-1. This shows both the more traditional research strategy choices deployed in reward research (in red), compared to those utilised in this research (in green). Each of the stages shown in the schematic is discussed in this chapter.

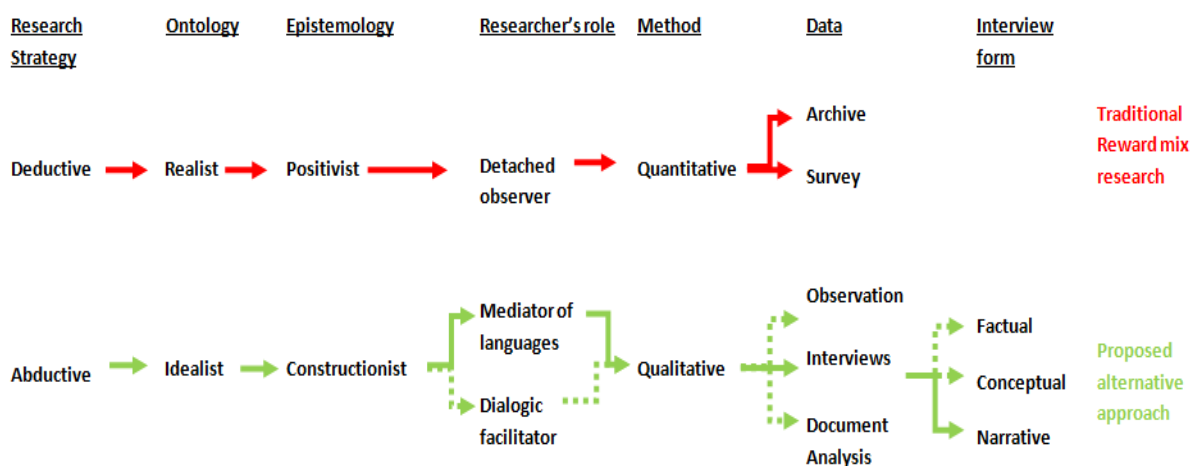


Figure 3-1 - Philosophical route map

Guba and Lincoln argue that the last 15 years discussion of research paradigms has been much less about “irrecoverable conflict” (2005: 192), which had characterised this debate previously, and more about research undertaken under different research paradigms “informing one another’s argument” (2005: 192). This is certainly the position this research approach takes with its overall aim of building on the deductive research carried out in the reward field to date through adoption of a different research

stance. In turn it is expected that the findings of the research will lead to further deductive testing in the future.

3.2.2 Ontological position

Blaikie defines ontology as “a branch of philosophy that is concerned with the nature of what exists” (2007: 13). The key choice to be made is between whether social reality is believed to be objective or subjective (Burrell and Morgan, 1979; Easterby-Smith et al., 2008). The objective or realist position proposes that it is possible for the phenomenon of interest to be studied independently of the researcher, given that it is believed to have an independent existence from the researcher. This is largely the approach taken by reward scholars (across all areas of reward research not just reward mix) to date through the use of statistical analysis of archival remuneration datasets or survey results collected by the researcher themselves. An alternative view is a subjective or idealist perspective which Blaikie notes is built on a belief that “social action is not merely behaviour but, instead, involves a process of meaning-giving” (2007: 17). These two ontological perspectives lay at the ends of a continuum of potential views on the nature of social reality (Blaikie, 2007; Easterby-Smith et al., 2008; Laughlin, 1995).

An idealist position is taken in this research consistent with the abductive research strategy pursued. There are a number of objective realities present in the reward area, such as organisations providing defined levels of monetary return to each employee in return for their efforts and that return is provided in some proportion, or mix, between base pay, incentives and benefits. Whilst the realist approach to social enquiry is well equipped to examine these objective realities, it appears less equipped to answer why organisations adopt the reward position they do. The reward mix literature review has

already identified that RMD is potentially complex with a large number of variables having been identified as being statistically related to the final reward mix established. However, this realist-based work has not adequately explained why the variables that are relevant are chosen over other potential influences. This research contends that, alongside the objective reward realities that do exist, there are also phenomena that are constructed such as RMD and the influences on it that varying internal and external factors may have. The literature review findings, and the emerging significance of institutional theory as a theoretical explanation of reward determination outside the more objective paradigm of agency theory, would appear to be consistent with this approach. Overall, the research aims to understand the different constructions and meanings that those interviewed put on their experience (Easterby-Smith et al., 2008).

3.2.3 Epistemology – How we come to know

Epistemology is “a theory of knowledge....of how human beings come to have knowledge of the world around them (however this is regarded), of how we know what we know” (Blaikie, 2007: 18). Choices need to be made about the epistemological position taken for research in line with the perspective the researcher has on what knowledge is. Consistent with the idealist ontological position taken, the research adopts a constructionist epistemological approach. Crotty defined constructionism as “the view that all knowledge and therefore all meaningful reality as such, is contingent upon human practices, being constructed in and out of interaction between human beings and their world, and developed and transmitted within an essentially social context” (1998: 42). Within this position the facts exist and are there to be discovered but it is individuals who make sense of the facts and construct meaning from the reality they see.

An organisation's reward mix is an outcome that will be arrived at within a social context. A range of individuals, through their ongoing interaction, are likely to have an influence on this outcome, through both formal and informal involvement (Perkins and Hendry, 2005). The research will examine this outcome and significantly the influences on it, as seen by REs and those who closely advise those individuals - RCs. The literature has shown that a range of institutional factors would appear to have an influence on reward mix decisions be they mimetic pressures from other firms, coercive pressures from government and regulatory bodies, or normative pressures through the conventions that have established themselves across the reward profession and been codified as best practice and spread through qualification, conferences and networking. Given this, exploring, describing and understanding this interaction will need to be carried out through social engagement to understand the process of meaning that they bring to all these factors.

3.2.4 A constructed research approach

The literature review shows that despite strong theoretical reasoning, in the form of agency theory, for how reward mix should be determined related to individual firm circumstances, many firms appear to be operating iso-morphically. The research questions focus on trying to establish empirically the influences on RMD and, once the drivers have been established, why these influences are significant. So, for example, if the research supports the findings of Eisenhardt (1988) and others, that isomorphic influences are strong in RMD, I will be looking to understand what the specific isomorphic influences are and why they are driving the behaviour of the REs being examined.

Burrell and Morgan (1979) identify that philosophical decisions need to encompass the extent to which the world being examined is objective or subjective, i.e. are there hard facts that can be examined and established? Does the reality exist independently of me as researcher and is just waiting for me to go out there to discover it, or do I as researcher through my interaction with those being researched have a role to play in constructing the reality?

This research adopts an epistemological position that does not believe that knowledge can only be formed from the study of causal relationships and examinations looking for regularities. These do exist, as acknowledged above with reference to money as a measurable unit of value that is given to employees in different tangible (base salary and bonuses) and less tangible (benefits) forms. However, the research question examines influences on RMD and the understanding individuals have as to why those influences are meaningful to them. Therefore the knowledge to be generated is developed subjectively and with sensitivity to the context in which it is being discovered. Significant in this approach is the interpretation I make of what I am hearing and seeing from the interaction with REs and RCs and the dialogue we have in developing the accounts on RMD. In doing this reflection will be key in my interpretation in “appreciate(ing) the different constructions and meanings that people place upon their experience” (Easterby-Smith et al., 2008: 59).

3.2.5 Recognising the role of the researcher

Vinnicombe and Turnbull (2002) note the importance of understanding your own experiences and personal preferences when determining a research strategy. They argue that researchers should explore their preferences and use them within the research

design, but with full awareness of their existence and how they might influence research outcomes. I outline in the preamble the influence my experience both in financial services and HR and reward management have had on the motivation for carrying out this research. I also believe this experience has influenced the philosophical position I am proposing to adopt. On joining academia I, like many other PhD students before me, threw myself into the literature. The reward literature is extensive and heavily dominated by a positivist research approach. Whilst finding the statistical relationships shown to exist between a range of factors related to reward strategy and more specifically reward mix interesting, I also, drawing on my own previous personal experience as an HR professional, felt this approach was missing significant elements that influenced RMD. My experience of reward determination had been much less clear-cut than I felt was suggested by the positivist research that I read. Decisions were rarely taken with reference to very specific hard data and clear strategic direction as often suggested in the research, as strategic direction was seldom clear-cut in what was a fast moving environment. Rather, my experience was one of reward strategy emerging through iterative dialogue drawing on my own and my team's interpretation of elements, such as the beliefs of our leadership team, the historical experiences of the organisation, practice elsewhere in the market and large amounts of benchmarking data provided by reward consultancies. We had to make sense of this data in the context of our organisation and the internal and external environment we faced. This all occurred before I even knew what ontology and epistemology were, or the role that they play in influencing research designs. From this it would appear that my chosen philosophical perspective is influenced by my interpretation of the world that I am looking to examine and how I have found, through my experience, that sense is made in that environment.

3.2.5.1 Behavioural preferences

Vinnicombe and Turnbull (2002) suggest the use of Myers-Briggs Type Indicators¹¹ as a useful tool when assessing personal preferences as a starting point for exploring how the researcher may prefer to collect data and make decisions, where the energy to complete the work will come from, and how priorities and planning will be carried out. The implications of my Myers-Briggs type for this research are summarised in Table 3-1.

Preference	Definition	Potential research implications
Extraversion	Where we source our energy from. Sources energy from being with people, focusing on the outside world and understanding what is happening, variety and action.	Well suited to iterative approach to theory building, i.e. developing ideas and exposing them to others for input at an early stage, and research in the field involving human interaction through interviews and networking.
Intuition	Perceptual preferences. Trusts instincts to make connections across diverse information. Values insight and creative thinking and generalising to larger meanings. Potential to overlook detail.	The generation of ideas and the building of models will appeal which should relate well to an abductive iterative approach to theory building. Care required not to overlook factual data that are presented in preference for more abstract and intuitive patterns that may be apparent.
Feeling	How we make decisions. Concerned with feelings of others, seeking to find out what is important to them, empathic. Tends not to critique others but find appreciative position of their perspective.	Supports the need for immersion in the data and through this developing deep accounts of what actors are saying and through that interpret their meaning from their own personal and unique standpoint. Aligns well with the constructionist position and the interpretation that is required from the data collection.
Judging	How we make time and prioritise. Plan and anticipate ahead, scheduling time carefully, making quick decisions. Believe regular steady effort leads to accomplishment and enjoys completion.	Supports a project and planned methodology which may be in conflict with the need to search in unplanned avenues as theory builds from the data gathering. Need to maintain discipline to ensure that rigour is applied to following those avenues and not compromised for the sake of meeting the timetable.

Table 3-1 – Myers-Briggs preferences and their implications for the research strategy

¹¹ An individual's Myers-Briggs Type is identified through the completion of a psychometric questionnaire intended to identify an individual's preferences with respect to how they make judgements and perceive situations. (Briggs-Myers and Myers, 1993).

3.2.5.2 Researcher stance

Within the context of both my experience and behavioural preferences, I need to ensure that my role as researcher recognises these preferences, plays to potential strengths and stays focused on answering the research question.

Blaikie (2000) suggests six potential stances for the researcher on a continuum of complete detachment to deep involvement, as shown in Figure 3-2.

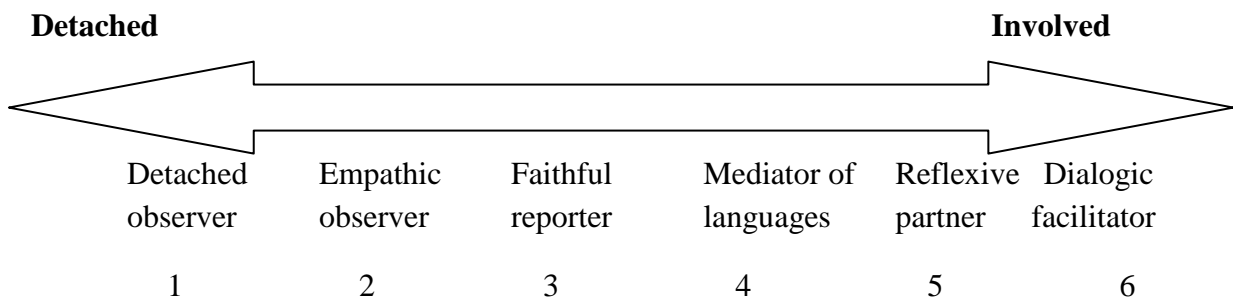


Figure 3-2 – Researcher stances

Stances 1 to 3 are based on the premise of detachment and are therefore inconsistent with the philosophical position taken. The reflexive nature of this research suggests one of stances 4-6 should be adopted. Stance 5 is more aligned to those typically taken by critical theorists or feminists with the researcher operating as a co-participant, with an objective of “emancipation of the participants from whatever kind of oppression they are facing” (Blaikie, 2000: 53). The raising of the actors’ consciousness of RMD that will come from the research may result in personal and organisational insights which are valuable to those individuals or their organisation (Habermas, 1987). However, given that the aim of the research is not to trigger action within individual organisations, nor is it underpinned by some judgement of societal failure, then this appears to be an inappropriate research stance. Stance 6 “attempt[s] to minimize their authorial bias by letting the natives speak for themselves as much as possible. The aim is to produce a

‘polyphony’ of voices rather than a single voice, in order to reduce bias and distortion.” (Fontana, 1994: 214). As the identified gap in the literature is one of confusion, because a multitude of perspectives have been offered on how reward mix is determined, it is proposed that although a range of views will be used to develop theory in this area these will be brought together into a unified scholarly theory of RMD. This leaves stance 4 whereby the researcher aims to develop a scholarly account based on the lay accounts of the actors involved (Giddens, 1976). This requires interpretation on behalf of the researcher and therefore can never be seen as detached or objective. This is consistent with the philosophical stance being taken in the research and supported by the author’s personal working preferences.

3.2.6 Summary

Laughlin (1995) identified that research strategy was not a matter of extreme either/or choices as they are sometimes presented, i.e. objective versus subjective, positivist versus constructionist. Rather, there are matters of degree in all the choices researchers face.

The methodological approach to be taken is as follows. Reward facts exist. Knowledge on these facts can be generated through examination of causal relationships and relationships between variables. Much understanding has been provided in the reward research field using this approach. However, understanding how reward mix is determined is not an area of objective fact – the determination process has to be interpreted.

Given the research question, the philosophical stance and influence of the researcher’s preferences, a largely qualitative approach is considered relevant. Research examining

the meaning and perspectives of individuals “lends itself to getting out in the field and finding out what people are doing and thinking” (Strauss and Corbin, 1998: 11). The next section outlines the precise methodological choices considered in taking the research forward, describing how they operated within the research.

3.3 Method

This section lays out the structure of the research method.

3.3.1 Data sources

Adopting a constructed viewpoint means working on the assumption that the factors influencing reward mix are determined as a result of human interaction. This does not mean that interaction is required with everyone who may be involved with the process, but rather that research needs “to decide which view offers us the best way of understanding ourselves and others and thus of guiding our research” (Burr, 2003: 32). Decisions have to be taken on whose views the research should access.

The process by which reward mix decisions are taken is likely to involve social interaction as a range of individuals within the firm are likely to have both formal and informal influence on the final decision, e.g. the Board, Executive Team, HR Director and RE (Perkins and Hendry, 2005), with their consultants’ support. In this context the research gathers data from two sources involved in this social interaction who can provide insight and help develop the understanding needed. The sources are RCs as close advisors to firms and REs as windows into organisational activities on reward mix. The justification for this choice of interviewees as a way of accessing appropriate data is now provided.

3.3.1.1 Socially derived

In line with Garfinkle's (1986) argument that individuals' perceptions are socially derived, and therefore drawn from their interaction with others, both the RCs and REs are valid sources of data on the RMD process. The data collected through interviews with these individuals not only represent the unique meaning given by the individuals but also wider social phenomena that influenced the respondents' perceptions and actions. Informants do not operate in a vacuum; they are socialised in the organisations they advise or work for and the meaning that other actors within these organisations may give to RMD.

3.3.1.2 Reward consultants (RCs)

The research used RCs as informants for two reasons. First, as acknowledged experts in the reward field they have relationships with REs and senior management in organisations and through this play an important role in reward decisions (Bender, 2011; Clark and Fincham, 2002; Conyon et al., 2011). They are an important component of the system that leads to RMD (Bender, 2011). Second, the difficulties of researchers carrying out participant observation of organisational process have been noted with respect to entering the field, establishing a role and building a relationship (Luders, 2004). However, Rynes and Bono (2000) noted the excellent access that RCs have to observe compensation practice and suggested forming alliances with these individuals as a way of furthering reward research. This research adopts this approach as part of the data collection, to use their insight and access as a separate but complementary perspective to that of the REs also to be interviewed.

The RCs therefore provide distinct data on both industry practice in RMD and firm-specific practice through discussion of specific consulting assignments they have conducted.

3.3.1.3 Reward executives (REs)

Two specific justifications are provided for the use of REs as the main source of data on the different interests, forces, practices and resources faced across the industry but also within their own firms.

First, potential bias is reduced through personal not organisational recruitment. Two methods of recruitment are possible. Informants are either recruited as representatives of their organisation or in a personal capacity. Buchanan outlines how recruitment in the latter way can lead to richer, more complete data as informants “speak for themselves and speak of the organization” (1993: 297), due to the difference in the implicit contract in place between researcher and informant (Hoffman, 1980; Burgess, 1984; Bressen, 1988). Individuals recruited as representatives of the organisation are under more pressure to display competence which can lead to their censoring information which may be detrimental to this display of competence or lead to an unfavourable view of the organisation (Buchanan, 1993). In addition, these individuals’ accounts may be further sanitized by a requirement that a report will be provided to the participating organisation on the research. In contrast, those recruited in a personal capacity speak as “a colleague with a mutual interest in the topic of interview. Respondents may then speak of their organisation, but do this in the context of speaking for themselves.....the interview is not located in the context of organizational permission and is thus not constrained by the cultural and moral pressures which that location

implicitly and typically creates” (Buchanan, 1993: 301). All REs were recruited in a personal capacity.

Second, more informed accounts are provided by using those closely involved with RMD as opposed to those who have little consciousness of the concept. The issue regarding using single informants to report on organisations is not new; a number of issues are well documented, e.g. memory failure and distortion, hindsight bias and self-justification to enhance self-esteem. However, using multiple perspectives within an organisation also raises problems. Kumar et al. (1993), in the context of survey research, note that response errors are likely to be higher when informants are not close to the phenomena being discussed. They suggest it is important to verify the competence of the individual to comment. The research uses REs as the senior individual in the firm with responsibility for the analysis and development of reward mix – either the HR Director in smaller firms or Head of Reward (or similar title) in larger organisations. The RC interviews, conducted before those with REs, identified that, unlike some reward decisions, e.g. budget level, the organisational reward mix decision is generally not a formal one. There was overall a lack of one ‘moment’ or established process where reward mix was raised, with the actual mix tending to emerge over time rather than as a result of a set piece decision. However, REs were seen to be the focal point for this informal process. As part of the exploratory work, I also looked to assess the competence of the REs as informants. Those interviewed appeared well placed to have deep technical insight into RMD and, significantly, were senior enough to have a wider organisational and environmental perspective of the decisions. Two interviews I conducted with non HR executive managers within one firm (Sales and Operations Directors) did not demonstrate awareness of organisational practice and

determination pressures, or wider sectoral knowledge. The lack of an established process and set discussion meant they found commenting on the issue problematic.

3.3.2 Levels of analysis

The research question which focuses on the reward mix determination approach was examined through two levels of analysis. First, reward practitioners, both consultants and executives, as informants on how reward mix is determined at an industry level, drawing on their insights and experiences. This allowed the research to explore whether the forces, pressures, interests and resource dependencies applying to RMD are strategically driven, uniform or untidy, and/or multifaceted. A second unit of analysis was also explored – the organisational level. First, drawing on the data from both the RCs and REs, this allowed the identification of variables that influence a firm's propensity to follow industry norm reward mix practice. Next, solely drawing on the accounts of REs speaking of the practice in their respective firms, the research explored what commonality exists between the REs' accounts of specific organisations' reward determination activity and the dimensions influencing individual firms' propensity to adopt a non conforming reward mix. Whilst accepting that adopting multiple levels of analysis adds complexity, the study of a whole situation is possible through the interpretation that others and the researcher have on the situation (Easterby-Smith et al., 2008).

3.3.3 Research options

A qualitative approach was selected as an appropriate way of establishing the constructed meaning put on reward mix decisions by those involved, advising or closely observing those decisions (Kvale and Brinkmann, 2009).

A range of qualitative techniques were considered including observations, analysis of texts, publicly available and internal, and case studies, before semi-structured interviews were selected. An assessment of each of these rejected techniques and conclusions drawn is provided in Appendix 4

Miles and Huberman (1994) argue that qualitative researchers should, where possible, look to increase the size of the sample used given the possibilities this presents in identifying a greater variety of similarities/differences. However, they warn that if the sample becomes too large then it can create issues of data management, making a study unwieldy. They note that “the price (of larger studies) is usually thinner data and at some point you say: why not do a survey?” (1994: 30). Whilst a survey is appealing with respect to time and ease of data collating compared to face-to-face interviews, it was rejected for various reasons. Whilst the research was keen to engage a relatively large number of key commentators/participants in RMD to allow a full understanding of RMD to be developed, it was important that the data collected were appropriately rich in order to provide insight into not just the ‘what’ of RMD, but also the ‘why’, so this explanatory element could be incorporated into the research outputs. Surveys are not considered to be effective tools to obtain depth of this sort (Blaikie, 2000).

Lofland and Lofland (1995) note that face-to-face interaction is the most complete method available to explore the thoughts and perceptions of individuals. The research piloted, and found to be productive, the use of laddering questions (Baker, 2002) as a method to do this, which could not be pursued through a survey.

3.3.4 Semi-structured interviews

There are a range of interview forms which can be utilised – computer-aided, focus group, factual, conceptual, narrative and discursive (Kvale and Brinkmann, 2009). A blend of three of these was used: initially, the interviews held were factual to gather data on the individual (i.e. background, experience, current role) and the organisation where they worked; next, concept clarification, exploring key concepts with the informant around what they understood by the term reward mix; finally, the bulk of the interview was narrative exploring “the stories the subjects tell” (Kvale and Brinkmann, 2009: 153). Hopf felt that semi-structured, focused and narrative interviews of this type allowed “combining a reserved, non-directive management of a conversation with an interest in very specific information and the opportunity for an object-related explanation of meaning” and “they are therefore superior to other interview variants” (2004: 204).

Given the knowledge we already have from the literature review of the often unconscious institutional factors that may have an influence on reward mix, it is likely that informants were not fully conscious of how these institutional effects are influencing their organisations’ policy. Consequently, deep exploration through narrative, semi-structured interviews was considered appropriate to allow the pressures to emerge and be explored (Kvale and Brinkmann, 2009).

My significant experience of interviewing in different contexts has taught me that interviews are not an ‘objective’ research method, but rather that dialogue between interviewer and interviewee creates the understanding of the situation being discussed. Although there may be objective facts that occur when reward mix is determined, the

REs and RCs interviewed will have their own perspectives on RMD; this will be reflected in their accounts of what influences the determination process and also the justification being sought about why certain issues such as resource dependency, employee control and institutional pressures, may influence the process.

One drawback of any interview approach is the retrospective nature of the accounts given. However, Chell notes that interviewees' accounts "are partial; but partial or not, biased or not, such accounts constitute their reality, and, arguably it is the way they view the world which shapes their future actions." (2004: 58). Given it is this reality being explored, an interview approach appears appropriate as the investigation method.

3.4 Research programme

Following the decisions taken on the overall research strategy, the two main stages of the research programme are summarised in Table 3-2.

Activity	Main purpose
First study - Examination of RMD – the RCs' perspective	Test initial findings from the literature review and begin the development of explanations for RMD. Improve richness of coding structure for later studies. Identify potential areas where lay and technical terms are inconsistent to help ensure use of the language of the informants, not academic technical language. Act as a distinct but complementary perspective to RE interviews.
Main study - Examination of RMD – the REs' perspective	Further development of descriptive determination model and development of explanations for determination process identified.

Table 3-2 – Research programme

Each of these stages will now be discussed.

3.4.1 First study - Reward consultants' perspectives

The purpose of this stage of the research was to gain insight into the field and through this begin the process of theory development around RMD. This is an important stage of the research given that it provides a distinct but complementary perspective on addressing the research question to that provided by the REs that follows. Whilst not triangulation (see section 3.5 below for comment on this) the use of multiple sources of data to explore the research question is an important part of ensuring that the findings make sense.

Ten RCs, i.e. individuals providing paid for advice to organisations on the design of their reward strategy including RMD, whom the author had met at industry conferences, were approached and asked to participate in the research. The understanding gained from the RC interviews provided an alternative perspective to the direct RE responses. The interviews were conducted to collect evidence of the RCs' experience of organisational practice, not their opinion on what factors should influence RMD. This was managed, where possible, by asking for real examples of practice the consultant had seen in their work. In addition, conceptual discussions of reward mix were carried out and factual data on who is involved in the reward mix decisions within organisations occurred to provide context for the RE interviews.

Semi-structured, largely narrative interviews, lasting 30 to 80 minutes (and an average of 45 minutes), were held with ten RCs from three global reward consultancies and one independent consultancy between December 2008 and October 2009. An interview protocol was developed building on a comprehensive literature review with respect to RMD. Although not possible to pilot the interview protocol, given the relatively small

number of informants available, it was reviewed by colleagues at Cranfield School of Management and a number of their suggestions incorporated. The final protocol is in Appendix 5.

With respondents' permission, all interviews were recorded and transcribed leading to 160 pages of single-spaced text. The data were then coded using NVivo 8 software against the conceptual framework derived from the literature review.

The interview findings are outlined in Chapter four.

3.4.2 Main study - Reward executives' perspectives

3.4.2.1 Initial exploratory interviews

Six exploratory interviews were carried out with REs from six different financial services firms. These were conducted in April-June 2009 ahead of the pilot interviews. The purpose of these interviews was to further test the conceptual model developed from the literature review and refined through the interviews with the RCs and to begin to see whether the research method chosen would be successful in soliciting the 'thick' description desired (Denzin and Lincoln, 2005). In addition the interviews were a useful source of interview leads for the main study. The exploratory interviews were conducted in a similar manner to the RC interviews, recorded and professionally transcribed for later review.

Two significant insights came from these interviews. First, it became apparent that rich data were often more forthcoming when the interviewee had an event or change on which to anchor their discussion. This assisted their thoughts on not only what influences the determination of reward mix but, significantly, why they felt the change had occurred. Second, the interviews identified that RMD was not a decision typically

taken in an established and formal process. What emerged was that reward mix was much more of an evolving concept within organisations. On no occasion during the exploratory interviews could the interviewees point to one formal process of determination, which was in sharp comparison to issues such as overall pay levels in the firms and agreement of pay structures (i.e. pay spines, job families or job evaluation factors) which were subject to at least annual formal review and sign off by an appropriate committee. This meant all the interviewees had to think through what was determining the mix they had in place and why they had got to that position, and caused them to ask questions of themselves. The example below from one of the exploratory interviews illustrates this point.

Why do we have benefits? What a good question. Given it's such a large component of the mix I should know that.

A significant pause then ensued before the interviewee gave the following response.

Having thought about it, there are a number of drivers but we don't actually question them on a regular basis.

The interviewee continued by discussing their thoughts.

3.4.2.2 Pilot interviews

Four pilot interviews were carried out in June-July 2009. Easterby-Smith et al. identified that the purpose of pilot interviews was to “test methodologies and to assess the feasibility of initial ideas” (2008: 24). However, given the extent of the initial exploratory work already carried out in this research project and the RC interviews that were already well underway at this point in the research programme, the focus of these pilot interviews was on testing the interview methodology that had evolved over the exploratory interviews. The protocol used in the pilots is shown in Appendix 7.

The pilot interviews were transcribed (details of the transcription process are given below) and the transcripts reviewed to establish what had worked effectively and whether any changes would be required. The interviews were reviewed against Kvale and Brinkmann's (2009) six interview quality criteria. All of these were met for each interview with the exception of one where the interviewee did initially begin to talk about reward level decisions as opposed to reward mix. I quickly identified this and carefully directed the interviewee's thoughts to reward mix. Overall what materialised was that the interview protocol, used in a people-centred (Rogers, 1976) and flexible manner to follow the flow of the interviewee rather than a predetermined direction of the interviewer, worked well with all the pilot participants settling well into the interviews.

The pilots also allowed me to test the data reduction and analysis techniques that I had planned for the main study (outlined in detail below). They were operated as described and no amendments were necessary. Due to the success of the pilots the data collected were also used in the main study now discussed.

3.4.2.3 Main study

A limitation of the interviews carried out with the RCs is that they provided their interpretation of RMD rather than a direct assessment from the protagonists involved, REs. The main study – interviews with REs – was carried out to gain access to their interpretation of RMD.

Thirty REs were interviewed from 30 firms¹². Those interviewed were senior individuals in the firm (on two occasions the business unit within a much larger firm) with responsibility for the analysis and development of reward mix.

Wolff (2004) notes a number of difficulties that can arise in gaining access to interview with senior management. Easterby-Smith et al. (2008) and Buchanan et al. (1988) argue that issues around cooperation levels will mean compromises have to be made regarding the 'rigour' of sampling. They suggest the researcher should start with personal contacts and sample from there, bearing in mind the need to look for similarities and variance – an opportunistic approach adopted in this study. Personal contacts (including REs that were met at remuneration conferences which I attended at this time), consultant contacts, Chartered Institute for Personnel and Development (CIPD) and British Bankers Association (BBA) introductions and 'snowballing' leads from interviewees (Miles and Huberman, 1994) were used. Non probability sampling of this nature was not seen as an issue given the aim of the study to develop theory rather than fully generalisable results. A map of interviews was built up by financial services sector (asset management, insurance, banking, capital markets, retail intermediaries, mortgages, etc.) to see the spread obtained through this pragmatic sampling approach and assess any consequences. Ongoing decisions of interviews to be conducted were taken with reference to the theory that was emerging.

I found little resistance in the interviews, with a number of the interviews exceeding the allocated time. The respect that I developed through contact with the REs was further

¹² In some larger firms multiple REs were in place, i.e. separate REs for the retail and wholesale entities in the firm.

confirmed by interviewees regularly (at the end of the interview) asking for my thoughts on how they viewed RMD and various invitations to come and speak to their colleagues about the research (see section on validity below for details). Appendix 6 sets out the interviewees, the financial services sector of their current organisation and their job title.

3.4.2.4 The interview protocol

The structure used in the interview was not changed from the pilot protocol shown in Appendix 7. This was derived from the literature review, the RC interviews and the second phase exploratory interviews carried out as discussed above.

The research question was intended to establish what factors the REs felt were driving reward mix choices and why these factors were significant. What emerged in the exploratory interviews was that interviewees were comfortable tackling this up-front after being ‘warmed up’ with some basic questions on their background, their conceptualisation of reward mix and a short outline of the mix that was offered in their organisation at that time. This approach elicited rich detail on the influences and began the process of probing into why these influences were felt to be important by the interviewee. What also emerged during this phase was the need to push for further understanding from the interviewee on why they felt the driver was significant beyond a first level justification. This is, in the words of Baker, intended to “force the respondent up a ladder of abstraction” (2002: 226). In addition, I used the interviews to explore each individual’s thoughts through focusing on an instance of reward mix change when one was raised by the participant. In carrying out the laddering, I followed a policy of “deliberate naiveté” (Kvale and Brinkmann, 2009) to ensure that I asked follow-on questions when I may have felt I already ‘knew the answer’.

Significant time was also given to allow the interviewee to think through and reflect on the questions asked and the answers they gave. Silence in interviews can be uncomfortable for the interviewer. I found the technique to be very powerful with the individual, unprompted, laddering themselves to a further level of meaning.

3.4.2.5 Carrying out the interviews

The interviews were conducted between June 2009-March 2010. All of the interviews were carried out in person in a range of locations across the UK. It was important that the interviews were face-to-face, given their open nature and the importance of dialogue and engagement in the process, which I felt significantly less comfortable managing over the phone. Ahead of the interview an email was sent to the interviewee setting out the broad areas to be covered and noting that I would be asking for permission to record the interviews. This was intended to ensure that the meeting took place and allowed the interview to begin reflecting on RMD before the session.

The 30 interviews carried out for the main study lasted between 32 and 73 minutes (and averaged at 57 minutes). With respondents' permission, all interviews were recorded and transcribed.

3.4.2.6 Interview introduction

Initial contact with interviewees usually began in the reception area of their organisation (only five interviewees sent secretaries to 'pick me up'). This provided an ideal time to begin to establish crucial rapport with the interviewee and conversations were begun often around the current business environment, how the organisation was finding the difficult market conditions etc. This was an important time as Kvale and Brinkmann note that "The subjects will want to have a grasp of the interviewer before they allow

themselves to talk freely, exposing their experiences and feelings to a stranger” (2009: 128).

My first question simply asked them to talk through their current role. This question allowed me to check that I was interviewing someone with an appropriate position for the research, but also allowed the interviewee to start confidently on a subject of which they had good knowledge.

3.4.2.7 Reward mix conceptualisation

The interview then commenced by asking the interviewee to outline what they understood by the term ‘reward mix’. This was intended to establish their conceptualisation of the term rather than imposing on them my definition or one derived from the literature. The findings on reward mix conceptualisation are discussed in Chapter five.

3.4.2.8 Interview section 1

The main body of the interview proceeded with open questions around what the RE felt influenced RMD in their organisation and why the elements raised were influential. The first question often revealed a shortlist of reward mix determinants. I took a written note of each determinant as it was raised so that once the interviewee had concluded their initial thoughts I could probe into each of the elements in detail to ladder down to why each of the elements raised were felt to be significant. This interview section often led to discussion of changes to reward mix that the RE had led. These were useful in allowing the interviewee to explore the motivation for the change as a means for them to more clearly construct their understanding of the reasons for reward mix change.

3.4.2.9 Interview section 2

“Interviewers should primarily adopt the role of attentive listener and contribute to the maintenance of the narrative through supportive gestures and non-directive brief comments. Only in the follow-up section do researchers have the opportunity of a more active contribution” (Hopf, 2004: 206). During the first section of the interview I offered no comment on any responses that were given. However, in line with Hopf’s position, section 2 was about more direct engagement. I signalled this to the interviewee by asking for permission to adopt a more direct approach. This section was then used to explore contradictions in what may have been said earlier. Specific probes were also employed to explore areas not raised that the literature or other interviewees suggested were important. Miles and Huberman note that interviewees can be selective with the information that they provide “sometimes deliberately, sometimes unwittingly” (1994: 56), and suggest the researcher should look to use techniques to minimise this. The specific probes were one way in which I attempted to do this.

3.4.2.10 Interview closure

The closure of the interview was used, as suggested by Gaskell (2000), to ask the interviewee whether anything had not been covered which they, on reflection, felt should have been. More often than not this proved remarkably productive with the interview extending as further insights emerged from the interviewee.

Miles and Huberman (1994) note the importance for validity of interview data of seeking feedback from interviewees on their position. I used the interview closure to summarise my understanding of what had been identified, the key drivers and the reasons for their significance. This was the start of building an individual model of RMD for each interview. This allowed the interviewee to correct any

misunderstandings I may have had and also helped ensure that my interpretation of the interviewees' position was as close to theirs as possible. Again, this often led to more discussion which provided a further rich source of data. Recording continued throughout this stage to elicit any further information that was given often in a relatively casual way (Easterby-Smith et al., 2008).

Some interviewees did ask who else had been interviewed for the research and although unable to tell them, due to confidentiality reasons, I was able to give an indication of the type of firms being interviewed (i.e. banks, insurance companies etc.). I was also asked for my thoughts on what the interviewee had said and how it compared with other REs' and RCs' perspectives. This allowed me to outline what the research was showing to date which I did through sketching out the current state of the model of RMD as I construed it. During the exploratory interviews I learnt to leave the recorder on at this point as this stage also led to further insights.

It was these discussions that also led to a number of requests for me to return at the end of the research to take the RE, their team and on one occasion their Executive Board through the research findings. I was happy to do this as a courtesy for their time in the interview, but also as a chance for me to obtain further practitioner challenge to the findings of the research as the theory was developing (see sense checking below).

3.4.2.11 Post interview

After the interview, I made my own notes on a post-interview sheet that was developed ahead of the exploratory interviews. This is attached as Appendix 8. The sheet allowed me to quickly capture my impressions from the interview both with respect to what I had heard but also how I had performed so that I could improve at future interviews.

These notes provided an initial invaluable dataset when the transcripts were analysed and the reflection carried out assisted in theory building which was underway throughout the time the interviews were conducted. In addition I sent the interviewee a thank you email and followed up on any documents they promised to send and also further RE introductions that they offered to make.

3.4.3 Interview data analysis

The interviews were analysed with reference to Miles and Huberman's (1994) three-stage process for analysis of qualitative data. First, the data requires reduction from its original form. Next, the data needs displaying so that sense can be made of the high volumes of data that have been generated. Finally, this reduction allows the drawing of conclusions and the building of theory from the thick description that has been generated. Consistent with the constructionist stance taken, this was carried out alongside ongoing collection of data (Easterby-Smith et al., 2008). The data reduction and analysis phases will now be discussed.

3.4.3.1 Data reduction

All the interviews carried out after the initial exploratory interviews were transcribed to "make fleeting conversational behaviour permanently available on paper for scientific analysis" (Kowal and O'Connell, 2004: 248). This was done by a professional transcriber and resulted in 519 pages of single-spaced text from the 30 main study RE interviews, in addition to the 160 pages resulting from the first study interviews with RCs. Whilst recognising the benefits of personal transcription with respect to getting close to the data and beginning to identify potential themes, these were outweighed by the need to keep the work on track and allow the focus to be on interpretation and analysis. In order to ensure quality and reduce the risk of incorrect transcription, which

has been identified as being frequent (Kowal and O'Connell, 2004), a process of corrective listening was carried out (Schmidt, 2004).

Handling large volumes of interview transcript data can be problematic (Bazeley, 2007). To make this process more manageable NVivo 8 software was used to assist in data reduction and analysis. Computer support was deemed appropriate for three reasons: first, to improve efficiency in managing the high volume of text which allowed a large sample to be used and therefore meant that saturation was more likely to be reached; second, the system allowed for transparent analytic assessment, such as cross-interview comparison and filtering; finally, as an encouragement to creativity, the software allowed me to experiment with the data without disrupting original data integrity.

The initial concepts identified in the literature review were entered into NVivo as nodes (points at which similar data can be identified) which were then built into trees (allows relationships between nodes to be built) in line with the relationships identified in the conceptual model. In addition, whilst the transcripts were being reviewed NVivo allowed the creation of free nodes (i.e. nodes that do not at that stage have any relationship with other nodes) where data can be identified. This was in line with Miles and Huberman's (1994) suggestion that "one method of coding – the one we prefer – is that of creating a provisional 'start list' of codes prior to fieldwork. That list comes from the conceptual framework, the list of research questions, hypotheses, problem areas, and/or key variables that the researcher brings to the study". The conceptual framework was the frame of analysis but this was applied with flexibility to allow data not fitting that frame to be captured elsewhere. Where free nodes were identified previous transcripts were reviewed to establish whether elements relevant to the newly

defined node were present in that text. Whilst time-consuming, this was productive in establishing new themes in the area under study.

NVivo also allows text to be coded against multiple nodes where, for example, two themes or ideas are raised by the interviewee in a section of discussion. This was significant in ensuring that as much of the meaning as possible that the interviewee was giving was captured against various aspects of the conceptual model and additional free nodes developed. This flexibility meant that the framework could evolve as the data were collected in line with Miles and Huberman's contention that "as qualitative researchers collect data, they revise their frameworks – make them more precise, replace empirically feeble bins with more meaningful ones, and reconstrue relationships. Conceptual frameworks are simply the current version of the researcher's map of the territory being investigated." (1994: 20).

No unit of coding was defined (i.e. word, sentence, paragraph), rather text was coded at whatever level was deemed appropriate to ensure the meaning that the interviewee was conveying could be understood in later analysis at the node level (Miles and Huberman, 1994). NVivo also captures data in each code in the wider context of the text around it (i.e. it shows not only the data highlighted for the node but also the area of text surrounding it). This was particularly useful in ensuring later analysis did not misinterpret the meaning in the transcript by reading it out of context.

The use of a second coder was considered but rejected. I believe that after over sixty interviews my coding and analysis will be more insightful than that carried out by an individual with less knowledge of the field (Milne, M.J and Adler, R.W., 1999).

3.4.3.2 Data analysis

Analysis was carried out through examination of all text coded at the same node. This allowed checks to be carried out that the data had been appropriately coded or, in some cases, sub nodes may be required to better display and analyse the data in a specific node. The final coding structure is presented in Appendix 9. Whilst the data were being allocated to nodes, I also took notes on ideas and themes that occurred to me during this analytical process.

Cross-case displays were also used as recommended by Miles and Huberman (1994) i.e. a meta matrix. This was done through a large Excel spreadsheet. This cross-case display allowed the examination of themes and trends across the interview data through the use of both frequency data but also yes/no analysis. In addition it allowed the collection of static data (see Appendix 6) and supported the data analysis discussed in chapter five (see Appendix 10).

3.4.4 Saturation

The research is about generating findings into theory and not wider generalisation to a larger population. Given this, the concept of how much data is enough is very subjective. However, “looking at many cases strengthens a researcher’s grasp of the empirical world and helps in discerning variation in the studied phenomenon” (Charmaz, 2005: 510). Miles and Huberman (1994) note the importance of having enough data such that you can have confidence in the theory that these data are assisting you to build, but not so much data that they become overwhelming and inhibit analysis and reflection of the data. In this context Gaskell (2000) suggests that interviews should be limited to between 15 and 25 cases. However, other authors suggest fewer are

necessary in order to build robust theory; Miles and Huberman (1994) and McCracken (1988) identify that 12 cases and eight interviews respectively was generally sufficient.

In this context, a target number of interviews was not set, but the interviews were carried out until a consistent picture was obtained and a coherent model developed from these accounts. This is in line with ‘theoretical saturation’ as outlined by Glasser and Strauss (1967). In total 61 interviews (plus further sense checking activities) were carried out as shown in Table 3-3.

Initial exploratory	13
Reward consultants	10
Reward executives – exploratory	6
Senior Managers	2
Reward executives – pilot interviews	4
Reward executives – main study	26
<hr/> Total interviews	<hr/> 61

Table 3-3 – Interviews completed

Further evidence that saturation was reached is also shown in Figure 3-3.

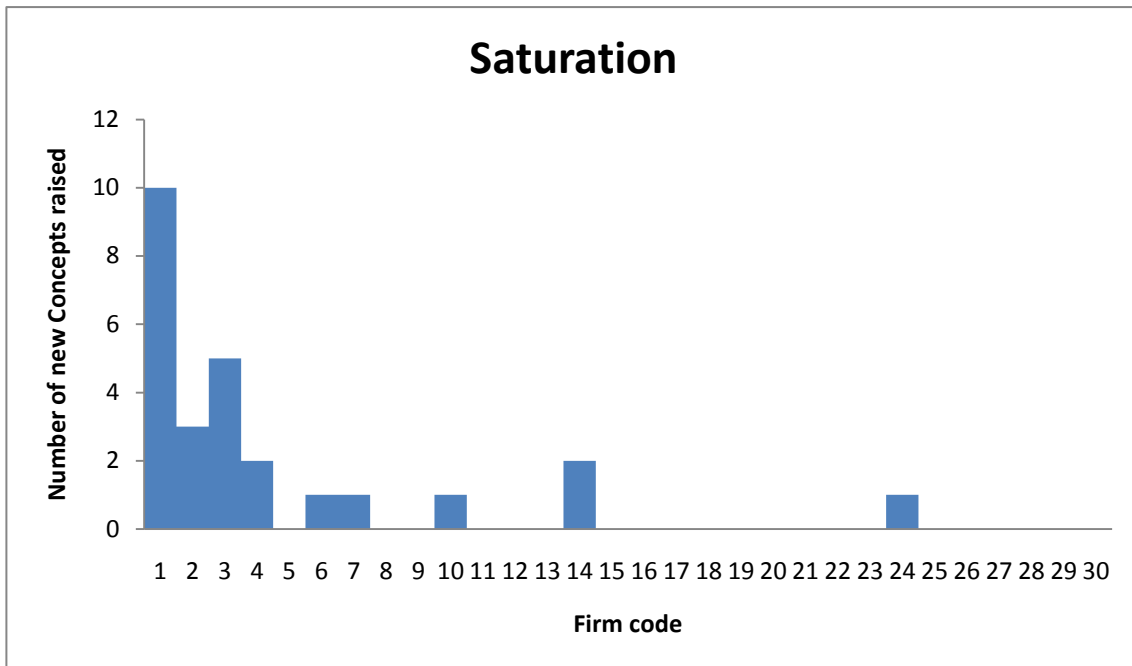


Figure 3-3 - Concept saturation

This shows the instance of new concepts that were seen as influencing reward determination emerging through the course of the RE interviews. As this graph highlights, only one new concept was raised (interview 24) between interviews 14 and 30.

3.4.5 Sense checking activity

Sense checking interviews were also conducted with representatives from different financial services trade bodies as a key population engaging with and commenting on RMD. The events in financial services and their impact on the sector and how it is regulated, had significantly increased trade bodies' interest on the way in which reward is managed and their interaction with their member firms on this issue. A number of the trade bodies had established specific policy expertise and working groups in the area of reward determination within their particular sector. Interviews were held with two

individuals from different trade bodies who had led policy making or lobbying activity on remuneration structures in the financial services sector on behalf of those bodies.

In addition, a number of the interviewees formally invited me back to present the findings of my research¹³. This was done on four occasions. The Financial Services Reward Group, an independent self-organised regular meeting of REs across financial services, a number of whose members I had interviewed, invited me to speak at their meeting in April 2010 when the data collection was nearly complete. Twenty-two financial services firms were represented at this session which comprised of a 20-minute presentation of the main model and typology developed and 25 minutes of their input and comment. In addition, I presented to the Executive Committee of one firm (for 45 minutes, to ten individuals including CEO, Finance Director, HR Director and other operational directors of the firm) to elicit their thoughts. Further I presented my findings to the entire reward team of a major banking conglomerate (2 hours of presentation and discussion with 10 individuals), and to the global head and UK head of reward from a major insurance group (90 minutes discussion). These sessions were helpful in obtaining immediate feedback on the theory that had emerged and also focused my thinking on potential practical implications of the research findings.

Presentations were also made to staff from two of the consultancy firms who had provided interviewees for the RC study. Again, this provided discussion and feedback particularly on the practical implications of the findings for the financial services reward sector.

¹³ During the research I sent regular updates on my progress and findings to the REs who I had interviewed to date. This was intended to keep the network I had built with the REs during and post the research.

All of these presentations and meetings allowed ‘member checking’ (Miles and Huberman, 1994). The robustness of the work was tested in particular to ensure that the abstract second order concepts derived from the first order lay concepts retained a close connection, ensuring that interviewees were able to recognise the accounts (Glasser and Strauss, 1967).

3.5 Validity, reliability, generalisability

Easterby-Smith et al. (2008) identify that the issue of research validity, reliability and generalisability depends on the philosophical perspective of the research. As this research adopts a constructionist perspective, they suggest that three tests have to be applied. On validity they ask whether “the study clearly gain(s) access(es) to the experiences of those in the research setting?” (2008: 109). Regarding reliability, the question is whether there is “transparency about how sense was made from the data?” (2008: 109) and finally generalisability is about whether the “concepts and constructs derived from this study have any relevance to other settings?” (2008: 109).

Validity was sought through careful method design and thorough use of exploratory and pilot testing of the method and specific interview techniques to establish, as much as was possible, that the meaning placed on the phenomena by the interviewee was discovered. Thirty-five interviews were carried out before the main study which allowed the area of phenomenon and the techniques used to investigate it to be extensively reviewed. Bryman notes that triangulation can be carried out through the use of “multiple observers, theoretical perspectives, sources of data and methodologies” (1989: 379). In this research multiple sources of data are used (RCs and REs), not to formally triangulate the findings but rather as part of the analysis as to whether they

make sense. The use of RCs was felt to be particularly helpful in this respect and the findings from these interviews are presented separately to allow the reader to see the specific insights gained from this part of the research. In addition, I used the sense-making sessions with trade bodies, the financial services reward group and the executive and reward teams that I presented to, to assist in testing and challenging my conclusions.

Reliability was sought through the rigour of the interview capture (i.e. verbatim recording and transcription) and robust data reduction and analysis techniques. These methods are transparently recorded in this chapter to allow others to see the techniques employed in forming the overall theory. Clearly the research process is a series of interpretations. Views and thoughts may change over time. However, it is felt that the process was robust enough to provide a reliable abduction of the interviewees' thoughts and the meaning they put on RMD.

Finally, no claim is made to wider generalisability. However, the theory generated has been presented at a range of academic and practitioner conferences and discussed in the sense-making sessions discussed in section 3.4.5. However, theoretical generalisation is possible because what is significant for this is not the statistical robustness of the number of people involved in the research but rather the variation in cases sought to help achieve maximal variation.

3.6 Conclusion to chapter three

This chapter presented the philosophical stance of the research and from this laid out the research design intended, consistent with that philosophical approach, to answer the research question set. A transparent approach to how the data were collected and

analysed was provided, alongside an outline of how the approach taken was assessed for validity, reliability and generalisability. The next section begins the presentation of the research findings through outlining the findings of the interviews with the RCs.

4 Chapter four: Reward mix determination: Reward consultants' perspectives

4.1 Introduction

The purpose of the next two chapters is to report the data collected to address the research question. This chapter gives the results from ten interviews with reward consultants (RCs)¹⁴. In chapter three I described how interviews with these key participants in reward strategy determination would be used to review the conceptual framework developed from the literature review and build an initial descriptive model of RMD. The interviews were intended to provide a distinct but complementary perspective on the research question to that provided by the REs that followed. The data are, therefore, presented separately so that the perspectives provided can be assessed alongside, rather than integrated within, those of the RE interviews.

In section 4.2 the RCs' perspectives on how reward mix is conceptualised in practice are presented, followed by, in section 4.3, presentation of the factors raised as influencing reward mix decisions. In section 4.4 I briefly draw conclusions from the interviews including presenting a generic descriptive model of RMD which is then built on and refined, in the context of the financial services sector, through the interviews with REs presented in chapters five.

Significant use is made throughout the findings of direct quotations so that the interviewees can be heard through the text. The quotations are provided directly so that as much as possible, the reader is able to get a feel for the interviews and the interests, pressures and resource dependencies they discuss. Each quotation is attributed to the

¹⁴ Elements of this chapter have been published in Chapman and Kelliher 2011.

RC who made the comment by reference to a number relating to the order in which they were interviewed i.e. RC1, RC2 etc.

Those interviewed had longstanding consulting backgrounds accompanied by further experience in other areas such as strategy consulting, actuarial science, research, graphic design, as well as senior level experience in reward management in industry. Given this they appeared well qualified to discuss RMD.

4.2 Reward mix conceptualised

Two definitions of reward mix were raised in the interviews. The first was based on monetary value. In this definition the mix was made up of two factors – fixed reward, i.e. as one consultant put it, that which “you can expect to get year by year by year”, and variable reward with the amount payable varying either in relation to overall organisational performance, or more specifically in relation to individual performance. Views varied as to the extent to which employee benefits were considered as part of the fixed element of the mix or whether they were worthy of separate consideration. One interviewee felt that given pension, generally the largest component of benefits, is largely dependent on base salary then it is effectively an extension of base salary. Others felt that given the significance of benefit costs as a proportion of the overall reward mix, and that it has a different purpose from base salary, it should be considered separately. However, what did emerge was the dominance of base salary, not just with respect to overall cost where it is generally the dominant element of the overall monetary reward mix¹⁵, but also psychologically with the focus of REs and employees

¹⁵ Some exceptions to this were identified by the interviewees around sales and banking employee environments.

being on this element of reward in strategy decisions (from the organisation's perspective) and job offer and retention (from the employee's perspective).

The monetary value definition was summarised by one interviewee:

What you are typically looking at is how are we segmenting the total spend that we are investing in an individual....the total defined contribution. (RC1)

Significantly, this view focuses on organisational cost, as opposed to measures of value to the employee which may be more commonly considered when looking at wider definitions of reward mix. All interviewees noted that there was a wider definition of reward mix which could be applied which, in addition to the monetary elements, included more relational elements such as career and learning opportunities, and work environment.

It can be having the right kit, good equipment to work with. It can be having good colleagues, a sort of high quality of work. It can be location. Very importantly it can be learning and development opportunities and career progression opportunities. (RC3)

It was felt that wider definitions were generally used by organisations, at least in rhetoric if not in practice, to better align the overall organisational offering to a package that better meets a wide definition of preferences of employees, "so that you have reward mix that has some chance of being motivational" RC6. Whilst all noting the existence of such an approach, a number questioned how widely it was adopted by organisations in their decisions on reward strategy and reward mix within it. Four of the RCs reflected that this approach was often more consistent with the models pushed by the consultancy firms than the reality of how the concept is used within firms where monetary definitions dominate.

I think there is a distinction between what they say they are doing and what they are actually doing and I think that in reality firms don't adopt a total reward mindset when looking at reward. (RC5)

4.3 Drivers of reward mix

Interviewees discussed a range of ways in which both external and internal factors influence reward mix. External elements raised were market benchmarks, legal, regulatory and taxation requirements, political and societal pressures and the state of the economic cycle. Internal factors discussed were business strategy and risk appetite, talent needs and employee preferences. Each of these is assessed in turn.

4.3.1 Institutional pressures

The interviewees identified mimetic and coercive pressures as dominant in RMD. Normative pressures were not raised.

4.3.1.1 Mimetic pressure - The market

The primacy of 'the market', through the examination and mimicking of the reward mix of other organisations, was uniformly identified as the main external influence on the reward mix decision. Informants generally referred to the market in the context of labour market pressures and the extent to which labour was seen to be scarce, as opposed to the overall competitiveness of the product market within which organisations were operating. No explicit discussion occurred regarding the influence product markets may have on reward mix, although one consultant did note that different sectors had differing mixes due to historically developed employee preferences, which were a legacy of the influence the sectors' capital structure had on reward structures at the time they were established.

There was seen to be relative safety in pursuing policies that were widely adopted by other organisations. This was explained by one informant:

There are organisations that actually say 'I am not taking chances, and I am going to do whatever the market does' and therefore they are prisoners of data in a way – and they can never have enough data. (RC1)

Consequently, the market was seen as promoting reward mix inertia with the following comment being typical:

.....everybody is waiting for each other, the market is telling them nothing and it requires balls to go out and do something different. (RC5)

Alongside the role of market data in managing organisational risk, it was also used by some more sophisticated organisations to identify competitor reward mixes with a view to understanding differences and ensuring that these differences were offering an advantage.

More sophisticated organisations now are looking at every detail of the reward mix and they are certainly basing that on market benchmarking they will be looking at norm data with other employers to see whether they are different and why. (RC3)

A number of examples were provided of organisations adopting this more 'sophisticated' approach and gaining, albeit potentially temporary, advantage. Nevertheless, these examples were the exception to wider practice, where ultimately mimetic pressures were felt to dominate at the expense of what the consultants considered to be more strategic thinking and reward mixes better aligned to the unique context of the organisation. The following comment aptly portrays this view.

We look for sameness, which we just wouldn't do with anything else that was either that costly or that strategically important to us. (RC5)

Where new innovative mixes were introduced, the speed at which the new practice was adopted more widely meant that enhancements to the mix were seen to deliver only temporary advantage. One consultant said:

I don't think companies realise what they entering into at a cost is yet another zero sum game where you will find no competitive advantage because everybody will be doing it. (RC5)

Confusion in what 'the market' actually meant and how it is seen in benchmark data was also considered. Interviewees identified that the common claim to be targeting market median was, by definition, almost impossible for everyone to achieve. This problem of data interpretation was also evident in how some organisations targeted competitive positions in each element of the mix and as a result may be 'overpaying'.

Most organisations look at – well they say they look at – total remuneration. In fact they don't, they look at element by element. What are our salaries like? What is our bonus like? What is our pension like? What are our cars like? (RC6)

Sectoral mimetic pressures were identified as strong, with a range of examples given of different mixes linked to particular sectors. For example, manufacturing with its ability to measure employee output, contrasted with the public sector where measurement was more problematic and expectations with regard to benefit provision more entrenched. In addition, reward mix norms have been formed in certain sectors that, as a result, have become firmly established in employee expectations. Examples given included the generous benefit component in the public sector and the high levels of variable pay in investment banking. One interviewee identified the level of capital required to operate in the sector as an important consideration in these mix decisions. Industries with high capital needs were identified as typically having higher proportions of defined benefits

as fluctuations in the cost of these, relative to the overall capital costs, were small and therefore had a much lower effect on the overall profitability of the business. This was in contrast to sectors where people costs were a higher percentage of overall cost, such as professional services, and thus the sensitivity to changes in these costs was much higher.

If you are running, say a shipping company, you won't care about a swing in the pension scheme funding because compared to the cost of owning all those ships and fuelling them and so on it's neither here nor there. (RC6)

4.3.1.2 Coercive influences

In addition to the mimetic pressures discussed above, a number of coercive influences on mix were identified, namely legal, regulatory, societal and taxation.

The significance of legal and regulatory frameworks in different countries was identified by five of the consultants, with the need for mandatory pension and sometimes wider benefits being the main target.

It's all a bit influenced by things like the social security systems and what does the State think that the State has to provide....[which] tends to influence what the private sector has to pick up...., which is why we get different benefit practices in different countries. (RC2)

The need for improved employee long-term saving, as well as wider understanding and responsibility for personal financial management, were identified as having some, albeit not large, influence on reward mix policies, particularly in relation to benefits and pensions provision. This partly reflects the government's desire for better citizen wealth management.

It's about encouraging employees to take more ownership of their financial future. So an employer is helping to mitigate the risk of lower potential

guaranteed retirement benefits by making sure that people take more personal active interest. (RC9)

These wider societal and political pressures were consistent with the predictions of institutional theory.

Whilst taxation was raised by six of the interviewees, its influence was considered to be more historical. Despite the fact that a large number of tax advantages were no longer available, they still exerted a significant influence on reward mix policies today. Company cars, which are still part of the reward mix for a number of professional roles, were repeatedly cited to illustrate this point.

At the time it seemed very tax efficient to provide a car benefit, so all of a sudden car benefits become prevalent and then if you are going to compete in the marketplace you have to have a car benefit – at the time its tax advantageous to do it and here we still are trying to get ourselves out of tax driven benefits. (RC2)

Defunct historical tax breaks were not limited to influencing benefits. Historically share options, a component of variable reward, that had been a tax-efficient means of delivering reward were still used.

So a lot of organisations have their share plans go quite a long way down the organisation and the reason for this is historically share options were tax favoured. (RC6)

The one area where the consultants felt tax regimes were still significant, with respect to real savings for both the employer and employee, was pensions. This, alongside political pressure, meant that they were still an important component of the reward mix for many companies.

4.3.1.3 Agency interests - Business strategy

Whilst acknowledging that in order to be successful reward mix should align the interests and efforts of employees with those required by the organisation in line with agency theory, the ability of organisations to do this was questioned. The difficulties associated with performance management and setting outcome driven targets that are genuinely within the control of the employee were raised. Exceptions to this, such as sales forces and manufacturing pieceworkers, were identified as groups where a clearer line of sight could be established between the daily work of employees and overall company performance. In this context they noted that variable reward schemes have typically been more akin to profit sharing, than genuinely performance-related pay and therefore not necessarily designed to motivate day-to-day behaviour, but rather share some of the organisation's success with employees who, however opaquely, may have contributed to it. This was summarised by one consultant as

....getting people to understand what ownership represents. (RC7)

The degree to which such variable reward schemes make up part of the overall reward mix was felt to be influenced by norms established in the particular sector, which in turn were often driven by the perceived scarcity of key talent and the preferences of that key talent for fixed or variable reward. It was suggested that motivation of employees comes not from organisational level policy decisions on mix, and specifically the amount of pay which varies with some performance-related variable, but rather local understanding of the individual. This was cogently explained by one consultant.

You need to understand what it is that motivates individual people and makes them want to perform and how different people perform in different ways. (RC3)

4.3.1.4 Agency interests - Cost management

The significance of the effective management of reward mix for cost management purposes was raised by all interviewees. Whilst not an agency theory explanation of mix, it was presented as a means by which both the principal's need for cost control and the agent's need for an attractive employment package could be better met. In this context the interviewees identified that a number of organisations used 'imaginative' reward mixes to keep costs down, whilst still maintaining an attractive overall package from the employee's perspective. This was typically done by introducing relatively low cost elements to the mix, such as career development and changes to the overall working environment, and then effectively communicating these items to segmented groups of employees. This was illustrated with respect to one client's overall reward mix.

...by appearing to create a positive image or working environment, then they can afford not to have to pay top dollar. (RC2)

This holistic approach was not commonplace, with cost management of the overall reward mix typically managed in a much more disjointed and market-led manner. The focus was on cost minimisation of each mix component. Three informants felt particularly strongly about what they saw as an accounting treatment of people and their overall reward packages with the following quote typical.

Firms see employees as a liability to be managed and the costs kept down..... [treating] them as a transactional commodity, [rather than] as a business partner, or even customer, where you are going to be much more sensitive about your mix. (RC3)

This approach has led to organisations focusing on base pay given, in one consultant's words, "the multiplier effect it has on some of the other elements of mix" which are

linked to this number (e.g. pension contribution, bonus, car allowance). This focus, however, may have been at the expense of attention to other areas of significant cost, particularly around benefits.

It can be really quite a drag on employment cost if you have a particularly generous benefit package. It might be much more generous than you need to give. (RC4)

Historically, prosperous times for organisations meant that cost control decisions and, in particular, the control of the benefit component of the mix, had not been the focus of reward activity.

The reward mix is taken for read and because we have had such good times the real decisions about what we should pay for and what the mix should be haven't had to be taken. (RC5)

However, a number of the RCs noted a shift to wider reward mix management, due to the large rises in medical and pension costs for defined benefit pension schemes. Critical attention on pensions from outside of the HR function was also on the increase. Finance departments were increasingly seen to be driving changes in the mix to reduce cost volatility with changes to accounting practices. Accounting changes had also focused the attention of institutional investors. They were now reported to be openly questioning the viability of defined benefit schemes. This had the effect of concentrating attention on the control of benefits and whether employers were generating real value for the investment from this element of the mix.

4.3.2 Resource perspective

4.3.2.1 Talent and employee preferences

The relationship between the scarcity of key talent and the influence that gives to those

staff to determine their own reward mix was raised by eight of the ten consultants and aptly put by one consultant:

The scarcer they [employees] are the more employee expectations weigh in. (RC1)

Nevertheless, sophisticated organisations assess all employee preferences in determining the right mix. This was illustrated by a number of consultants with examples from various sectors, the following quote being representative.

If you talk about a research scientist then the opportunities to publish, the opportunities for professional recognition, the opportunities for learning and development and having a really state-of-the-art lab are going to matter a lot to them ...but if you thought about a call centre employee who was a student and who was doing this to keep the loan to a reasonable level, the drivers for themmight be having good kit, having a supervisor who didn't breathe down their neck and treated like a grown up. (RC3)

Employees' awareness of the typical mix for roles was also reported to have been accelerated by the availability of relevant data on the internet. This was seen to be exhibiting a moderating pressure on innovation within the mix. This led one consultant to suggest that, as a result of this uniformity, employee expectations have been institutionalised by sector or profession, rather than being based on the real underlying preferences of employees.

That [industry practice] has conditioned your expectations as you have grown up through your career, your expectation is market practice and your expectation becomes your preference...It's a conditioned response. (RC3)

4.3.3 Explanations for inertia

Alongside these drivers of reward mix decisions, significant comment (all raised the issue) was made on the reasons for the dominance of institutional pressures or, as

termed by the consultants, inertia in reward mix. Two recurring reasons were given for this inertia – the quality of HR and the effect of organisational history and legacy arrangements. These two areas will be considered in turn.

4.3.3.1 Quality of HR

All of the consultants raised the issue of HR quality as a key moderating variable on the extent to which reward mix was influenced by industry norms rather than the specific strategic intent of the organisation. The overall impression of the quality of HR and its leadership was generally low. The importance of aligning reward mix to business strategy was raised on a number of occasions. However, the occurrence of HR executives consciously doing this was disputed as the following quote illustrates.

A lot of reward decision makers nod to strategy, but don't actually understand what it means and therefore what it means for reward. (RC5)

Further, a split between the reward function and other elements of human resource management was identified which was felt to have particularly significant consequences for ensuring reward mix was aligned with recruitment and talent management programmes.

All of that spreadsheet-based reward that we can look at is viewed as a different entity to the stuff about leadership and progression and the stuff about the kind of environment we work in.... it requires quite a broad thinking HR director to weave those two things together. (RC5)

A number of the consultants noted that the low quality of thinking meant there was a lack of understanding with regard to what reward mix was trying to achieve, with the default position again being what the market does and what has been done in the past. This is illustrated below with reference to benefits.

Do you know, I don't actually think a lot of people know why they offer benefits to be fair – you just do. (RC2)

Research into the drivers of benefit provision has been limited too. Various studies have provided a range of sometimes contradictory drivers (Hume, 1995; Wright, 2004; Taylor and Earnshaw, 1995; Terry and White, 1997) resulting in no dominant theoretical approach emerging in this area of reward management (Perkins and White, 2008).

The problems arising from lack of leadership from the reward community was representatively summarised by one consultant.

It is a failure on the part of the HR community, the reward community and the consulting community to convince real decision makers that people are important and that the reward levels and mix can genuinely have an effect that is causing this. (RC5)

4.3.3.2 Organisational history

Alongside the perceived low quality of HR, organisational history was identified as influencing reward mix inertia (raised by seven consultants).

Organisations are always to some degree hostages of their history and you do find organisations where there are taboo words and taboo practices. (RC3)

The influence of history was felt to be particularly significant for the general employee population when compared to executive reward mix. This was attributed to the relative ease by which Executives' reward packages could be changed, given the negotiation was with a relatively small number of individuals as opposed to wider organisational reward change affecting much greater numbers.

In truth at executive level making changes... is reasonably easy to do because you have got a small population of people who are not going to rock the boat in

a dysfunctional way. They may kick their toys out of the pram, but they are not going to go on strike.....Taking stuff further down into organisations is much harder to do because you can have serious industrial relations problems if what you are doing is, or is perceived to be, a worse deal. (RC6)

Where little organisational history was present, such as was the case for newly formed organisations, conscious and economically driven choice of reward mix was seen to be exercised. However, as an organisation matures in the words of one consultant “they start professionalising”, leading to shifts in reward mix and the development of accepted practice. This is congruent with a path-dependent perspective that change is difficult even when rationally, and in line with contingency theory, other choices would produce a more optimal position (Scott, 2008).

4.3.3.3 Breaking down the inertia – The role of events

One finding of the research was that although inertia was strong, crisis events could break it down (raised by six of the ten interviewees). A number of examples were quoted of clients that were reviewing their reward mix to manage costs down in the economic conditions present at the time of the interviews. This was largely viewed as an opportunity to make the reward mix more effective, through differentiating the offering from competitors and breaking free of the isomorphic pressures that were perceived to exist.

You have to follow the crowd when everything is going fine. When things are a little different that is when you can be more different from other organisations. (RC4)

Alongside the economic downturn, mergers were also suggested as potential catalysts which could instigate a more effective use of reward mix in organisational strategy.

If you are in crisis, if you have been taken over, if you are merging, you have

cover to tackle those things. (RC6)

From these examples it can be seen that, although pressures to maintain the status quo are strong, organisations have used events to catalyse change. However these were seen as the exceptions to the wider practice of conforming to industry norms that have developed in line with perceived labour market patterns in the sector.

4.4 Implications for main study

This chapter has examined the RCs' perspectives on RMD. The interviews have provided an alternative insight into practice through the perspective of a participant observer rather than an assessment based solely on the views of those directly involved.

The interviewees did not, on the whole, give accounts in line with agency theory. Mimetic and coercive institutional pressures were found to be significantly more influential through market benchmarking and the development of industry norms. Normative isomorphism was not found.

Figure 4-1 shows a descriptive model of RMD developed from the findings (using the methodology proposed by Whetten (2002))¹⁶. The main constructs in the model are market forces and reward mix, mediated by industry norms. Note the relationships between these constructs are not seen as causal. However the arrows are intended to indicate my interpretation of the relationship that the RCs identified existed between the elements discussed. The industry norms were seen to emerge from the specific market forces organisations face.

¹⁶ See section 6.2 for a more detailed account of the form this descriptive model takes.

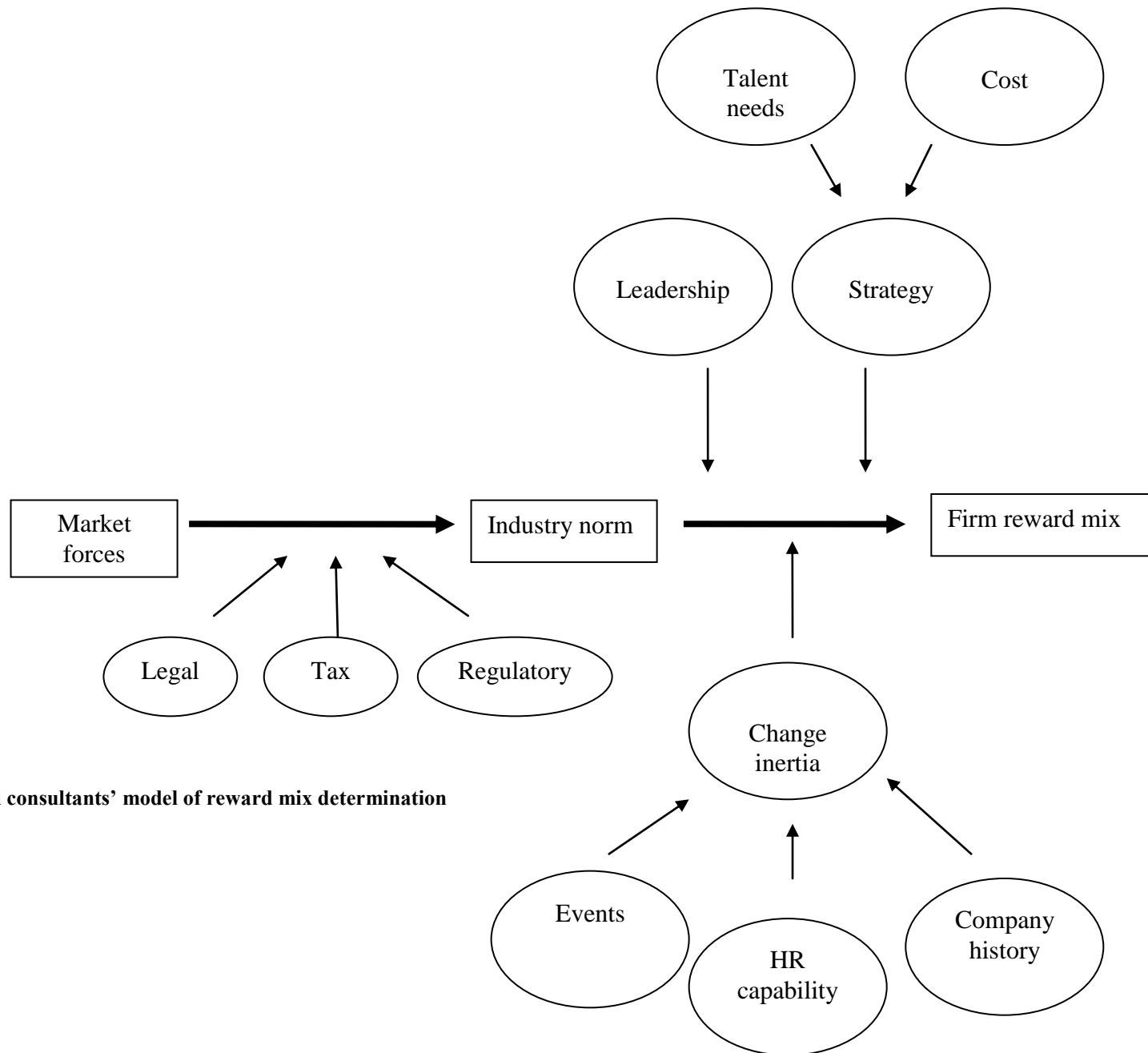


Figure 4-1 – Reward consultants’ model of reward mix determination

The constructs shown above and below the main sequential association are considered moderators in the relationships shown, i.e. the presence of these factors may change the main relationship when present. The influence market forces may have on industry norms is moderated by legal factors, such as minimum wage legislation, tax changes such as changes to pension legislation, or regulatory changes. The transmission of the industry norms to organisational reward mix policy is also seen to be influenced by a number of variables. First, leadership beliefs and how they influence employee behaviour. Second, the organisational strategy and how its execution is affected by specific talent needs and cost pressures. Finally, the extent to which change inertia exists. This inertia is found to depend on the capability of the HR function in managing reward mix reform. Company history and legacy arrangements were also found to further restrict change. However the occurrence of events such as recession or mergers can act as a catalyst, breaking down established norms and practices.

The descriptive model developed challenges agency theory as an explanation of RMD. Institutional factors seem to be endemic in the decision making process. The significant role of the labour market highlighted in the interviews and the relationship between market pressures and talent shortages are consistent with the main premise of resource dependency. Employee power was seen to be influencing the reward mix given to these individuals based on their own, rather than the organisations' preferences, which then may become established as industry norms (Tremblay et al., 2003; Balkin and Bannister, 1993).

The findings presented a number of implications that were considered further in the interviews with the REs. Doubts were expressed by the RCs as to the breadth of reward

conceptualisation that applies in reality with a wide definition including benefits and relational returns being raised but scepticism as to whether in reality reward management was considered as holistically as this conceptualisation implies. In addition, further exploration is required of what defines the market and how product and labour markets may have similar or different influences on RMD.

In addition, a number of factors raised in the RMD literature were not raised by RCs. Concluding that they are not factors in RMD would be premature, especially given the number of interviews involved. These ‘missing’ factors are further explored in the RE findings presented in the next chapter.

4.5 Conclusion to chapter four

This section reports the findings of interviews with acknowledged reward experts and participant observers in RMD. The interviews established that the conceptual framework was a suitable approach to coding the data albeit with one element – institutional theory – dominating the decisions taken. Further, the framework was developed into a descriptive model of the determination process which will be developed through analysis of the findings from the interviews with REs and discussed in chapter six. The results also aided in developing my understanding of the concepts involved (particularly reward mix) and the field to be studied ahead of the RE interviews. Additionally, a more refined set of codes for these interviews was formed for the next stage of interviews from the development of the initial descriptive model of RMD. The next chapter report the findings of these interviews.

5 Chapter five: Reward mix determination: Financial services reward executives' perspectives

5.1 Introduction

In this chapter I set out the findings from the interviews conducted with 30 reward executives (REs) from the financial services sector. As discussed previously REs were chosen as informants, given the close involvement they have with RMD in firms. As argued in chapter three, potential bias in their accounts was reduced through personal not organisational recruitment, allowing them to speak *of* their organisation rather than organisational recruitment whereby informants speak *for* their organisation. The REs provided data both on how they saw the overall reward mix practice across the sector, in particular the strength of the industry norm and the factors that have led to the development of such a strong norm position, alongside their assessment of their own firms' practices in this area.

The findings of the RCs' interviews, outlined in chapter four, showed that analysis built on the three main dimensions of the conceptual model developed from the literature was a suitable means to analyse the discussions on RMD. This conceptual model was built upon three dominant theories provided by the literature on RMD – agency, institutional and resource dependency. As presented in chapter three, these three perspectives are central to the analysis and interpretation of the extensive interview data, although the findings are presented with regard to staying true to the accounts provided by the REs, rather than some externally imposed conceptual structure. The findings explore the pressures that REs believe are an influence on RMD across the financial services sector and specifically their own firm's RMD. Are certain influences dominant over others? Do firms respond differently to the pressures and if so how does this influence their

final reward mix decisions?

Figure 5-1 presents the flow of the chapter. The figure presents, for each section in chapter five, the question the section examines, the areas raised as being important in addressing this question and finally the section of the interview protocol (provided in Appendix 7) from which the data were gathered. Figure 5-1 shows how the chapter first examines, in section 5.2, how reward mix is conceptualised by the interviewees and the factors that are found to influence this conceptualisation. Three conceptualisations are presented and the implications of each of these discussed. Section 5.3 examines the determination process with respect to the hierarchical nature and (in)formality of the reward mix decision and the extent to which the process is a coherent one. In sections 5.4 and 5.5 I then examine the central concept emerging from the RC interviews reviewed in chapter four – industry norm – and how that is viewed by REs. This section explores the significance of this concept on RMD in the financial services sector. In addition, it also examines the REs' perspective on why an industry norm position has emerged, through examination of the main determinants of the norm, but also the moderating influences on the relationship between these determinants and the industry norm benchmark. Section 5.6 examines the relationship between the industry norm position and individual firm reward mix, through examination of the dimensions which are seen to influence individual firms' propensity to follow the industry norm position. Finally section 5.7 goes on to explore the extent to which the dimensions identified by REs and RCs as catalysts for firms to adopt a non industry standard reward mix were seen to be present in each of the interviews conducted and, from this, develops a typology of firms based on the extent to which they were inclined to follow the industry norm in place.

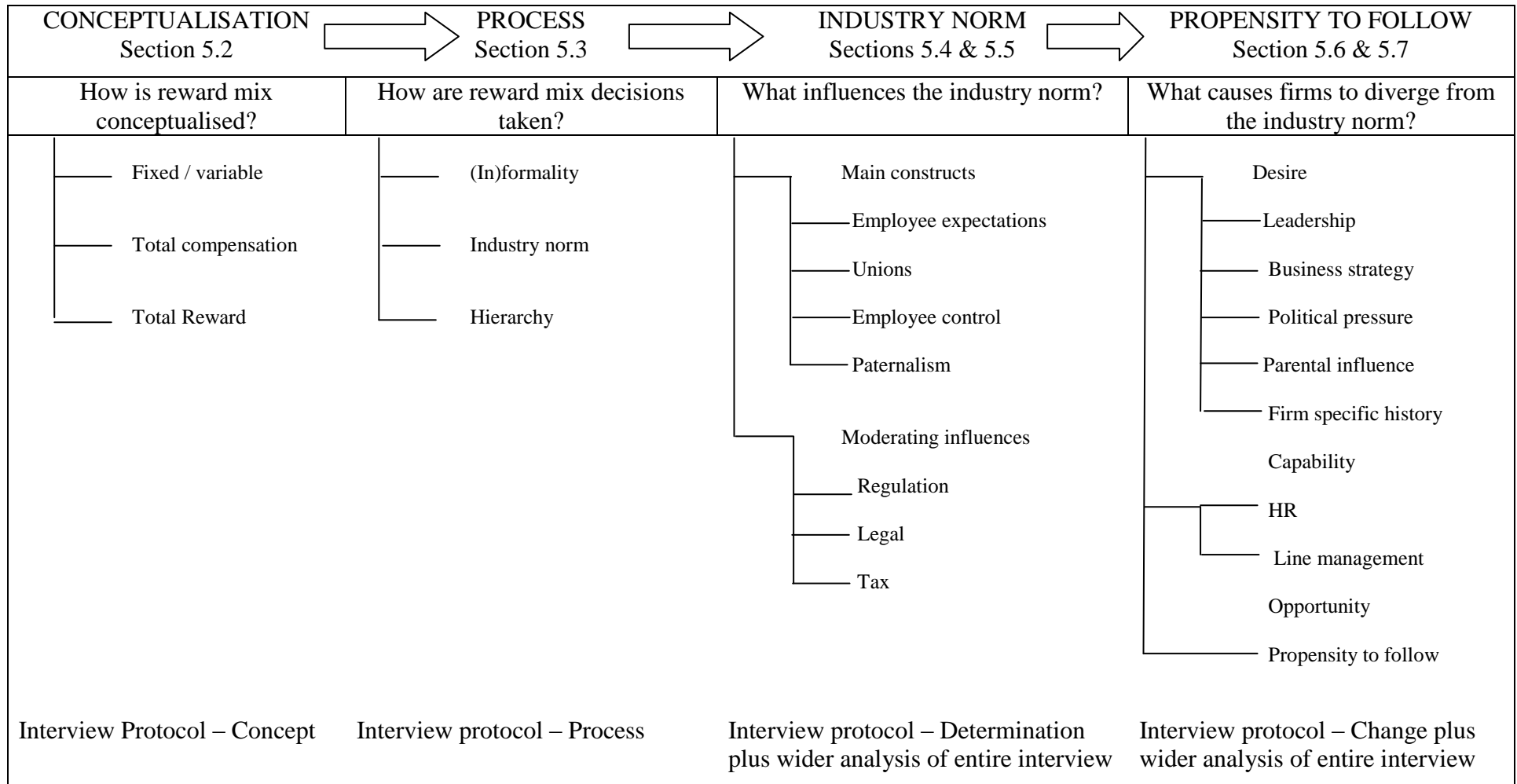


Figure 5-1 – Flow of chapter five

Significant use is again made throughout the findings of direct quotations so that the interviewees can be heard as much as possible through the text. The quotations are identified by RE as outlined in Appendix 6 with, for example, RE1 referring to the RE speaking of firm one and so on. In addition, to aid transparency, the number of REs offering a particular perspective is noted through the findings, in line with the recommendation of Easterby-Smith et al. (2008) that providing more precise figures can further substantiate the weight put on the evidence and, in addition, make clear when voices are dissenting to a wider, more general point being made.

5.2 Reward mix conceptualisation

This section examines how reward mix is conceptualised by the REs interviewed. Before examining the influences that the REs perceive are operating on RMD we need to establish what they understand by the term, what commonality or differences of understanding exist and from this how any differences might influence their perceptions of the influences on RMD.

Three broad definitions of reward mix were raised.

- ***Fixed/variable*** – The balance between the fixed components of reward, in particular base pay, and the variable components of bonus or incentives both long- and short-term. No consideration of benefits or relational returns.
- ***Total compensation*** – The proportion of each element making up total compensation, namely base pay, short- and long-term incentives or bonuses and benefits which have a financial value. No reference to relational returns.
- ***Total reward*** – Holistic consideration of all elements making up total compensation plus wider regard to non financial relational elements that were considered a reward

for work.

The first two definitions were based on monetary value, but varied in the specific elements which were included. In the first definition, the mix was made up of two factors – fixed reward and variable reward, with the amount payable varying in relation to some overall measure of organisational or individual performance.

There's very much a focus on pay mix at base and bonus level, and the split between the two. (RE15)

This definition was particularly prevalent among the REs from the four investment banks, with variable pay dominating all the other elements of the mix as illustrated by the following comments:

It is about cash compensation. We're not very holistic in the way that we think about reward. (RE16)

This was attributed to the large proportion of the overall reward mix that could be made up of bonus, even for support staff, which meant consideration of benefits and relational elements of mix were immaterial.

It's not benefits as they just aren't significant enough. (RE20)

As well as the four REs from the investment banks, three other REs detailed how their firms took this narrow conceptualisation of reward mix management.

Beyond this narrow approach, a second definition was provided which included tangible employee benefits (i.e. benefits with a monetary value) in the reward mix definition.

What you are typically looking at is how are we segmenting the total spend that we are investing in an individual....the total defined contribution. (RE29)

Significantly, this view focuses on organisational cost, as opposed to measures of value to the employee, which may be more commonly considered when looking at wider definitions of reward mix. REs from 20 firms spoke of their firms taking this total compensation approach.

The third conceptualisation offered was a more holistic approach encompassing not just the monetary factors but wider non financial rewards that accrue to an employee through their work. Three interviewees spoke of this wider approach being adopted by their organisation.

So it is about pay, it is about benefits, it's about well-being, it's about the working environment, it's about the health and safety infrastructure we have around them, it's about having subsidised Costa on the site, it's about free parking. It really is about working ... it even includes, when we talk about the [firm name] offer to individuals learning and development. (RE19)

The REs explained that this wider approach was felt to align the overall organisational offering to a package that more appropriately meets a wide definition of preferences of employees. The perspective of reward mix was taken through the lens of the employee and the value they place on reward as opposed to the monetary-based definition which was generally taken from an employer-cost perspective.

It means a whole variety of things. But it means compensation, and it means benefits, and it means short-term, and it means long-term. It means other things as well, if you want to look at other things that employees value like learning opportunities and career development and so on. (RE24)

The extent to which this wider approach to reward mix was taken may be related to the background of the individual RE. Of the three firms that the REs reported were taking a total reward approach to reward management, two (one HR Director and one Head of

Reward) of the REs came relatively recently (within the last five years) from non reward backgrounds, namely development and recruitment. Both of these individuals noted their wider perspective was an influence on how they approached reward management and the interactions they had with colleagues within their firms.

Whilst not reported as being adopted within their firms, the holistic approach to reward mix management was raised by ten interviewees who spoke of their aspirations to move their firms towards this approach. Despite the desire to manage reward in this manner it was generally seen as problematic due to the difficulty of pulling together such a variety of rewards not managed by one part of the HR function.

So [Firm name] has a lot of schemes and initiatives across the HR piece rather than just reward and performance management. So it's integrating those, and I think that is the biggest challenge, particularly from my experience of [Firm name] because we are not together as one HR. (RE27)

Despite being considered by the REs and others within their firms as a compelling approach it was just seen as being too difficult to implement.

Largely because in this business we don't have the level of sophistication to actually be able to incorporate it. (RE3)

However, total compensation accountability, which was the responsibility of 29 of the REs interviewed (the other interviewee did not have formal responsibility for the firm's benefit offering which was the responsibility of the employee relations team), was much clearer and could be managed more as an integrated whole.

It's difficult to get people to cotton on when they operate outside your direct control, because people really think in silos still, even within HR. The bigger the organisation, the worse that is actually. (RE5)

In addition, four of the REs noted that their firm's line management was typically focused on a very narrow fixed/variable definition, given the role they played in decisions of base pay and bonus, compared to the generally corporate decision on benefits.

If you're going to talk to people in business, to people on business lines, they will talk about fixed and variable split. So in terms of the business, if we want as reward practitioners to start talking to them about the whole sphere of reward then the re-education feature needs to be there. (RE28)

5.2.1 Summary

In summary, the research found three definitions of reward mix adopted by the REs. The dominant approach was a total compensation definition although both narrower (fixed to variable) and broader (total reward) conceptualisations were also presented. Next, the findings on the process by which reward mix is determined are examined.

5.3 Determination process

Ahead of examining the findings on the influences on RMD, this section examines the RMD process and whether it may have a role in influencing how we view the determinants of reward mix. The interviews identified that RMD was not a decision that was seen to be typically taken in an established formal process.

There isn't a – there have never been thinking or statements that say well we think the reinsurance mix should be this proportion of salary, so on and so forth. There has never been that rigour of thinking. (RE1)

Only on one occasion did an interviewee point to a formal process of RMD in operation in their firm, which was in sharp contrast to issues such as overall pay levels in the firms and agreement of pay structures (i.e. pay spines, job families or job evaluation factors) which were subject to at least annual formal review and sign off by an

appropriate committee.

The group has got a formalised body for reviewing all this sort of stuff, which we've called PayNet. It's a body of people from the central HR functions in pay and the business people, and we review periodically issues to do with philosophy and mix and so on. (RE24)

Much more typical was the following response,

But has there ever been a committee decision? No, it just happens. (RE26)

The reward mix typically emerged over time through the aggregation of the separate decisions underpinning the mix, namely base pay level, bonus level, benefits provided and overall non financial returns delivered. It was not considered to be one thought-through decision. Papers were not prepared assessing the firm's reward mix position, nor meetings held nor minutes taken of the thinking behind the mix and the overall reward mix decision. Discussion of reward mix amongst firm's management was not seen to occur, as it was believed that management were not generally aware of the concept, but rather focused on the separate decisions making up reward mix.

It's an unconscious decision. (RE22)

In addition, this often meant that these separate decisions were influenced by different elements as illustrated by the following interviewee:

But in terms of thinking about the mix concept, that thinking just won't exist. What will exist will be what I have said, specific decisions around each component dependent on the issues most relevant to each one and what is going on in the company at the time a change is proposed. (RE1)

Overall, decisions on reward mix were not viewed as being taken in a holistic manner. Base pay decisions were generally seen as being driven by market levels (heavily

influenced by formal and often highly analytical benchmarking) and the need to attract and retain employees. Bonus decisions were similarly influenced by market benchmarks for total cash (i.e. base pay plus bonus) but were also moderated by the firm's overall revenue or profit. The market benchmarks influenced the proportion of either revenue or profit to be distributed into a bonus pool. The market benchmark position was a strong influence on the benefits that a firm would offer, but as a separate consideration from the cash compensation comparison just discussed. However, whilst the market was important, with very much a view to ensuring that the overall benefits package remained competitive relative to other firms, other considerations were sometimes also relevant with respect to employee welfare and health, tax efficiency and legal compliance. The extent to which these were important considerations varied between firms and is discussed further in section 5.5.

Further evidence of separate decision making, as opposed to a coherent consideration of the whole package, came from the REs speaking of their firms as subsidiaries of larger parent groups (10 of the 30 REs interviewed worked for such firms). These REs, on the whole, highlighted how they perceived control was typically exercised from head office in two areas: first, on the operation of bonus schemes, largely due to regulatory interest in their home countries as the firm's main regulatory contact was typically at group level; second, on share schemes due to the importance of effective investor relationship management when determining share based awards.

Well, Head Office would have pretty much control over the types of plan that we offer. So whereas we have previously offered stock incentives for new joiners, that changed this year and we moved towards a more cash-related scheme as head office was concerned about investor relations. (RE7)

Much less influence was seen on base pay and benefit offerings, which were largely left to local control.

The philosophy is a minimum standard that it applies on benefits and then countries have to work within those guidelines and build a set of competitive and fit-for-purpose schemes. (RE24)

Within this context there was no evidence from the REs of the subsidiaries adjusting base pay, which adhered to local market benchmarks, to take into account the rest of the mix that had been imposed on them.

With respect to these separate decisions, what emerged was the dominance of base salary. This was predominately due to its significance on overall cost, given it was the dominant element of the overall monetary reward mix¹⁷. However, it was also seen as having the largest effect on employee's propensity to accept job offers and their retention.

5.3.1 Organisational level and role

The interviewees identified a relationship between the level (i.e. in the firm's hierarchy) and role of employees, to the actual mix that was offered. What emerged was that different mix policies were in place for three distinct groups. First, senior managers – defined as those responsible for the strategic direction and accountable for the overall performance of the business. This group had a higher proportion of the mix devoted to longer term incentives. Next, sales staff – those engaged in direct customer contact with a view to securing business for the firm. Their reward mix was one of relatively high proportions of the mix in short-term incentive programmes linked to either individual or

¹⁷ Notable exceptions to this were identified by the interviewees around some sales and investment banking environments where bonus was the largest element in the reward mix.

team-generated revenue. Finally, general employees – those not in senior management or sales roles.

Sales staff have their own bonus scheme and therefore their mix is different from other staff. For other people outside the sales team the discretionary pool is generally dependent on level. (RE13)

Typically benefit offerings were considered more ‘egalitarian’ with standard packages being offered to all employees, although the level of certain benefits may be related to salary, e.g. the amount of life assurance, which would typically be a multiple of base salary. However, some benefits were also identified as being linked to an individual’s place in the organisational hierarchy. Certain benefits were only provided, or provided at a higher level, as employees moved up organisational levels.

Are they hierarchical? There are some-, there are some which are hierarchical. Also, perk cars are-, are available only to sort of senior managers. Private medical insurance, for the most part is again only available to senior managers. The rest of the benefits tend to be sort of like all the same so whether you’re, you know, the filing clerk or the CEO the same pension scheme would apply to you. (RE25)

In addition, one RE reported that during the recent economic downturn their firm had looked to protect the overall package for more junior employees when cuts were made to the provision up the organisational hierarchy. This was justified on paternalistic grounds. The firm was keen to protect its lower paid workers from the effects of the downturn which were seen as having a more significant influence on their lives relative to higher paid employees who were seen as being more able to share the firm’s financial difficulties.

So therefore when times were getting tough this time last year – prices of gas, petrol and everything was really going up – so what we decided to do was

having put the whole salary review process together and we decided to cut the chunk that was £75,000 and above, anybody who got a salary increase on £75,000 and above, we took it away and gave it to the bottom of the organisation. (RE2)

It was apparent that the interviews identified clear differences in the reward mixes for these different levels in the organisational hierarchy and for certain role such as sales and executives. However, when questioned about these hierarchical and role-related differences in reward mix, what did emerge from the interviewees was that although actual reward mix outcomes were different (i.e. different mixes were deployed) the determination process was the same. The following quote illustrates this point:

We think through the same areas – what the market is doing, what employees expect, what the senior team think is the right approach – and then develop the right mixes. (RE30)

The industry norm position for the level and role was the main determining factor. One notable exception to this was the process for firms' executive employees (i.e. CEO and other executive directors) which was significantly more formal, due to the nature of the design and approval process (requiring Board approval through the Remuneration Committee) and the transparency of the individual end result, given that the reward mix would be published.

5.3.2 Summary

In summary, the REs identified that the determination process was a considered but informal process developed largely from the aggregation of the decisions made with respect to base pay, bonus and benefit provision. Whilst differences in outcomes did vary between organisational hierarchical level and types of role the thought process to get to these outcomes was the same. Benchmarking was central to the determination

process and the issue of the industry norm position underpinning these benchmarks will now be examined.

5.4 Industry norm

Having examined how the REs conceptualised reward mix and their accounts of the informality of the determination process, this section now examines the main focus of the research question, namely the influences that the REs saw on RMD. Whilst the interviews demonstrated the relevance of the elements in the conceptual framework developed from the literature, in line with the RC interviews, they showed a clear dominance of the concepts underlying institutional theory. Discussions were, with two notable exceptions detailed later in this chapter, dominated by interviewees outlining how the influence of practice in the market shaped the mix their firm offered as illustrated by the following typical quote given when a participant was discussing the influences of their firm's reward mix.

Market driven. Because everybody else does, that is the short answer. (RE30)

The dominance of market practice and the interviewees' understanding of the market will now be explored.

5.4.1.1 The role of the market

The primacy of the market was identified in all the interviews as being a factor which required consideration when developing reward mix approaches. The market was defined in two ways. First, it was defined with reference to the market for labour – seen as the skills, knowledge and experience that the firms required in doing their work. This was by far the most dominant understanding of the term with the following quote being a typical response.

It's all about the skills, knowledge and experience you need to have and keep. That's how we think about our market when benchmarking our package. (RE29)

Second, a minority of REs(six) also made reference to the product market that their firm was operating within and, in particular, the issue of the volatility of revenue which was typical in their firm's product market.

The type of business we are in has greater volatility of results and, therefore, a bigger element of variable pay is helpful if you've got more volatility, because you've got more flexibility in your costs. (RE30)

Given the dominance of the first definition of the market, discussions largely focused on the influences on the labour market and how this market was established through formal and informal benchmarking activities. The role of benchmarking will now be reviewed.

5.4.1.2 Benchmarking

All the REs interviewed explained how their firms carried out some form of benchmarking of the reward levels of other 'similar' firms. We have already seen how decisions on each of the individual components making up the mix (i.e. base pay, bonus, benefits) were typically seen as being taken independently. This was generally through the receipt of benchmarking data from the range of reward consultancies providing reward benchmarking services. These benchmarks were largely separate datasets for cash compensation (base pay and bonuses) and less frequently a separate exercise on benefit packages, given this was seen as more problematic.

You can benchmark salary, bonus, total cash, even stock to some extent, but benefits, even the basis of cost is problematic and then how do you get a true comparison of one benefit package against another when some are hierarchical, some are flat ... it is fiendishly problematic. So we have never done it. (RE1)

No RE reported that their firm carried out formal benchmarking of the more relational

returns that accrue to employees. Assessment of other firms' positions in this area was either not carried out, consistent with the narrower conceptualisation of reward mix generally taken, or, where a wider approach was considered, assessment of other firms' practices was carried out through informal networking. The difficulty of accurately assessing other firms' non financial offerings was seen by one interviewee as a positive. They identified how this allowed their firm to differentiate in this area as a key retention tool, safe in the knowledge that the lack of transparency in the market would mean that any innovation would be less likely to be replicated by competitors.

I think the less tangible elements of reward are where you can really differentiate yourself and make a statement about what working at the company really means. It's difficult to benchmark that or replicate it if it doesn't fit with who you are as a company. (RE17)

5.4.1.3 Sources of data

Given the significance of the labour market in influencing the reward mix outcome it is sensible to examine where companies source these data. The REs outlined how their firms used a variety of sources.

You access the market through different means and therefore it's a sort of external factor which simply shines a light on your position in the market. (RE1)

Four sources of benchmarking data emerged through the interviews. First, the use of formal benchmarking reports provided by RCs with Watson Wyatt, Towers Perrin, McLagan, Monks, Mercer and Computer Economics explicitly raised as benchmark suppliers. Second was the use of relationships with recruitment consultants as a means of gathering market intelligence, through update bulletins they provided on how they see reward in the recruitment market or more informally through discussions.

Then you've got your agencies that you use that you can call on and just say, look, can you give us some ideas on what's happening out there in the market, what companies are planning on doing, and so on. (RE13)

Next, REs from eleven firms noted how their firm was a member of a financial services reward network group which had been established by a selection of REs. This group met regularly to discuss reward trends and market shifts and share data and intelligence. Finally, nine REs cited the route of ongoing informal networking, which they carried out amongst their peers in order to gain an impression of the market and the activities of other firms.

As outlined above, formal benchmarking reports were reported as being used extensively across the firms interviewed. Benchmarking was typically carried out against other financial services firms in the same geographical region as opposed to comparisons with firms from other sectors in other regions, with the exception of the large scale retail operators as shown by the following example:

I think the other thing that you probably need to remember is that we don't just fish in the financial services sector pool for our people to work in a branch. (RE4)

The account of one RE appeared to suggest that their firm was a significant exception to the general approach to benchmarking. The RE discussed how their firm carried out only limited benchmarking activity and this was not against other financial services firms or roles, but against the legal, accounting and professional services sectors. This was described as being a conscious decision taken in order to differentiate the firm's mix from other financial services firms and position it relative to these professional advisory businesses, rather than the sales focus dominant in their section of the financial

services industry.

Because we are different in what we do it [benchmarking] is quite difficult. There are no other IFAs that pay their advisers in the way that we do. We have had to create our own benchmark using hybrids from other sectors as we were looking for our staff to move from the role of sales to one of professional service. Therefore we looked to these advisory sectors for the benchmarks. (RE2)

Interviewees explained how their firms' choice of benchmark data providers was driven by both their coverage of financial services, but also their role specialisms (e.g. IT, HR, sales, etc), with the REs explaining how they used a mix of providers depending on the mix of their workforces relative to the coverage and expertise of the firms.

Geographical location of the firms interviewed also appeared to have a role to play. Nineteen of the REs' firms were based in London. All but one of these firms identified formal benchmarking as the primary driver of their reward approach. However, the REs interviewed from the eleven firms based outside London were less inclined to carry out formal benchmarking in order to understand what was going in their local geography. Typically, they would rely more heavily on data they had collected through their own recruitment activities, local recruitment agencies and local networking groups to get a feel from the local market.

Every time we hire somebody we go through a process of understanding the benefits of the company that they have left, and we also work with recruitment agencies and we get benchmarking from them. (RE11)

However, the role of informal networking was not confined to the non London-based firms. Eleven of the REs interviewed referred to the significance of informal networking as a key source of data on reward mix trends and emerging patterns

considered by their firm. This was illustrated by one interviewee who, while outlining the significance of formal benchmarks on reward determination, sought to add how informal networking was also useful.

We are also involved in the Financial Services Reward Group. This is really, really handy because you just get a kind of holistic view really of what other people are facing at the same time. (RE7)

The significance of informal approaches to understanding other firms' activities was raised in the context of looking forward at trends, rather than backwards at history, which was identified as one of the main problems with the formal benchmarking data that were collected.

One key issue with that is by the time you get all the surveys, they're nine months out of date already, so it's very difficult to go out there into the market and find out what other companies are doing and that's where you rely on your networks. (RE13)

This was seen as particularly problematic at the time of the data collection because of the state of flux that REs saw in reward practices, due to the financial crisis and lack of certainty that existed over exactly how to implement the regulatory rules that the FSA had introduced.

There is no clarity in the market at the moment. It's impossible to define. It's very... as last year, what people are doing is very driven by their own facts and circumstances, and it means that you can't just say 'well, that's what they're doing so we should do the same thing.' (RE16)

5.5 Influences on the industry norm benchmark position

I have just reviewed the significance of the market benchmark or industry norm on RMD. All firms were seen to monitor the market, albeit through different methods. In this context, this section examines the influences on the industry norm position that was

so central to the accounts provided. Why was the industry norm position as it was? What influenced the development of the norm?

Interviewees offered four explanations for the benchmark position being as it was. These four main constructs in the formation of the industry norm – employee expectations, union expectations, employee control and organisational paternalism – will now be discussed, followed by a review of the items which were seen to moderate the effect of these constructs on the market benchmark when they were present – regulation, legal requirements and taxation.

5.5.1 Employee expectations

The importance of employee expectations on forming the industry benchmark position, and therefore what should be offered by the firm, was highlighted by all of the REs interviewed. Concern was repeatedly raised that any divergences from the market position made their firms vulnerable to attraction and retention issues.

We have to offer because that is what the market offers. These core areas are not an area where it is sensible to be different as that brings in risk around employee expectations of what they should get when working for a bank and we don't want to challenge those assumptions. (RE6)

The strength of employee expectations of what a package in the financial services sector should look like was highlighted on a number of occasions. These expectations were felt to be a particularly strong feature of the financial services market due to the close proximity of firms to each other in London both in the City and Canary Wharf areas (where 19 of the REs' firms were based) and the mobility of staff in this sector. Employees were seen as being particularly well informed about what the overall package typically looked like in the sector and in turn what they therefore felt they

should receive.

There is a huge amount of information out there if you can find it – if you are linked into the network.....so everybody knows what everybody else is getting.....you go into any of the City wine bars and sit next to a crowd of bankers, its 90% certain that someone will be discussing their pay. (RE10)

This pressure was not confined to London-based firms, but was also apparent in the accounts of the three REs from firms located in the home counties, who although recruiting locally, noted the effect of London norms and the influence this had on their employees' negotiating position.

We are in an area of high employment generally. We have quite a tough job in the sense that we are not in London, but we have a vast majority of our population in the professional areas who are more than happy, more than willing to work in London because it is a very quick jump on the train. So you have the tension between not wanting to be paying huge London salaries, but also trying to counter that, you have to be aware of them. (RE3)

This pressure was seen as significant due to the perception that there was a general shortage of talent which the REs believed allowed groups of employees to dictate the terms of their reward mix in line with their market-formed expectations.

If I think about the UK, I think in some ways, or maybe I should say London, which is different, it is quite an adult, transactional relationship which is, you know this is the employer, here I am as the employee, this is what I've got to offer, what are you going to pay me for that? Which is why you don't see the loyalty around, you know, people jump. (RE17)

This was amplified by a perception that employees often had greater loyalty to their profession rather than the firm for which they worked. This created a greater sense of an appropriate reward mix for the profession which people then expected to receive.

I think one of the interesting things about this labour market is that there is more

loyalty to the profession than to individual companies. People look at themselves in comparison with their opposite numbers in [firm name] or [firm name] rather than within the company. (RE2)

The relationship between firm and employee was often portrayed as being imbalanced, with employees holding a powerful position over the firm and the firm constantly feeling the need to justify that the package was attractive relative to other firms.

I make constant reference to McLagan because we constantly regard ourselves as an organisation that needs to prove its paying market. [Firm name] is proving to its bankers that they are paid more or less how they would be paid somewhere else. (RE16)

Consequently, the process of benchmarking was seen as being as much about confidently communicating the reward package to employees, as well as to management. This often led to a relatively defensive position being adopted with reward communications revolving around comparisons of what was being offered elsewhere.

What we do want to be able to say is come to [firm name] for the opportunities that it provides you, and, by the way, you will get a market competitive reward package to support that, so we will look to make sure that we at least pay you the same as what you'd expect to be paid in any other similar organisation, whether it be a [firm name], whether it be a [firm name], whether it be an [firm name] or a [firm name]. (RE15)

A number of interviewees contrasted this position to that faced in other sectors they had either worked in or had received benchmark data on. The main differences that were highlighted were the size of the potential returns that were typically made by financial services firms, the reliance on individual talent rather than financial capital in achieving these returns and the perceived shortage of talent to allow the substitution of lost skills, should an individual move from the organisation. All of these were contributing to a

stronger bargaining position for the employees than perhaps was typical in other sectors.

We have a small number of individuals who personally have very strong contacts and have very strong market relationships enabling them to bring in business or they happen to have the context. We are heavily dependent on these individuals as they drive high proportions of revenue and profit. This has a knock-on influence on the rest of the business in that we also want a degree of consistency across the piece. (RE1)

This employee power was raised by REs interviewed from firms covering all sub sectors of financial services. Significantly, the effect of this power to dictate the package by revenue generators was seen to have been an influence on the packages across the organisation with a pattern emerging for all staff.

So again, it's more of a reward for success because small numbers of people can have a very big impact. This has knock-on effects to other employees in the same area, a sort of coat tail effect with the mix of all affected by the rainmakers. Consistency does matter here so if the top earner's package is heavily variable then it will mean that secretaries too get a higher proportion of bonus than may have been the case in more traditional secretarial roles in say retail. (RE1)

Employees' knowledge of the overall industry reward mix was felt to be particularly strong and this was a heavy influence on their expectations about the appropriate reward mix that they received.

5.5.2 Union influence

The second influence on the industry reward mix was Trade Unions. Ten of the REs described how they saw their employees' union playing a role in RMD. These were predominately in the retail sector of financial services and concerned with more junior, non management, levels of employees. None of the REs from the eight solely wholesale firms raised unions as an influence. Unions were seen as playing a role in

looking to maintain the historical reward mix position that had been established. The REs reported that there was an inherent conservatism within the unions, which they attributed to a desire for, as much as possible, there to be equality of treatment across the workforce, not just within the firm but also across firms in the marketplace.

The agenda for the union has always been to try and harmonise everything because there have been some big anomalies....because they're representing their members and they think that their members at the same level within the same organisation should have the same opportunities in terms of salary and bonus and benefits. (RE25)

However, this was sometimes encouraged by management with their use of benchmarking data in communicating with the unions and in negotiating the annual pay review percentage.

It's not just a case of going along to the benchmark houses and just picking up any data. We will take it to two or three levels down in terms of detail. And it helps you to communicate the position; it helps you to sell the change to the trade unions. (RE12)

The unions' interest was reported as being on an item by item basis rather than through consideration of all the elements forming the reward mix at the same time. This was in line with the approach that the REs reported was conducted within firms (discussed in section 5.3). The REs who had dealings with unions noted that it was their impression that although the unions would typically have input on all elements of the mix, their main interest was the annual salary review and the negotiation of the 'pay pot'.

They are most interested in pay, by a long shot. They are then probably next most interested in defined benefit pensions and protecting what is currently in existence. (RE5)

The REs reported that their experience in dealing with the unions meant that they

believed that as well as a desire for fairness, the unions were also driven by paternalistic concerns for their members and ensuring that the package provided for a range of different needs.

I think it's just natural to them. I think paternalism is just in their nature. (RE23)

However, the extent to which they really understood their members' real expectations and needs was disputed. One RE identified issues with what he perceived as the unions' dislike of variable pay, which he believed was not in line with employees' beliefs as explained in the following extract:

Well, I think that their position is that they don't like variable pay. They'd rather have as much as possible in base because it's certain, it's guaranteed. Benefits that depend on it like pension are obviously enhanced. I think there's the perception in the unions that variable pay... it's subject to things like favouritism, for example, you know. (RE23)

What did emerge was the REs' view that their influence was contextual depending on how the firm more generally viewed unions and the extent to which the relationship was seen as being a productive route with which to engage with their employees.

So I think it is a positive – they wouldn't necessarily always agree with what we have done, but I think it is good because it regulates in the sense that... it keeps us honest.... they don't formally regulate us, but they regulate our actions in the work that we do. (RE27)

5.5.3 Influences on employee expectation – Historical reward patterns

The interviews provided further insight into the REs' thoughts on what had caused the formation of such strong employee and union expectations. Twenty-one REs identified that these expectations were shaped by historical reward patterns formed over several decades which were strongly engrained in employees' expectations and therefore were

seen as being particularly difficult to change.

This way of rewarding staff has been around for a long time, they expect to be rewarded that way and we are not in a position to break those expectations. (RE13)

This was illustrated by eight of the 21 REs in relation to a number of benefits that continued to be offered to employees, despite the original reason for their introduction having long since disappeared. This was particularly the case for benefits introduced because of tax concessions that the government had made available, but was also raised with respect to the employee demographics of the organisation. The benefits continued to be offered because employees had become accustomed to receiving them and firms were reluctant to change, fearing the employee disruption that change may cause, given the strong expectations they were dealing with. For example, one RE noted how private health cover had been introduced as an attraction and retention tool for a relatively mature workforce. However, over time, the RE's firm had seen its workforce demographics change dramatically to a much younger workforce. However, the healthcare benefit is still perpetuated.

It's crazy really that we continue to offer private medical cover for our staff. I'm not sure they value it at all but we haven't changed it as I'm not sure how they would react. (RE8)

These historical reward patterns were seen to have been formed by a combination of two factors. First, the interviews identified how the REs felt owner beliefs about the role of reward structures were significant in forming historical reward patterns and, through this, influencing employee expectations over time – in particular, the role played by incentive and bonus schemes in controlling employee behaviour, and

employee benefits and the responsibility firms felt for the welfare of their employees both for paternalistic reasons, and with respect to their search for productivity and engagement effects. Second, the general structure and profitability of the sector, i.e. product market effects, had led to the formation of a general sense of entitlement amongst employees with respect to the sharing of wealth created in the industry between the owners of the firms and these employees. Each of these will now be examined.

5.5.3.1 Control over employees

Agency theory suggests that reward mix, at least with respect to the balance of fixed and variable elements within that mix, will be established in line with management of the conflicting interests of owners and employees. This theoretical position was not overwhelmingly supported in the interviews. Thirteen of the respondents talked of alignment in this way.

The best way of getting the alignment between the employee interest and the shareholder interest is obviously to have people as employee shareholders, but also for the employee shareholders to have bought and put their hand in their pocket and to have bought part of their stake. (RE14)

Furthermore one interviewee rationalised the use of market benchmarks with reference to employee alignment and control.

The market may dictate the mix we offer but there is a good reason why the market is as it is. The banking mix helps incentivise our employees to drive sales which we need to survive. (RE4)

Where the interviews discussed alignment as a key element, interviewees did note that it may be less about the use of incentives to directly and overtly influence employees' behaviour, and more about employees sharing in the wealth that they felt that they had

generated.

So it's legitimate to pay someone one million pounds if they've brought in twenty million quid's worth of revenue, but if they don't bring it in the next year we don't want to pay it to them and we won't. (RE18)

There was general scepticism about whether the reward mix was genuinely acting as an influence on behaviour, but rather was more about employee expectations of their entitlement to their 'share' of the revenue generated. These accounts supported the contention that the variable component of the reward mix was more about recognition and entitlement than a pure incentive.

On our team we debate sometimes whether or not we think the-, the-, the level of the bonus is going to change somebody's-, somebody's behaviour or contribution level because of the bonus that we offer. We always think that the answer is always no, that people who will deliver will always deliver because they are just that sort of individual that you've got in your team and don't need the carrot of a-, a bonus to incentivise them. It's just something they get because it's acknowledgement of that contribution. (RE25)

The emphasis placed on incentives in the reward mix was further challenged as not being in the interests of firm owners as it was felt that the effect on behaviour might not be in line with the longer term interests of the firm. It was suggested that incentive-based pay can cause problems with respect to potentially encouraging inappropriate risk-taking behaviour that was not in the longer term interests of the firm, as employees carry out transactions or encourage customer sales that were inappropriate and could, over the longer term, actually destroy value in the firm. A number of examples of this occurring were provided with respect to the 'mis-selling' of financial products to customers in the areas of pensions, endowments and payment protection insurance. These product sales had been rewarded with a bonus immediately following the sale,

but later were seen to be unprofitable as compensation had to be paid to customers when it was discovered that the sales were inappropriate.

As an employer, I don't think that would be a responsible thing to do. I think we should be encouraging to think of the short-term versus the long-term. (RE11)

Finally, interviewees questioned whether the incentives payable through bonuses could in reality be truly varied with firms' performance and therefore be genuinely aligning principals' and agents' interests. They cited recent cases of their firms paying out bonuses despite making significantly reduced profits, or even losses, as they were concerned about the effect non-payment would have on overall employee morale and through that motivation, retention and performance going forward.

For all our talk about alignment of interests between management and shareholder, we didn't actually mean that because when push comes to shove, you still need to pay your management team for doing work even if shareholders are not receiving pound for pound the same benefit. And that is a massively important point. It's a point that no one was prepared to acknowledge while share prices were going up. We have alignment – you win, I win. But it doesn't work the other way round. (RE19)

This also limited the extent to which reward mix through higher proportions of variable pay was seen as being able to align the costs of the business with its overall performance.

Well we see regularly firms paying out bonuses in poor or even loss making years. Although they are meant to vary with firm performance, it is still hard to break employees' expectations that if they have individually worked hard then they should get some form of bonus reward. (RE16)

5.5.3.2 Paternalism

The extent to which employers had certain responsibilities to their employees which

could be, at least partially, met through the way in which their reward package was delivered to them was raised by 22 of the REs interviewed as being an influence on the industry norm position.

You have to have some form of benefits from a corporate responsibility perspective, you want to ensure that your employees are to the best of the organisation's ability looked after. (RE10)

However, overall the interviews showed that the REs believed that their firms were becoming less concerned with delivering reward to employees in order to manage their welfare, but were rather expecting employees to take more control over areas that historically might have been the preserve of the firm, especially around pensions. This had occurred gradually over time in line with the shift in coercive pressures, largely from government, on company pension provision, but also the overriding concern of cost management that 18 of the REs raised as a major consideration at their firm.

So really we went through almost every-, well, we did every single benefit where there was a cost to the business for having that benefit and said, look, do we want to sort of like address whether or not we continue at the same level or reduce it. But in-, I think in the end, we-, we decided that we weren't going to do some of the things that we could have done to save money and we felt that on balance that was-, it was the right thing to do for our employee's health, welfare and futures. (RE25)

Moreover, one RE noted how a shift to employees taking greater responsibility for their own investment decisions was in line with a wider shift in their firm to encourage greater personal accountability and responsibility for business decisions to help make the firm more fleet of foot and improve its competitiveness.

We need to get employees to think about things in a different way, take more accountability, more responsibility, and I think from that perspective reward has a part to play as well in the fact that we are changing the employee deal here,

whether it's implicit or explicit. (RE15)

A number of the REs commented how their firms had shifted to increased employee choice in how benefits were provided to them through the adoption of flexible benefit systems. However, even here some restrictions were made on this employee choice as the firm looked to deliver a base minimum for certain benefits, particularly life assurance and critical illness cover, in order to meet what it felt were its moral obligations in these areas.

We look at the benefits package that we would consider to be standard and we said right which elements do we believe as a responsible employer, cannot be removed? (RE3)

However, firms moralising over benefit provision was seen as problematic by one interviewee:

It's almost arrogance for me to assume that I know how you would wish to be rewarded, because what you fall into, the trap you fall into, which most organisations do, is a leadership of a corporation believes that their own personal drives and value set are actually representative of the entire corporation – well they are not because in the FTSE 100 there are only 100 CEOs, yet the FTSE 100 employ, I don't even know – 7 million people who are driven by different aspirations, desires. (RE26)

Discussions about the extent to which firms had responsibilities to their employees tended to focus on the benefits package that was offered, but this was not exclusively the case. Four REs noted that their firms had identified they had a wider responsibility to their employees and putting high proportions of their reward at risk was not seen as responsible behaviour by the firm. The REs noted that their firms felt that employers had a responsibility to ensure the fixed proportion of their reward was at least enough for them to achieve a standard of living appropriate for their role. This included the

need to ensure that they could secure mortgages and meet family commitments in years to come in which bonuses may not be payable due to poor firm or individual performance.

Well, one, people need to have a base salary to be able to do things like buy mortgages and so on, to live, there has to be ... people need to know that if there was a very poor year and there was no bonus, that they do have the minimum amount of income, so the security of having a base salary. (RE13)

In addition, these REs discussed how they believed putting high proportions of pay at risk was not in the firm's interest as it was seen as potentially inducing levels of pressure and stress on employees that may not be conducive to effective performance.

As an employer, I don't think that would be a responsible thing to do. I think we should be encouraging them to think about longer term performance and not putting too much short term pressure on results. (RE11)

Further justifications for paternalistic behaviour were also provided. However, these were often as much about the firm and improving firm performance as they were about employee welfare. First, certain insurances within the mix were seen as crucial for ensuring employee health and therefore attendance and productivity at work.

There's things that we did, like introduce things like private medical insurance, we introduced a doctor, we introduced a number of health and well-being points a couple of years ago, and the key driver for that was ensuring that people are healthy and they get treatment for any illnesses or diseases as early as possible so there's no barriers to their recovery, but the other benefit was you're saving time on them being out of the office. (RE13)

Less prevalent but still raised by three REs was the importance of managing the firm's liability to an employee's family should death occur, or illness leaving the employee unable to work. The need to continue to deliver some form of income when employees

were unable to work or provide a payment to the employee's family on the event of death therefore was not solely an act of paternalism, but rather one of reputation management.

People can be very stupid and not provide for themselves in some issues and if someone dies and they haven't got any death benefit while investment banks don't have a particularly strong reputation position, we do worry a little bit about our reputation. (RE10)

Eight REs also raised an issue that their firms were increasingly having with the delivery of reward through provision of the firm's equity to employees, either directly or in the form of options. Concern was raised about the extent to which over time this would mean that a high proportion of the employee's wealth and future income was dependent on the firm's performance. Although this increased individual and firm alignment, as outlined in agency theory, it also created investment concentration risk for the employee. A rational position for the employee was seen as more diversified through investment of accumulated wealth in a more balanced portfolio. One RE noted that this had become particularly acute at his firm when its share price had fallen by over 90% in the year preceding the interview and therefore had seen large numbers of their employees lose relatively sizeable amounts of money as they had held shares provided by the company both within and beyond vesting or deferral periods. The collapse of Lehman Brothers was also identified as having seen this risk crystallise for employees.

I mean clearly people who worked at Lehmans lost most of their worth through the collapse in those share prices, so I mean a very significant issue for them..... It means that there is a certain concern around the whole notion of being tied into... well, this concentration.... It raised that whole question about is it legitimate to ask employees to put all their wealth into the firm's stock, and

that's clearly not an investment strategy you're advised to do. (RE18)

Finally, six REs noted that their firm believed operating in the financial services sector presented a certain obligation to assist employees in managing their finances. This was particularly relevant to firms operating in the pensions sector who, as a result, felt the need to offer relatively generous employee pensions and also provide advice on managing retirement risk in line with the standards provided to their customers. The message that was sold to customers with regard to the importance of long-term savings had to be congruent with how the organisation delivered its reward. This did have the effect of making the overall package more attractive than that offered by non financial services firms operating in the locality which had benefitted both recruitment and retention.

We, as an employer in this sector, have to give employees a progressive way to gain wealth and handle debt. That is going to be a much more attractive relationship than one that just coldly hands me the money and leaves me to get on with it. (RE9)

5.5.3.3 Industry structure and profitability

Seven REs speculated that the historical structure and overall relatively high profitability of the sector (pre financial crisis) were influencing factors in informing current reward mix expectations that employees had. For example, two of the REs from investment banks noted specifically that their historical structure as partnerships before the reforms to the City that occurred in 1987 with the 'big bang' were still influencing today's reward mix. These partnerships had operated with partners receiving high proportions of their reward in variable pay related to the firm's profitability. This had endured post big bang even though the individuals concerned no longer faced the downside liability.

A lot of what we see now has endured from pre 1987. High rewards for high risk taking, just that the risk taking is now on behalf of the shareholders not your own pocket. (RE10)

In addition, they were seen to have high levels of power to insist on getting the market package and influencing it so that it was increasingly generous both with regard to its size, but also how it is paid, especially around the entitlement to share relatively high proportions of the overall revenue.

The variable pay element grew out of the fact that the profits were so large and it became possible for ... the market for employees became so hot it became possible for employees to bargain, basically, for a much bigger portion of the income that they brought in than in other industries. (RE20)

This was felt to have permeated throughout the sector and was a strong influence on packages at all levels and for all types of roles.

5.5.4 Moderating employee expectations

Having examined the main constructs seen to be determining reward mix and, in particular, the influence employee expectations and their formation has had on the use of industry norm positioning by firms, the chapter now reviews the findings with regard to a number of moderating variables, i.e. variables that change the relationship between employee expectations and industry norm reward mix when they are present, that were identified. These were regulatory change, legal and taxation matters.

5.5.4.1 Regulatory change

The coercive nature of regulatory pressure on the mix was reported as influencing the thinking of the REs and their accounts of the RMD approach within their firms, given the industry discussion on the appropriate regulatory framework which was underway at

the time of the research¹⁸. Whilst significant uncertainty was present at this time about what the final regulatory requirements might be, it was reported as beginning to influence thinking, with 22 of the REs identifying the changing regulatory landscape as a moderating influence on market practice at that time. The following quote was typical of the REs' comments that this pressure would make a difference to reward mix structures across the industry.

Well the big one for us at the moment is the FSA code..... that code I think will have the biggest impact on financial services remuneration for fifteen years at least. I have no doubt about that. (RE4)

The increased regulatory attention was identified as defining more clearly 'best practice' with respect to reward mix, which in reality meant that the benchmarks followed may become even sharper in the future.

We're licensed to operate and we obviously get inspected. They set a minimum standard that we find quite helpful, even though there might be a minimum standard on some things that we don't need to follow, if you see what I mean. (RE24)

Adherence to this newly emerging industry norm position was also considered important as it provided a good narrative for firms to explain their position to their stakeholders.

I think if the business is trying to demonstrate to the group that it's managing its risk and its reputation well, it's a great story to say we have met all the requirements. It's a good place to be. (RE24)

Meeting the regulatory requirements was also seen by a number of REs as a discipline

¹⁸ The interviews were carried out when, in the UK the FSA, which had some form of regulatory responsibility over all the firms interviewed, was consulting on and implementing new remuneration restrictions (known as the FSA Code), for major banks, building societies and investment firms.

on firms to do what was seen as the right thing for their customers through their reward offering.

But treating the customer fairly, we work very hard with the FSA to ensure that we are fully compliant with that. It's really embedded in our culture, it's part of our main business strategy aligned to it. (RE27)

Generally, with one notable exception (discussed in further detail in section 5.7.1.3), non compliance with the regulations was not seen as an option. Furthermore, the coercive nature of the new regulations was not always seen as a negative outcome. The existence of regulation was a means by which REs could push through changes that they wanted to make to their firm's reward mix.

And I have used the regulator as the reason for why we should be doing things which are good practice, very helpfully actually. (RE1)

However, the extent to which this coercion would have a lasting effect on the benchmark position was doubted by a number of interviewees who felt that the institutional framework established in the industry would endure, despite the moderating regulatory pressure for change.

It's very much a culture that is going to take years and years to shift. (RE5)

5.5.4.2 Legal pressures

The extent to which legal, non regulatory, constraints were seen to operate on RMD were relatively limited. Whilst acknowledging that a range of legal factors influenced reward determination around areas such as reward level, with the minimum wage being cited, and reward structure, with equal wage considerations being raised, the extent to which they influenced the actual reward mix materially was weak as illustrated by the following comment.

But those are really, to me, more noise on the line, as opposed to something which fundamentally drives it. (RE26)

There were two exceptions to this. First, the restrictions on some groups of employees' reward mix due to Transfer of Undertakings (Protection of Employment) regulations (TUPE)¹⁹ following mergers or takeovers, which required organisations to maintain certain elements of reward for groups of staff transferring from one to another.

Well partly it's for legal reasons, so there will be elements protected under TUPE, of course. (RE17)

Second, pensions were raised as a further area where legislation was an influence on the overall mix. Two legal developments were seen as influencing the pension component of the overall mix. First, the introduction of age discrimination legislation which had caused some firms (four) to change the structure of their pension schemes.

We also offered quite generous pension contributions which were actually based on length of service. Obviously age discrimination legislation came in and really put paid to that and we had to rethink very, very carefully. (RE8)

In addition, the impending UK reform of company pensions' provision coming with the introduction of personal accounts through the National Employment Savings Trust (NEST) was highlighted as an influence on the industry benchmark position. This requires firms, from 2012, to enrol all employees automatically into a NEST pension scheme, unless they offer a suitable alternative, and contribute at least 3% to this fund.

This was reported by the REs as causing a number of the firms to consider the structure of their pension scheme, in particular the level of contribution being made by the

¹⁹ The Transfer of Undertakings (Protection of Employment) Regulations 2006 is legislation designed to protect the rights of employees in a transfer situation enabling them to enjoy the same terms and conditions, with continuity of employment, as before.

organisation and the likely take-up rate.

We will have to consider the whole affordability of our reward package in light of the personal account changes. (RE11)

5.5.4.3 Taxation

A specific subsection of legal constraint – taxation – was raised by 24 of the REs interviewed as an influence on the industry benchmark reward mix. However, the influence was not considered as strong as the regulatory and legal coercive pressures and the employee expectations already discussed. The tax regime was seen to be influencing the reward mix “at the edges” rather than being a central influence on RMD.

We use the tax concessions that are available..... The tax regime points you in a direction because both us and our staff can get a better deal through exploiting the tax provisions. We aim to do that to everyone’s benefit. (RE3)

Certain tax advantages arising from salary sacrifice arrangements involving benefits such as pensions and childcare, where national insurance payments could be avoided, were embedded in the industry practice. However, more complex tax schemes were not uniformly taken up. The extent to which these more complex options were used was seen to be dependent on two elements. First, the capability of the organisation to manage the complexities that certain schemes around shares, pensions and capital gains tax regimes for employees presented.

We were once bitten, twice shy on that one. We did try a number of years ago instead of actually paying a bonus, we actually gave staff free shares in the company and never again. The tax legislation around it is still working its way out. (RE8)

Second, was the firm’s philosophy on its role in assisting employees manage their tax liabilities more effectively. A position articulated by five REs was that their firms

would not actively manage mix with a goal of lowering tax liabilities of their employees as this should be left to employees to manage.

We are so risk averse it's untrue. Certainly from a tax perspective we have a stated policy that we will not do anything to assist employees in avoiding tax, which is giving us, you know problems, with the budget changes that were announced. (RE15)

However, eleven REs identified that their firms' use of these more complex tax avoidance schemes was an important part of what the firm could do to maximise the value of reward to the employees. This was particularly apparent during the research when the UK government increased the level of personal income tax payable by employees earning over £150,000 to 50%.

The 50% tax rate is going to affect the mix because there's going to be much more of an incentive to see how we can structure packages to ... it's not tax evasion but tax avoidance, so what are the most tax efficient schemes that we can have, and maybe that's going to be more of a draw away from paying more as cash in terms of the bonus and things like that, so that's definitely going to drive ... especially amongst our higher earners, how we structure the reward mix. (RE14)

This shift in personal tax rates for the highest paid was seen by the REs as a 'tipping point' for a number of firms with the management of employee tax liabilities likely to become increasingly proactive than had historically been the case. The following quote, which was provided before the change to the 50% tax rate was made, was given in the context of media speculation that the rate would increase.

I think we are pretty close to the level of tax that people see as reasonable, any increase on where we are now is going to start people saying ok, actually we are going to start doing something about it. (RE10)

Furthermore, one RE spoke of one globally active firm which was looking to transfer

fully tax change risk from employees to the firm through consideration of net payment agreements with employees. This was felt to be necessary due to the global nature of the labour market in financial services and the resulting multinational workforce which operated in London and other key centres.

The point about that is that the people are saying to us, well, you want to operate out of London. I shouldn't have to pay the penalty for that. They're just as happy working out of any other city..... Most of our people would happily go to Zurich, happily go to New York, happily... love to go to Hong Kong. (RE18)

5.5.5 Summary

The industry norm emerged as the main influence on firm reward mix positioning. The strength of established employee expectations of what reward mix should be delivered was identified as influential in setting the norm position. These expectations were attributed to the established historical patterns that had emerged through a combination of the influence of owners' beliefs with respect to controlling and motivating employees, some paternalistic responsibilities that they historically had felt and the particular characteristics of the financial services sector with respect to its profitability and structure. Whilst significant, these employee expectations were seen to be moderated in their effect on the industry norm with legal, taxation and in particular regulatory coercive influences disrupting the transmission of these expectations through to the overall industry norm reward mix.

Whilst the industry norm was strong the research did also identify how firms could diverge from this mix. These findings will now be presented.

5.6 Diverging from the industry norm

The findings discussed above show the strength of employee expectations on reward

mix across the financial services sector and the influences, such as historical reward patterns, contributing to the development of these expectations. In addition the findings demonstrate the moderating role that legal, taxation and regulatory coercive forces play in influencing the industry position.

The REs' accounts were consistent in raising the influence concern over the attraction and retention of key employees was having on RMD, with firms reluctant to step away from the industry norm position due to strong employee expectations that they should receive this industry position.

*I'd love to say that business is the prime driver of the reward mix, but I think that heritage, history and the hiring market is probably a bigger influence.
(RE30)*

However, during the interviews, changes that firms had made to their reward mix were explored in order to understand the extent to which firms felt compelled to follow the industry norm and, where they did not feel this compulsion, what influenced their decisions to adopt a non industry norm reward mix. This section discusses the influences in order to develop an understanding of why a firm may diverge from the industry norm position.

The changes that were raised are shown in the final column of the table in Appendix 10. Of the 30 firms of which the REs spoke ten provided examples of reward mix adjustments they had made that moved them away from the benchmark position. Most common were adjustments to benefit schemes, either enhancement or reduction to higher value benefits, such as pension contributions or medical cover relative to the benchmark, or provision of additional benefits, such as retail and leisure voucher

schemes. Five firms differentiated their reward mix in this way. In addition, five firms had changed the proportions of overall reward payable between fixed and variable compensation relative to that suggested by the benchmark. These firms had increased the proportion payable through base or fixed salary relative to the variable or bonus award.

Through the REs speaking of these changes that their firms had made, alongside the accounts of REs where they had felt inhibited in making changes, a number of factors emerged as significant in determining the extent to which firms were likely to move away from the established norm and differentiate their reward mix.

The overriding influence on behaviour and the desire to adopt the industry norm benchmark position was the security that operating either at or close to the benchmark was perceived to provide. The need to operate within a 'safe harbour' of the mix offered by other firms in the market and, specifically the perceived danger of being the first to move away from this 'safe harbour' was widespread.

There is a considerable concern in the market about first mover disadvantage whoever moves first will lose. (RE10)

Only ten REs spoke of what they saw as their firms having both sufficient conviction in their ability to manage the risk that moving away from the norm was felt to imply and, alongside that, belief that moving away from the benchmark position would deliver a competitive advantage to lead them to deliberately target reward mixes away from the general market consensus.

The extent to which REs believed firms were willing to take a risk and operate outside the perceived 'safe harbour' of the industry norm position appeared to be formed

through the interplay of two variables. First, the firm's desire to resist the industry norm and differentiate its reward mix. Second, alongside the firm's desire to operate to some degree away from the established industry norm was the firm's capability to manage employee expectations should such a move away from the norm be attempted. The dimensions identified as influencing this desire and capability will now be reviewed.

5.6.1 Desire to differentiate

The REs identified five dimensions as influencing firms' desire to differentiate their reward mix away from the industry norm – leadership, business strategy, political pressure, parental influence and firm specific history. The findings related to each of these influences are now presented.

5.6.1.1 Leadership

The focus of the leadership team was highlighted as significant in reinforcing mimetic behaviour by 17 of the REs who identified how the leadership in firms set the tone for the significant role of market norms in setting the mix position. Leaders wanted to know what reward practices other similar firms were adopting and then generally their expectation was that their firm should operate in line with that position. The interviews highlighted how, on the whole, the REs saw the leadership of their organisation as reluctant to take risks with regard to the operation of the organisation's reward strategy in contrast to other areas, such as strategy and marketing, where differentiation was believed to be actively sought. This was seen as an explanation for the dominance of market benchmarking in influencing reward levels, bonus scheme operation and benefit packages and, through these separate decisions, the overall reward mix. Moving away from the benchmark was considered a high risk strategy for firms. This was clearly

articulated by one interviewee who stated:

We appear to be risk averse when it comes to decisions of reward and reward mix but risk loving with respect to strategy, and marketing. The same leaders influence but very different risk perspectives. (RE1)

A number of explanations were provided as to why this may be the case. First, four REs speculated that the background of the leadership team was influencing the importance they attached to benchmarking, not just reward positioning but all aspects of organisational performance.

I think it tends to be the people who have worked in bigger organisations, so they come very much from benchmarking culture and they come from a culture where you're not just maybe benchmarking your benefits and your salaries, where you're constantly benchmarking your performance, and particularly on our investment side, your performance against your peers. (RE14)

In addition, a further six REs noted that this conservatism was reinforced by the nature of decision making in the firms.

Quite often in... we're a classic example of a traditional financial services organisation because it's death by committee, you know. Nobody is willing to stick their head above the parapet – very cautious, very risk averse. (RE15)

Alongside this, was concern that operating a different position from the safe harbour of the market benchmark might attract negative publicity, especially at the time of the interviews when financial services remuneration news stories were rarely far from not only the business pages but the front pages of the media. Fourteen REs identified this as an issue.

Public perception is very important to us. It is absolutely key. (RE15)

The perception of others related not only to the media but also the equity analysts and

the rating agencies, given the significant influence they had on investor sentiment and, through that, firms' share prices. This was aptly illustrated by one interviewee with reference to their firm's credit standing.

You know, we say that we're proud to be boring. Boring is the new sexy because we feel that's one of the reasons why the bank has remained strong and still has its AAA rating. (RE20)

This position of safety was reinforced by a perception that divergences from the norm would only lead to negative publicity.

There is a fear, I think that is probably the right expression, of getting that silly newspaper headline and that is not to be underestimated. (RE20)

In addition, the credibility of the HR function was seen as an issue by 13 of the REs, with the firm's leadership looking for external assurance of the 'right' position for the reward strategy, with this often coming through consultants and the benchmarking data that they were able to provide.

I think it's part of their make up anyway. Let's not just listen to what our internal people are saying but ... I guess it's just seen a bit as, well that's what they're paid to do totally out there in the marketplace, so there must be some substantiating evidence that they're bringing to the table. (RE8)

Whilst generally identified by the REs as a relatively conservative influence on mix decisions, and a force pushing the organisation towards the industry norm, five REs noted how their firm's leaders were the catalysts for change. This was particularly apparent at one organisation that had adopted a reward mix diametrically opposed to the industry norm consensus (section 5.7.1.3 gives details of the nature of this differentiation). This was attributed largely to the vision of the CEO and his desire to radically differentiate the firm from those against which it was competing.

But [name] is just a fantastic CEO. He is very open, he is very honest and I knew where we were heading, where he wanted to take the organisation. (RE2)

5.6.1.2 Business strategy

Two aspects of firms' strategy were raised by the REs as being pertinent to the firms' propensity to differentiate their mix relative to others – firm size and their customer and supplier relationships.

5.6.1.2.1 Firm size

The firm's size was raised as an influence on the extent to which they considered the benchmark data in determining reward mix. Four REs discussed how they believed that their firms' size, relative to their competitors, gave them the opportunity to operate a reward mix away from the industry norm.

Often people will say well what do other people do? What do [firm name] do, or what do [firm name] do? ... What do our big competitors do? And I say, I don't really care very much what they do because we are big enough that we should do what we want to do. (RE7)

However, this was not a universal position with a RE from another large firm in its market sector showing how they felt that size does not necessarily build confidence to adopt a reward mix away from the industry norm.

We are the largest of our kind of business in the world – or if not the largest, we are the second. So why should we worry about what the slightly bigger or slightly smaller competitors are doing in what we do? Why don't we do our own thing? And I don't think we have the confidence and that is problematic. (RE1)

In addition, three REs also identified size as a barrier, within their firms, to adopting a more innovative approach, especially in the area of total reward, given how it pulls on areas that traditionally do not sit within the compensation and benefits function as

illustrated by the following:

Actually I have worked in small organisations and huge organisations and I have found that that is a lot easier in small organisations....., I found that a lot easier to get that going just because there are only a few people you need to get within that discussion to make that start to happen. (RE5)

5.6.1.2.2 Customers

As well as being dependent on employees, six REs identified the influence their customers had on the mix chosen in their firm. One RE noted how her firm had departed significantly from the industry norm position to allow the reward mix offered to their employees to be used as a marketing tool to clients.

It is important that what we do looks right to the client should this come up or should they see something in the press or on our website. In fact, as you know, we actively promote what we do on reward here because we want clients to know how we reward our employees and through this the benefits we think that brings to the service we give to them. (RE2)

Product market influences were also seen as being present with elements of the mix offered because these were products that they offered to customers. This was identified as being particularly relevant by REs in six firms that provided, as a significant business stream, pension products to their customers which, in turn, they felt compelled to deliver to their employees in their mix.

Obviously the pension benefit because we are a pensions company, we felt as an employer we ought to be promoting very strongly that if you save well for your retirement. So that was always a benefit that was going to be generous because of the nature of what we do. (RE8)

Furthermore, for those firms providing tax planning services for clients, this business was seen by their REs as an influence on their own reward mix design with regard to the use of tax efficient reward delivery vehicles.

It would be sensible though that if we are looking at tax changes and what they mean for our clients that we reflect this in our work with our employees' reward packages. (RE2)

5.6.1.3 Political pressure

Eight of the REs interviewed raised political pressures as having an impact on their firms' behaviour and their appetite to adopt a mix that differed from the industry norm position. This pressure came in two ways. First, indirectly through concern over the general media focus on the reward mix in place. Second, directly through intervention for those firms subject to full or part State ownership, or subject to restrictions under certain guarantee arrangements provided by the State. Six of the firms were under direct government influence at the time the REs were interviewed.

The REs noted how the media pressure, whilst not having a dramatic effect on actual mix, was causing firms to reflect, following assessment of the benchmark data, on how the mix may be perceived externally in the media and with government and regulators.

In 2008 all of our bonuses were obviously subject to quite a lot of media attention in [Firm name] and our CEO only two weeks ago, three weeks ago asked people to consider voluntarily giving them back at the senior levels. (RE3)

However, a more dramatic effect was seen by REs working for those firms directly subject to government control either through ownership or support through the range of State-backed guarantee schemes that were in place at the time of the research. Here the industry norm position was still significant but the coercive force of the new 'owners' had meant that divergences from this benchmark had occurred. This was summed up by one RE who worked for a firm not subject to the restrictions, commenting on this market change.

The impact of government intervention and then government rhetoric has been – mostly the rhetoric rather than the intervention itself – has been the driver of significantly increased salaries in those firms which have major government investments in them. And the question really was whether other firms would follow them. (RE18)

Government intervention appeared to be having an influence on a number of firms' behaviour, but this had not fully translated through to all firms and was considered unlikely to do so, given the strength of mimetic pressures permeating the rest of the market. However, what had emerged was that this intervention had caused some uncertainty in reward mix benchmarks and potentially weakened the clarity with which the industry norm position was viewed. This in itself was seen as presenting a challenge for a number of firms as illustrated by the following:

There is no such thing as the market at the moment. It's impossible to define. It's very... As last year, what people are doing is very driven by their own facts and circumstances, and it means that you can't just say 'well, that's what they're doing so we should do the same thing. (RE16)

This uncertainty led one RE to speculate that in reality two benchmark reward mix positions were forming, one for government-influenced firms and one for the rest of the market.

There used to be a very tight range around base, very tight in the market, I think that's changed. So there'll become a very wide range around base, and so you'll have those banks that pay low base, high bonus, and you'll have those banks that pay high base, low bonus. (RE20)

5.6.1.4 Parental influence

Of the thirty REs interviewed, ten worked for subsidiaries of other entities. The extent to which their firm was seen as having autonomy over their RMD, compared to how much was mandated from the parent group, did vary. Restrictions were an issue for

these firms, with directions as to the appropriate reward mix, or at least certain components of that mix, coming from their parent groups. This was aptly illustrated by one RE from a parent firm who had acquired a significant number of other firms over the last decade. Their approach to managing the reward mix of these subsidiaries was very clear.

The philosophy has been - you are acquired, you will do what we do. There is no debate. (RE26)

A number of explanations were given for the role that parent groups played in determining reward mix. First, there was pragmatism with the centralisation being operated for administrative ease and cost management reasons.

If you look at the size of the organisation and the costs that we were able to commit to the infrastructure, we didn't see any point in reinventing the wheel in going out and finding our own pension advisers and setting up a pension scheme. So we would piggy back on their arrangements. (RE11)

Second, recent changes in the regulatory regime and wider concern about reward management structures and the balance between fixed and variable reward had meant that parent companies that had previously let their subsidiaries operate with autonomy were taking much greater interest and control, especially around bonus policies.

When we first set up as an organisation five years ago there really wasn't a huge level of interest in what we did, they didn't actually really know what people were paid and as long as we were doing great business, then they were really happy. Increasingly over time that has changed, there is now a real interest in what we are paying. (RE3)

Finally, stronger control was also identified over share-based elements of the mix. This was attributed to the need for the firm to keep control over the shares that were being allocated to ensure that they were appropriate with respect to shareholder interests and

avoiding unnecessary dilution.

They abolished the share option scheme and they said we are bringing in another long-term incentive. To be perfectly honest with you, some of the rules they have set around the scheme, if we were setting it up wouldn't have been rules we would have set. Culturally they are quite different to [firm name]. (RE11)

Overall, the theme, where control was exercised, was one of bonus and share-based elements of the mix being heavily controlled, benefits being influenced but with some freedom to adapt to local expectations and base pay being left to the local team to determine in line with the benchmark data on local labour rates. This meant that mix was not considered holistically and that the different reward components were not assessed collectively in the overall decision making process. This contributed to a frustration amongst a number of the REs due to the lack of autonomy they perceived their firm having, and a concern that this meant they were out of line with local labour market practice.

We are bringing in a new bonus scheme to be in line with the FSA and regulations and that is being designed from Frankfurt. I actually have a bit of an issue with that because I am just hoping that they do take into account the particular type of market that we have in London, which is not the same as the investment banking market in Frankfurt. (RE10)

However, the trend of parental control was not uniform with a range of REs noting the freedom within their firm for the operation of reward mix.

The philosophy is a minimum standard that it applies on benefits and then countries have to work within those guidelines and build a set of competitive and fit for purpose... and there's a lot of variety because things like pensions are definitely not standard globally in the marketplace. They vary enormously. (RE24)

5.6.1.5 The influence of history

Five REs noted how, although the industry benchmark was important, specific historical factors solely related to their firms led them to operate elements of the mix that were not fully consistent with this benchmark. First there were legacy contractual positions that meant that non industry norm conforming positions were adopted.

There were a lot of legacy arrangements, and as you try to understand how did we get to where we are now, there were variable elements in the old, shall I say, [firm name] package, but not very much, and it really went through a phase where cash was king, so everything was consolidated into base pay. Benefits was very, very meagre. (RE17)

In addition, one RE noted how his firm was reluctant to move away from the historical position they had adopted, even when this was not consistent with the current industry norm, given the high level of investment that had been put into the development of what were perceived to be relatively sophisticated reward mixes.

It has taken us a lot of effort to get to the mix that we have now and I'd be reluctant to overhaul this given the amount of investment that has occurred. The benefits of changing would not outweigh the cost of making the change so why would we throw away all that we have done. (RE28)

Finally, three REs noted specific historical cultural factors within their firms that led them to operate away from the mix in certain areas. This is illustrated by the following quote.

Where we have come from as a company is really important. If it is right for us then we will use this to resist the benchmark. (RE24)

5.6.2 Capability to differentiate

Having reviewed the findings with regard to the five influences on the overall desire firms have to diverge from the industry norm, I now look at the influences affecting

their capability to differentiate their offering. Two dimensions became apparent through review of the interview data – HR capability and capacity, and line management capability. These will now be discussed.

5.6.2.1 HR capability

The strength of the isomorphic pressures and resource dependencies meant the pressure to conform to the industry norm position that was firmly entrenched was strong. Eleven of the REs identified that any divergences from the industry norm position required significant HR capability in managing change and, in particular, managing potential employee unrest arising from offering a different package from what they would generally expect. This capability was often acknowledged as lacking by the protagonists themselves, the HR professionals. This was particularly true of the wider reward management capability in HR business partners, a structure that was common across the firms interviewed. The business partners, including HR Directors, were seen as key conduits of change in all HR areas including reward, but overall the confidence of the REs in their ability was relatively limited and this acted as a break on pushing through more radical reform.

You've got a lot of good to average HR people, not all of whom are comfortable in the reward space. How many HR people, how many HR Directors would you say are comfortable in the reward space? (RE21)

This capability also related to the appetite of the reward and HR team itself, in the absence of any leadership pressure, to actually go through changes to the reward mix given the stress that managing change in this area could create.

It's a lot of angst to go through some of these things. Generally if we can avoid making changes then we will. (RE25)

Furthermore, trust in HR by business leaders and employees was seen as relatively low. The function's track record was not considered strong enough for these groups to have confidence that any changes proposed were appropriate and that the risk in moving against the industry norm was therefore worthwhile.

I think there will be too much cynicism and not enough trust to enable us to do that. (RE1)

In addition, it was not only capability to manage change that was a concern but also the function's capacity to reform reward mix practice. This was illustrated in the context of the ongoing changes to the legal framework underpinning reward policies.

I guess on the one hand that kind of legislation should/could make you think about things and be a bit more creative. But sometimes you kind of haven't got time to step back and be creative about a global programme and so you just tweak the edges. (RE6)

And size did not appear to be a factor in this area.

You look at a big company like this and think wow, they would have it all fixed; they would have it all sorted; they would be at the cutting edge of everything. ...but no, it is an operational reactive function there just literally hasn't been the headcount previous to offer more support. (RE7)

The lack of capability and capacity within HR functions was also offered as a reason for why consultants were often influential in managing reward change within firms.

We didn't have any experience in-house at all and it's such a sensitive area, we really wanted to make sure we got it right. (RE9)

In all, seven REs believed their HR capability was strong enough to bring about reward mix change. However, no pattern emerged across these firms with regard to their size, location, union representation, ownership or financial services sector.

5.6.2.2 Management capability

Barriers to change were not only identified as being limited to the capability of the HR function to push through changes away from the established norm. The significance of management's capability to manage reward change and, in particular, communication with employees was raised by seven REs. One participant in a large retail firm noted that its line managers had well-established views which had been formed by the market position and reinforced the entrenched employee expectations that already exist.

*That's a very interesting area which we have not been able to deliver on because of folk lore assumptions by management.... unfortunately management who have got to a point where many of them – this is a gross generalisation, but its true – have got stuck in a rut that unless they believe they incentivise people, people will come to work with the intention of doing a bad job, it's very difficult to get them to a place which says this is a load of bollocks and actually people will come and do a good job because actually they are inspired to do a good job.
(RE26)*

5.6.3 Opportunity to differentiate

Alongside the dimensions influencing a firm's desire and capability to differentiate from the industry norm position, one further dimension was found to influence both the firm's desire and also its capability to resist this pressure – opportunity.

Whilst the findings have shown that isomorphic pressures are strong, twelve REs were able to point to examples of practice that they had carried out within their firms that went against, to varying degrees, the established industry norm. Exploration of these change events identified a high degree of opportunism. Three specific events were identified as opportunities to reform the reward structure. These will now be discussed.

5.6.3.1 The financial crisis

As already noted, the research was carried out at a time of significant dislocation in financial markets across the world. These events had a major effect on a wide range of

firms across the financial services sector. This was a key business issue at the time of the interviews. However, eight REs identified that the crisis was also acting as a catalyst for a more fundamental review of their firms' reward approach.

It's not politically correct to say this openly but the crisis was useful in helping us move our reward practices forward. We were able to make a range of changes that previously no one was interested in because times were so good, so why upset the boat. (RE21)

The crisis was an influence not only to those firms that were suffering relative financial weakness, but also as an opportunity for firms who considered their position to be one of relative financial strength. This had afforded them the opportunity to position their mix to be more attractive than the industry norm to the most successful revenue-generating staff and attract them from other firms, despite regulatory pressure in this area.

We are using our strength to aggressively focus our mix in the way these key people like it. We are keeping bonuses high and deferrals low, the State-owned firms just can't match us either in level nor in structure. (RE18)

5.6.3.2 Regulatory change

We have already identified that various regulatory developments were seen as a strong coercive constraint on the industry norm which was generally pursued by the firms interviewed. However, as well as being a constraint, changes in regulation were also seen by twelve REs as an opportunity to challenge established entrenched internal beliefs on reward mix and make wider changes. They were seen as an opportunity to initiate reviews and, through this, potentially change the structure of reward from inside a firm.

They gave us stuff to hang our hat on that we think we needed to change

anyway. It was a good excuse. Certainly Treating Customers Fairly was. Retail Distribution Review, you know, it's yet to impact, but TCF was definitely a case of saying, hey, there's some stuff here that provides a good excuse to insert some of the controls that we want. (RE21)

Moreover, whilst the REs sometimes found that the regulatory change underway was helpful, they did note that it was not causing fundamental reform, rather providing a chance to manage some change at the edges of the overall policy

We used the FSA, the regulatory change, helpfully actually as a means to make a number of reward changes.... but it didn't fundamentally make us say oh we better stop paying bonuses or change the mix. It was at the edges. (RE1)

5.6.3.3 Merger

Eight REs identified mergers, that their firms had been through, as times when more radical reform of reward mix was considered, including whether to depart from the industry norm. Explanations for this were threefold. First, there was the relative freedom it brought with respect to the legal contracts that were in place with employees which were reviewed at this time. Whilst safeguards did exist as to the extent to which they could be changed, they were not as large as changing terms in a 'normal' business operation.

We are going through a big harmonisation process, so ultimately we are going to be changing people's terms and conditions of employment, we are going to be changing people's contracts. So there is a whole legal overlay to what we are doing and it captures the terms and conditions piece in that. (RE4)

In addition, mergers presented an opportunity to break historically entrenched reward mixes that had developed over time and allow the organisation to return to the industry norm.

Because-, because we were separate companies – [firm name1], [firm name2],

[firm name 3] – we had different terms and conditions. And I think it was-, in part, it was a case of looking at what the external market might expect people to be receiving in terms of a benefits package and trying to deal with any transitional arrangements basically to try to harmonise terms and conditions. (RE25)

Mergers were identified not only as an opportunity to deal with the immediate issues around aligning terms and conditions of staff by looking for commonality, but also as a time when more fundamental reform could be considered.

We discussed loads of different things but ultimately we said let's go to the full – if we are going to give people bad news, let's make it as bad as it gets and just do it. (RE1)

5.6.4 Summary

In summary the research identified eight elements that in combination increased the likelihood that firms would not adopt the industry norm reward mix. These were shown to be influential on the firm's desire and capability to resist the strong institutional pressures to conform, especially when operating in combination with some opportunity to change the mix due to a crisis, merger or other major event such as a change in leadership. These eight elements are discussed further below.

5.7 Specific firm propensity to follow the industry norm

The table in Appendix 10 shows for each firm discussed by the REs, the extent to which each of the desire, capability and opportunity dimensions outlined in section 5.6 were found to be present in the accounts provided of how the firms determined their reward mix. Representative quotes from each of the interviews against these categories are also provided in Appendix 11 to provide transparency to the assessment made in the table. In addition, Appendix 10 shows whether the RE was able to provide examples of changes that had been made to his/her firm's reward mix that took it away from the

industry norm.

Appendix 10 highlights a number of important results. The table shows that at least one dimension of desire to change was present in the accounts of the REs speaking of firms that they identified as having made a change to their reward mix which took them away from the industry norm. From this we can tentatively conclude that ‘desire’ is a necessary condition of movement away from the industry norm. Furthermore, the degree to which a firm diverges from the industry norm appears to be further influenced by the extent to which either one of the desire dimensions is held particularly strongly, or that there is more than one of the desire conditions holding.

Whilst having one of the desire dimensions present is a necessary condition of divergence from the industry norm, it does not appear to be sufficient. For divergence to occur, at least one of the ‘capability’ dimensions must also be present. However, the table also shows that capability without the requisite desire appears to mean minimal divergence from the industry norm position.

The findings can be used to categorise firms based on the extent to which they are willing and able to diverge from the industry norm. Three positions emerged. These are show diagrammatically in figure 12 which presents a three-way typology of firms based on their propensity to diverge from the industry norm.

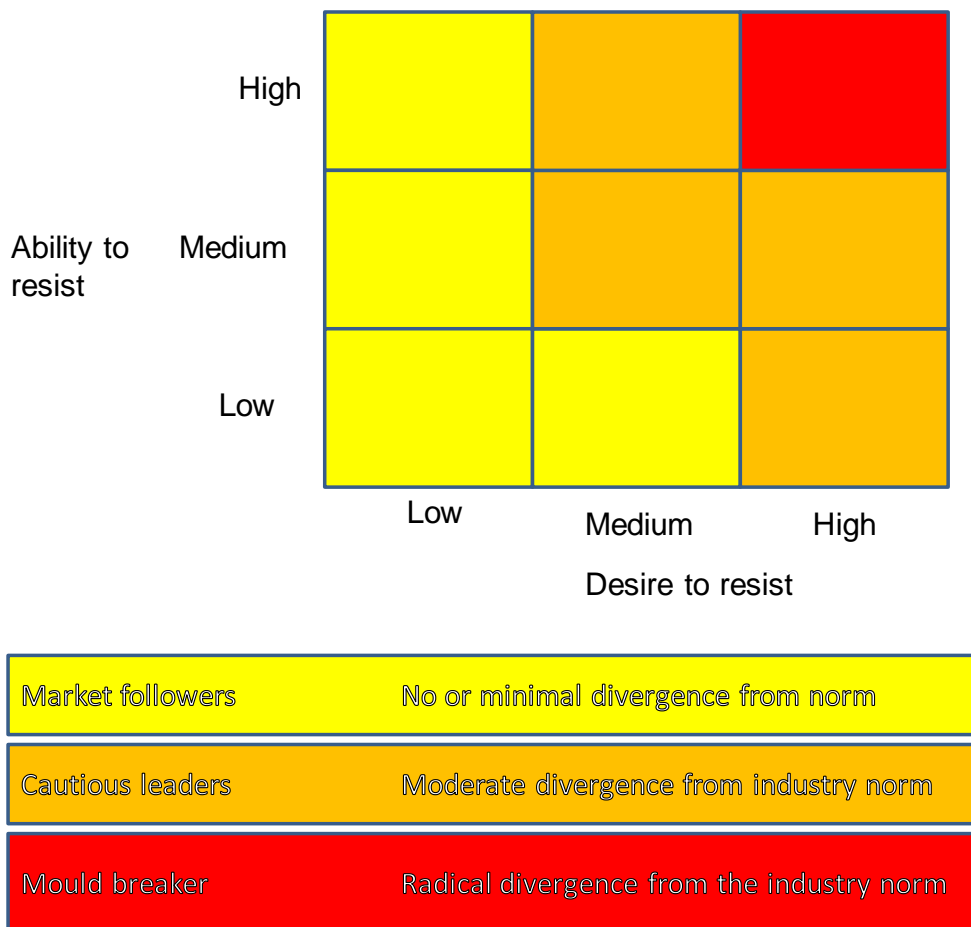


Figure 5-2 - Typology of firms

These three categories of firms will now be reviewed.

5.7.1.1 Market followers

From the accounts of the REs speaking of their firms, twenty of the firms were categorised as operating in line with the industry norm position – this position demonstrating the dominance of the industry norm in influencing reward mix positions. The REs’ accounts suggested that these firms had made no, or only minimal adjustments, to the industry norm position.

It comes back to the sheep mentality doesn't it, just following at a slight distance. (RE28)

Analysis of the REs' accounts appear to identify that these firms typically had low desire (none or only one of the desire dimensions present) to operate outside the industry norm position. Six firms were identified as having higher levels of desire for change, with two of the desire dimensions present, but these only operated in tandem with one or usually none of the capability dimensions leaving the desire to operate away from the industry norm unfulfilled. These firms have been described as market followers and would be positioned in the yellow sections of the grid in Figure 5-2. The accounts suggest that mimetic pressures are particularly strong within this group. They are outward facing in their RMD looking for what their competitors are doing, both informally through conferences and networking, but also a strong use of benchmark data to establish their reward mix.

The leadership within these types of organisation were identified as being keen to understand what others were doing, why any divergence in their reward mix had occurred and what was being done to 'correct it'. The market position is considered a 'safe' position with respect to meeting employee expectations and ensuring an ongoing ability to recruit and retain staff in what is perceived as being a highly competitive marketplace.

5.7.1.2 Cautious leaders

A series of accounts suggest that there is a group of firms who operate with moderate changes to the industry norm position. Accounts of these firms indicate that they had a stronger desire to operate away from the industry norm reward mix position than the twenty market followers, exhibited by two or more of the desire dimensions being present. The reports of eight REs suggest their firms were operating with moderate differentiation from the industry norm. These are positioned in the orange sections of

Figure 5-2 and have been described as cautious leaders, given the lead that they were providing to others in the market, but always with ‘an eye on’ what the market is doing to ensure they do not stray too far from this position.

We would do if there was a need to, we are not slaves to the market. (RE27)

Three of the REs from firms categorised as cautious leaders, identified their size as being a key factor in providing them with the commitment to adopt a more innovative position with respect to their reward mixes. However, even these larger firms were also cautious about moving too far away from the established industry norm. The REs for these firms believed the risk that this may damage the organisation’s ability to attract and retain employees, due to strong employee expectations around the mix, was greater than the benefits that may accrue in this area from radically differentiating their reward package, as illustrated by one interviewee:

So part of you says well let’s be the leaders rather than the followers, which is OK. But you still have to compete in those markets and you still have employee expectations which are heavily influenced by what they see going on in the market so you do need to follow the market practice to an extent. (RE5)

In addition, opportunistic behaviour was apparent in the REs’ accounts from these firms with ‘events’, either internal such as a change in leadership, or external such as a takeover or merger, providing opportunities to change the reward mix and innovate. However, changes resulting from these events were still managed within the context of the relative safety of remaining within touching distance of industry norm reward mix.

5.7.1.3 Mould breakers

Finally, the accounts of two REs led to their firms being identified as having both high desire and capability to operate away from the industry norm position. This appeared to

have led them to have highly differentiated reward mix positions relative to the industry norm. This small group have been categorised as mould breakers and are shown in red in Figure 5-2. The REs' accounts from these two firms paid significantly less regard to industry norm reward mix than the other accounts. Mix was seen as being developed in relation to strong beliefs around the role of reward in influencing behaviour and supporting company strategy on the part of the leadership team and how the reward structure should therefore be aligned consistent with their distinctive company strategies. A strong desire to operate differently from others in the market was present in order to secure competitive advantage.

For one firm, an investment bank operating in central London, the RE's discussion suggested that this was about attracting the best staff through resisting the changes that were occurring to the industry norm position due to the moderating effect regulatory pressure was having at that time. The RE described how the firm was proactively resisting strong pressures that were present for all firms in this section of the financial services industry, to raise the proportion of bonus to be deferred, increase the proportion of fixed pay making up the mix and eliminate the offering of bonus guarantees. The firm was considered atypical, with other firms falling into line with these coercive changes.

The changes were being resisted in order to secure significant advantages with respect to what were seen as financially weaker and more politically constrained competitors.

Anything they do to make it more difficult for any other investment banks to compete is fantastic. (RE18)

This led the RE to believe that although others would want to follow their resistance of

the coercive changes, they would be unable to do so. This was due to the combination of direct, firm-specific, political pressure faced by those where the government was providing direct support and the relatively weak capital bases that they were carrying caused by the losses they had suffered during the financial crisis which could not absorb any additional capital charges that may be imposed by the regulator as penalties for adopting this non regulatory compliant mix position. This weakness was not seen as being shared by this firm.

We are saying 'How much is it going to cost us?' We will pay the additional capital cost. (RE18)

This RE identified that the firm was using its relative financial strength and strong business rationale (to use this position to attract and retain the highest quality of staff), aligned with strong line management commitment to resist the recent changes in this sector, to differentiate itself accordingly.

The RE from the second firm, a long-term saving adviser and wealth management firm, also identified that her firm had radically moved its reward mix away from the established norm. She discussed how the norm in their sector of the financial services industry was a position of high proportions of 'variable' pay for employees linked to individual performance metrics (largely outcome not behavioural metrics). However, she described how this firm had established a position of high proportions of fixed reward through offering significantly higher salaries than the market but with much lower bonus potential, alongside a very broadly defined benefit offering. To keep the overall pay level the same as the market, the variable component remaining was small (typically no more than 10% of total compensation) and performance-related, but at a

company not individual level.

Big bonuses for a few stars was not consistent with the values, payout based solely on sales regardless of whether the sale was justified were not consistent with the values, hierarchical benefits were not consistent with the values. (RE2)

This particular RE did not expect the rest of the industry to follow their position unless coercive constraints (especially regulatory change) impose this change on them.

We are leading the way, but the others won't follow unless the FSA forces them to. (RE2)

This non conformist position was, as in the first case, believed to be driven by a clear business rationale, with the RE describing how the firm was looking to show clients how its reward offering was in clients' interests and aligned with the advice provided.

We actively promote what we do on reward here because we want clients to know how we reward our employees and through this the benefits we think that brings to the service we give to them. (RE2)

Attraction and retention concerns have been a problem with this radical departure from the industry norm (in contrast to the other mould breaking firm where the package was seen as significantly more attractive than the newly emerging norm post-regulatory pressures). On making the change, the RE identified that retention and recruitment were problematic as employees found the shift difficult to understand, given how different it was from the industry norm and the strong expectations that existed that this was the way people were rewarded in this sector.

Some people got off on the way, they didn't like the new environment, they didn't like not being listened to as they saw it – typically. (RE2)

Note, this is despite the fact that what had not changed was the overall level of total

compensation (which does remain heavily influenced by market pressures), but rather how that reward is delivered to employees.

Both of these mould breaking positions are consistent with Lazear's contention that reward mix can be changed without increasing costs (Lazear, 1998). Both firms noted that the reward level they operated was still constrained by the market, and they used market benchmarking to ensure they continue to pay around the market level. However, what was not constrained was the reward mechanisms which they used to deliver the overall reward level.

The limited evidence of mould breaking may suggest that the institutional pressures are too strong for this level of differentiation to occur regularly. What did emerge from these cases was that although the institutional pressures are apparent, they are resisted due to the leadership team's beliefs on what is the right thing to do for each of these firms and strong HR change management capability which has shown its strength in making the change happen with limited disruption to the employment base.

5.8 Conclusion to chapter five

This chapter sets out the findings from thirty interviews with REs from financial services firms examining the influences on RMD. The chapter, after first examining how REs conceptualise reward mix and how the RMD process operates at their firms, reviews the influences that apply in the formation of an industry norm reward mix position or benchmark, namely strong employee expectations, and moderators to these expectations in the form of legal, regulatory and taxation pressures. The findings then go on to examine the extent to which firms feel compelled to follow this industry norm position through examining moderating variables that influence an individual firm's

desire and capability to adopt a divergent reward mix position

Building on the findings presented this chapter then outlined why some firms feel able to resist the norm position and operate alternative reward mixes. Three groupings of firms were identified, depending on the extent of differentiation they pursue – mould breakers, cautious leaders and market followers – with the characteristics of each group examined.

Chapter six takes the findings and initial analysis presented in chapters four and five and from this reformulates the conceptual framework first introduced in chapter two and developed further in chapter four, into a descriptive model of RMD in the financial services industry. In addition, the chapter positions the research findings in the context of the reward mix literature discussed in chapter two.

6 Chapter six: Discussion

6.1 Introduction

In chapters four and five the findings from the interviews with the RCs and REs were presented. In this chapter I discuss how the insights from the interviews conducted help address the research question – What influences RMD in financial services organisations? In doing this, I systematically build a descriptive model of RMD based on the process of theory building established by Whetten (2002) and, in addition alongside this, position the findings of the data within the context of the reward mix literature discussed in chapter two.

This chapter is therefore organised as follows. Sections 6.2 and 6.3 present models of industry norm reward mix development and firm specific RMD. These are then aggregated in section 6.4 when an overall model of RMD is presented. Sections 6.5.1.1, 6.5.1.2 and 6.5.1.3 assess the model developed in the context of the agency, institutional and resource dependency literatures introduced in chapter two. In addition section 6.5.1.4 discusses two other theoretical perspectives that were found to have relevance – path dependency and strategic compensation. Section 6.5.3 discusses how an appropriate combination of all these theoretical positions provides an overall theory of RMD. The final section summarises the chapter.

6.2 A descriptive model of industry norm development

Sutton and Shaw observe that “Theory is about connections among phenomena, a story about why acts, events, structure and thoughts occur” (1995: 378). In order to tell this story with respect to the findings, this chapter develops a descriptive model of RMD in the financial services industry. This is developed as a way of structuring the findings

such that relationships which the REs and RCs have identified can be seen. It is not an analytical model showing definite causality, but rather a diagrammatic representation of my interpretation of what I heard during the research presented in a logical manner to support wider understanding of this area and aid the discussion which follows. Whetten noted that diagrams of this nature are useful “as visual aid(s) that helps storytellers highlight the main features of their explanations” (2002: 50). In this context, the lines and directional arrows shown in the model indicate relationships believed to exist by the actors themselves with the interrelationships shown being drawn from my interpretation of their accounts. The model presented is by definition exploratory in nature and should be considered academically as ongoing work available for others to test some of the hypotheses that the descriptive model suggests.

The findings outlined earlier highlight the significance of the industry norm on the final reward mix position taken by the firm. The framework developed from the RC interviews in chapter four (Figure 4-1) focused on the influences of market forces, in particular what were described as labour market influences, on the overall industry norm position, moderated only by specific legal, tax and regulatory requirements that may be present. The data from the interviews with the REs provided greater clarity over what, at least in the financial services sector, is meant by market forces and the importance of employee expectations as the primary influence on the industry norm reward mix. Employee expectations were seen by both REs and RCs as being the reason why benchmarking of market reward mix was so significant as there was a general belief that adopting a reward mix position away from the established norm would not be consistent with expectations employees have and therefore would cause problems with regard to attraction and retention. This was even raised as being the case

when the differentiation from the benchmark position was intended to make the overall reward mix more advantageous for employees.

This relationship is represented in the first stage of a model of industry reward mix norm development shown in Figure 6-1 with the arrow showing the direction of influences found in the accounts that were heard.

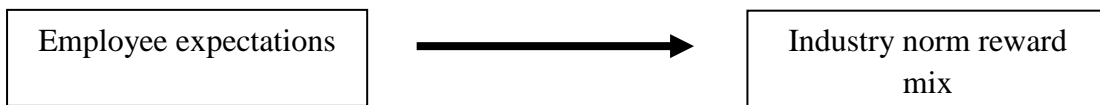


Figure 6-1 – First stage industry norm reward mix model

Employee expectations are seen to both influence, and be influenced by, union representation, when this is present in firms. The addition of the union influence on the industry norm reward mix is shown below.

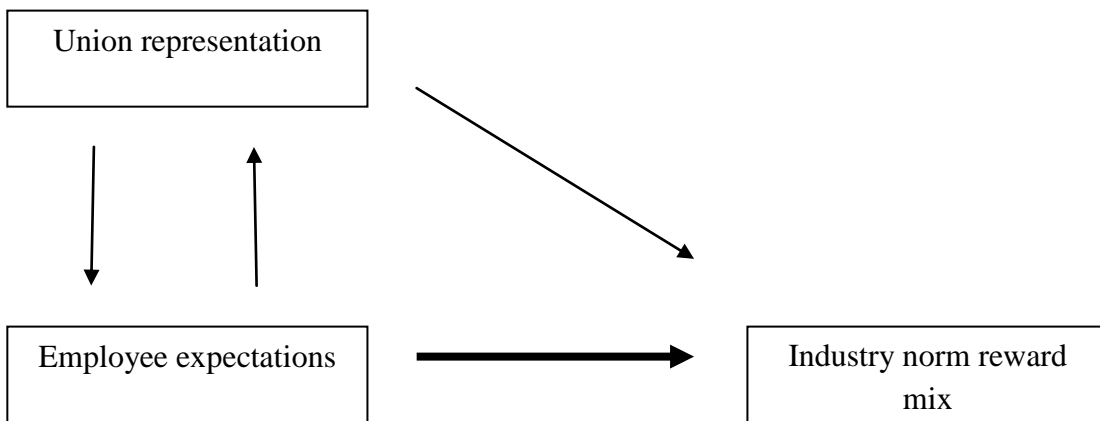


Figure 6-2 – Second stage industry norm model

Employee expectations (and those of their unions where present) were believed to be driven by strong historical reward patterns formed over several decades which were strongly engrained in employees' expectations and therefore were seen as being particularly difficult to change. These patterns were seen to have been formed by a

combination of two factors. First, the interviews identified that the general structure and profitability of the financial services sector, i.e. product market effects, had led to the formation of a sense of entitlement amongst employees with respect to the sharing of wealth created in the industry between the owners of the firms and employees. Second, owner beliefs about the role of reward structures were significant in forming historical reward patterns and, through this, influencing employee expectations over time – in particular, the role played by incentive and bonus schemes in motivating employee behaviour and benefits, and the responsibility firms felt for the welfare of their employees both for paternalistic reasons, and with respect to their search for productivity and engagement effects. This is shown diagrammatically below.

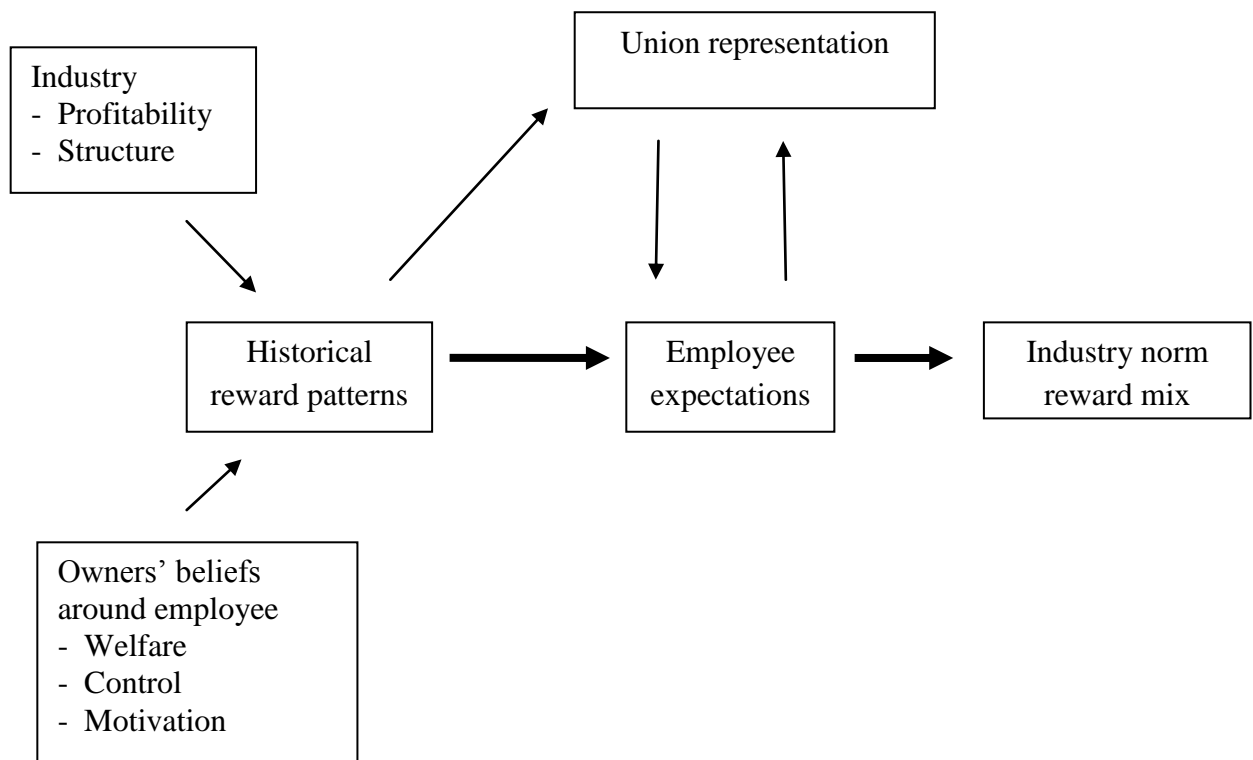


Figure 6-3 – Third stage industry norm model

Finally, the interviewees identified that employee expectations, although the main determinant of the industry norm position, were not acting unfettered on the benchmark position. Three key moderating variables were present, affecting the transmission of these strong employee expectations through to the final industry norm: the influence of legal, taxation and regulatory requirements on remuneration structures. These are shown in the final model of industry norm determination – Figure 6-4.

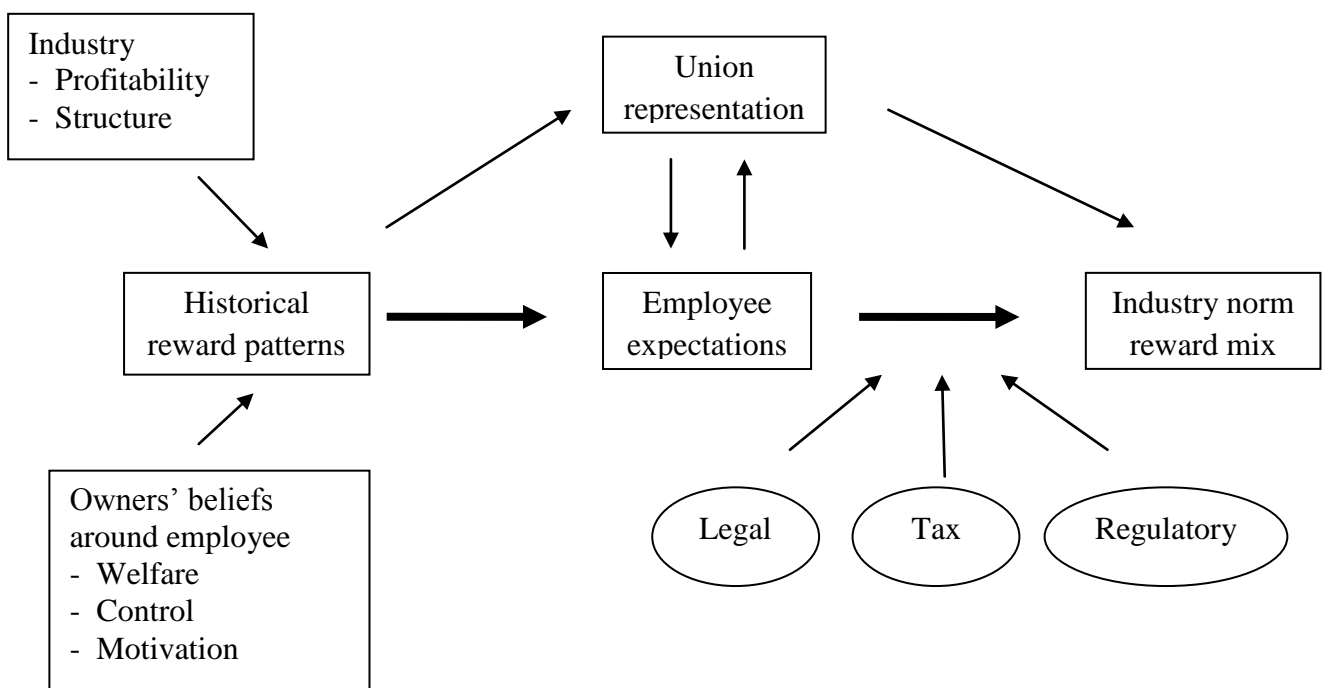


Figure 6-4 – Final model of the development of an industry norm

This industry norm reward mix was seen by the interviewees as the starting point for firms' RMD. However, the research found that not all firms adopted the industry norm or benchmark position. The next section will discuss the factors that the interviews identified as influencing the propensity of firms to follow the norm position or operate an alternative reward mix.

6.3 A model of firm reward mix determination

The interviews, with both RCs and REs, identified that there were risks associated with diverging from the industry norm reward mix with respect to the effect this may have on the ability of firms to attract and retain employees due to the strong employee expectations that had built up over a prolonged period of time (Note: this was even felt to exist when the changes to mix were believed to be positive for employees). In chapter five we saw that the extent to which firms were willing to take a risk and operate outside the perceived 'safe harbour' of the industry norm position appeared to be formed through the interplay of two variables. First, the firm's *desire* to resist the industry norm and differentiate its reward mix which was seen as being influenced by the following five dimensions:

- **Leadership** – The appetite of the leadership to adopt reward mix positions that differentiated the reward offering to employees from firms competing for the same labour.
- **Business strategy** – Specific and unique positioning with respect to each firm's product and customer management strategies.
- **Political pressure** – Exerted on the specific firm rather than the market as a whole. The strength of this influence was further dependent on the extent to which the firm in question was subject to State control through participation in some form of Government support following the financial crisis.
- **Parental influence** – For those operating as subsidiaries of overseas firms, specific parental requirements with regard to the reward mix that were not necessarily in line with the industry norm reward mix in the UK.
- **Firm-specific history** – The influence of enduring historical, but firm-specific,

positions and precedents.

These five dimensions could be further categorised into desires driven from within the firm through leadership, business strategy formation and firm-specific history, and coercive externally driven desires generated for the firm by others shown by either direct political pressure or parental dictum. This distinction is significant in that it helps identify what actions the firm can take to manipulate the dimensions itself (i.e. those from within) and which it was simply a matter of reacting to (i.e. external pressures).

Second, operating alongside the firm's desire to operate to some degree away from the established industry norm was the firm's *capability* to resist the institutional pressures formed in the industry norm. This was influenced by two dimensions:

- *HR capability and capacity* – To manage any change from the industry norm position and the potential implications this may have for attraction and retention of employees holding industry norm expectations with respect to their reward mix.
- *Line management capability* – The findings identified that managing employee expectations could not come solely from the HR function but were dependent on line management understanding and supporting the messages in their daily interaction within their teams. Therefore the capability of line management to work with HR in managing and communicating differences to the industry norm to their teams, and managing any implications, was important in adopting a non conforming reward mix position.

In addition, one further dimension was seen in the findings to influence both the firm's desire to resist the institutional pressure to conform to the industry norm, and also the firm's capability to resist this pressure – opportunity.

- **Opportunity** – The presence of an opportunity, both to act as a catalyst for change and therefore influence the firm's desire, and also a justification, largely to employees, of the need for a differentiated approach relative to the norm and therefore influence the firm's capability to change. These events were found to be firm-specific financial crises, regulatory pressure and mergers/takeovers.

The presence of these variables had the effect of weakening the strength of the relationship between the industry norm and the reward mix actually deployed by the firm. This base relationship is shown as:



Figure 6-5 – First stage firm reward mix model

The model is then completed by the addition of the desire and capability moderating variables discussed above – see Figure 6-6.

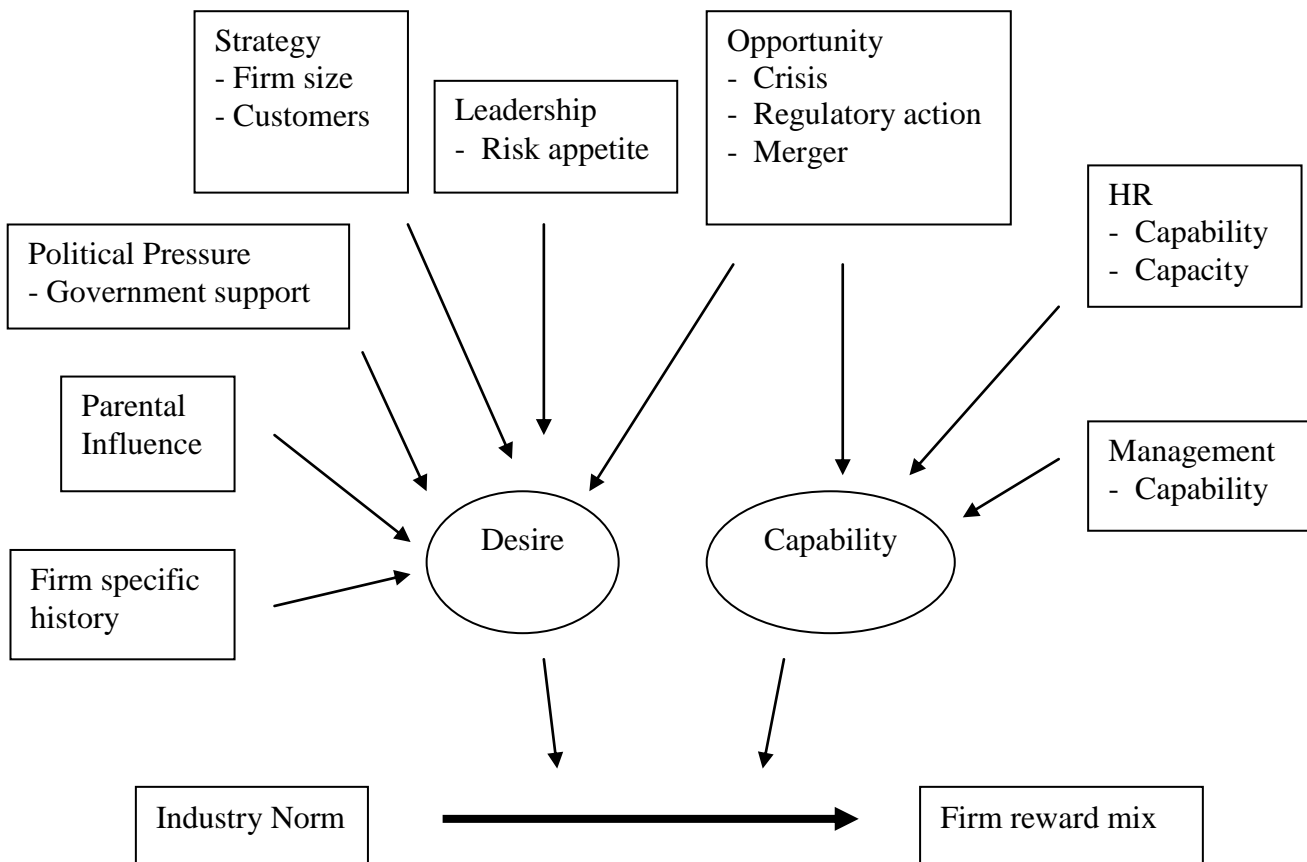


Figure 6-6 - Model of firm reward mix determination

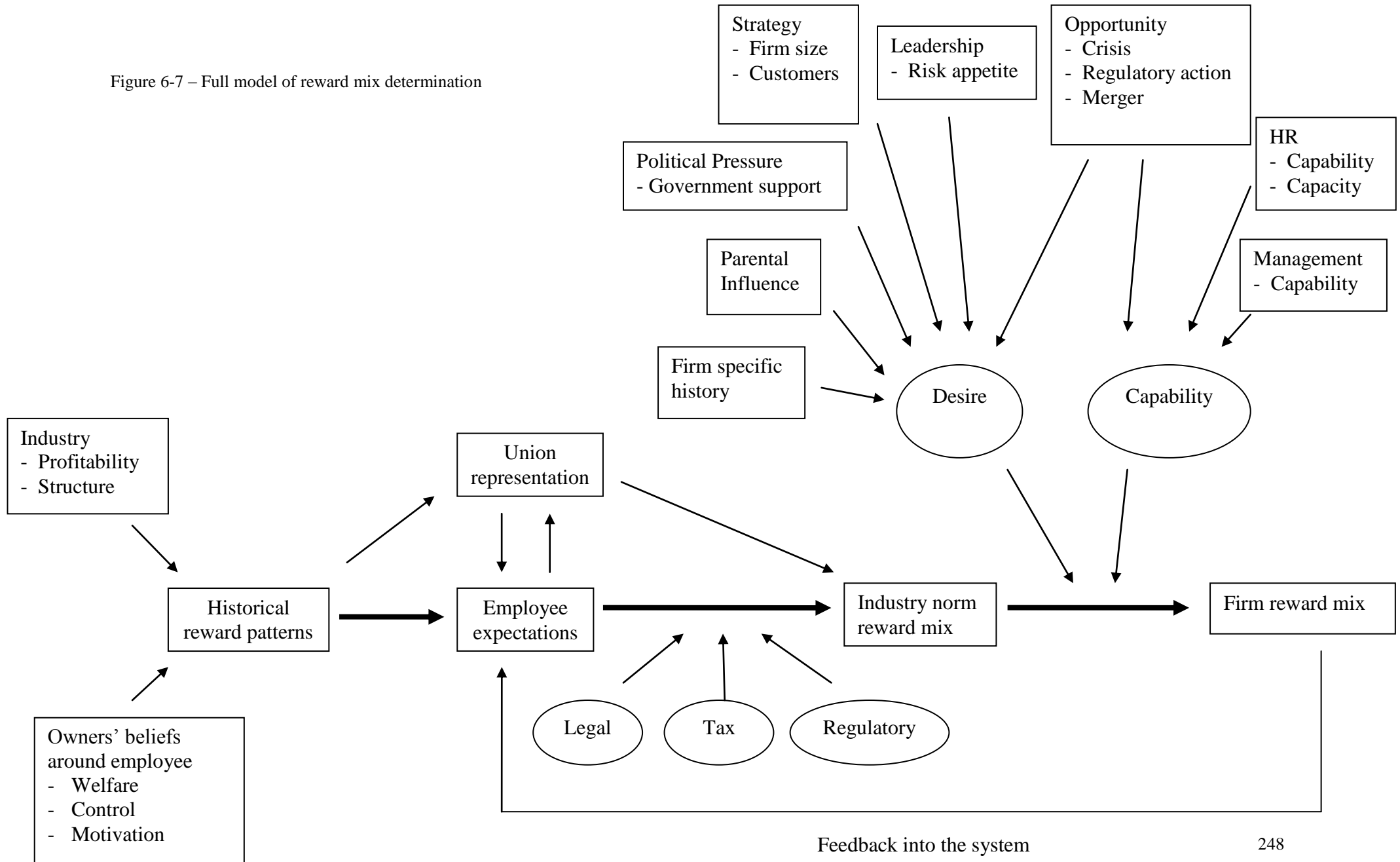
6.4 Overall model of reward mix determination

In chapter two I developed a conceptual framework from the academic literature on RMD (Figure 2-1). In chapter four this was then developed through interviews with RCs into an initial descriptive model of RMD (Figure 4-1). Finally, in this chapter, with further reference to the findings from interviews with REs currently working in the financial services industry, this has been developed into an overall model of RMD. In section 6.2 I developed from the findings a model of industry norm reward mix development and in section 6.3 a model of firm RMD. These can now be combined to

form a complete model of RMD, in the context of the financial services sector – see Figure 6-7.

The final model also incorporates a feedback loop. What emerged from the interviews was that the model was not a static one. A feedback loop was present between the individual firm reward mix and employee expectations. Where firms did diverge from industry practice this would eventually be communicated back into the wider labour market. The extent to which this feedback loop was influential was seen as being influenced by the size of the firm, with larger firms being seen as more significant in moving general employee expectations when they did diverge from the industry norm position. This is incorporated into the final model shown in Figure 6-7.

Figure 6-7 – Full model of reward mix determination



This chapter will now examine the insights from the model developed through positioning the discussion in the context of the reward mix literature discussed in chapter two and in particular the theoretical approaches found to explain mix decisions found in the literature.

6.5 Implications for the theoretical understanding of reward mix determination

6.5.1 Theoretical perspectives

In chapter two we saw that although RMD research has been carried out there is still no one paradigm emerging from the work (Gerhart and Rynes, 2003). This may be because the determination of mix is inherently complex, or that the list of factors that statistical work has identified as being related to RMD has muddied the field and we need to develop a framework to better understand these multiple influences. Gerhart and Milkovich (1992) noted that we should be looking to adapt the range of theories that have emerged to improve our knowledge of reward systems. In this context the literature suggested that three theoretical explanations for how firms determine their reward mix were worth exploring further:

- Agency theory
 - To manage potential misalignment between principals and agents.
 - Reward mix is intended to minimise shirking when monitoring is difficult/costly. Relative weight of incentives versus fixed reward will be managed to optimise the alignment of agents' and principals' interests.
- Institutional theory

- That coercive, mimetic and normative institutional forces create significant pressures on firms to be similar in how they operate in their search for legitimacy.
- Reward mix will be influenced by other organisations and market practice to gain legitimacy. The extent to which these constraints operate for each firm will influence how much freedom of choice the firm actually has in its operation.
- Resource dependency theory
 - Organisational decisions are strongly influenced by those controlling ‘critical resources’.
 - Reward mix will be influenced by the relative strength of employee groups determined by their criticality to organisation success.

In this section I will discuss the model of RMD developed above within these theoretical perspectives and comment on how the insights that the model provides support, refine and add to what we know already about RMD through these perspectives.

6.5.1.1 Agency theory

Agency theory demonstrates how reward mix can be used to attempt to align employee and employers interests as it is felt that “Paying individuals to do X causes them to do X” (Prendergast, 1999: 11). However, the literature identifies that a number of barriers exist to managing reward mix in this way. First, the additional cost employers are seen to incur when managing mix in this manner, as employees require compensating for the higher risk that variable pay implies given the relative uncertainty of payment which exists (Tremblay et al. 2003). Further, the theory proposes that the extent to which it is

rational to pay this additional cost, or risk premium, depends on whether roles can be monitored easily by the management team to ensure that workers are not shirking from their responsibilities and how much this monitoring costs, compared to the extra reward payments which are required due to the risk premium payable (Eisenhardt, 1989a) .

6.5.1.1.1 Control, attraction, retention

The agency prescriptions around aligning employees with the financial interests of the shareholders were a relevant consideration discovered in the research, although not the dominant issue in RMD as is perhaps suggested by the volume of research carried out under this theoretical perspective. This result is perhaps surprising, given that the financial services sector is characterised by relatively high proportions of reward being paid through bonus, which is consistent with an agency consideration of using reward mix of this type to control and direct employees' behaviour (Gomez-Mejia and Balkin, 1992; Delvey, 1999). REs' accounts showed that they believed organisational success was aligned with employee reward during the period before the financial crisis when firm returns were relatively high and alignment therefore provided high levels of reward for employees as they took their 'share' of the revenues generated. However, with the financial crisis, this relationship has been seen to break down with REs noting that aligning employees' financial interests directly with the firm's shareholders was fine in theory, but that their organisations had not seen this through to its full and logical conclusion of zero bonuses when losses were recorded, for fear of significantly demotivating employees.

What emerged was that reward mix was not used to control employee behaviour, through, for example, minimising employee shirking, as proposed by agency theorists. Thus the risk premium that theory suggests is paid when using variable performance-

related rewards such as bonus schemes (Tremblay et al. 2003) was excessive as it was not withdrawn when performance outcomes for the firms were relatively poor as was seen for all the firms of which the REs spoke.

Much more significant were the considerations of attraction and retention. Throughout the accounts, the proportion of incentives in the mix was justified, not with reference to the prescriptions of agency theory, but rather the need to avoid changing the mix away from the strong employee expectations that were present in the financial services sector for fear of causing attraction and retention issues for the firm. This did not mean that the proportion of variable pay in the overall mix would not have an influence on those currently employed by the organisation through incentive effects, but this was, at best, a secondary consideration. This was apparent for the two mould breaking firms identified in the research. The RE from the investment bank (RE18) noted that his firm was explicitly resisting the coercive changes in the mix being made by the financial regulator in order to have a more attractive package than their competitors and, through this, they were actively looking to recruit from other investment banks that were seen to be constrained, or in financial difficulties, and therefore unable to resist the constraints. The RE from the second mould breaker (RE2) outlined how her firm faced some retention difficulties, when it dramatically increased the proportion of fixed reward at the expense of variable pay. This was initially seen as unattractive to employees simply because it was different from what was seen in the wealth management / advisory market from which they recruited. Employees still expected a bonus, even when their fixed reward had been increased to compensate for its removal. This behaviour can be examined in relation to one of the assumptions of agency theory – rationality. Agency theory assumes that all parties to the economic exchange operate rationally (Eisenhardt,

1989a). However, the findings show that the REs did not believe that employees had the level of sophistication and understanding of their reward in order to operate in this theoretically rational way. An alternative explanation may be that employees were acting rationally, but were exercising poor judgement regarding the best economic outcome for themselves.

Theory proposes that the shift of reward from variable to fixed pay, and therefore guaranteed, is theoretically a more favourable position for employees as risk to their income stream had been removed (Lazear, 1986; 1999). However, RE2 explained that when they increased the certainty in the package in this way a number of employees still felt the need to leave the firm for the more established reward mix that continued to be offered by their 'market following' competitors. This was consistent with the overall strength of employee expectations that was discussed by both RCs and REs and how this dominated RMD. Historical reward patterns were stronger than the suggested theoretically rational assessment of the optimal position – again, suggesting that poor judgement was being exercised by employees regarding the optimum position, economically, to adopt.

Additionally, the findings showed that a number of REs cautioned how too high a reliance on incentives to align or control behaviour and incentivise employee performance could lead to a misalignment of employee/employer interests. Two explanations are offered. First, the damage that aligning interests in such an economic exchange may encourage short-term behaviour which, although bringing positive results in the short-term, were not in the longer term interests of the firm. The need to consider time horizons when considering the role of mix in incentivising behaviour was seen as

important at this point in time for the financial services industry, given the consensus, at least among regulators and politicians if not all practitioners, that the reward mix had encouraged excessive short-term risk taking that was not in the interests of the long-term sustainability of firms (McCarthy, 2008; Darling, 2008; Financial Times, 2008; Institute of International Finance, 2009; FSA, 2009b; Chapman, 2009).

In addition, over-reliance on variable reward as a control and directing mechanism was potentially seen as being counterproductive due to the possible effects this approach might have on employee welfare through creating an environment of pressure and stress which may lead to lower levels of performance.

These concerns with the role of incentives in aligning behaviour led to the development of an alternative perspective on the role of mix in aligning interests between employer and employee which will be discussed next.

6.5.1.1.2 A more holistic alignment of interests

What emerged from the research was that the RCs and the REs did see a role for reward mix in aligning employer and employee interests. However, this was not solely through the use of incentives to control behaviour, but rather a more holistic desire to look at employee needs within the whole package and evaluate how best to meet those needs in the belief that this would lead to higher commitment, productivity and performance. The participants generally believed that the provision of a package which met employee needs through market competitive base pay, a bonus reflecting recognition of their contribution to organisational success (as opposed to reward for compliant behaviour), benefits that supported their welfare and provided protection against unforeseen events and wider relational factors such as respect of their home life, would lead to higher

performing individuals through engendering higher levels of commitment and performance. Aligning employee behaviours through reward was important, but was not conceived as narrowly as proposed in the agency control and monitoring manner.

This could be seen in the discussion surrounding why organisations provided employee benefits such as medical and health-related support. Provision of these employee benefits was not with some altruistic intention, which many noted was their understanding of the origin of a number of employee benefits, but rather a business-focused approach whereby ensuring that employees remain fit or recover quickly from illness or injury through the provision of health-related support was in both employees' and employers' interests. The alignment of employees' and owners' interests was seen as important but was not viewed as narrowly as currently suggested by the economics-based literature within which agency theory is found. A true, more balanced, alignment of interests was what was being sought, not one based on assumptions of shirking, control and monitoring. A refined agency theory may be required to account for this perspective.

6.5.1.1.3 Conclusions

Overall, significant questions are raised about the applicability of pure agency theory as an explanation of RMD, supporting the conclusions of Eisenhardt (1988), Conlon and Parks (1990), Deckop et al. (1999) and Fernandez-Alles et al. (2006) that, on their own, the theoretical prescriptions of an agency approach to reward mix are found wanting. In particular, the fundamental assumptions of rational employees whose interests are different from their employers' are disputed, as firms take a more holistic, broader approach to RMD than is suggested by agency theory, in the belief that productivity and commitment is raised through ensuring that employees share in the success of the

organisation (but not necessarily the failure) through bonus schemes, and are protected through a range of benefit offerings. This is not, as perhaps was the case historically when benefit packages were first introduced, due to paternalistic considerations by the firm, but rather a rational assessment of the attraction, retention and commitment benefits of operating reward mix in this way.

The explanation for why these elements of agency theory need developing was that a wider perspective is taken on the reward mix with the need to create an overall package that both attracts and retains staff by meeting strong expectations of what the mix should look like, supports their well-being and health to ensure that they can remain productive at work as well as enjoy their home life, and creates commitment to the company through meeting a variety of their needs through reward. This approach was seen as a more powerful way of encouraging behaviour that was in line with the principal's interests. This explanation contradicts the media / popular opinion present at that time with respect to financial services reward with its focus on monetary gain alone amongst those working in the sector. This suggests that it is perhaps time to develop the economic perspective of agency theory and adopt a wider perspective on employee alignment taking into account the need through all the elements of reward mix to align employees' behaviour through building commitment and engagement not just by controlling and managing shirking.

Based on the discussion of the findings of this research presented above, the contribution of this research to our understanding of RMD from an agency theory perspective is summarised in Table 6-1. This shows how the findings either support, refine or add to theoretical explanation, and summarises how the findings achieve this.

	Agency	This research
Purpose of reward mix decisions	To control and direct behaviour towards the objectives of the principal especially when monitoring is difficult/costly	Refined. Reward mix not seen solely as a device to control employees. Alignment of interests between employees and employers is important but with a view to gaining commitment and higher performance rather than directly controlling behaviour.
Main Assumptions	<p>Rational decision</p> <p>People are self interested, risk averse</p> <p>Goal conflict exists between owners and employees</p> <p>Information asymmetry</p>	<p>Refined with respect to employees. Employees are seen to be concerned with protecting the historically informed reward mix position, despite the fact that other mixes potentially offer higher levels of utility (e.g. higher levels of fixed reward).</p> <p>Partially supported. Employers are seen as relatively risk averse due to their lack of desire and/or ability to break the strong institutional norm position in place.</p> <p>Refined. Whilst conflicts may still exist, there was also the potential for alignment of interests, especially through benefit provision, which can often be used to meet congruent goals of both employees and employers (e.g. employee welfare).</p> <p>Not raised in the interview accounts.</p>
Organisational reaction	Rational active management	Supported. Rational active management but with different outlook.
Implications for reward mix	Relative weight of incentives versus fixed reward will be managed to optimise the alignment of agents' and principals' interests	Refined. Reward mix is deployed in order to meet strong employee expectations and, through this, secure their commitment and performance in line with the principal's interests.

Table 6-1 - Research contribution to our understanding of RMD from an agency theory perspective

Consequently, the results from this study support the call that we should extend our investigation of RMD beyond an agency perspective. A pure agency-based approach appears to overestimate both efficiency and rational drivers of decision making in reward mix choice, and underestimates the institutional and political power-related pressures that may be relevant to organisations (Barringer and Milkovich, 1998; Bartol and Locke, 2000). Furthermore, the weaknesses of agency theory's narrow conceptualisation of reward mix have been highlighted, with firms generally having a wider consideration of what reward mix means to them and how this influences employee alignment. In this context an institutional perspective will now be examined.

6.5.1.2 Institutional theory

Institutional theory suggests that coercive, mimetic and normative institutional forces create significant pressures on firms to be similar in how they operate in their search for legitimacy. The extent to which these constraints operate for each firm influences how much freedom of choice the firm actually has in its operation (Gerhart and Rynes, 2003; Crystal, 1991; Carpenter and Wade, 2002; Treiman and Hartmann, 1981; Slichter et al., 1960). This theoretical perspective was well supported by the research and forms the core of the model of RMD developed and shown in Figure 6-7.

The model shows that the need for legitimacy was generally defined with respect to meeting expectations of employees, both current and prospective, as opposed to other stakeholders such as shareholders and government, and wider societal expectations. This is consistent with Suchman's definition of legitimacy as "a generalised perception or assumption that the actions of an entity are desirable, proper or appropriate within some socially constructed system of norms, values, beliefs and definitions" (1995: 574) with employee expectations being the socially constructed position.

DiMaggio and Powell (1991) identified three ways that isomorphism influences organisational decisions – coercive, mimetic and normative pressures. All three are, to varying degrees, seen in the research findings. Each of these will be discussed in turn in the context of the findings on RMD.

6.5.1.2.1 Coercive isomorphism

Coercive isomorphism results from the combination of both formal and informal pressures on organisations by other organisations on which they have some mutual dependency. The research found that the dominant industry norm reward mix position was established following the application of a number of coercive moderating pressures on employee expectations (Figure 6-4). The industry norm position was only weakly influenced by legal pressures. Much stronger were the coercive pressures, and through this the formation of a revised industry norm, coming from the operation of financial services regulators, who were particularly active at the time of the research in defining new rules for financial services rewards. The REs interviewed, with one exception, accepted the moderating shift that this regulatory coercive change had brought to the previously defined norm position. This was attributed to the regulators' power with respect to providing the licence that firms needed to operate in the financial services sector, and also over their profitability through their capital setting powers. This provides support to Pfeffer and Salancik's (2003) conclusion that, typically, politically driven coercive forces will be applied across the board and consequently are likely to restrict adaptability and flexibility across the sector. One of the mould breaking firms was an exception to this position, given its desire to resist the changes for attraction and retention reasons, and also its ability to do so because of its strong financial position and management desire to gain competitive advantage from the regulatory change. This is

in line with Oliver's (1991) contention that, whilst an extreme position to take, organisations may take a conscious decision to ignore regulatory requirements through a rational assessment of the consequences of such action. However, the research extends the application of this regulatory coercive pressure as the pressure was not only operating at a sectoral level, but was also significant (for those firms receiving some form of direct Government support at the time of the research) at an individual firm level as Government looked to impose certain restrictions on how they operate their reward mix.

Van der Stede (2003) and Roth and O'Donnell (1996) contended that a further source of coercive pressure was the presence of "intracorporate isomorphism" (Van der Stede, 2003: 268), reflecting the strong influence of parent companies on business unit policies including reward design. Significant evidence of this was found, with a range of parental requirements for subsidiaries and branches in place which meant these firms often found they were adopting a reward mix away from the UK industry norm position. This created considerable frustration for a number of the REs, given the limitation they believed it imposed on the reward mix at their firm. Whilst appearing efficient from the parent groups' perspective (specifically in relation to the use of variable pay and share related payments) it was often seen as out of line with the local market conditions and employee expectations in the UK financial services labour market. The research extends our understanding of this "intracorporate isomorphism", or at least its application within the financial services sector, given the explanation for its prevalence invariably being increased coercive regulatory and political pressure in the home market that is then applied across the globally active firms to host countries within which the firms operated, often irrespective of host country, industry norm, reward mix

conventions. This was particularly significant in the financial services sector as whilst regulators were seen as attempting to introduce similar remuneration regulations across national boundaries there were still seen to be material differences in regulations reflecting different national approaches to the topic.

Furthermore, our understanding of parental coercive pressures was further enhanced, given the research finding that parental pressures were not just coercive: with head office dictating policy as was the case for a number of share-related schemes and bonus policies which were mandated from head office, but also mimetic: with the business unit mimicking successful business unit or head office practices particularly with respect to avoiding extra design costs when a practice within the group was seen as being successful, or normative: adoption of a corporate template already available in the organisation which was raised with respect to operating reward administration more efficiently than would be the case if separate infrastructure was put in place in the subsidiary. The distinction that DiMaggio and Powell made between coercive, mimetic and normative isomorphic pressures was not clear-cut for parental isomorphism which crossed all three classifications. This is in line with Mizruchi and Fein's (1999) contention that there is much overlap in the categories, and many examples of isomorphism could be given alternative classifications.

6.5.1.2.2 Mimetic isomorphism

Mimetic isomorphism contends that organisations model their reward mix on that adopted by other organisations (Eisenhardt, 1988; Taras, 1997; Segalla et al., 2006). The research provides strong support for the existence of mimetic pressures in the financial services sector at this time. The default position, or starting point, in RMD was what other firms were doing. Operating at the industry norm was seen as a 'safe'

operating position, given it meant that the firm's reward mix approach was broadly in line with the vast majority of firms with whom it was competing. Although firms recognised that this meant they were not gaining competitive advantage through reward mix differentiation, they did identify that in turn they were not exposing the organisation to potential uncertainty which operating away from the norm was felt to present, especially regarding the strong, historically formed, expectations of employees seen in the research. A number of the interviewees saw this as a passive adoption of the practice of others, as generally expected in the institutional theory literature (Conlon and Parks, 1990; Fernandez-Alles et al., 2006). However, this was not always the case with a judgement of the risks of differentiation often leading to what was felt to be a rational decision to adopt the industry norm reward mix position. This is consistent with the findings of Norman et al. (2007), in their research on the airline sector, and Arrowsmith and Sisson (1999), in their work on the engineering, printing, health and retail sectors, and their contention that organisations look to avoid uncertainty and diverging from standard practice introduces a level of uncertainty in comparison to other organisations. The research showed that adoption of the industry norm position was not always passive, but rather was often a conscious consideration of the firm's risk appetite. Where differentiation from the norm was extensive, the risk appetite was higher with the gains expected from this level of differentiation outweighing the potential costs with respect to attraction and retention difficulties. Furthermore, the findings showed that there was a range within which differentiation was seen as relatively low risk (the position adopted by the cautious leaders) and was therefore the stance adopted by more organisations than the more radical mould breaking positions of a much smaller number of firms. This focus on risk was perhaps unsurprising given the

importance of risk management activities in the operating models of firms in the financial services sector.

Whilst the mimetic pressures were strong the research did not support a number of contentions that others have made with reference to the sources of mimetic behaviour. The research did not find that mimetic behaviour was driven by firms looking to model themselves on organisations that are seen to be successful, but rather found that isomorphic behaviour was more habitual. The symbolic and practical reliance on benchmarking activity was strong evidence of this habitual approach with all the RCs and REs interviewed, including the REs from the two mould breaking firms, identifying the significance of benchmarking data on shaping their reward strategy in some form. In addition, there was only limited evidence of consultants playing a significant role in diffusing practice across firms beyond their role in facilitating the sharing of reward data through their benchmarking services, which of course was a strong factor confirming the conclusions of Eisenhardt (1988) and Crystal (1991). They were not the powerful facilitators of isomorphic reward mix practice portrayed by Barkema and Gomez-Mejia (1998).

In addition, the research showed that only limited support can be given to Main et al.'s (2008) and Pfeffer and Salancik's (2003) conclusion that larger scale organisations were better able to resist mimetic pressures, through influence and financial strength, and therefore adopt practices more in line with their strategic goals. The two mould breakers were not large relative to the other firms that were studied, although one was exploiting its relative financial strength in adopting a contrarian reward mix stance. The propensity to fall into the cautious leader category did appear to have some relationship

to size, with a number of the REs working at very large banking conglomerates carrying out incremental innovation of their mix. However, as shown in chapter five, this was often attributed to size but moderated with caution led by concern over even large firms' ability to adopt a reward mix significantly away from that generally expected by employees. Size may have given the firm a desire to differentiate, but they were generally wary as to their capability to manage the change, especially with regard to managing employee relations.

Finally, the accounts of how both product market and owners' beliefs influenced the formation of employee expectations historically, as shown in figure 6.3, provides support to Tolbert and Zucker's (1983) contention that the influence of institutional pressure is lower, and other elements will drive decisions, in what they described as the pre-institutionalised phase of a sector. A number of the REs made clear links to the historical structure of the financial services industry, the overall profitability which this structure had generated and owners' beliefs, both with regard to motivating employees through relatively high proportions of variable pay and paternalistic tendencies through generous benefit packages. However, the sector was now considered firmly institutionalised and these historical factors reduced in significance. This provides support to the theoretical work of Wright and McMahan, in the context of all HR practices, which noted the possible influence of history, suggesting that "organisation practices can be institutionalised through an imprinting process whereby the practices adopted at the beginning of the organisation's history remain embedded in an organisation" (1992: 314). The research extends this theoretical explanation in this context, given the discovery that the practices which emerged in the sector many decades ago had become embedded, not just in individual organisational practice but

also employee expectations and sectoral practice, with new firms adopting the institutional position through mimetic practice.

6.5.1.2.3 Normative isomorphism

The evidence supporting the presence of normative isomorphism was weaker (especially in the accounts of the RCs) but nevertheless did exist. Normative pressures stem from the search for credibility, through professionalising the area of reward management which leads to the arrangement of practice into codified principles and accepted standards (Barringer and Milkovich, 1998). These practices are then spread through the networks of individuals leading reward decision within firms, i.e. the REs interviewed. Social networks were identified as existing amongst the reward practitioners both sectorally, through groups such as the Financial Services Reward Group, which has over 20 financial services firms as members, and the local HR gatherings in place for all the non London-based firms. However, these forums were less about codifying practice, but rather mimetically establishing what each was doing both qualitatively and, in some instances, through the sharing of reward data. No evidence was found to support another element of normative isomorphism – the codification of knowledge through qualifications, training programmes etc. No reference was made to the influence that training or qualifications had had on the behaviour, recommendations and actions of the REs. The finding that normative pressures were not influential can be explained in the context of the previous discussion of mimetic and coercive behaviour within this sector. The networking that was done was carried out with the aim of understanding more fully the practice of others to ensure that mimetic legitimacy could be gained with employees. The interviewees were conscious of the information flow that occurred across employees in the sector and

therefore the importance of staying fully aware of the practice of others who were recruiting from the same employment market.

6.5.1.2.4 Diverging from the industry norm

The research clearly finds that institutional pressures are strong – coercive, in influencing the industry norm, and mimetic, in explaining why firms adopt similar positions. It also identifies the significance of employee expectations in leading firms to follow the industry norm positions and the historical drivers of these expectations. However, the RMD model also shows a number of dimensions that influence the desire and capability of firms to operate away from the strongly entrenched industry norm position. These explain why the industry norm reward mix, whilst dominant, is not all-pervasive in determining reward mix practice.

6.5.1.2.5 Risk appetite

The research showed that the organisation's risk appetite was important in determining the extent to which it would diverge from the industry norm position. A number of firms found that they had both the desire and capability to adopt a reward mix away from the industry norm position. Sanders and Tuschke termed these “institutionally contested practices”, and defined them specifically as “new organizational practices that face stiff opposition from key constituents in potential adopters’ primary institutional environment” (2007: 34). This research identified one particularly strong ‘key constituent’: employees and the influence their expectations were having both on the norm reward mix in place and the inertia that was present within firms to move away from this position. Sanders and Tuschke (2007) identified four processes that facilitated the spread of a non conforming position (and perhaps creating a new norm position): exposure to other institutional contexts where the practice is considered legitimate, CEO

education, organisational learning and regulatory/legislative change. The first – exposure to other institutional contexts where the practice is considered legitimate – was found in one of the mould breakers with its reward mix more aligned with that operating in the professional services sector (e.g. legal and accounting professions) than the financial advisory sector in which they operated. This firm’s RE described how the firm prided itself in the way it was willing to look beyond its current setting and draw from others. The role that CEO education and background played in influencing divergence from the norm position was not found, neither was organisational learning (although the financial crisis was causing some reflection on the appropriate reward mix, but in the context of regulatory pressure, rather than an internal learning process). However, regulatory legitimisation was identified as one of the key drivers of firm-specific divergences from the current reward mix norm. What was not yet clear was whether this regulatory pressure would “open the floodgates” (Sanders and Tuschke, 2007: 207) to what were previously seen as contested practices, such as lower levels of variable pay, increased deferment of bonuses and the elimination of bonus guarantees for which the regulator was pushing hard.

The explanation as to why the industry norm reward mix was so pervasive was ultimately one of a firm’s risk appetite for differentiation. This risk appetite was found to be formed through assessment of the gains expected to accrue from the adoption of a non standard position, with respect to, say, productivity increases or improved attraction of certain staff against the cost accruing from the potential accompanying loss of legitimacy with current and future employees. This supports the conclusions of both Meyer and Rowan (1991) and Sanders and Tuschke (2007) that a sustained competitive advantage by differentiation of this nature will be dependent on the ratio of benefit to

cost. However, the research extends their work by providing the dimensions against which an assessment of these cost and benefits would be made, i.e. the drivers of firm desire and capability for differentiation.

Overall, what the research showed was that small levels of divergence from the institutionally established norm were often considered acceptable as they were seen to bring higher benefits than costs. However the interviewees' accounts provided evidence that firms were nervous about larger deviations from established norms due to the perception that this would have negative consequences for attraction and retention of employees with strong industry-defined reward mix expectations. Consequently, firms may have some flexibility about their reward mix and be able to differentiate their overall reward package, but the extent of differentiation was seen as constrained by the institutional pressures that have been discussed. This adds further support to the conclusions of Deephouse (1999) and Norman et al. (2007) that a more rational form of institutional behaviour was present with mimetic positions adopted through conscious thought, rather than the passive conformity suggested by many.

6.5.1.2.6 Conclusions

The research supports the literature in that it shows that institutional pressures do exist, and are influential. However, the study extends the understanding we have of these isomorphic tendencies in RMD within the financial services sector. Isomorphic pressures generally were not found to be automatically and uniformly followed, with non industry norm positions of different degrees being adopted by firms dependent on the extent to which they have both the desire and capability to break from the employee expectations that so heavily influence the mix. The source of the power of these employee expectations is explored further in section 6.5.1.3 in the context of the

literature on resource dependency.

Based on the discussion above, the contribution of this research to our understanding of RMD from an institutional perspective is presented in Table 6-2. This shows how the findings either support, refine or add to theoretical explanation and summarises how the findings achieve this.

	Institutional	Contribution of this research
Purpose of reward mix decisions	Conformity with other organisations and market practice to gain legitimacy	Add. Conformity with other organisations and market practice is important but the legitimacy being sought is with respect to current and prospective employees.
Main Assumptions	<p>Organisations seek legitimacy</p> <p>Organisations conform to norms</p> <p>Process of satisficing behaviour</p>	<p>Supported.</p> <p>Refined. Generally interviewees saw how firms look to conform but where the desire to differentiate and the capability to manage the differentiation was strong the interviewees believed that firms were able to break free from the norm position.</p> <p>Supported. Many REs recognised that the industry norm position was potentially not optimal for their firm but recognised it was better than operating a mix away from the norm given the risks this implied with respect to employee attraction and retention.</p>
Organisational reaction	Passive conformity or rational legitimacy seeking	Supported. Both types of behaviour were seen. Some REs outlined how their firms passively conformed to the industry norm position, whilst others rationally conformed through risk assessment of options around non conformance.
Implications for reward mix	Reward mix will be influenced by institutional norms and the extent to which operating within these norms confers legitimacy	Add. Reward mix will be influenced by institutional norms and the extent to which operating within these norms confers legitimacy with current and future employees.

Table 6-2 - Research contribution to our understanding of RMD from an institutional theory perspective

6.5.1.3 Resource dependency

A resource dependency approach states that organisational reward mix decisions are strongly influenced by those controlling what are termed ‘critical resources’, where resources are deemed critical if their loss causes the organisation to cease operation or face material disruption (Pfeffer and Davis-Blake, 1987; Balkin and Bannister, 1993; Yanadori and Marler, 2006). In contrast with most accounts of institutional theory, decisions are seen to be taken consciously with a view to actively managing the dependency in order to try and reduce it.

There was strong evidence of employees having significant influence over their reward mix, with REs noting that employees’ expectations were the primary driver of RMD. What was less clear was whether this was because all employees or just certain employee groups were deemed to be critical. The literature states that the extent to which a resource is deemed critical is influenced by the availability of substitutes for the resource. Both the RCs and REs noted the importance of their organisations attracting and retaining talent in order to ensure success. Furthermore, talent was seen as relatively scarce which, in turn, increased the dependence that the interviewees believed firms had on this talent.

Much of the resource dependency-related reward mix literature focuses on identifying which groups of employees are deemed as critical and therefore, through the power this is perceived to give them, are able to exert a strong influence on the reward mix that they receive. This has led much of the literature to focus on ‘special’ groups such as executives, salespersons, and research and development staff (Tremblay et al., 2003; Gomez-Mejia and Balkin, 1992). This research suggests that, at least within the financial services sector, there should be a broader focus on criticality of employees

beyond these 'special' groups and into the wider employee population. The findings showed that firms' assessment of which resources are critical, and therefore have power over the organisation, was not as specific as the segmentation previously applied in reward mix research. The accounts given suggested that influences on RMD applied across large groups of staff. Differentiating between groups of staff was less noticeable than might have been expected, given earlier research findings of the importance of the 'special' groups highlighted above. A general concern over the attraction and retention of all staff pervaded the discussions, with a desire to meet expectations (albeit sometimes different) for varying groups of staff. In addition, a cascading effect was noted with policies put in place to secure critical talent, such as relatively large bonuses or generous benefit arrangements, cascading through the organisation with, to some degree, all employees benefitting from the reward mix approach designed for the 'critical' employees. This was in line with the predictions of equity theory, with REs attempting to ensure the generosity of the packages their firms provided to certain groups of employees, both with respect to bonuses and benefit provision, did not comprise general perceptions of fairness across the firm.

The focus on employees as critical resources, given their significance in the revenue generating process in the financial services sector, was unsurprising. In addition, unions with their role in bringing together employee voice to greater effect and their influence over the supply of labour, were identified as being a dependency that required managing with respect to their influence, especially around the role variable pay (Arrowsmith and Marginson, 2011) and benefits played in the mix (Budd, 2004; Freeman and Medoff, 1981). The study did not support earlier findings that the management of perceived resource dependency was a strategically conscious response as opposed to firms simply

complying with isomorphic pressures (Oliver, 1991). Typically RCs and REs did not give accounts that showed a depth of analysis over areas determining how dependent a firm is on employee groups, such as the autonomy and complexity of roles, but rather referred to wider concerns over retaining and recruiting individuals. This contradicts both the findings of Crystal (1991) and Eisenhardt (1988) who contended that what set resource dependency apart from institutional theory was how organisations respond to coercive pressures. They reported that a resource dependency perspective was a more autonomous or strategically conscious response, compared to the more automatic and unconscious response of institutional theory. As we have seen, for many financial services firms, institutionally motivated behaviour was carried out through a conscious consideration of the risks implied by differentiation, including consideration of resource dependencies. In this context, this suggests that resource dependency is not a separate explanation of RMD but rather a component of the extended institutional theory discussed in section 6.5.1.2. This will be explored further in section 6.5.3.

Furthermore, evidence was only found to support two of Bartol and Martin's (1988) seven factors that influence the level of dependence an organisation has on an employee, or group of employees. Whilst concern was raised about the specialist nature of financial services roles and the replaceability of employee skills, given skills shortages in this sector, no support was provided from the RC nor the RE accounts for the other factors raised in their research, namely task uncertainty, ability to clearly monitor performance, performance visibility, task centrality and organisational connections. This supports the work of Elvira (2001), also conducted in the financial services sector, that reward mix was generally seen as being significant in managing attraction and retention, rather than detailed considerations of specific dependency

factors. The research found no evidence that REs acting for their firms applied the analytical level of sophistication implied by the seven factors identified in Bartol and Locke's (2000) work.

Moreover, the contention of Balkin and Bannister (1993) that 'powerful groups' would be able to determine their own mix, with the organisation overlooking other reward issues, such as internal and external equity with other groups of staff on whom the organisation is less dependent, was not supported. As already noted, the interviews showed evidence of a cascading effect of reward mix with the overall philosophy around fixed and variable pay and the role of benefits being widespread, even if the magnitude of reward (i.e. overall level) were less so.

6.5.1.3.1 Conclusions

The research shows that whilst dependence on employees was important it was not, as envisaged by resource dependency, a discernible focus on critical groups. Of greater concern to the REs was the attraction and retention of employees across the workforce, and therefore the need for the reward mix to conform to industry norms in order to meet employees' expectations.

Based on the discussion above, the contribution of this research to our understanding of RMD from a resource dependency perspective is presented in Table 6-3. This shows how the findings either support, refine or add to the theoretical explanation and summarises how the findings achieve this.

	Resource Dependence	Contribution of this research
Purpose of reward mix decisions	Acquisition of business critical resources	Refined. Differentiation between employee groups as critical and non critical is not as discerning as implied in resource dependency theory. Concern is over the attraction and retention of employees generally.
Main Assumptions	Rational decision Control of critical resources leads to power	Supported. Rational decision. Add. Employees have power with respect to the overall importance they have in the business models of financial services firms.
Organisational reaction	Rational active management	Refined. Decision to adopt industry norm position generally taken with reference to rational considerations of attraction and retention.
Implications for reward mix	Reward mix will be influenced by the relative strength of employee groups determined by their criticality to organisation success	Refined. Attraction and retention issues were present across the workforce, therefore were not solely influenced by relative strengths of employee groups, rather the overall strength of employee expectations.

Table 6-3 - Research contribution to our understanding of RMD from an resource dependency theory perspective

6.5.1.4 Other theoretical perspectives

The research identified two other aspects of theoretical considerations that are now discussed in the light of the empirical research.

6.5.1.4.1 Path dependency

The model developed through the research shows that institutional factors are seen to be endemic in RMD. In this context it is not surprising that path dependency emerges from the accounts provided, given its similarities to institutional theory (Scott, 2008). The

research identified that the initial starting point, i.e. the current organisational reward mix, is often key with adjustment of this position, or anchor, the route taken to change rather than a ‘blank sheet of paper’ review. This is consistent with a path dependency explanation that a policy develops in such a way that it is difficult to change the direction the policy has taken (perhaps, for example, the prevalence of high proportions of variable pay in financial services reward mix) even when alternatives would, from a standing start, produce ‘better’ solutions (Scott, 2008).

Path dependency theory has typically been applied to technological developments, e.g. the development of the QWERTY keyboard (David, 1985), given the high set-up costs which are typically a barrier to change in that sector. However, North (1990) contends that it applies to wider institutional change, given that the conditions supporting path dependency (other than high set-up costs) are learning effects (i.e. when time and effort are invested in a particular situation then there will be a reluctance to change), adaptive expectations (i.e. latecomers see a widely adopted practice and are therefore more likely to adopt the practice) and what Scott called the “primacy of early events” (2008: 122), namely early decisions creating a defined direction. At an individual firm level, the findings of this research support the existence of learning effects and the primacy of early events, with both identified as explanations for the strength of the institutional norm and how the norm was established historically. However, this was not a strong influence consistent with the findings of Arrowsmith et al. (2010) who noted that, although still present, path dependency was a fading influence.

6.5.1.4.2 Strategic compensation

The findings did find evidence to support Gerhart and Milkovich (1990) and Baker et al. (1988) in their conclusion that industry characteristics such as product demand will

influence reward mix. This was not operating at an individual firm level, but in concert across the sector via the role these factors played in forming the industry norm through their effect on employee expectations. In addition, the extent to which firms then follow that norm was in a number of cases seen to be influenced by the firm's specific business strategy as predicted by Gomez-Mejia and Balkin (1992) and Rajagopalan (1997).

What was not apparent was a direct association, by those interviewed, to the specific factors that earlier research had shown were directly related to reward mix, such as product diversification (Gomez-Mejia, 1992; Kerr, 1985) and company life stage (Chen and Hsieh, 2005). Relationships between these variables and reward mix may have been proven by earlier statistical work, but dialogue with those involved showed these were generally not conscious relationships that they raised.

Furthermore, at an individual firm level the results provided support and further explanation on Stroh et al.'s (1996) conclusion that the level of turbulence an organisation is facing, perhaps brought about by restructuring or downsizing, would also influence reward mix. The interviews showed that this turbulence was used opportunistically by firms to create both the desire and improved capability of the firm to move, albeit often marginally, away from the defined industry norm position.

In addition, Stroh et al. (1996) speculated that the use of variable pay was about transferring risk to employees using variable reward strategies to manage the additional variability in revenue and profitability that they are facing at this point in their history. However, what was seen in the research through taking a wider conceptualisation of mix, was that the transfer of risk was much more prevalent in benefit packages, with the shift from defined benefit to defined contribution benefits, than in management of the

narrow agency-based definitions of reward mix in cash compensation.

6.5.2 The significance of the context

6.5.2.1 Sectoral

The research was conducted in the financial services sector in the UK during 2009-2010. This was a turbulent time for this sector with the period seeing significant government intervention in the banking sector to ensure its ongoing stability, substantial media and political interest in reward structures across the financial services industry as a result of this crisis, and the perception that reward structures contributed to the crisis through the proliferation of reward mixes which encouraged ‘excessive’ risk taking.

As we have seen in the previous discussion the importance of the sectoral context and the historical environmental conditions that had been seen in the financial services industry appear to have been significant in explaining some of the findings. This is particularly apparent in three areas – the overall profitability of the industry, the influence of regulation and how it was changing during the research, and the impact of the financial crisis. Each of these is now briefly discussed.

The REs characterised the industry pre-financial crisis as a sector of relatively high profitability which was identified as a significant dimension in understanding why the industry’s norm reward mix had developed as it had. The relatively long period of success that had occurred before the financial crisis had led to an ever-increasing demand for labour, seen as being a major contributor to the overall strength of employee expectations on overall reward mix. This was believed to explain why employees were perceived as such significant stakeholders and, through this, why their expectations exerted such a strong influence over RMD. This influence, aligned with the historically

perceived high profitability generally of the sector, had led to relatively high proportions of 'variable' pay as firms looked to share the success that had been achieved with employees, and the creation of relatively generous benefits packages as employees looked to secure as favourable a reward package as possible.

In addition, the regulated nature of the sector was clearly playing a role but will potentially limit the extent to which the research findings are more widely generalisable outside of this sector. All the REs interviewed worked for firms that were regulated by the FSA. Before the financial crisis this may have been of little consequence to the REs as the regulator's interest in their remuneration structures had been relatively limited. However, the crisis meant there was significant focus by the regulator in the UK, and its equivalent authorities around the world, on RMD and the implementation of constraints on this process. This is seen in Figure 6-4 as a moderating influence on the industry norm position derived from the historically formed employee expectations.

Finally, the financial crisis that was underway both preceding and during the research had caused some serious reflections by practitioners, both RCs and REs, on RMD and amongst REs had triggered an increase in the desire to make changes to rectify perceived problems that were present. However, overall capability to make changes remained a serious concern.

6.5.2.2 Firm context

The analysis of the data collected included clustering the findings with respect to looking for any trends and relationships between the type of financial firm of which the RE was speaking (e.g. investment bank, wealth management firm, financial advisor, insurance etc.) and the RMD approach adopted. What emerged was that the

prominence of the industry norm and the influence of employee expectations on this norm applied across all these groups. ‘Sub sector’ was not seen as an influence on the significance of the concepts identified and discussed above. A difference was found with respect to the conceptualisation of reward mix, as discussed in section 5.2, where REs speaking of the investment banks were generally seen to have a narrower interpretation of reward mix than REs from the remaining firms. This was attributed to the relatively extreme mix taken in this sector with respect to high proportions of variable pay relative to fixed pay (including benefits) which meant that wider definitions were relatively insignificant.

6.5.2.3 Individual context

In addition the data were examined, again through clustering, in relation to the characteristics of the REs themselves, based on whether they were largely from reward or non reward backgrounds and also whether their experience was more generally from financial services or other sectors. Again no discernible relationships between the accounts provided and these characteristics were identified. The one exception to this was with respect to the conceptualisation of reward mix discussed in section 5.2 where the two REs with relatively limited reward backgrounds (their experience was predominantly in recruitment and development) provided a more holistic conceptualisation of reward mix, capturing not just financial but also non financial reward. However, whilst interesting, it is not possible to draw further conclusions from this, given the limited data from which this finding was made.

6.5.3 Combining theoretical perspectives – An integrated theory of RMD

6.5.3.1 Revisiting inputs to RMD

One of the criticisms made of the reward mix research to date is that despite the large amount of research carried out, we know little about RMD as there is no dominating paradigm explaining the process (Gerhart and Rynes 2003). This research set out with the aim of providing greater clarity of how reward mix is determined. We saw in chapter 2, Table 2-5, how a ‘shopping list’ of inputs to RMD had been suggested by the largely deductive research carried out to date. In Table 6-4 I repeat these ‘shopping list’ variables and summarise the extent to which they were significant in the research findings.

Theoretical perspective	Decision driver	Significance in this research
Agency	Alignment of employee effort	Not as perceived by agency theory as solely a means to reduce or manage employee shirking. Alignment of effort was also about looking for ways to build reward packages that both meet the desires of employees whilst managing costs for employers.
	Managing monitoring costs (spans of control and contract type)	Not as perceived by agency theory in an analytical approach to RMD. Cost control was important, but was not seen as a trade-off between monitoring and spans of control, but rather optimising reward such that it met employee desires whilst keeping costs as low as possible for the employer.
	Business Risk	Not raised.
Institutional	Legal requirements	A moderating influence on the transmission of employee expectations as to their reward mix through to the industry norm position.
	Political and societal pressure	Was an influence over the regulatory change that was occurring in reward in the sector. This exhibited itself as a moderating influence on the transmission of employee expectations to the industry norm position.
	Taxation and other regulations	A moderating influence on the transmission of employee expectations to the industry norm position.
	For subsidiaries of multi nationals, parent group	An influence on firms’ desire to differentiate their position from the industry norm reward mix.

Theoretical perspective	Decision driver	Significance in this research
	policies	
	Union pressures	An influence on the transmission of employee expectations to the overall industry reward mix norm.
	Historical precedents	Strong influence on both the employee expectations of an appropriate reward mix, but also individual firm's propensity to follow the industry norm reward mix.
	Benchmarking others' practice	Strong element. Central construct in RMD being the industry norm mix which is ascertained largely through separate benchmarking of the components making up reward mix.
	Consultants' advice	Less prevalent than suggested in the literature although they perform a key role in collation and provision of the industry benchmarks.
	Professional networks	Play an important role in the communication of the industry norm reward mix to REs across the sector through groups and conferences.
	Codification of practice in reward qualifications	Not raised.
	Organisational exposure to other institutional settings	Not raised.
	CEO and board members' business education and experience	Not raised as an influence although the CEO was seen as significant in influencing the firm's risk appetite for differentiation from the industry norm mix.
	Cost of loss of legitimacy against benefit of differentiation	An influence in the firm's decision as to whether to differentiate its reward mix from the industry norm or take the safer route of adopting this position.
Resource dependency	Attraction and retention of critical employees/ employee groups	Employee expectations were significant. However not solely about key groups but wider understanding of the generality of expectations and through this a strong influence on the industry norm reward mix developed.
	Union dominance	An influence on the transmission of employee expectations to the overall industry reward mix norm.
	Task complexity and the need for specialist skills	Not raised.
	Ease of employee monitoring and performance	Not raised.

Theoretical perspective	Decision driver	Significance in this research
	visibility	
	Substitutability of skills	Not raised.
	Task centrality	Not raised.
	Organisational connections	Not raised.

Table 6-4 - Significance of ‘shopping list’ factors in this research

As the detail in this table shows, a number of these inputs have been found in this research and therefore appear in the descriptive RMD model shown in Figure 6-7. The model provides order to the variables that were raised by the interviewees. The ‘shopping list’ has been rationalised and ordered through the RMD model. The next section now pulls the explanations gathered into an integrated theory of RMD.

6.5.3.2 An integrated theory

We saw in chapter two that the three theoretical approaches used to examine RMD – agency, institutional and resource dependency – appeared similar in that they all examine managerial decisions from a perspective of those decisions being influenced by external factors, i.e. ownership structure, critical resource holders, institutional norms. Each of the approaches also operates with similar dependent and independent variables. Where the differences between the theoretical approaches lie is in the assumptions they make about both firms’ and employees’ behaviour and the outcome of this behaviour on final RMD. These differing assumptions are shown in Table 2-4. This research, through taking multiple perspectives in assessing the problem, has been able to review and challenge those assumptions and from this develop a unified and practitioner-led theory of RMD coming through the RCs’ and REs’ voices on the issue, rather than abstract assessment through reviewing statistical data. Adopting the same format as Table 2-4 this unified theory is shown in Table 6-5 which presents the main premises,

assumptions, organisational reactions and their implications for reward mix from this research. This meets the call by Gerhart & Milkovich (1992) for reward scholars to refine existing theories as a productive direction for reward research generally.

Research findings	
Purpose of reward mix decisions	Conformity with market practice in order to gain legitimacy with current and prospective employees.
Main Assumptions	<p>Strong employee expectations of receiving the industry norm reward mix.</p> <p>Goal alignment often exists between employee needs and firms' requirements.</p> <p>Employees are not always acting rationally, often resisting change to a potentially non optimal historical norm.</p> <p>Firms are typically risk averse, seeking out the safe harbour position of the industry norm.</p> <p>Process of satisficing behaviour by employers.</p> <p>Firms follow the industry norm unless both the desire and capability to differentiate their position are present.</p>
Organisational reaction	Both rational legitimacy seeking, with respect to employees, and passively conforming to industry norm position, depending on firms' specific circumstances.
Implications for reward mix	Reward mix will be influenced by institutional norms and the extent to which operating within these norms confers legitimacy with current and prospective employees.

Table 6-5 - Summary unified theory of reward mix determination

As the table shows, this unified explanation identifies the strength of institutional pressures on firms to conform to an agreed norm with the aim of gaining legitimacy with both current and prospective employees. Firms still have room for manoeuvre in

the form of strategic choice influenced by the strength of their desire and capability to differentiate their mix from this strong, institutionally reinforced position as they look to reach a satisfying position. This, alongside employees potentially irrationally resisting change, can mean that a suboptimal reward mix may be in place for both employer and employee.

This is only, to the best of my knowledge, the second study (the first being Barringer and Milkovich's (1998) theoretical assessment of these three areas plus transaction cost theory) that has combined these three perspectives and the first that has involved empirical research with practitioners in developing our knowledge of RMD.

6.6 Conclusion to chapter six

In this chapter I discussed the findings of the research in relation to the research question and the context of previous research findings. This discussion leads to the development of a descriptive model and a unified theory of RMD.

The discussion identified that the most prevalent theoretical perspective from the literature – agency theory – was found to be limited in its explanation of how RCs and REs viewed the RMD process, with institutional pressures, including resource dependencies, being more significant. This contradicts the overall premise of the literature, outside an institutional theory perspective, that given that reward mix can be changed without increasing costs (Lazear, 1998), then organisations may face less difficulty in differentiating themselves in this area. Generally, the contention that “[P]ay mix is where the action is in differentiating organisations” (Gerhart and Milkovich, 1992: 669) was not well supported, with the exception of the two mould breaking firms. Organisations still felt significant difficulty in differentiating through

reward mix. The 'safe harbour' of industry practice is sought, with the industry norm being seen as the rational place to be, given firms' lack of desire and capability to make changes and consequent risk assessment of the consequences of making such a shift having taken place.

In summary, my findings suggest that reward mix is determined by institutional norms and the extent to which operating within these norms confers legitimacy with current and prospective employees. The extent to which these norms then determine the reward mix for individual firms is determined by a combination of both the firm's desire and its capability to differentiate its position from the prevailing position in the sector.

The final chapter summarises these results and identifies the contribution of the research before reviewing the implications for practitioners and, having acknowledged the research's limitations, making a number of suggestions for the direction of future research.

7 Chapter seven: Conclusions

7.1 Introduction

This thesis set out to understand what influences RMD in financial services organisations and why these influences are significant. This work is positioned in the reward mix literature and the explanations provided to date through the lenses of agency, institutional and resource dependency theories. To situate the work, I first developed a conceptual framework of RMD from the reward literature in chapter two and developed a series of research questions. After outlining the research design in chapter three, I then developed and assessed this framework through interviews with RCs as acknowledged experts in the reward field with relationships with REs and management in organisations and, in addition playing an important role in RMD. These interviews identified the existence of a strong industry norm influenced by labour market forces and the existence of various moderating influences on how this norm is transmitted to actual organisational practice. In chapter five I reported the findings of interviews with 30 REs from financial services firms. These interviews identified the significance of employee expectations in influencing the industry norm reward mix, alongside seven dimensions which influence an organisation's propensity to follow the industry norm position. This chapter then examine these seven dimensions further in the context of each of the accounts of firms provided by the REs involved in the research. This analysis identified three categories of firms dependent on the extent to which they had both the desire and the capability to resist the industry norm position in order to gain advantage through differentiating their reward mix. 'Market followers' had both low desire and capability to move away from the perceived safety of the industry norm reward mix position, whilst 'cautious leaders' saw some benefits from

differentiation, whilst still ensuring that they did not diverge dramatically from the norm. These positions were in contrast to the accounts of two ‘mould breaking’ firms found in the research. These firms had adopted radically different reward mixes from the industry norm in order to align the reward mix more clearly with their distinctive business strategies. Chapter six then uses the findings to extend the conceptual framework developed from the literature into a descriptive model of RMD in the financial services sector. It concludes by positioning the research within previous work on RMD. This argues the need for a broader focus on institutional and resource dependency influences on reward mix, and a revised consideration of a number of the assumptions of agency theory.

In this chapter, section 7.2 provides a summary of the research project, before section 7.3 addresses the research question developed at the beginning of the thesis. Section 7.4 presents the contribution of the research to both academia and practice. Finally, section 7.5 acknowledges the various limitations of the research, whilst section 7.6 suggests potential routes for further investigation before the thesis concludes with my closing reflections.

7.2 Research approach

In order to address the research question – What influences RMD in financial services organisations? – the research adopted a qualitative approach through interviews with people advising reward decision makers, RCs, and actual reward decision makers themselves, REs, as people well placed to discuss RMD. The research followed three stages – conceptualisation and identification of research question, data collection and theory building (see Figure 1-1).

7.3 Addressing the research questions

The main research question examined was: What influences RMD in financial services organisations?

Following analysis of the data, the simple ‘answer’ to this question is, in line with Eisenhardt’s (1988) earlier conclusion, the need to conform with market practice in order to gain legitimacy. However, legitimacy is found to be with respect to employees’ expectations of the reward mix that should be provided in the financial services sector. This conformity is both a position of passive conformity for some firms, as suggested by DiMaggio and Powell (1991), but for others it is much more a rational assessment of the risks associated with differentiation, in line with the work of Norman et al. (2007). Beyond this simple explanation, the findings show that the REs identify that a small number of firms have adopted a differentiated position (10 REs spoke of their firms in this way). These firms had either moderately moved their reward mix away from the industry norm position (cautious leaders) or in more limited cases radically adopted a significantly different reward mix position from the industry norm practice (mould breakers).

The propensity of firms to differentiate their reward mix from the dominant industry norm was a function of both their desire to differentiate and their capability to make desired change happen. The desire to change was seen to be influenced by coercive pressures from their parent organisation, government intervention in their operation and strategic reasons with respect to leadership beliefs, customers or suppliers, whereas the capability to move away from the industry norm, where change is considered desirable, was seen to be a function of both HR and management capabilities. Additionally, both

the desire and capability to differentiate the reward mix were influenced by opportunities for change being presented in the form of mergers or acquisitions, or firm-specific financial crises which provided the ‘excuse’ to make the change happen.

A number of sub research questions were also posed. These are repeated below.

RQ2a To what extent is the alignment of principal and agents’ interests and the issues of monitoring and control an influence in RMD?

RQ2b Why are they / Why are they not an influence?

RQ3a To what extent are coercive, mimetic and normative institutional pressures an influence on RMD?

RQ3b Why are they / Why are they not a influence?

RQ4a To what extent do the reward mix preferences of critical groups of employees influence RMD?

RQ4b Why are they / Why are they not an influence?

The answers to these questions are heavily weighted towards the coercive and mimetic pressures introduced in question RQ3a. The descriptive model developed in chapter six shows the powerful influence of the industry norm in determining individual firms’ reward mix positions. This is attributed to the strength of employee expectations in forming that mix, reinforced by a general position of risk aversion to adopting non conforming mixes for fear of not meeting those employee expectations and the consequences, with respect to attracting and retaining employees, that this was felt to present.

Generally, consideration of alignment of principal and agents' interests (question RQ2a) was not a factor in decision making, or at least not as prescribed by the agency theorists. Alignment was considered, but with regard to looking for ways to build reward mixes that met the needs of employees, in areas such as long-term saving, security and their health and well-being, which meant they were productive in their work. The use of incentives, as proxies for monitoring and to exercise control, was not generally supported. A more holistic interpretation of human nature and its interest and commitment to work was provided, rather than an account built of the need to control workers' behaviour through financial incentives.

Finally, RQ4A proposed that resource dependent effects would be significant. Whilst dependence on employees was important this was not, as envisaged by resource dependency, a discernible focus on critical groups, but rather a general awareness of the importance of attraction and retention across the workforce and the need for the reward mix to work with this by conforming to industry norms and, through this, meet employees' expectations.

7.4 Contribution

7.4.1 Academic – Theoretical, empirical and methodological knowledge

The contribution of the research to scholarly knowledge is both with respect to the findings of the research, but also, in a more limited way, with regard to the method by which the research conclusions were drawn. The study reviews and challenges the assumptions of previous research on RMD and from this develops an integrated theory through the eyes of a pivotal player, the RE, as called for by Gerhart and Rynes (2003) and Taras (1997). Further, these individuals were recruited personally, rather than as

representatives of their organisations, allowing them to speak of, rather than as representatives speaking for, their firms, so that they could speak freely of the practices and problems that their firm faced in determining its reward mix. In addition, the insights of RCs were also used as suggested by Rynes and Bono (2000).

The research examined three theoretical perspectives that have largely been used deductively to examine RMD. The results support a number of the findings of earlier literature, particularly with respect to the significance of institutional pressures on reward decision making firms (Eisenhardt, 1988; Conlon and Parks, 1990; Crystal, 1991). However, they also challenge, refine and add to the assumptions, and conclusions of the theoretical perspectives examined.

For agency theory, the research challenges the narrow conceptualisation of reward mix that agency studies typically take (e.g. Gerhart and Milkovich, 1990; Boyd and Salamin, 2001; Werner and Tosi, 1995; Gerhart and Trevor, 1996; Bloom and Milkovich, 1998), and a number of the underlying assumptions held with regard to employee behaviour and the way in which this behaviour can best be managed. The results extend agency theory into considerations of employee alignment beyond monitoring and control, suggesting that a wider interpretation should be taken. Alignment can both fulfil a variety of employee desires, whilst at the same time lead to increased commitment and performance.

With respect to institutional theory, the need for legitimacy is identified as critical in firms' activities (supporting the conclusions of other authors such as DiMaggio and Powell, 1991; Carpenter and Wade, 2002). However, this legitimacy is identified as being primarily focused on practices that are legitimate in the eyes of employees (and

where present their unions as representatives of employees) rather than wider social and economic legitimacy (Suchman, 1995). Further, the research findings extend the conclusions of Norman et al. (2007), from their examination of the airline industry, that adopting institutionally legitimate positions can in fact be a fully rational activity and not, as others have argued, passive (Eisenhardt 1988, Conlon and Parks 1990 and Van der Stede (2003)). Assessment of the additional risk that moving away from the 'safe harbour' of the market benchmark would imply was carried out by REs acting for their firms. A large proportion concluded that the risk of differentiation outweighed the potential benefits which could be gained and, therefore, concluded that the safe harbour position should be adopted.

Finally, the findings show that specific resource dependencies are not the main focus of practitioners. Resource dependencies are significant but not, as suggested in previous research, through a focus on 'special' groups but rather a wider concern about attraction and retention across the workforce.

The combination of these three theoretical explanations and the integrated theory that this approach has developed is unusual but is part of an increasing trend towards using complementary theoretical perspectives to deepen our knowledge of reward mix, particularly to counter some of the criticisms that have been made of agency theory alone in explaining the phenomenon (Eisenhardt, 1989a; Fernandez-Alles et al., 2006; Berrone and Gomez-Mejia, 2009). This combination has led to a more complete understanding of institutionally driven behaviour in this sector.

From these insights, an integrated theory of RMD is presented along with a model of this theory and typology of firms' propensity to follow the industry norm. This theory

and model has provided greater order to the ‘shopping list’ of variables that have previously been shown to be related to RMD. Whilst institutional pressures are the main driver of determination behaviour, our understanding of these pressures has been enhanced by incorporating insights from the agency and resource dependency perspectives.

The work also makes an empirical contribution providing evidence on the practices and responses of financial services firms in the post crises environment and how they are reacting to regulatory and market based pressures at this time. Specifically we now have understanding about how the combination of both a firm’s desire and capability to differentiate their reward mix informs their judgement of whether to ‘break free’ from the established institutional norms. These factors were not, as agency theory suggests, a rational assessment of control and monitoring of employees (Gomez-Mejia and Balkin, 1992; Wiseman et al., 2000; Delvey, 1999), but rather consideration of parent and government intervention where relevant, strategic examination of customers and product market, alongside the existence of opportunity to change and HR and line management ability to make the desired differentiation occur. The empirical identification of these two key factors which supported firms adopting non industry norm positions – desire and capability – may also be applicable to other non reward settings. This suggests further exploration of these dimensions may provide additional insight into divergent firm behaviour in other institutionally influenced settings.

Finally, much of what we know about RMD is known through a positivist research approach. However, an emerging body of work has developed, taking a more constructionist approach to reward determination, albeit largely at an Executive level,

as a potential means to establish not only what is driving reward decisions but significantly why (e.g. Bender, 2004; Perkins and Hendry, 2005; Bender and Moir 2006). Methodologically, the approach taken in this research adds further weight to this emerging body of work being qualitative in a largely quantitative field. The findings and analysis developed from the interviews demonstrate that rich data can be established through qualitative work, as suggested by the call from deductive statistical reward researchers that we should also be entering the field as well as surveying it (Gerhart and Rynes, 2003).

7.4.2 Implications for practice and policy

The research is intended to act as a prompt to REs to think more consciously about the influences on their firms' reward mix, to ensure that these influences are genuinely in line with business need, however this may be defined. The findings showed that many REs felt their firms were not passively conforming to industry norm practice, but consciously assessing the risk with regard to whether their organisation should adopt this position. Others were not consciously assessing this position for their firm. If Gerhart and Rynes' (2003) conclusion that, with respect to strategic reward decision making, "pay mix is where the action is" then practitioners need to be consciously assessing the risks rather than passively conforming. The theory and models presented are a means by which this active consideration can begin.

This process of greater proactive consideration of RMD has already begun as a result of the research. The interviews themselves caused participants to reflect on what was influencing reward mix and, from that, what they believed should be driving reward mix decisions. The descriptive model developed also allows REs to consider how the

combination of factors influencing their reward mix compares with others (unsurprisingly something they are keen on!) and, in particular, how the eight moderating dimensions to the dominant mimetic pressure faced could be manipulated for their firm to allow more strategic changes to reward mix to be implemented. Contact with interviewees, post the research, has seen them begin to manage the identified moderating factors proactively as they look to move their organisation away from the industry norm position currently pursued, to better differentiate themselves from others.

The development of a stronger theoretical base for understanding the determinants of reward mix choices will also assist policy makers in furthering their understanding of the extent to which organisational free choice and institutionally determined choice influence final reward choices when discussing policy options and, consequently, the level at which any regulatory intervention should occur. If labour markets and institutional factors dominate, as the research proposes, and therefore operate as a significant constraint on firm choice, this may suggest the need for macro level regulatory policy intervention to change reward practice (if this is felt desirable for social or political reasons). Discussions have already been held to this effect with regulatory agencies and trade associations to input the findings to their longer term research plans on financial services reward policy making.

7.5 Limitations

Despite the interesting findings of this study, a number of limitations must be acknowledged arising out of its method, context and sampling. I have from the start of the research continually reflected on the research approach and significantly my role

and influence as the researcher on the process and, through that, the results of the research. Through this limitations section whilst I acknowledge this influence, this reflection has not led me to conclude that I would have changed the design with the power of hindsight that such reflections allow.

The research is a UK-based study of the RMD process through the eyes of direct protagonists in that process. Interpretation needs to consider that participation was at the discretion of those protagonists. No individual who was approached openly turned down the interview, but a small number did not return e-mail requests which were made after previous 'warming up' of the contact, i.e. at a conference or through a mutual acquaintance etc. This may have been due to time constraints of the potential interviewee, but could have been due to wariness of discussing the subject. Although within this context the sampling carried out was both pragmatic and opportunistic, whilst attempting to be purposeful, seeking out variation and challenge to the emerging theory where possible. Nevertheless, there may be some element of bias in the findings due to voluntary nature of participation and the self selection that this required.

Of those that did participate, it is fair to assume that where they were uncomfortable with how they saw RMD, given the topicality and regulatory and press coverage at the time of the fieldwork, they may have been concerned about airing views, despite reassurances made around confidentiality. The use of personal rather than representative recruitment was intended to reduce this risk and reflections after each interview did not indicate that the interviewees 'held back' with a range of forthright views being presented.

A further limitation is the use of the REs and RCs to provide a perspective on RMD.

Other qualitative studies have looked to triangulate individual perspectives with views from others within a firm involved in reward decision making (e.g. Bender 2004). However, the intention of this research was always to take the RE's perspective as a valid one in its own right, given that the frames that the RE holds will be a strong influence on future behaviour (Chell, 2004) and the significant role they were found to play. Their recruitment personally, as opposed to as organisational representatives, in line with Buchanan's (1993) articulation of this approach as a means to gain franker accounts, was intended to increase the freedom with which they felt able to speak. Whilst there is, of course, no way of knowing whether a different design taking the views of other individuals who are involved in the reward mix decision making process, such as the CEO or Finance Director, would provide different conclusions, the general uniformity of accounts given to date, by both RCs and REs, gives some comfort that the results achieved were a reasonable reflection of RMD within the firms examined. Furthermore, additional sense-making activities carried out, individual and group meetings with others involved in the process alongside review meetings with trade bodies, provided further corroboration that the ideas developed were reasonable.

Next, concerns could arise over the interviews themselves, on whether the accounts I heard were what was said or that my questions somehow led the interviewees to construct an inaccurate account of how they see RMD. One potential way of managing the impact of this limitation would have been to engage in observing the practice of the interviewees. I would have then been able to observe them in the practice of carrying out RMD. However, the lack of a defined moment of RMD and potential access constraints meant this was not possible. Whilst controls were put in place to manage this risk (as outlined in chapter three), the interpretation and resulting theory developed

is based on my interpretation of these accounts. However, the extensive use of quotes in presentation of the findings is intended to give the reader some form of direct access to what was said and from that reassurance that my interpretation is rigorous.

Finally, the research is clearly positioned to examine reward mix in the UK financial services sector in 2009-2010. Certain elements of the findings are likely to be context-specific, given the regulatory activity and the specific nature of the financial crisis which was influencing the sector at the time of the research. REs from other sectors may have had different interpretations of RMD. If it was the purpose of the research to generalise to a wider population, or to provide some claim to a universal position for RMD then this would be an issue. No such claim is made. So whilst the sectoral focus limits the extent to which the findings may be useful in other contexts, it also provides richness to the contribution, given the significance of understanding behaviour in the area of RMD in the financial services industry at this time.

7.6 Further research

The findings suggest a number of areas for further research both within the context of RMD but also other aspects of Human Resource Management.

The descriptive model presented was not developed in order to test or prove specific hypotheses, rather to present a scholarly account of the relationships that practitioners and those who closely advise them felt existed in the area of RMD. The overall aim of this approach being one of building on the deductive research carried out in the reward field to date through adoption of a different research stance. This is in line with Guba and Lincoln's assertion that research should be undertaken under different research paradigms to assist in "informing one another's argument" (2005: 192). In this spirit of

epistemological harmony it is suggested that the findings and conclusions of this work could lead to further deductive testing. The descriptive model does present a series of potential hypotheses that would lend themselves to future testing. For example, constructs could be developed for the seven dimensions that were found to influence a firm's propensity to diverge from the norm to examine the contexts in which these may be influential. Further analysis of how reward mix has statistically changed over time would also be useful in examining how historical reward mix patterns are influencing employee expectations over time.

The research also challenged the definition of reward mix used in research to date. A narrow definition considering fixed and variable pay has historically been applied (see section 2.2.2). The insights provided by both the RCs and REs identified that research in the future should look where possible to widen the definition used to at least consider employee benefits in any testing that is carried out, but ideally also look for ways to measure the relational elements that were seen by a number of the participants as an important part of the reward mix.

Furthermore a challenge is presented to agency theorists. The research suggests that we should look to develop the analytical rational economic perspective of agency theory through adopting a wider perspective on employee alignment taking into account the need through all the elements of reward mix to align employees' behaviour to that of the principal through building commitment and engagement not just by controlling and managing shirking. Extension of agency research to consider wider type of principal - agent alignment would be useful in taking forward the findings of this research

As noted above, the research was set in a specific context, financial services, at a

specific time, post financial crisis, with significant media, political and regulatory interest focused on reward practices at that time. Although rich insights were found and developed, it is not possible to contend that the results can be more widely generalised. Further research into RMD in other sectors would be productive in understanding whether the conclusions are specific to the financial services sector, or if some of the findings apply more widely across other sectors. Consideration could be given in this research to the extent to which the regulatory environment may play a significant role through examination of sectors that are also subject to some form of regulatory control (such as the oil and pharmaceutical sectors) and those that are not. Examining different sectors in this way would also further explore the extent to which product market forces may be the driving force behind labour market pressures given the earlier conclusions of Brown (2008) on their significance. Furthermore given the heightened regulatory, political and media focus on reward mix in this sector at the time of the research a further potentially useful variation would be to repeat the research during a time when this interest had ended to see how this changed the findings.

Moreover, the identification of the two key factors which supported firms adopting non industry norm positions – desire and capability – may be applicable to other HR practices other than reward. Examination of how the desire and capability of firms relates to their propensity to break from norms in other HR practices would be worthy of examination to see if there is consistency across HR disciplines.

The interviews have provided an insight into organisational practice, through discussion with those involved in the process, i.e. RCs and REs. Both these groups highlighted the significance of employee expectations as a substantial influence in RMD.

Consequently, it would be interesting to assess the employee perspective on reward mix (both directly and through their Unions) to understand these expectations, how they influence the employee's behaviour and the extent to which, where firms are looking to diverge from the industry norm, it may cause changes to this behaviour. Whilst not widespread this could be examined both qualitatively through research with employees, but consideration could also be given to an experimental approach examining the dissonance potentially caused by changing reward mix relative to some defined historical and expected pattern.

Two aspects of the method adopted in the research are also considered worthy of further exploration. Despite Rynes and Bono's (2000) observation that alliances with RCs may be productive in furthering reward research, collaborations have been relatively limited. Given the insights gained in this work through one such collaboration, further research ascertaining consultants' perspectives on this and other reward-related research areas would appear to be potentially fruitful. The experience from this research is that RCs were keen to collaborate further in academic work. Finally, the use of personal rather than organisational recruitment is worthy of wider adoption, especially in areas seen as organisationally sensitive, where the opportunity to talk of the organisation rather than for the organisation may lead to more open conversations. I believe that this form of recruitment provided deeper insights into RMD in this sector at the time of the research.

7.7 Concluding remarks

This thesis has addressed the research question – What influences reward mix determination in financial services organisations? In doing this it has developed an understanding of the complexity of RMD in the sector and provided a contribution to

both the research literature and practice in this area, not just through this document, but through the engagement I have had with academics, practitioners and consultants during the research. It has given me great pleasure when I have been asked to return to meet the academics, practitioners and consultants who have contributed to the research to present my findings and continue our discussions. Understanding and explanation has been presented which should provide value to both the academic debate and to those tasked with making reward strategy happen in organisations.

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Appendix 1 - Outputs and dissemination of research

The following list of references presents the outputs the author has produced, or contributed to, during the course of his doctoral research.

Academic papers

Chapman, J., Kelliher, C. (2011), Influences on reward mix determination: Reward consultants' perspectives. *Employee Relations*, vol. 33, no. 2, pp 121-139.

Chapman, J., Kelliher, C., Reward mix conceptualisation and determination: A review of the literature.
Chapter in forthcoming reward book - *Pay and Reward Systems in Organizations - Theoretical Approaches and Empirical Outcomes* edited by Prof. Dr. Conny Herbert Antoni, Work and Organizational Psychology, University of Trier.

Academic conference papers

Chapman, J., Kelliher, C. (2010), Managerial choice, institutional pressures, employee preferences. What determines reward mix? Observations from the UK financial services. British Academy of Management HRM 2010 Conference, London, 22-23 April 2010.

Chapman, J., Kelliher, C. (2009), Reward mix conceptualisation and determination: A review of the literature. EASIM 2nd European Reward Management Conference, Brussels, 26-27 November 2009.

Chapman, J., Kelliher, C. (2009), An examination of reward mix policy in the financial services industry, British Academy of Management, Brighton, 15-17 September 2009.

Chapman, J., Kelliher, C. (2009), An examination of reward mix policy decisions: A Consultants' Perspective, Manchester Metropolitan University 5th Performance and Reward Conference, 1 April 2009.

Practitioner journal papers

Chapman, J., Cotton, C. (2010), Managing reward risks: an integrated approach, 2010 reward risks survey, CIPD, September 2010.

Chapman, J., Cotton, C. (2010), A systematic approach to reward risk identification, *Strategic HR Review*, March 2010.

Chapman, J., Cotton, C. (2010), Worth the risk. People Management, February 2010.

Chapman, J., Cotton, C. (2010), Rewards in the U.K.: Top ten risks, Workspan, January 2010, WorldatWork.

Chapman, J., Cotton, C. (2009), Taking a risk, Pay & Benefits Magazine, November 2009.

Chapman, J., Cotton, C. (2009), Managing reward risks: an integrated approach, CIPD October 2009.

Practitioner conference presentations

Chapman, J. (2010), Reward management: Risks and challenges for the third sector. Agenda Consulting Third Sector Conference, 20 October 2010.

Chapman, J., Davidson, I., Murray, J. (2010), Reward, performance and risk. CIPD Reward Conference, 23 February 2010.

Chapman, J. (2009), Reward risk management. E-Reward Annual Reward Conference, 4 November 2009.

Chapman, J. (2009), Risk aligned remuneration. MMK Reward management seminar, 29 October 2009.

Chapman, J. (2009), Reward and risk management. Oracle Corporation Reward Management Seminar, 22 October 2009.

Chapman, J. (2009), Regulation and reward. Marcus Evans Annual Financial Sector Compensation and Benefits Conference, 25 June 2009.

Appendix 2 - Specified activities as defined in part II of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001

- accepting deposits;
- issuing e-money;
- effecting or carrying out contracts of insurance as principal;
- dealing in investments (as principal or agent);
- arranging deals in investments;
- arranging home finance activities;
- operating a multilateral trading facility;
- managing investments;
- assisting in the administration and performance of a contract of insurance;
- safeguarding and administering investments;
- sending dematerialised instructions;
- establishing etc. collective investment schemes;
- establishing etc. stakeholder pension schemes;
- providing basic advice on stakeholder products;
- advising on investments;
- advising on home finance activities;
- Lloyd's market activities;
- entering funeral plan contracts;
- entering into a home finance activity;
- administering a home finance activity;
- agreeing to do most of the above activities.

Appendix 3 - The significance of the research context

The financial services sector contributes a significant proportion of overall UK gross domestic product (chart 1). In 2007 it contributed 8.3%, up from its low of 5.2% in 2000. This growth is in direct contrast to the reduction in the prominence of the manufacturing sector in the UK which since 1995 has fallen from 20.3% to 12.4% (Office For National Statistics, 2010a).

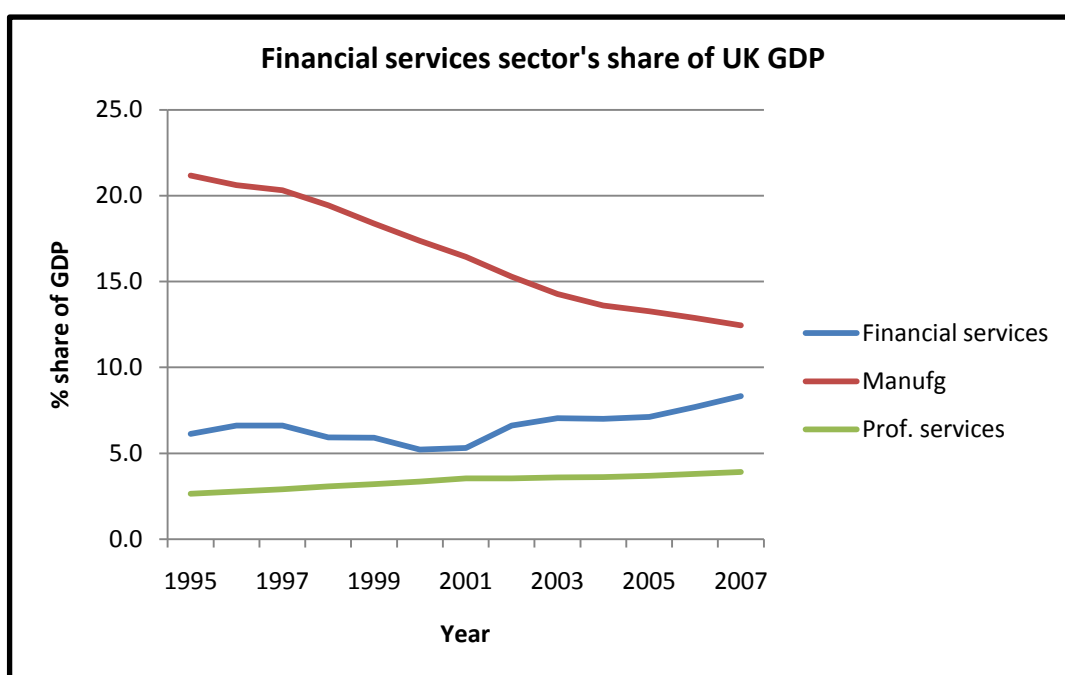


Chart 1 – Financial services sector’s share of UK GDP

This is higher than a number of other major financial centres – US, Japan, France and Germany – as shown in chart 2 (McKenzie, 2009).

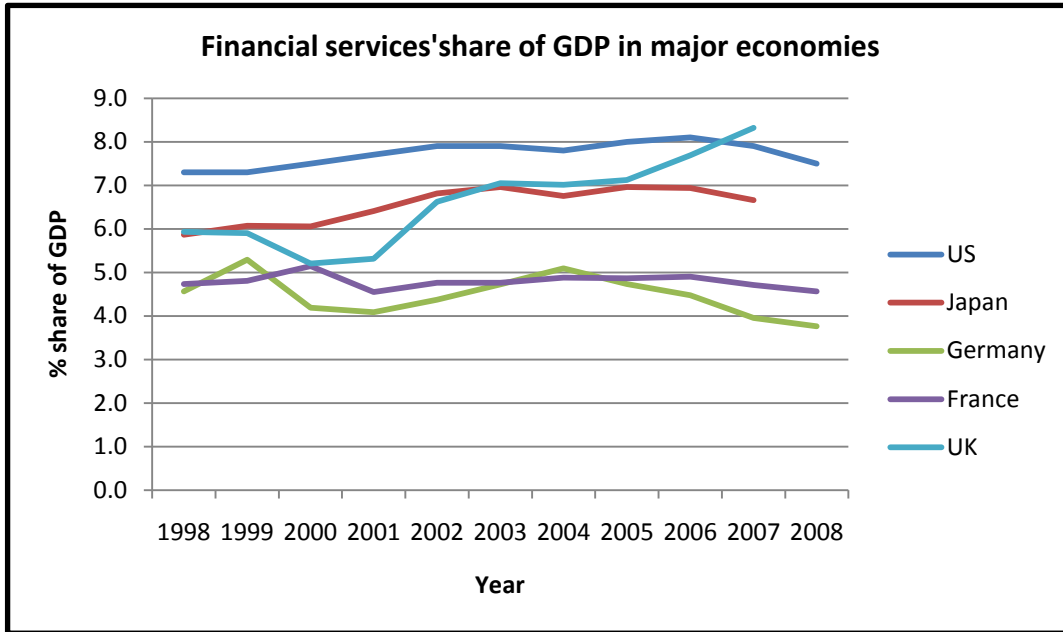


Chart 2 – Financial services’ share of GDP in major economies

The importance of the sector is further illustrated with reference to the contribution it makes to UK taxation receipts both through corporation and income tax. Official data from HRMC (McKenzie, 2009) identify corporation tax receipts of £11.6bn (26% of overall corporation tax) and income tax of £18.7bn (15% of all income tax) in 2007 the latest year both sets of data are available (Chart 3).

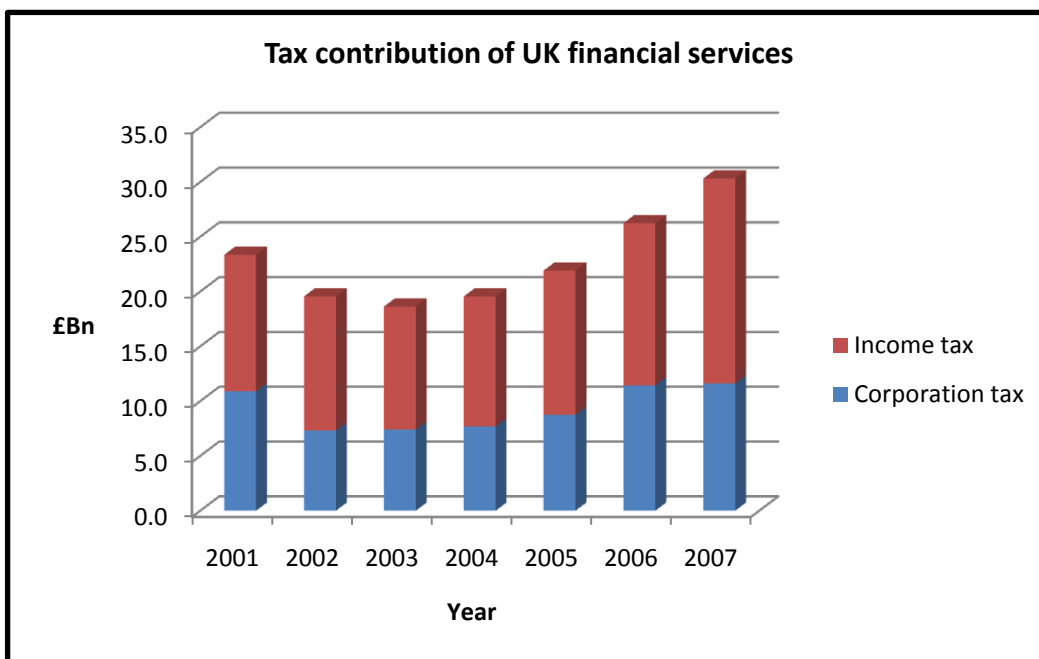


Chart 3 – Tax contribution of UK financial services

In addition the sector employed over one million people in June 2009, accounting for 3.5% of overall UK employment, which stood at 28.9 million at the same date (Office For National Statistics, 2010a). This illustrates the significant value add of the sector given that employment share is less than half the contribution made to GDP of 8.3%. This employment was largely concentrated in the London region with around one third of employment being centred in that area. However as Chart 4 shows the sector did employ people from across the UK.

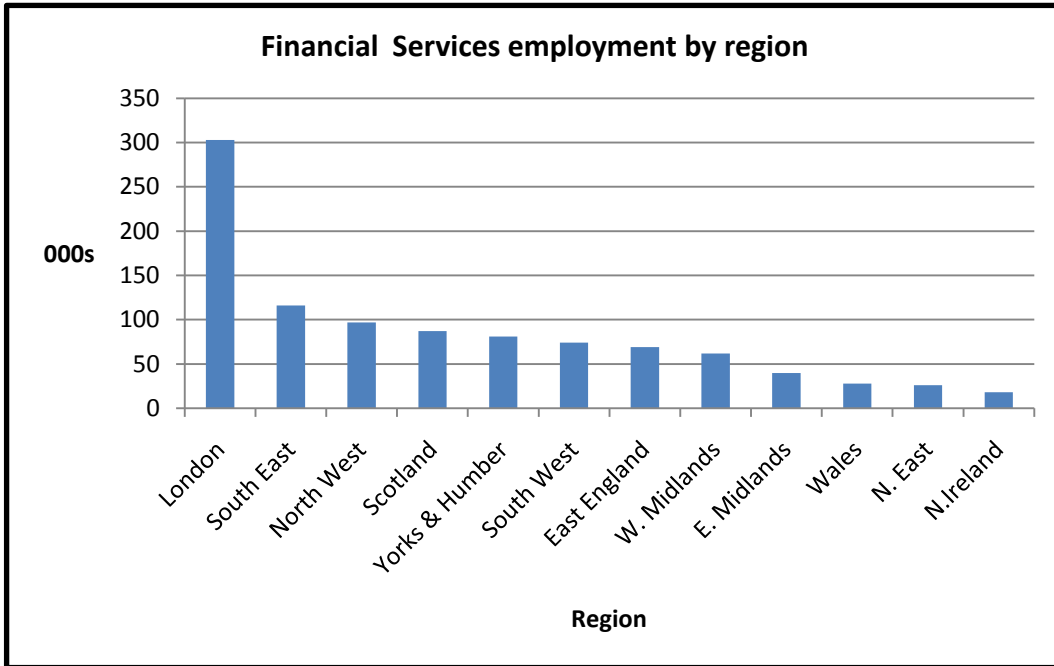


Chart 4 – Financial services employment by region

Appendix 4 - Review of rejected research methods

Method	Conclusion
Participant observation of reward strategy decisions meetings	Lüders (2004) identified the particular difficulties faced from participant observation with respect to entering the field, establishing and maintaining a role and building a relationship. The issue of observation was floated with the reward consultants and practitioners interviewed during the exploratory research. What emerged was immediate rejection of such a possibility due to reasons of sensitivity of the data that is discussed (i.e. people's reward) and the level at which discussions are generally held (Executive Committee and RemCo meetings). This is in line with findings from previous qualitative studies of reward, albeit at executive level, where access has been problematic for interviews (Bender, 2004; Main et al., 2008). In addition, the lack of one focal point or 'moment' where a reward mix decision was taken was raised, where the actual mix tending to emerge over time rather than as a result of some set piece decisions was identified. It was not clear what would actually be observed. As a result this method was rejected as an appropriate way of examining the research question.
Analysis of publicly available texts – annual reports and organisation websites	This approach has been adopted in previous reward research at the executive level with researchers noting how they review Director Remuneration reports ahead of interviewing REMCO chairs, members or HR professionals (Bender, 2004; Ogden and Watson, 2008; Main et al., 2008). Clearly data are available for publicly listed organisations on their Executive remuneration as required by the Companies Act 2006. Public disclosure of remuneration detail for levels below executives is more restricted. There is no legal requirement for disclosure of details on employee reward mix beyond showing overall employment accounting costs. However, companies do typically include some further detail on their employee reward structures in their annual reports and on their website. A sample (15) of financial services organisations' annual reports and websites were reviewed for details on reward policy. Overall, the texts were very basic and provided no insight into the rationale for reward mix policies beyond general statements on attracting and retaining employees. Consequently, content analysis of these texts was not used although public data available were reviewed ahead of interviews with reward executives to contextualise the researcher into the overall reward structure in place at the reward executive's organisation.
Analysis of publicly	A number of bodies prepare and publish case studies on organisations. The outputs of three such organisations were reviewed. E-Reward ²⁰ produces case studies on a range of organisations' reward practices. Since E-Reward was created in 1999 it has

²⁰ E-Reward develops email and web delivered news reports, best practice guides and case studies on reward matters.

Method	Conclusion
available written texts / case studies	<p>published 62 case reports (as at 17 February 2009). These are generally in depth and provide detailed assessment of the organisation and their stated motives for the reward structures, often including reward mix, being discussed. However, only five of the case studies produced were on financial services firms. For this reason they were not used in the research although I have read each report and they form part of my general base of knowledge in the area. CIPD resources were also reviewed. Detailed accounts of organisational practices are relatively limited. CIPD reward-related outputs are typically research reports and survey results. Cases are sometimes reported within these studies but they are short form (around one to two pages). Given their lack of depth they were not considered appropriate for the research. Finally, Incomes Data Services (IDS)²¹ pay report research was considered. Although reports could not be reviewed first-hand as this required a prohibitively expensive subscription, a review of the titles and summaries of recent reports issues was carried out supplemented by my knowledge of the reports pre June 2008 when I had access to these data. The general purpose of the IDS reports is to provide data and commentary on pay settlement trends across the economy and on particular sectors. It also provides wider reporting on changes in terms and conditions of employment. Whilst some summary reports have been written on financial services, particularly on bonus settlements, these are typically data-led macro level reporting rather than analytical assessment of motives. Again this lack of depth of assessment and focus on data rather than motives and processes means that this data source was not considered appropriate. Overall, this method of research was therefore rejected.</p>
Analysis of internal documents	<p>A number of reward researchers have used internal documents as a means of gathering data on organisations (Trevor, 2008; Bender, 2004). Where access is granted these have been found to provide a further insight and means of assessing the data provided in interviews. However, they have noted the general reluctance of organisations to supply these data as they are generally confidential and commercially sensitive in nature. To rely on internal documents as the primary source of data would be risky. However, during interviews where the issue of documents was raised, interviewees were asked if they would be willing to supply them.</p>

²¹ IDS is an independent research organisation providing information and analysis on employment law, diversity, pay and reward, HR and pensions.

Appendix 5 - Reward consultant interview protocol

Background

- Outline of role and background.

Concept

- What do you understand by the term reward mix?

Process / Factors

- What factors do organisations take into account in determining their reward mix?
- Why do you think those factors are important to organisations?
- What in your experience causes organisations to change their reward mix?

Examples

- Without breaking any confidences can you talk me through specific assignments where determination of reward mix has been the main or an important issue?

Close

- Are there any elements of reward mix determination which you see in the organisations you consult with that we haven't discussed today?

Appendix 6 - Reward executive interviewees

Firm	Role	Sector	Employees	Location
RE1	Head UK Reward	Insurance	5000	London
RE2	HR Director	Wealth management and advice	650	Berkshire
RE3	Reward Director	Retail Banking	500	Berkshire
RE4	Reward Director	Conglomerate Banking	120000	London
RE5	Head of Reward	Retail Banking	120000	London
RE6	Director Compensation & Benefits Europe	Retail Banking	66000	Sussex
RE7	Senior Reward Analyst	Credit Cards	3000	London
RE8	HR Director	Pensions administration and advice	200	Suffolk
RE9	COO - Main Board	Pensions administration and advice	150	Sussex
RE10	Head of Reward	Investment Banking	1200	London
RE11	HR Director	Credit cards	350	London
RE12	HR Director	Long term savings	4500	Edinburgh
RE13	Head of Compensation and Benefits	Wealth management	135	London
RE14	HR Director	Wealth management and advice	100	Kent
RE15	UK Head of Reward	Long term savings	26000	London
RE16	Head of Reward	Investment Banking	750	London
RE17	Head of Reward	Retail banking	18000	London
RE18	Head of HR UK	Investment Banking	26000	London
RE19	Head of Reward	Insurance	2150	Cambridgeshire
RE20	Head of Compensation and Benefits	Conglomerate Banking	60000	London
RE21	Head of Reward UK	Retail Banking	75000	Edinburgh
RE22	Global Head of Reward	Insurance	5000	London
RE23	Global Reward Director	Insurance	22000	London
RE24	Reward Director	Investment Banking	2800	London
RE25	Head of Reward	Wealth management	10000	London
RE26	Reward Director	Conglomerate Banking	135000	Edinburgh
RE27	Head of Reward	Retail banking	26000	London
RE28	Head of Reward	Retail banking	10000	London
RE29	HR Director	Hedge Fund	150	London
RE30	Head of Reward	Banking conglomerate	15000	London

Appendix 7 - Reward executive interview protocol

Background

- Title, role, reporting lines, responsibilities, previous roles
- Organisation – Business, products etc.

Concept

- What do you understand by the term reward mix? Is this the same as that adopted by your current organisation?

Section 1

Determination

- What is the current reward mix at the organisation?
- How did you arrive at that mix? What drives the choices? (laddering for reasoning)
- Do you know what reward mix other firms in your sector operate? Does your mix differ from theirs? If yes why? If not why don't you differentiate?

Change

If a change event is identified use to probe

- Tell me what happened to cause the change? Why did it happen?
- How did the change happen? Who was involved?
- What role did you play? Did you initiate the change? If yes why? If not who did? Why did they do this?
- What approval was required? Why was this approval felt necessary?
- How did you feel about the change?
- What were the consequences of the change?

Process

- Who is involved in decisions on the reward mix?
- What interests and perspectives do the different parties bring?
- Who is dominant in the decision?
- Where are the final decisions on reward mix policy made?

Section 2

Depending on the initial answers, potential probes

- Are there any legal or regulatory constraints on the reward mix policy you adopt? If yes which aspects of legal / regulation?
- Are there any tax regulations that have an influence on your reward mix choices?
- Do you consider employees' preferences for different mixes? If you do, what has this shown you and how has this influenced your mix policy?
- Has the recent turbulence in the financial services industry caused you to review your reward mix? If yes, how and why?
- Do you receive external consultancy advice on your reward mix? If yes, what support do you receive?
- Do you benchmark the overall reward mix? How do you go about this benchmarking?

Close

- Are there any elements of how you determine reward mix that we have not covered today which you think are important?

Appendix 8 - Contact summary sheet

Name	
Organisation	
Date	
Location	

	Data	Comments
Role		
Responsibilities		
Sector		
Reward Mix content		
Reward mix proportion		
Influences identified unprompted		
1.		
2.		
3.		
4.		
Parties involved in decisions		
Role of benchmarking		
Prompted influences		

5.		
6.		
7.		
Action Points		
My reflections		
Model		

Interview checklist

Pre interview email sent with background and protocol	
Thank you email sent and any actions followed through	
Contextual notes written up	
Action points actioned	
Recording transcribed	
Recording saved in folder	
Transcript checked	
Transcript saved in folder	

Appendix 9 – Coding structure

1 Approach

1.1 Process

1.1.1 (In)Formality

1.1.2 Authority

1.1.3 Committees

1.1.4 Decision taking

1.2 Roles

1.2.1 Consultants

1.2.2 Employees

1.2.3 Executives

1.2.4 Finance Director

1.2.5 HR Director

1.2.6 Parent

1.2.7 REMCO

1.2.8 Reward Executive

1.2.9 Risk

2 Background

2.1

Interviewees

2.1.1 Interviewee background

2.2.2 Interviewee role

2.2.3 Organisation business

2.2 Mix

definitions

2.2.1 Conceptualisation

2.2.1.1 Fixed-variable

		2.2.1.2 Holistic total reward
		2.2.1.3 Total compensation
	2.2.2 Hierarchy	
		2.2.2.1 Strong role
		2.2.2.2 Weak role
	2.2.3 Organisational package	
3 Explanations		
	3.1 Change	
	3.1.1 Competence	
		3.1.1.1 HR Capability
		3.1.1.2 HR Capacity
		3.1.1.3 Management capability
	3.1.2 Leadership	
		3.1.2.1 CEO leadership
		3.1.2.2 Executive leadership
		3.1.2.3 HR Leadership
	3.1.2 Opportunity	
		3.1.2.1 Company financial crises
		3.1.2.2 Financial crises
		3.1.2.3 Merger
		3.1.2.4 New leadership
		3.1.2.5 Strategic change
	3.1.3 Pragmatism	
		3.1.3.1 Administrative ease
		3.1.3.2 Opportunism
	3.1.4 Risk appetite	
		3.1.4.1 Risk aversion

		3.1.4.2 Risk loving		
3.2 Economic	3.2.1 Agency			
		3.2.1.2.Principals perspective		
			3.2.1.2.1 Behavioural	
				3.2.1.2.1.1 Aligning employee effort
				3.2.1.2.1.2 Managing monitoring costs
			3.2.1.2.2 Business risk	
				3.2.1.2.2.1 Company lifestage
				3.2.1.2.2.2 Cost management
				3.2.1.2.2.3 Risk sharing with employees
			3.2.1.2.3 Paternalism	
				3.2.1.2.3.1 Employee personal responsibility
				3.2.1.2.3.2 Employee security
				3.2.1.2.3.3 Employee well-being
3.3 Organisational	3.3.1 Institutional			
		3.3.1.1 Coercive		
			3.3.1.1.1 Legal	
			3.3.1.1.2 Parent group	
			3.3.1.1.3 Political	
			3.3.1.1.4 Regulatory	
			3.3.1.1.5 Societal	
			3.3.1.1.6 Tax	
			3.3.1.1.7 Union	
		3.3.1.2 Mimetic		

		3.3.1.2.1 Benchmarking	3.3.1.2.1.1 Analytical
			3.3.1.2.1.2 Informal
		3.3.1.2.2 Employee expectation	
		3.3.1.2.3 Geography	
	3.3.1.3 Normative		
		3.3.1.3.1 CEO- Leadership background	
		3.3.1.3.2 Codified practices	
		3.3.1.3.3 Consultants advice	
		3.3.1.3.4 Networks	
		3.3.1.3.5 Organisational exposure to other settings	
		3.3.1.3.6 Reward Education	
	3.3.1.4 Path dependency		
		3.3.1.4.1 Cost-Benefit	
		3.3.1.4.2 Historical precedence	
3.3.2 Resource dependence	3.3.2.1 Acquisition critical resources		
	3.3.2.2 Critical partners		
		3.3.2.2.1 Customers	
		3.3.2.2.2 Shareholders	
		3.3.2.2.3 Suppliers	
	3.3.2.3 Ease of employee substitution of critical employees		
	3.3.2.4 High value generation		
	3.3.2.5 Unions		

Appendix 10 - Assessment of firm's desire and ability for differentiation

The table below shows for each firm discussed by the REs in the research, the extent to which each of seven moderating dimensions was found to be present in the accounts provided of how they determined their reward mix. A plus (+) shows that the dimension was raised as an influence, with more than one plus (++) indicating it was raised on several occasions as a key driver of changes to the reward mix away from the industry norm position.

Representative quotes from each of the interviews against these categories are also provided in Appendix 11 to further aid transparency to the assessment made in the table. In addition, the table below shows whether the RE was able to provide examples of changes that had been made to the firm's reward mix that took it away from the industry norm.

Firm	Desire					Opportunity	Capability		Recent change to mix	Type of change
	Leadership	Business Strategy	Political pressure	Parental influence	Firm history		HR Capability / Capacity	Line Management Capability		
1				+					Minimal	Merger harmonisation leading to minimal adjustment to benefits.
2	++	++		n/a		+	++	+	Radical	Radical shift in proportion of fixed to variable pay and uplifting of benefits. Change focus of employees from sales to advice in line with business strategy.
3			+	+		+	+		Moderate	Reaction to financial crisis by parent Moderate adjustment of bonus and share schemes in line with parental guidelines.
4			+	n/a		+			Minimal	Merger harmonisation. Minimal adjustment to incentive schemes.
5		+	++	n/a		++			Moderate	Political pressure - Moderate shift of fixed : variable proportions.
6			+	+		++			Moderate	Parental pressure for cost savings driven by firm's financial position and State

	Desire						Capability			
Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history	Opportunity	HR Capability / Capacity	Line Management Capability	Recent change to mix	Type of change
										support required due to the financial crisis. Moderate changes to pension scheme and share schemes.
7		+							None	N/A
8	+	+		n/a		+			Minimal	Merger harmonisation. Minimal changes to bonus scheme and benefits package.
9				n/a	+				None	N/A
10				+		+			Minimal	Changes to bonus and share scheme mandated from head office.
11				+					None	N/A
12						+	+		Minimal	Gradual change to benefit package to move away from historical anomalies relative to the market position.
13									None	N/A
14	+			n/a					None	N/A
15				n/a					None	N/A
16				n/a					None	N/A
17				n/a	+	+			Minimal	Merger. Minimal changes to benefits packages, some incentive schemes and share plans.
18	+	++				++		+	Radical	Resisting market norm (driven by regulatory changes) shifts into fixed pay, deferment and guarantees.
19		++		n/a	+		+	+	Moderate	Developing and promoting relational and low cost benefits options in order to differentiate offering and compensate from

	Desire						Capability			
Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history	Opportunity	HR Capability / Capacity	Line Management Capability	Recent change to mix	Type of change
										lower levels of salary and bonus.
20				+		+			None	N/A
21		+	+	n/a		+			Moderate	Regular refresh and addition to benefit scheme for attraction purposes. Shift of some variable reward into fixed due to political pressure.
22				n/a					None	N/A
23				n/a					None	N/A
24		+		n/a	+				Minimal	Some limited changes to certain entities due to supplier / joint venture partner requirements.
25		+		n/a		+			None	N/A
26			+	n/a		+	+		Moderate	Regular refresh and addition to benefit scheme for attraction purposes. Shift of some variable reward into fixed due to political pressure.
27			+	n/a	-	+	+		Moderate	Regular refresh of benefits for attraction purposes. Also innovating on incentives and performance measures used.
28				n/a	+	+	+		Minimal	Harmonisation post merger, particularly around some incentives schemes for non sales staff.
29				n/a					None	N/A
30			++	n/a		+			Moderate	Political pressure - Moderate shift of fixed : variable proportions.

Appendix 11 – Table of illustrative quotes from interviewees

Desire to differentiate

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
1	We appear to be risk averse when it comes to decisions of reward and reward mix but risk loving with respect to strategy, and marketing. The same leaders influence but very different risk perspectives. This is a challenge for all reward professionals in managing leaders' expectations while looking to innovate and differentiate the offering.			Now actually the role has got more complex because as one of the things the US are saying is that they are actually going take over more of the reward strategy which is going to be an interesting challenge for them because of course, I am not sure whether they entirely understand the nature of the marketplace here and the tax issues and the rest of it.	
2	But [name] is just a fantastic CEO. He is very open, he is very honest and I knew where we were heading, where he wanted to take the organisation, which is really a professional services type so it's kind of what I was	The way we reward our people says something about what we really stand for as a company and the way we want to do business. We don't want to be one of those firms saying the customer really matters and then having			

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
	used to. (RE2)	bonus plans that encourage selling at any cost. The sector has got a really bad name there we want are changing to break away from this image and that type of behaviour as we feel what is right for the customer will in the long term be right for the profit and success of the company.			
3			In 2008 all of our bonuses were obviously subject to quite a lot of media attention in [Firm name] and our CEO only two weeks ago, three weeks ago asked people to consider voluntarily giving them back at the senior levels. In our business that was pitched at probably no more than a dozen people. But anticipating where the shift and then where everything was at we have actually already written into our rules something that says even if everything is achieved we still have override that says we can reduce it or remove it entirely at	When we first set up as an organisation five years ago there really wasn't a huge level of interest in what we did, they didn't actually really know what people were paid and as long as we were doing great business, then they were really happy. Increasingly over time that has changed, there is now a real interest in what we are paying.	

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
			our complete discretion.		
4			Overlaying that however, was as part of the TARP negotiations with the government, we were required for a 100% deferral not a sort of third, two thirds.		
5		You know at the end of the day we are now we are by far the biggest [firm type]. So part of you says well lets be the leaders rather than the followers, which is OK.	I think in this environment, a company like this wants to meet its obligations under the FSA, clearly it does.		
6			So that is not really clear yet, but I can feel the appetite in the organisation to get out from under that restriction.	So on paper it can look decentralized, but in terms of where things and how things are approved, it's absolutely centralized company.	
7		Often people will say well what do other people do? What do [firm name] do, or what do [firm name] do? ... What do our big competitors do? And I say, I don't really care very much what they do because we are big enough that we should do what we			

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
		want to do			
8	I think it's part of their make up anyway. Let's not just listen to what our internal people are saying but ... I guess it's just seen a bit as, well that's what they're paid to do totally out there in the marketplace, so there must be some substantiating evidence that they're bringing to the table.	We never wanted to be just another insurance company, and in our very early literature for investors, we actually make the statement that we set out to be different and I suppose it was a way of being different and not being like everybody else.			
9					There's some smaller things in the reward mix that [firm name] do because we've always done them for a long time and it's part of our culture and heritage and it's a bit old fashioned, maybe, but we would want to do it to retain that commitment and buy in.
10				But the big exception is going to be we are bringing in a new bonus scheme to be in line with the FSA and regulations and that is being designed from	

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
				Frankfurt. I actually have a bit of an issue with that because I am just hoping that they do take into account the particular type of market that we have in London, which is not the same as the investment banking market in Frankfurt.	
11				The style of the package is about reward mix actually determined by the parent company. So we would piggy back on their arrangements.	
12					
13					
14	I think it tends to be the people who have worked in bigger organisations, so they come very much from benchmarking culture and they come from a culture where you're not just maybe benchmarking your benefits and your salaries, where you're constantly benchmarking your performance, and particularly on our investment side, your				

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
	performance against your peers. So they come from that sort of culture. (RE14)				
15					
16					
17					There were a lot of legacy arrangements, and as you try to understand how did we get to where we are now, there were variable elements in the old, shall I say, [firm name] package, but not very much, and it really went through a phase where cash was king, so everything was consolidated into base pay. Benefits was very, very meagre.
18	Success is everything for the firm's management. They will look for every way possible to steal an edge on the competition.	The second is anything they do to make it more difficult for any other investment banks to compete is also fantastic. I mean it strikes us that we're all in a little walled garden and they're			

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
		<p>slamming the door shut, and if you're a survivor you're in a group of five or six now, whereas before there was thirty or forty. It's fantastic. Fortunately, [Firm name] is inside that garden so we think it's great.</p>			
19		<p>And this feeds in to something that we're starting to have ... a discussion that we're starting to have with the board now, which is going back to where I started on the [firm name] offer, in, okay, so what does [firm name] as an employer mean to you as a board?</p>			<p>I think that goes back to being a much smaller company, quite paternalistic, and as we've grown there are elements of that paternalism that have remained, which now are not necessarily beneficial to the organisation as a whole, but the same people are in situ, and so that same mentality is still there.</p>
20				<p>And they feel they've been proved right, that the Anglo Saxon approach did not work, and the Americanisation of the bonus culture, which really came over from the US, an even if it would have happened in the UK, you know we had all these structures in place, the</p>	-

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
				American banks moved in, and all these structures fell away. So the attitude in the [country] is... this has to change, and so there's a very, very strong sense of that.	
21		So it's actually the business driver thing. I suppose more commonly what you get is ensuring that the misalignment is not too bad between business strategy and reward programmes.	The crisis has had some effect on our reward with Government exerting pressure on what we do.		
22					
23					
24		What a joint venture looks like is a business, and one of the business partners runs the business and the others are partners, not running the business but they're sharing the costs. If [firm name] is the partner that's running the business, it may want to apply all its systems and processes to all the people who work in			Where we have come from as a company is really important. If it is right for us then we will use this to resist the benchmark

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
		<p>that joint venture, but the partners may be unhappy about that because some of [firm name]'s systems and processes carry cost beyond what they might find acceptable, so we've got that other little bit of complexity around the place with these joint venture arrangements that we have.</p>			
25		<p>Historically it must have come about because we-, we felt that we needed to provide some level of protection for employees and support them when times are bad sort of thing. So I guess that's what we do for our customers in terms of the financial services institution, looking after people who find themselves in unfortunate situations</p>			
26			<p>We are clearly under huge pressure from the authorities there's no getting away from</p>		

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
			that.		
27			But treating the customer fairly, we work very hard with the FSA to ensure that we are fully compliant with that. It's really embedded in our culture, it's part of our main business strategy aligned to it. So again I think that does keep you honest, we haven't had any problems, but we would always ensure that what we were doing takes into account those regulations.		
28					It has taken us a lot of effort to get to the mix that we have now and I'd be reluctant to overhaul this given the amount of investment that has occurred. The benefits of changing would not outweigh the cost of making the change so why would we throw away all that we have done.
29					

Firm	Leadership	Business Strategy	Political pressure	Parental influence	Firm history
30			The regulatory punch and slap has created a reaction, a significant influence on how we organise the variable component of our mix.		

Capability and opportunity to differentiate

		Capability	
Firm	Opportunity	HR Capability / Capacity	Line Management Capability
1	Opportunities have presented themselves and we have used them.		
2	The establishment of the new [firm name] when we merged with [firm name] was the original catalyst for change.	We focused a lot of time and energy in to getting the change right. I had the full confidence of [CEO's name] to make it really work.	We had to get line management on board as they had to sell the change to their people. This was where the change was really successful.
3	Now after everything that we went through last year we have got a number of overrides, a number of gates.	We had to gear up to meet the regulatory challenge but we are pleased with how we have handled that.	
4	Well we have got a point in time to do it ... whenever you do any sort of take over integration it is an opportunity that you don't want to lose. So number one now is a great time to do it.		
5	It's an opportunity to take a step back and think about what we really want to do as an employer and what sort of employer do we want to be.		
6	But this year, because the economy is so bad and it affects our business so much.		
7			
8	The acquisition presented us with a major opportunity to make changes.		

		Capability	
Firm	Opportunity	HR Capability / Capacity	Line Management Capability
9			
10	I think we are pretty close to the level of tax that people see as reasonable, any increase on where we are now is going to start people saying ok, actually we are going to start doing something about it.		
11			
12	We have quite a unique culture, and what we've tried to do is not take advantage of the current crisis just to push through changes that would have materially affected the fabric of the organisation, so we've been able to keep things that other organisations may well have thought about just removing.	I think I'll always look for an angle on which we can be different.	
13			
14			
15			
16			
17	Now, it may be that through the recession we've been through and the turmoil that some of those things will change.		
18	Again, in the broader context it's fantastic that the government and the regulators are involved in all this for a number of reasons. I mean the first is that it... I mean		The key is the management team are driving our aggressive stance. They are in the lead in

		Capability	
Firm	Opportunity	HR Capability / Capacity	Line Management Capability
	we don't want to pay a penny more to our people than we have to, full stop. I mean if they can drive the whole market down that's great. I'm not sure they'll be able to but, you know, we're happy to stand by as passive observers and watch them try and do it.		confronting the market changes that are occurring.
19		We spend a lot of time seeking employee views and input on the whole reward package. We analyse it all and use this along with the exit and retention data to mould the offering	The business owns it, because essentially any staff costs come out of the business budget, so we have to have the buy in from the business for it.
20	Our parent it acquires, often keeps the local name, and then over a period of time, usually through parachuting [name of nationality] guys in there, [firm name] them.		
21	They gave us stuff to hang our hat on that we think we needed to change anyway. It was a good excuse. Certainly TCF was. RDR, you know, it's yet to impact, but TCF was definitely a case of saying, hey, there's some stuff here that provides a good excuse to insert some of the controls that we want.		
22			
23			
24			
25	And I think it was-, in part, it was a case of looking at what the external market might expect people to be		

		Capability	
Firm	Opportunity	HR Capability / Capacity	Line Management Capability
	receiving in terms of a benefits package and trying to deal with any transitional arrangements basically to try to harmonise terms and conditions.		
26	I believe you say opportunistically. That is way you build it.	We have had a very good track record of evolving our reward package, especially the benefits where I believe we are a market leader.	
27	We haven't made any drastic changes based on economic conditions but we may have to in the future. So we would always monitor the market and the economic conditions.	So [firm name] has a lot schemes and initiatives across the HR piece rather than just reward and performance management. So it's integrating those, and I think that is the biggest challenge, but we are achieving a lot not only aligning the initiatives within HR, but also relaying the message, communicating the message to employees that it is the whole package.	
28	The merger gave us a great opportunity to simplify everything.	It was driven out of the HR function, looking at external practice, where we wanted to drive performance more effectively.	
29			
30	There was some element of first move advantage as well. By doubling your base pay salary you were getting advantage in the hiring market.		