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Title

Why Are Your Reward Strategies Not Working? The Role of Shareholder Value, Country Context, and Employee Voice

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Abstract: The article suggests that when reward strategies fail, that is because they are frequently subsumed to a meaningless search for 'best practice' to deliver shareholder value that could be applied uniformly across countries, sectors or workplace contexts. For instance, executive compensation schemes incorporating stock options are focused too much on delivering value for shareholders, and ignore other important stakeholders such as employees. Flexible benefits schemes tend to be designed and implemented top-down, without employee involvement and customization to their needs. The article argues that reward practice should move away from shareholder-value reward to stakeholder reward making full use of employee voice mechanisms as a key ingredient of workplace innovation. It considers the case of 'shared capitalism' practices and outlines the benefits of broad-based employee ownership schemes. The article concludes by offering prescriptive advice for their application to enhance productivity and boost employee satisfaction.

Keywords: Compensation; Employee voice; Employee Share Ownership; Reward; Workplace Innovation; Profit-sharing

1. INTRODUCTION

Human resource managers and reward professionals are often puzzled by the failure of reward strategies to increase productivity, boost job satisfaction and enhance company performance. The article argues that the failure of reward strategies is due to three main reasons. First, any innovative reward strategy should not be subsumed to a meaningless search for 'best practice' that could be applied uncritically in uniform reward packages. Second, much of the reward practice is overly focused on aligning the interests of top managers and CEOs with those of shareholders, while ignoring the main bulk of employees in the organization. Third, HR professionals miss the point that innovative workplace strategies do not operate in a vacuum and top-down approaches frequently backfire.

The article proceeds as follows. The next section substantiates the problem of 'best practice' and 'shareholder value' obsession by considering examples of problematic reward practices that are widely diffused but fail to deliver expected benefits. The third section discusses the variety of cultural and institutional contexts and how key dimensions have different implications for appropriate reward strategies. The fourth section considers the main building block of the solution, which includes an enhanced role for employee voice as a key pre-requisite for successful workplace innovation. The fifth section examines the example of 'shared capitalism' that includes broad-based employee ownership schemes as an innovative reward practice that is likely to enhance productivity and boost employee engagement and innovation. The sixth section provides prescriptive advice on the key issues that professionals need to keep in mind whilst implementing innovative reward schemes. The final section concludes.

2. THE PROBLEM: OBSESSION WITH BEST PRACTICE AND SHAREHOLDER VALUE

Many human resource practitioners and reward professionals –and especially management consultants- are fascinated by the idea of coming up with some sort of ‘best practice’. This is understandable, as best practice is useful as a shortcut to crack difficult problems that are recurrent. It is much easier to consider what the leading organizations in each sector are doing, dub this as ‘best practice’ and then try to replicate these practices. Despite a large body of rigorous academic research (e.g. Edwards, Sanchez-Mangas, Jalette, Lavelle, & Minbaeva, 2016; Festing, 2012) that suggests that this usually ends-up in shooting yourself on the foot, the logic is appealing. The same ‘best practice’ logic has been applied to reward practices.

One notorious example of failed best practice that is linked with attachment to shareholder value is the so-called ‘golden parachute’. A golden parachute is usually a clause in an executive’s employment contract specifying the level and type of severance package that the executive will receive in the event that their employment is terminated. There are many recent examples that made some of the biggest headlines. For instance, the ex-CEO of Hewlett-Packard, Léo Apotheker, failed to turn around the fortune of the company, but he walked away in 2011 with $23 million for 11 months’ work (Stewart, 2011). Another example comes from McDonald’s ex-CEO Don Thompson, who abruptly retired from the brand in January 2015 amid accusations of tumbling sales and a failed strategy, but left with a generous ‘golden parachute’ and even more, continued to be on McDonald’s payroll for $3 million to offer ‘consulting services’ (Lutz, 2015). Despite the continued annoyance of the public with generous ‘golden parachutes’, even after apparent failure, this continues to survive as a ‘best practice’ in the ‘war’ for talented CEOs.

HR professionals have spent too much time and energy tying together executive pay with shareholder value. William Lazonick powerfully argues that the widespread influence of ‘shareholder value’ principles may have brought profits, but not necessarily prosperity (Lazonick, 2014). When a company ascribes to the shareholder value corporate governance model, the primary goal is the maximization of shareholder value by addressing the ‘principal-agent problem’ (Aguilera & Jackson, 2003). Payment of top management is linked directly to shareholder value in order to align the interests of the principals (shareholders) to the agents (management). Therefore, performance-related pay (PRP) systems such as bonuses and stock options seem appropriate. But the reward system does not have a built-in mechanism that prevents such rewards from unintentionally encouraging unethical or counterproductive behaviors (Aguinis, Joo, & Gottfredson, 2013; Kerr, 1995). For instance, in the case of experiencing lower profitability, the top managers may decide in favor of downsizing by shedding out employees in order to easily improve returns on capital indicators.

The widespread diffusion of ‘shareholder value’ best practice principles can be further fleshed out with the widening of the CEO-to-worker pay gap. According to State of Working America Report released by the Washington-based Economic Policy Institute, the CEO compensation was about 20 times higher than average worker pay in 1965, 123 times higher in 1995, and 231 times higher in 2011 (State of Working America, 2012). But these aggregate figures conceal much wider gaps that may be found in companies. Bloomberg calculated the CEO-worker pay ratio in S&P 500 companies (see Michaels, 2015): Union Pacific CEO pay was 262 times higher than average pay, Community Health Systems CEO earned 414 times more than average employees, whereas the McDonald's CEO earned 644 times more than the average worker.

The widening CEO-to-worker pay gap and the diffusion of stock options is not only characteristic of the United States, which is attuned to the short-term orientation of its model of capitalism (Whitley, 2009), but is observed across the globe. The increased use of 'variable pay' schemes in these countries denotes the intrusion of 'shareholder value' principles in their otherwise stakeholder corporate governance systems (Aguilera, Filatotchev, Gospel, & Jackson, 2008, p. 484; Aguilera & Jackson, 2003). The increasing obsession with 'shareholder value-oriented' best practice puts in jeopardy the feeling of organizational justice across stakeholders involved and this renders them problematic. If the top executives of a company are promised stock options and profit sharing, then these should be extended to lower-level employees to enhance the feelings of procedural and distributive justice (Aguinis et al., 2013).

But the failure of 'best practice' reward practices is not only observable at the top of the pyramid and the so-called 'fat cats'. For instance, reward professionals have become increasingly focused on the practice of 'total rewards'. Yet, fewer than half of UK employers actually have a defined total rewards strategy, while 9 out of 10 firms feel their rewards are not well implemented and operated in practice (Brown, 2014, pp. 147–148). The problem is also evident in the various flexible benefits schemes and their surprisingly low take-up by ordinary employees. According to research by the HR consultancy Towers Watson, only 27% of companies offered a flex scheme, and 32% of employers said take-up of such schemes was lower than expected (Hemsley, 2013).

Against this background, Kochan (2012, p. 72) warns that we need to 'rebalance shareholder and stakeholder considerations' and that 'executives have been urged to think as much about stakeholders as they do about shareholders'. Rebalancing shareholder and stakeholder orientations requires also shifting our attention to how best practices may fit with the cross-national variety of institutional and cultural contexts, which are characterized by different institutions and different norms of justice and attitudes towards risk.

3. REWARD AND COUNTRY CONTEXTS: A CROSS-NATIONAL PERSPECTIVE

'Best practice' approaches are also likely to fail if they ignore cross-cultural nuances and cross-national institutional differences. HR managers need to customize and identify 'best fit' strategies that are compatible with local cultural and institutional contexts. However, this does not mean that there is no learning that may take place from identifying 'good practices' of workplace innovation. There are several elements in the cultural or institutional context that may influence the application of rewards strategies, but here we focus on two key factors: risk and uncertainty avoidance (cultural context) and flexibility in wage determination (institutional context).

According to Geert Hofstede one of the key components of national culture is uncertainty avoidance, which is defined as the 'degree to which members of a society feel uncomfortable with uncertainty and ambiguity' (Hofstede, 1985, pp. 347–348). As shown in Figure 1, some countries such as Japan, France and Italy have a high score on uncertainty avoidance. By contrast, other countries are comfortable when dealing with uncertainty and this includes China, Sweden and the United Kingdom.

[INSERT FIGURE 1 ABOUT HERE]

This cultural variation has vast implications on a number of HR policies including reward. On the one hand, a low level of uncertainty avoidance means that uncertainty is seen as a normal feature of life, people may be risk-lovers or at least comfortable with ambiguous situations, and hence motivated by achievements. On the other hand, a high level uncertainty avoidance means that uncertainty is seen as a threat that must be fought and minimized, people are likely to be averse to risk or fear ambiguous situations and are motivated by security. Either case has implications for the choice of the 'best fit' reward system, and warns against trying to standardize reward systems across countries. In countries with high uncertainty avoidance the proportion of 'variable pay' to total reward should be minimized, as employees might be discouraged and demotivated by the uncertainty entailed in the variable component that is tied to performance. In this case, the reward strategy may demotivate employees and may have unintended consequences encouraging counterproductive behaviors (Aguinis et al., 2013, p. 243; Kerr, 1995). By contrast, in countries with low uncertainty avoidance there is much greater scope in introducing variable components of pay tied to performance criteria.

Along the same lines, the variation across institutional and regulatory contexts matter. Mercer, a well-known consulting firm offering advice on global reward and benefits always includes details of the institutional context in their Country Reports on Worldwide Benefits and Employment Guidelines (Mercer, 2016). These include information on benefits provided by the welfare state and social security system (e.g. retirement, disability, medical benefits), the employment rights prescribed by the labor law framework (e.g. annual leave, parental leave, working time regulation), and the character of the labor relations system (wage determination, representative associations, etc.).

The above have important implications for reward and benefit schemes. For example, benefits such as private medical insurance may be valued in countries, where there is no universal healthcare system such as the United States, but may be seen as redundant in countries with extensive National Healthcare Services, such as the United Kingdom. Indeed, this explains to a large extent the low-take up of flexible benefits schemes in the UK and across Europe (Hemsley, 2013). Figure 2 shows the vast differences in institutional frameworks governing pay setting across countries. Some countries such as Finland, Italy, Germany and Sweden have a high degree in the centralization of wage determination and this allows for limited flexibility. By contrast, other countries follow more decentralized wage determination systems, whereby wages are set by each individual company, for instance, Japan, the United Kingdom, and the United States.

[INSERT FIGURE 2 ABOUT HERE]

This institutional variation has important implications for reward strategy. Indeed, recent survey evidence from Europe suggests that the impact of performance related pay on productivity varies across national institutional contexts (Kornelakis, Veliziotis, & Voskeritsian, 2016). On the one hand, decentralized wage bargaining means that reward systems may be negotiated either at the individual employee-level (especially for executive pay) or negotiated by union representatives as part of company-level agreements. On the other hand, strong centralization of wage bargaining means that there is less scope to implement those at the individual company level. But companies may still get the best of both worlds, ensuring a 'level-playing field' across the industry and implement variable pay systems at company or branch level alongside negotiated salary scales (Kornelakis, 2014). Either case has implications for the choice and implementation of the 'best fit' reward system, and warns against meaningless efforts to standardize reward practices across countries. Indeed, recent international evidence suggests that there is no unambiguous standardized transfer of practice from home country multinationals to their subsidiaries in other parts of the world (Edwards et al., 2016). This lack of unambiguous global standardization persists and warns against 'one-size-fits-all' strategies and 'top-down' implementation of solutions that may be detrimental to employee's engagement and satisfaction.

4. THE SOLUTION: WORKPLACE INNOVATION AND EMPLOYEE VOICE

Considerations of how the future of work would look like thirty years ago appear to be equally relevant and applicable in today's workplace. Key concerns revolved around innovative workplace practices that would enhance intrinsic and not only extrinsic rewards and boost job satisfaction and productivity (Kalleberg, 1982, p. 80). Although workplace innovation is not a new concept, it has been given new meaning and attracted a renewed interest in recent years. There is broadly some consensus on what constitutes workplace innovation across the two sides of the Atlantic. According to Pot (2011, pp. 404–405) workplace innovation is defined as 'the implementation of new and combined interventions' in the fields of work organization, human resource management and supportive technologies and these include 'performance-based pay, flexible job design and employee involvement'. Workplace innovation has also been used as a term in the US to designate those bundles of HR practices that have been previously captured by terms such as 'high performance', 'high-involvement' or 'high-commitment' work practices or systems (Kochan, Appelbaum, Gittell, Leana, & Gephardt, 2009).

A common thread between the European and the American approaches to workplace innovation is the emphasis they attach to collaborative and participatory arrangements that ensure employee voice and involvement. Employee involvement is considered as one of the key areas that contribute to more intrinsically meaningful jobs, leading to higher satisfaction, higher commitment, and better operational performance (Batt & Colvin, 2011). Similarly, Kochan (2012, p. 68) suggests that enhancing employees' voice through labour-management partnerships is one of the cornerstones of 'high road' HR strategies that drive the productivity and performance of organizations, in addition to: selection of employees with polyvalent skills; significant investment in training and development; trust-based relationships; and compensation systems that align the firm's and the employees' interests. But how can the firm's and employees' interests be aligned?

5. THE EXAMPLE: SHARED CAPITALISM AND BROAD-BASED EMPLOYEE OWNERSHIP

One of the innovative ways to align the firm's and employees' interests has been dubbed as 'shared capitalism' by the Harvard University Professor Richard Freeman and his colleagues (Freeman, Blasi, & Kruse, 2010). The research project was carried out under the auspices of the National Bureau for Economic Performance (NBER). So, what *exactly* is shared capitalism?

'Shared capitalism' is a term that may capture a variety of schemes that promote broad-based employee ownership, e.g. Employee Stock Ownership Plan (ESOP), Employee Stock Purchase Plans (ESPP), Profit sharing schemes, Gain sharing schemes, and broad-based stock options (Freeman et al., 2010, pp. 4–5). This means that shared capitalism does *not* include reward systems based on individual performance (e.g. commissions), or other forms of CEO-pay tied stock market indexes.

The evidence from the NBER study suggests that tying employees' pay to workplace performance is expected to induce employees to increase effort, strengthen their commitment, make them more willing to share information, and to decrease perennial problems of employee turnover and absenteeism (Freeman et al., 2010). The latter is especially important in teamwork settings, where cooperation and information sharing among employees is crucial for success and the resultant growth of productivity and profits 'creates the potential for the proverbial "win-win" situation, with workers and the firm sharing the benefits of the increased production' (Freeman et al., 2010, p. 7). The shared capitalism practices are also expected to improve innovation in processes, products or practices. Employees whose pay or wealth is tied to the firm's performance are more likely to suggest ideas for innovative products or production technologies, and to help implement these ideas (Freeman et al., 2010, p. 8).

Apart from the evidence from the United States offered by the NBER study, there is plenty of case evidence from the United Kingdom that employee ownership makes good economic sense. Recently, the Chancellor of the Exchequer, George Osborne, and the business secretary, Sajid Javid, attributed the share price performance of Royal Mail to the efforts of its 135,000 employee owners and, by way of thanks, the government gave employees an extra £50m of stock (Hurlston, 2015). Some of the more successful companies in the UK are renowned for their use of employee share ownership schemes such as UBS, Prudential, British Telecom and ASDA (Calnan, 2015).

6. IMPLICATIONS FOR REWARD PRACTICE

Rebalancing shareholder and stakeholder orientations requires a cultural shift in organizational practice. The obsession with narrow success indicators such as profitability has exacerbated widespread inequalities and compromised prosperity (Lazonick, 2014). The cultural shift should start from the top, and prompts a rethinking of the kind of undesirable behaviors the current reward systems encourage. One of the suggestions is to redefine what 'success' means in organizations. For instance, non-financial performance measures should constitute at least 50% of performance-related executive pay and include measures such as employee engagement; customer satisfaction; and social/environmental performance (High Pay Centre, 2013, p. 7). The move to 'stakeholder reward' is also accomplished if reward strategies distribute gains to a broad base through shared ownership.

6.1.Consider the Local Institutional Context

Multinationals are increasingly located across different countries and there are incentives that the local institutional framework may provide to encourage the spread of share ownership schemes. In countries such as the United States and the United Kingdom, a variety of shared ownership plans receive tax-benefits and these should be carefully scrutinized, before the choice of the appropriate system. But more generally, the broader institutional context should be taken into account. If wages are predominantly set by collective bargaining with the representative trade unions, then the negotiation of a share plan should come under this umbrella to avoid the share plan backfiring with dissatisfaction from the representative trade unions. The point of the share plans is facilitating a win-win strategy on how to 'increase the size of the cake' not just how to split it.

6.2.Be Sensitive to Cultural Diversity

As discussed above, several multinational companies operate across different countries with fundamentally different cultures. We explored one dimension of culture, uncertainty avoidance, but there are other dimensions that may create barriers to a wider diffusion and implementation of a shared ownership scheme. The shared ownership strategy as part of the global rewards strategy should be translated into the local context effectively. What might work and be appealing in a country, which is generally comfortable with uncertainty, like the United States, may not be equally appealing in a country with strong uncertainty avoidance, such as Italy. To address this, it helps to have 'trained individuals as "ambassadors" on the ground who understand the local cultural nuances and are able to adapt messages accordingly' (Woodward & Aslam, 2012, p. 3). The shared ownership plan should not only be promoted from expatriates or through standardized newsletters from the headquarters. The generic and uncritical application of shared ownership schemes into uniform packages risks diminishing the benefits of adopting such strategies.

6.3. Involve Employees in the Design of Shared Ownership Plans

It is imperative to involve your employees early on, at the design stage of a shared ownership plan. It is more likely that they would feel that they 'own' the plan and not just shares, if they have participated in the design. There is a large variety of options e.g. gain-sharing schemes, profit-sharing schemes, sharing stock, and configurations (annual, deferred, etc.). Taking into account the employees' preferences while devising the plan can help tremendously towards its success. Questions that may arise include: do the employees in your organization prefer receiving the reward of their effort in the form of stock (share plan) or cash (profit-sharing)? Do they prefer to accumulate the rewards in a fund (with minimum retention period) or get the reward annually? Understanding your staff and their preferences would go a long way in defining and implementing a successful shared ownership plan.

6.4.Use Different Communication and Employee Voice Channels

Successful rewards communication programmes are based on messaging that addresses emotional needs and answers the most important question for employees: what's in it for me? (Woodward & Aslam, 2012, p. 2) This needs to come together in the form of an engagement campaign that involves employees 'bottom-up' rather than as a 'top-down' initiative. The fashionable social media may appear tempting (Woodward & Aslam, 2012, p. 3), but not everyone in an organization feels comfortable with it. Indeed, for the digitally connected employees, various forms of intranet voice mechanisms and Internet-based social media may be appropriate, while other workers may feel more comfortable with such traditional voice mechanisms as suggestion boxes, meetings with the manager, and toll-free hotlines (Miles & Mangold, 2014, p. 407). Social media may be an untapped resource in this respect but it needs to be used carefully alongside other mechanisms of employee voice and communication (Miles & Mangold, 2014). So do not forget traditional voice channels alongside the new ones. There are different employee voice mechanisms across countries; both formal (trade unions, works councils) and informal (quality circles, newsletters, forums, suggestion schemes) and these should be exhaustively used to communicate the mutual benefits that can be derived from a shared ownership plan. Finally, employee shared ownership plans and communication campaigns about them are constantly improved through continuous employee engagement and feedback.

Action plans that respond to feedback makes employees believe that their voice is being heard, which is essential to maintaining a fully engaged workforce.

7. CONCLUSION: FROM 'SHAREHOLDER-VALUE' REWARD TO 'STAKEHOLDER' REWARD

The article set out to answer the following question: why do reward strategies fail? The article argued that the failure of reward strategies is due to three main reasons: (i) there is an increasing obsession with shareholder value; (ii) reward strategies are subsumed to a meaningless search for 'best practice' irrespective of country context; and (iii) many reward strategies are implemented top-down without adequate consideration of employee voice. The article first substantiated the problem with best practice reward systems that is rooted to an obsession with shareholder value. Examples of these 'failed' best practices include the golden parachutes of CEOs and the total reward/flexible benefit packages and their low take-up from employees. Then the article moved on to examine how cross-national institutional and cultural variation may have a different implications for reward practices. A large body of research argues against 'one-size-fits-all' strategies pointing out the cultural and institutional variation across countries. Then the article suggested that a key building block of any solution should be channeled through employee voice mechanisms and involvement practices.

The article considered the case of 'shared capitalism' practices that incorporate a variety of broad-based employee ownership schemes. These help to move beyond narrow shareholder-value reward towards 'stakeholder reward'. Employee ownership is a key practice that may address the widening CEO-to-worker pay gap and there is evidence that has the potential to create win-win outcomes. The article concluded by offering prescriptive advice for the application of 'shared capitalism' practices, which require customization to truly enhance productivity and boost employee engagement and satisfaction.

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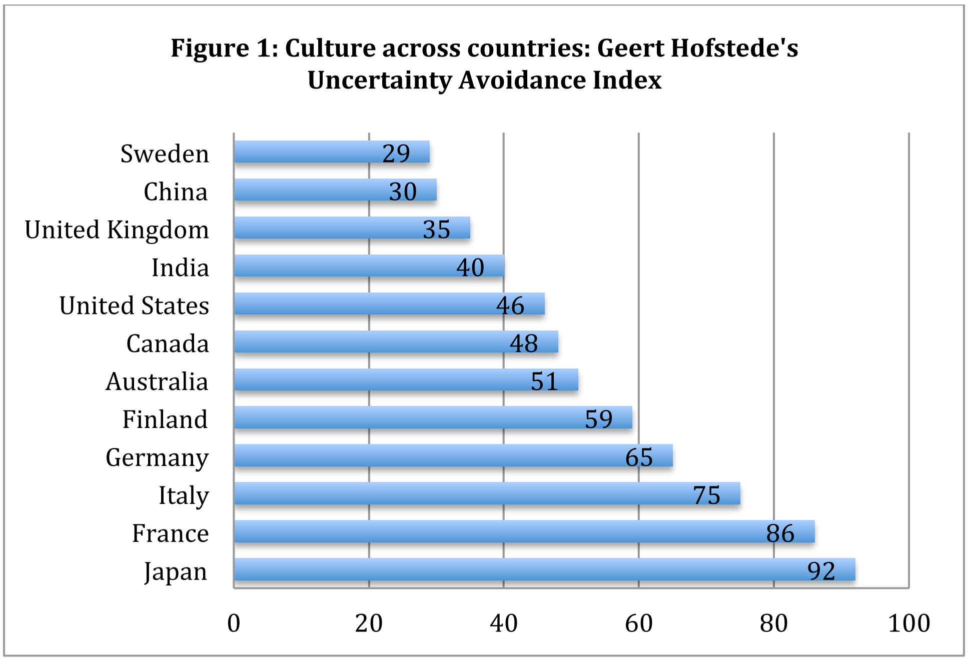
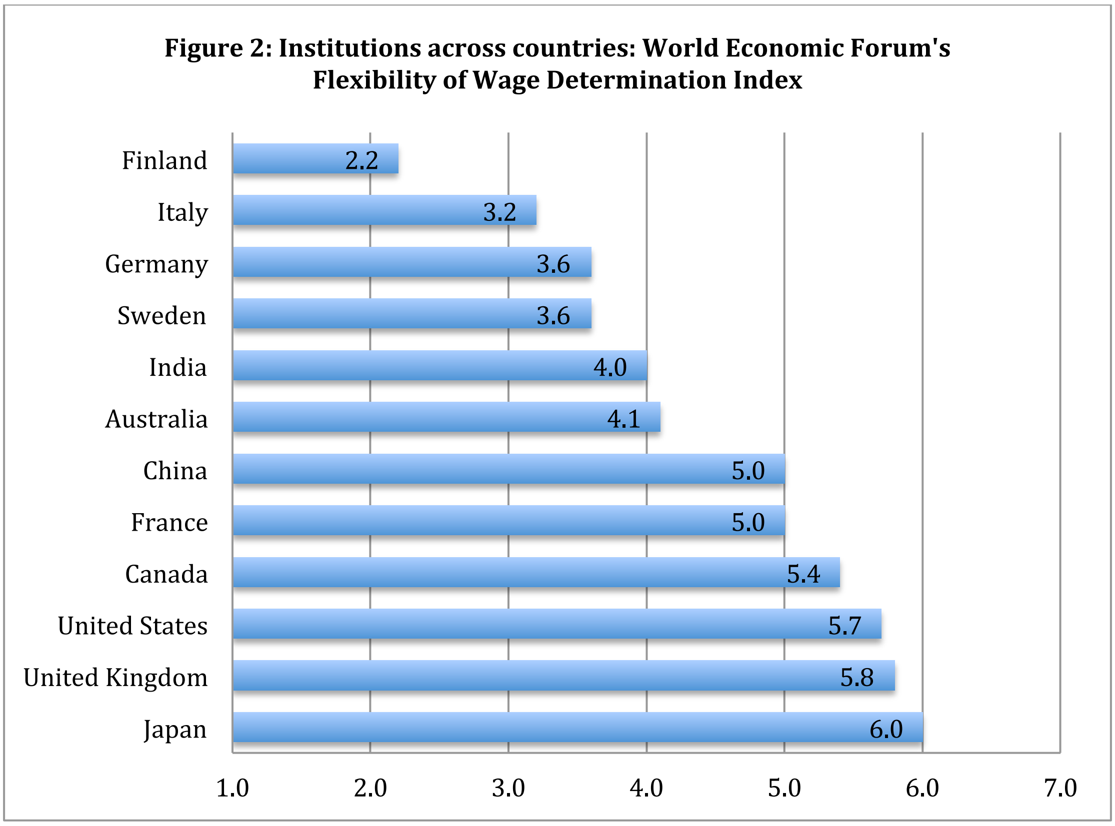
Annex: Figures



Note: The uncertainty avoidance index ranges from 0 to 100 and higher numbers indicate higher uncertainty avoidance.

Source: https://geert-hofstede.com/.



Note: The Flexibility of Wage Determination Index ranges from 1 (wages set by a centralized bargaining process) to 7 (wages set by each individual company). Source: http://reports.weforum.org/.