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PRINCIPLE-BASED PAY: ESTABLISHING A FIT

BETWEEN ORGANIZATIONAL PURPOSE AND PAY PRACTICES

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Compensation is one of the oldest moral issues. The prophets in the Old Testament condemn those who cheat workers from their wages. "Woe to him . . . Who works his neighbor without pay, and gives him no wages" (Jer. 22:13). In the Middle Ages, wages was based on a natural law notion of parity that was characterized within the natural law tradition as a "just wage." In the 19th century, David Ricardo associated wages with market wages, and Karl Marx thought the capitalist market wage would eventually cause the masses to revolt bringing down the capitalistic system. A great deal of attention over this long history has focused on the issue of fair compensation. The focus of this attention, however, has not been situated within the purpose and mission of the company. The notion of compensation was abstracted out of where it was practiced, namely the organization, and placed either in the natural forces of the market or the principles of ethical theory. What has been given little focus on this debate over pay is the context of organizational purpose where pay practices take place, and how compensation *fits* within this context. Milkovich and Newman point out that "little research has been done directly on the relationship between pay systems and the culture and values of an organization." They explain that this may stem from the ambiguity of culture and values within the organization.

Recently, Lawler, Milkovich and Newman, and others have brought the compensation issue into context with a company's strategic view. They argue that compensation within the organization cannot be understood within a vacuum. Lawler compares compensation systems within the organization "with the decisions involved in designing a building. The decision making needs to begin with the purpose of the structure--in the case of a building, what it will house; in the case of a pay structure, what type of business strategy it should support." He goes on to explain that "Without establishing strategic objectives in areas such as the kind of behaviors to be motivated, the kind of people to be attracted and retained, and the type of structure that an organization wants to operate with, it is impossible to design a reward system that adds value to the organization." Lawler and others are placing pay as an extension of a company's strategy that focuses on the fit between strategy and pay practice. In their classic article on strategic and practice fit, Miles and Snow discuss strategic fit as a process and a state. A fit between strategy and practice is an attempt to "*align* the organization with its environment and to *arrange* resources internally in support of that alignment." They argue that the "basic alignment mechanism is *strategy*, and the internal arrangements are *organization structure* and *management processes*."

Lawler's insight of connecting compensation to strategy has provided me the framework to connect compensation to the purpose of the organization. What Miles and Snow, and Lawler do not address is how the purpose of a company fit with the organizational structure and management processes, particular in our case of pay. I argue that a more basic alignment mechanism than strategy is the purpose of the organization. It is the purpose of the firm which aligns the strategy. Both the purpose and the strategy align the organization with its environment and arrange the internal organization's structures and processes accordingly (to provide goods and services according to the purpose and strategy). It is the purpose and strategy of a firm which defines the mission of a company. Of course, things are never so neat, nor are organizations (let alone individuals) ever so consistent. The perfect fit is never accomplished, but it is something to strive for. Hence, fit is in constant process.

In order to limit this paper, I will take Miles and Snow's notion of fit, but examined it in terms of the fit among purpose and structure on the topic of compensation. Purpose provides the soul of an organization, its reason for being, its end, etc. The purpose of the company should infuse and inform the various structures of the company. In many mission statements, an organization's commitment to employees is stated. From this purpose of the organization, principles can be developed to help form a compensation policy. An organization's compensation cannot be developed within a vacuum. While configured in light of the competitive environment of the market, compensation does not simply have to be determine by such an environment. An organization has to respond to the market, but its purpose can prevent it from simply being dictated by the market.

While purpose is important in all areas of an organization, it has particular significance in compensation because of the sensitivity of the issues. If an organization touts the importance of employees through slogans such as "employees are our most important resource" but then fail to as they say "put their money where their mouth is" the accusations, of inconsistency, hypocrisy, duplicity, etc. are made and are difficult to get rid of. The purpose of an organization defines and outlines a self-identity, but if the identity is not manifested in practice. A consistency must exist between purpose and practice. Through a consistency between purpose and practice, a culture develops which penetrates the psyche of all employees. The purpose is no longer just a statement but an actual sense or feel experienced within the organization.

Yet, if employees experience inconsistency between what their organization claims about them and what practices, such as compensation, it institutes, cynicism, apathy, and disdain are not far behind. By living in an institutional context where they experience contradictions and perceive manipulations, employees lose excitement about their work as well as any possibility for fulfillment. Employees perceives owners and executive managers as hypocrites. They have lost credibility as leaders, and consequently have lost employee commitment to the organization. In such cases, purpose statements do more harm than good. Common sense would indicate this would lead to poor performance. If an organization changes to a degree which misfits the purpose and compensation structures, cynicism, poor morale, and other negative effects will most likely occur. For those organizations whose purpose statements mean very little, it would be better for

them never to had a purpose statement because of the strong dose of cynicism from employees.

However, the issue here is not only of consistency, but the content of consistency. The content of consistency is equally important than the consistency itself. An organization that says its employees are means to profits, and treat them as means to profits are consistent. But the content of the consistency has serious problems. Leider claims that "people who perform most energetically, creatively, and enthusiastically are those who believe they are contributing to a purpose larger than themselves." This of course is not always true. Many profit based people are extremely motivated, and many high-idea minded people are incompetent and uncreative. But as an organization, people committed to common social goals act more as an organic unit than an organization committed to primarily monetary goals. However, the world is a funny place, and people get motivated is odd ways which make such outcomes difficult to predict. What seems not difficult to predict is the quality of life within the organization.

Purpose

Campbell and Nash provide a helpful framework to examine the overall mission of a company. They define the mission in terms of four dimensions: *purpose, strategy, values, and practices*. The *purpose* of the company defines the companies reason for existence. "Why does the company exist?" This question is answered in three primary ways which is discussed further in the paper. The *strategy* of the company is its commercial logic. How does a company manage its external competition in light of its purpose? "Strategy "links purpose with behavior." A business needs not only a philosophical rationale but also a commercial rationale. Good intentions or foundations can only take a business so far. Business' compete in a competitive market. If they fail to understand that market, they will fail as a business, no matter how noble their purposes are. The *values* of the company are a further instansiation of its purpose filtered through the competitive environment it finds itself. Values of the company are the beliefs and moral principles of the company that provide the basis of its culture. Values such as openness, cooperation, participation, quality and forgiveness will give a radically different culture than values of exclusive hierarchy, conformity, nonparticipation, quantity, and fear of reprisal. The *standards, behaviors, and practices* are the flesh of the company. How does the company actually behave? This behavior is manifested in the skills, staff, systems, style, structure.

PURPOSE

Why the Company Exists

STRATEGY VALUES

Competitive Position Beliefs and Principles

Commercial Dimensions Cultural Dimension

STANDARDS, BEHAVIORS AND PRACTICES

Policies and habits that

underpin the distinctive competence

and the value system

The goal of a company's mission is to establish a fit among the four elements of a mission's framework. Is there integrity among the four or is there an incoherence? A sense or culture of mission occurs when there is a match between the values of the organization and those of the individual. When the individual has an emotional bond of commitment to the mission. Strategy and values are the intermediate step of linking the purpose of the company with the actual practices and policies that the company does. "Purpose and strategy are empty intellectual thoughts unless they can be converted into action, into the policy and behavior guidelines that help people to decide what to do on a day-to-day basis."

There are three main rationales of a company's existence. Each of these three rationales for the purpose of an organization provides an orientation (not the actual practice) of a company's pay practice. 1) *Shareholder Purpose*: the company exist to benefit shareholders (unidimensional). A manager's responsibility is to create as much wealth for the shareholder. "All decisions are assessed against a yardstick of shareholder value. . . 'The shareholder is King.'" As the director of one company stated "All of our businesses are for sale all of the time. If anyone is prepared to pay us more than we think they are worth, we will sell. We have no attachment to any individual businesses." This approach instrumentalizes compensation to shareholder wealth--whatever compensation practice maximizes shareholder wealth is used. This may mean that employees are paid very well because by paying them well they produce more. But treating them well is not principled-based but rather it is accidental. Next year or 10 years managers may find that because of the labor market, exploiting employees may further shareholder value. This of course causes a motivational problem for employees. Why would employees be committed to higher productivity just so as to increase shareholder wealth? The answer, according to this theory, is that employee wealth is increased in tandem. The assumption here is that employees are motivated by money, and just in case they are not, they will be motivated by losing their job if they do not produce.

2. *Stakeholder Purpose*: The company exists to benefit the primary stakeholders, namely, customers, employees, community, and shareholders (multi-dimensional). Companies such as Ciba-Geigy, Monsanto, Johnson and Johnson, etc. develop mission statements that commit themselves to various stakeholders. Dist. Corp. states that it "will exercise responsibility in our dealings with all our stakeholders and in the case of conflict balance the interests of employees and shareholders on an equal basis over time." This ultimately is unsatisfactory. While it is far more preferable than the shareholder model, how does one equally order two stakeholders? Somewhere along the line, one stakeholder takes precedence over another in light of the purpose of the business. Conflict is difficult to

resolve between two equally competing interests--it often gets resolved through strikes, arbitration or closing the plant. If conflicts are to be resolved in less hostile ways among stakeholders, conflict needs to be contextualized in a larger purpose or theory of the firm. Some unifying principle has to order the conflictual claims of shareholders so as to prevent a battle of individual interests. Whether equal treatment of two stakeholders is possible, since rights among stakeholders tend to be always in conflict, the stakeholder model is still a far better model than the stockholder model.

3. *Common Good Purpose*: To avoid or at least mitigate the conflictual claims among stakeholders, the organization must have a purpose where the various stakeholders see themselves as participants for a larger purpose in which their interests are also served.

The purpose or end of the company that is beyond the collective interests of individual stakeholders. A planning director from a British company stated that "I don't get excited about making money for shareholders. I like to help businesses succeed. That's something I can get excited about. I believe our future depends on it--I don't just mean this company, it's about the future of the nation, even the international community." The planning director is articulating a vision of the common good.

The common good has been defined as "the sum total of those conditions of social living, whereby people are enabled more fully and more readily to achieve their own perfection." The common good is an organization principle which simply states that in organizing resources, the end is always the human person. Organizations have an important part in creating those conditions or structures which favor the development of the human personality, particularly in light of the products and services they produce as well as the work community they create. It is important to note that the common good is not a summation of individual stakeholder goods, but a set of social conditions the organization creates through its products and services and its internal organizational structure to facilitate personal fulfillment. The common good brings to light that the organization is a social institution whose first and foremost responsibility is the human person.

While organizations have the right to pursue their own particular interests, this cannot be done outside the common good which promotes human dignity. Organizations will pursue various interests whether in oil, circuit boards, education, housing, financial, etc., but the interest that is pursued must be directed toward creating conditions and structures which create a more humane organization and society. Organizations are an indispensable factor in creating the social conditions that develop an environment where people can achieve fulfillment. Without financial, agricultural, educational, and commercial organizations, society and those individuals within society suffer greatly. Yet, society also suffers greatly when any of these organizations decide to direct their purpose to one interest at the expense of the common good.

What an organization is for--its purpose, provides the foundation in answering what compensation is for? These questions may assault the sensibilities of the practical minded manager who may respond: "Just Do It!" or "Why Ask Why?" If such managers find

advertisement slogans good managerial thinking, then such purpose questions are superfluous. But according to some research, the failure to articulate organizational purpose leads to a reactive and eventually unprofitable future. Yet, the question is not only that one has a purpose but also the content of the purpose. I argue that if one does not believe that employees are only of instrumental value for shareholders, but rather they have inherent dignity that must be respected, four principles are essential: need, contribution, order and dignity. It is on these principles that an adequate compensation policy can be set. To keep focus, I want to address how the purpose of an organization interconnects with the pay practices of a company. I realize that a complete treatment of pay cannot be divorced from the environment and culture of an organization. What I want to do is to show the importance of a firm's purpose in providing an orientation to pay practices. Based on a common good purpose, what would the compensation of the firm look like? The rest of this paper will examine this question.

Compensation in Light of the Common Good: Four Principles

If an employee is seen as more than just an instrumental function of shareholder wealth, then the notion of compensation can be open to a principle-based determination. While the economic goals of an organization are a necessary dimension to its existence, they are not exhaustive of the purpose of an organization. In terms of compensation, there are also human and societal goals that do not eliminate but rather orders the economic goals of an organization. For example, compensation has a formative effect on both those who provide the compensation and those who receive it, as well as a formative effect on society. The hot issue of executive compensation should be analyzed not only by how it affects the bottom line or whether the market will allow it, but also by asking how does it affect the fit between fit and practice, how it effects all employees (including the executives), and how it contributes to the good of society. Compensation, both in terms of those who receive it and those who give it, must be guided by justice so as to serve society and the person.

In other words, compensation is an opportunity to practice virtue (or vice) which is an opportunity to become good (or bad). Fundamentally, people who are involved in determining compensation should be concerned about the kind of persons people become in terms of compensation. This concern is rooted in the virtue tradition which is constantly asking the human *telos* question: "What kind of person ought I become?" which serves as the basis to "What kind of organization ought we have?" and "What kind of society should we become?" To restrict the discussion of compensation to market forces misses the fundamental human question of who we are and what kind of economic community ought we become? It also fails to address that our acts are an important factor in who we are. Actions and choices shape who we are. To view compensation merely as a market force where one earns as much or as a little as one can belittles the importance of compensation in the formation of human character.

If employees are included in the purpose of the firm as a non-instrumental value, then the principles of compensation must focus on two very important questions: what is paid and how does it affect the employee and the organization? *What is paid* focuses on the actual

amount of money according to two criteria: *need* and *contribution*. People ought to be paid according to their human needs as well as according to their contribution. Figuring out what need and contribution will add to in a pay check is a complex process and riddle with various economic and noneconomic factors which we will discuss below. *How is it paid* focuses on the effects pay has on the *dignity* of those paid as well as the economic and social *order* of the organization.

The Principle of Need: The Foundation to a Just Compensation

The Judeo-Christian tradition, as well as other non-western traditions have insisted that a human person, as employee, is entitled to receive sufficient compensation to lead a human life with dignity. We call this the *Principle of Need*. Need establishes a kind of threshold. Rates of compensation for full-time employees that fall below this threshold are at least morally suspect, and probably illegitimate. The principle of need is based on the notion that the full and proper development of the human personality requires sufficient material goods for the development of the person's faculties. John A. Ryan calls this a living that serves as "the minimum amount that is due to every wage earner by the mere fact that he is a human being, with a life to maintain and a personality to develop." Because work is necessary for the preservation of one's life and the procreation and education of offspring, compensation must entail a wage commensurate with the necessary or physical character of human work. The wage contract is a way and for many *the* way of providing the necessities of human existence--to sustain workers and their families in a relatively comfortable life that includes adequate shelter, medical care, food, pension, relative security, etc.

The statistics concerning the distribution of wealth and ownership in relation to remuneration of workers in the U.S. are disheartening. John Cort notes the following:

Between 1978 and 1987 the number of *working* U.S. citizens in poverty grew by nearly two million, or 23 percent, while the number of those who work full time and still remain in poverty grew by 43 percent. Meanwhile the top one percent of our citizens grew 50 percent richer and the bottom 20 percent became eight percent poorer. In 1988 that bottom 20 percent received only 4.6 percent of the national income while the richest 20 percent received 44 percent, the lowest and highest percentages respectively since the Census Bureau first reported them in 1947.

While isolated statistics described above can be a simplistic picture to a complex problem, there seems to be general recognition that too many people who are trying to support families are not able to satisfy basic needs through their work. There are of course a fair amount of people in the US who are irresponsible in their spending habits which lead to basic needs not being met. But such over-consumption of frivolous items does not take away from the growing amount of people who are finding themselves below the poverty level and who are working (see graph in Howard Rosen's paper delivered at ND conf).

The Principle of Contribution: The Importance of Equity

The principle of need is developed from the moral dimension the employee's need for consumption. If compensation does not provide the basic needs of food, shelter, savings, familial needs, etc., something is fundamentally wrong with the system. But compensation is a complex system within a complex organization, and cannot be determined only one dimension. Another important moral dimension for determining wages is the employees productive contributions to the organization. Some employees because of effort, sacrifice, skill, training, education, experience and so forth contribute more to the organization than other employees. Compensation must be connected to the notion of "equity" that links the question of distribution to questions of production and economic growth. Equity is justified not by consumption, that is, a living wage, which is characterized by what is needed for a family to live comfortably. Equity is judged by the contribution of an employee's productivity and effort within the context of the existing amount of profits and resources of the organization. Compensation must be linked to productivity, growth, and distribution so long as the needs of the workers are provided.

That employees should receive a share in the result of their work commensurate with their contribution to that result is an ancient principle. The contributory dimension becomes part of the edifice upon the foundation of need. While placing a price tag on the employees contribution may be difficult in practice, the principle is clear and offers guidance at least in cases of extremely high compensation. Very high levels of compensation cannot be justified unless it can be reasonably shown that an employee, most likely an executive, has made a contribution commensurate with the reward.

The condition of pay according to contribution is mixed in the US. While more corporations are instituting pay for performance programs, a concentration of these programs find themselves in the upper levels of the corporation. Lawler explains that out of the *Fortune 1,000* companies--13% of the companies had no incentive pay. Of the 87% of the companies who did have incentive pay 49% had only 1% to 20% of their employees on an incentive program, and of those employees a fair majority were salespeople and upper executives.

Part of the cause of the disproportionate income distribution in U.S. organizations is that traditionally, financial incentives and bonuses such as profit sharing, stock options, and the like have remained exclusively at the top of the organizational structure. For example, in a *Conference Board* study of 491 companies it was found that 58% of them had top executive bonus plans while only 11% had employee profit sharing plans, 8% had all-employee bonuses, 3% had group productivity incentives, and less than 1% had cost-control incentives. This finding partially explains how corporate executives and upper level managers in the U.S. are the most highly paid among Western industrial countries. While in Japan the level of pay of lower ranked employees has increased faster than the level of top executives, the opposite trend is true in the U.S. For example, Chief Executive Officer (CEO) pay in the U.S. for 1986 rose 29% from 1985; whereas production and non-supervisory workers pay in the same year rose 1.8%. In 1990, the difference between a Japanese executive and an average Japanese worker pay was 17 times; whereas the U.S. CEO was paid 85 times greater than an average U.S. worker. This is up from 30 years ago when the U.S. executive pay was 42 times greater than the

average worker. This is amplified by the fact that the government reduced the maximum tax rate from 70% to 33%. Not only are CEOs getting paid more but they are getting to keep more as well.

Without canonizing Japanese organizations, it can be said that they have been able to establish a form of equity in their pay system by integrating labor and management to serve the common interests of the company. Their remunerative structure has kept salaries to levels more comparable to the work that is being done. The Japanese corporation also distributes bonuses proportionately to the employees work. The failure among U.S. companies to distribute financial incentives and rewards has led many American employees to disconnect their work from rewards of creativity, perseverance, and other characteristics associated with work (although this is changing). For example, Japanese and U.S. workers were asked in a poll who would profit from an increase of productivity and quality in the plant. Only 9% of the U.S. workers felt they would accrue the benefits compared to 93% of the Japanese. If U.S. CEOs aspire to foster enhanced organizational teamwork and a sense of corporate purpose, how can they expect to motivate the managers and workers when their own compensation is widely viewed as excessive, possibly a hundred times more than the average worker of a particular firm?

The Principle of Order: The Importance of Stability

If pay was only a matter of paying an employee according to need and contribution, the issue of pay would be simple and easy to implement. However, pay has a significant impact on the social and economic order of the firm, industry, and society. Pay has a significant effect on operating expenses and consequently revenues (although the proportional effect in many firms is decreasing). Pay also has a significant effect on employee attitudes and work behaviors which affects revenues through the quality of employees; turnover; strikes; work slowdowns; quality of employee in terms of skill and productivity, etc. Highly competitive markets make it difficult to increase pay, since passing pay increases to customers lead to higher prices which leads to decrease sales. On the other hand higher wage rates may have the opposite effect of increasing productivity and quality. Wages set too high or too low in the organization without concern of the long-term profitability both in terms of shareholder value and worker productivity can undermine the very existence of the organization. On a societal level, wages set too high or too low can have serious consequences concerning inflation, unemployment and recession. The determination of wages must be set within the economic context of both the organization and society, since undermining the economic order undermines the social and moral order.

Principle of Dignity: The Importance of Participation

What happens to the person in the process of compensation? We could conceivably have all three criteria satisfied above but still have a very inhumane compensation program. Some companies can meet the principles of need, contribution, and order, but the process of time/motion and nonparticipation causes serious problems on the development of the worker. What happens to a person in a traditional, non-participative, excessively

hierarchical organization? What if pay is simply understood as a productivity tool? Respecting the dignity of the worker would entail participation and involvement of employees in compensation plans. This would most likely lead to commitment to the plan, knowledge of the system is increased, more information is brought to bear, with participation. There are of course risks of participation such as self-interest taking over; more time; sustainability of participation; decentralization that leads to fragmentation; etc.

While it is difficult to quantify the participatory status of the workplace in the U.S., as in the section on remuneration, one study projected that approximately 60%-70% of all workers participate little if at all in the decision making of their workplaces. Even though many companies may have some form of worker participation, often only a few employees are involved. For example, the U.S. General Accounting Office reported that 70% of 476 large companies had some form of participative management; however, 70% of those companies studied had less than half of the employees involved in those programs.

Structures of Compensation in Light of Compensation Principles

The way the principles get operationalized in compensation structures will depend upon the strategic goals of the company. Principles do not simply get translated without taking the *circumstances* of the environment seriously. Principles have a flexibility to them to adopt to various structures, competitive environments, and organizational cultures. In terms of pay, there are five fundamental structures that principles will find themselves engaged with: *base pay, benefits, pay for performance, market and process*. Companies will also find both limits and opportunities concerning pay depending on the competitive environment they find themselves in. For example, competitive environments are influenced by the industry a company is in. Based on the industry (hi-tech, manufacturing, service, nonprofit, etc) and the strategy taken affects the ways principles are carried out. For example, some companies may choose to higher variable pay that other companies because of the competitive, low profit margin industry it is in. But this does not mean that principles are infinitely flexible. One has to very careful to respect the integrity of the principles and avoid the rationalizations that reduce principles to window dressing. Again, this is where a misfit occurs between purpose and practice that serves as a recipe for cynicism.

Below is a matrix that summarizes the engagement of pay structures and pay principles. Due to space and time, I will only discuss those boxes that are bolded.

Pay Structure Need Contribution Order Dignity

<i>Base Pay</i>	Living Wage	Skills/Knowledge	Input/output	
<i>Benefits</i>	Health/Security	Rights	Stability	
<i>Performance</i>	Initiative	Effort, Talent	Flexibility	Creativity
<i>Process</i>	Belonging	Information	Hierarchy	Participation
<i>Market</i>	Regulations	Excellence	Competition	Freedom

1. *Base Pay*: Lawler points out that base pay is determined on the nature of the job performed and/or the person who performs the job (skill and knowledge based). Those companies who pay on the basis of the job performed evaluate each particular job on a point-factor system. It starts by describing the activities of every job. Each job is given a point value on the basis of work factors such as experience needed, problem solving ability, training and knowledge, accountability demanded. The higher the point value for the job, the higher the pay. Many organizations choose this form of base pay because "it facilitates making comparisons to what other organizations are paying." Job-based pay also guarantees a high degree of internal pay equality within the firm itself by having a quasi-quantified pay system on jobs.

Increasingly, however, companies are turning to "skill-based pay." Skill-based pay is used in 40% of *Fortune* 1000 firms, although only a small percentage of the workforce are able to participate in the program. Skill-based pay is most commonly used in R&D departments and skilled trades. There are three kinds of skills: vertical (managerial), horizontal (trade), and depth (technicians). Individuals are paid for the number, kind, and depth of skills that they develop and utilize. The kind of skill development must be linked to how it will serve the strategy of the organization. The advantages of skill-based pay over job-based pay is flexibility, employee control over compensation, reinforces that employees are really the most important factor in the organization, and encourages self-management.

Whether one uses job or skill based pay will be heavily determined by the strategic perspective of the company. Lawler does a good job of explaining what base pay, that is, job-base or skill-based fits one's strategic outlook. But a company's strategic outlook will not guarantee, by itself, that the base pay will be adequate to meet the needs of the employee. For Lawler, low base pay is problematic not because it violates the inherent dignity of the employee. Rather, low base pay "can cause significant problems in recruiting and retaining the best and the brightest individuals. It can also lead to an internal culture of low esteem and to feelings that the organization in general is second

best and lacks the resources to do a first-rate job." The question in such reasoning is what happens when low base pay is strategically advantageous at a rate that fails to meet the "needs" of employees, such as in a flooded labor market, or when, as Lawler himself notes, "human performance is not a major determinant of organizational performance"? His primary focus is that pay should be strategy and market driven. It is precisely here that we see the weakness of only a strategic approach, since employee pay becomes instrumental to strategic interests, rather than instrumental to the need and dignity of the employee.

Employee pay cannot be isolated by corporate strategy, but it cannot be totally determined by it either. A certain tension will always exist between the good of the employee and the good corporate strategy, but if corporate strategy is the dominant paradigm in which compensation is determined, then employees become instrumentalized to the competitive interests of the firm. Depending upon how the complete pay structure is developed, at the very minimum, one's base pay should meet basic human needs, that is, a living wage.

In rare circumstances, an employer might be released from the obligation to pay a living wage if the resources were truly not available to do so. More frequently, an employer might be released from the obligation to compensate in accordance with contribution as a result of insufficient resources. This might occur in times of crisis, whether general or specific to a business or industry, or when a business is starting out or expanding significantly. Ordinarily, though, the employer would be obligated later to compensate employees for their sacrifice when resources become available through stock for example. It would not be the case, however, that employees could be rightly denied their living wages so that resources could be used to reward executives.

This discussion is not deny that executives should earn more because of the importance of their talent and decision making abilities. But as Michael Novak points out, most of the high compensatory rewards

do not go to inventors or discoverers, but rather to managers of large corporate enterprises, of which top managers are only small, if crucial, parts. There is something supremely social in their achievements. What they did, they did not do alone. Their achievements rest upon the intelligence, enterprise and creativity of many others in their firms--and upon the social system (the U.S. political economy) that make their efforts possible. It is wrong to award them as if they were Lone Rangers."

Or as Dean McFarlin points out, "company performance rarely, if ever, hangs on the work of just one individual [or a couple for that matter]."

When employees become more educated and skilled, they will want to tend to express their opinion more, which because of their increased education and skill will be a more competent and worthy counsel. Because of their information, employees become more valuable to the company, creating a more reasonable proportion of value to the hierarchy of talent on which base pay can be determined. While the decisions of executive management is still important and valuable, they become more dependent and linked to the decisions and counsel of those within the organization. Hence, the argument that executive management are worth their pay of 100 times than their employees become less plausible. If employees become more skilled and train, the value of their work becomes a more important contribution to the health and wealth of the firm; hence, the value of each member of the firm in terms of financial success becomes less disproportionate than in a company that reflects a Taylorian split where talent, skill and information is relegated to management. Where possible then, organizations would better serve the principle of need (as well as contribution) if base pay could be linked to appropriate skill and training.

2. *Benefits:* Benefits within the organization has become extremely complex as well as expensive. Sheppeck and Schechter list over 50 items of benefits in their survey on compensation. Benefits account for an increasing portion of the total compensation. One survey indicated that benefits went from 24.7% of total compensation in 1959 to 41.4% in 1980 (Wallace and Fay). For the purposes of this paper, benefits are restricted to medical, pension, and short-term disability.

Benefits serve a dual role which in most cases can be complementary but others contradictory. The dual role as with base salary is that 1) benefits are used to attract and retain employees, and 2) they serve as a safety net for employees. In attracting and retaining employees, companies will increase or decrease benefits in light of the competitive market. How successful human resource managers are in attracting and retaining employees will depend on their strategy and astute reading of the market. Lawler points out that a company strategy that calls for a stable group of employees, concern for employees and fixed labor costs will result in more benefits. However, a company that calls for "short-term employment relationships, flexible labor costs, high levels of entrepreneurial behavior, and large amounts of pay at risk" will result in less benefits.

Lawler's strategic approach is insightful and helpful, but there are serious limits to it from the purposeful perspective I have adopted in this paper. Benefits should not only be driven by strategic considerations but also and more fundamentally it should be need driven particularly in the key areas of pension, health and life insurance, and short-term disability. For example, Lawler points out that Apple has no retirement plan since it does not want to recruit security oriented people. Because of Apple's entrepreneurial spirit, its strategic view of benefits is to avoid security minded employees. Lawler points out that one technology company he knew of "had no benefit plans because it did not want employees to stay with the organization; it wanted turnover so that it could hire new graduates who would know the latest technologies." It is here that strategy becomes problematic precisely because it violates the principle of need. There is nothing wrong with wanting the newest techniques and technology; however, the means of firing people

or not providing a basic need such as a pension instrumentalizes the relationship between employer and employee which violates the dignity of employee. There are other alternatives for innovation besides fostering high turn-over. such as training the employees in the newest technology.

It is precisely here that strategy needs to be countered by purpose and values. The purpose of the company will hopefully value the employee enough not to execute their strategy at the expense of the basic need of security. One of area of benefits where the needs of the employee and the strategy of the company can coalesce is Employee Stock Option Plans (ESOPs). ESOPs are defined as qualified retirement plans. A trust is established where a company contributes either as a contribution or through a profit sharing plan or borrows money which is converted into stock. That stock is, in turn, held under the names of the individual employees. When employees retire, they usually sell their stock back to the ESOP which new employees can then purchase. Currently, approximately 8,000-10,000 U.S. firms and 8-10 million workers are involved in ESOPs. This represents a twenty-fold increase over the last ten years. If this rate growth continues, 25% of the workers in the U.S. by the year 2000 will have some direct ownership in their firms.

The various tax benefits granted by Congress since 1974 to encourage ESOPs have been a major impetus behind its success. Congress has created a tax structure which removes obstacles and makes it easier for all workers to become part owners of their workplace. Government provides tax breaks to financial institutions which loan organizations the capital to establish a trust. For example, not only are the principal payments deductible for the organization, but so is 50% of the interest income received by the bank. This has caused loans to ESOPs to jump from \$1.2 billion in 1986 to \$18 billion in 1989. Government also provides tax incentives to the organization by allowing companies to deduct the dividend payments on the stock held by an ESOP. Because of these tax breaks, employees often receive stock at a discount.

Strategically, ESOPs may serve the company well, but its existence in a company needs a wider rationale to serve the overall purpose of the company. For example, 85% of private ESOPs prohibit employees from voting with other stockholders unless the issue voted on concerns selling, liquidating, moving, or merging the company--a stockholder right which cannot be legally restricted in ESOPs. Furthermore, the administrators of the trust established by the ESOP are appointed not by the workers but management. As a result, their decisions may tend to serve the interests of management. If ESOPs are to serve their function of providing the needs of security for an employee, it has to be viewed in larger terms than strategy.

ESOPs also tend to create more order within the company.have achieved positive results, although serious problems remain. W.L. Gore and Associates, Levi Strauss, Harley-Davidson, Polaroid, Avis, Quadgraphics, Weirton Steel, and others have reported better relations among workers and managers, as well as increased productivity and quality. As a deferred plan, ESOPs tend to build commitment among the workforce--employee stability and longevity. This can also contribute to the employees understanding of the

business. In ESOPs, profits are poured back into the organization to make it stronger and more competitive by continual modernization, research and development, human resource development, and so forth. This in turn contributes to the economic order and success of the enterprise through long-term capital investment. Contributing to the economic order as owners, workers and CEOs have a long-term vested interest unlike some investors who strategically look for short-term gain. Workers and managers tend to prevent short-term minded hostile takeovers that attempt to cash in on companies with one time strikes in stock price. This in turn contributes to the economic order of society.

3. *Pay for Performance*: Performance pay can take place on 3 levels: 1) individual (merit pay, bonuses, executive stock options, etc.), 2) team and/or departmental (gainsharing), 3) divisional or organizational (profit sharing, stock ownership--ESOPs). These levels and their corresponding programs are variable pay elements which depend on the performance of the individual, group, division, and firm. These programs again serve a dual role: to attract and retain high performers and to reward employees for their effort, talent, and sacrifice which I called above the principle of contribution.

Rewarding employees on the basis of contribution can facilitate a more equitable compensation system within an organization. One way of building equity into the pay structure of an organization today is through profit sharing and gainsharing. The two plans are different in that they vary on what criteria is the basis for the rewards. Profit sharing is based on the improved profitability of the firm, that is, the company pays the employee a percentage of any residual profits. This form of compensation became somewhat popular in the 1950s and 1960s when many organizations experienced unprecedented growth and perceived that profits would continue year after year. Profit sharing was considered a good idea for two reasons: 1) it distributed profits fairly by sharing them with everyone who contributed; 2) it was considered a good incentive to motivate employees. Profits, however, did not increase year after year, which became a major problem with profit sharing. After receiving a couple of profit sharing bonuses, employees began to expect the bonuses. However, when profits as well as the bonuses shrank, employees who worked hard but received no reward became disgruntled and eventually lost interests in furthering productivity. External factors such as economic climate, government regulation or deregulation, tougher competition, bad debt expense, depreciation procedures, and so forth affected the organization's profitability. These external factors are clearly outside the control of the worker. In profit sharing plans, then, the link between worker productivity and corporate profits is not always direct.

Profit sharing has a large system orientation that is described as a "total system incentive approach" since it links motivation and reward to profits. It either rewards or penalizes the whole organization in its relation to profitability. Profit sharing can function effectively as a long-term plan and incentive so long as adequate information on a frequent basis is provided to inform the employee of the financial status of the company. If employees are honestly informed as well as included as active participants of the organization, most likely they will feel apart of the firm and be concerned about the long-term profitability and viability of the firm. If they are not informed they will most likely only be concerned about the size of the check they receive. Profit sharing also needs to be

complemented by a short-term plan that measures the immediate effects of productivity and reward. That plan is gainsharing.

Gainsharing is based on the improved productivity of the individual worker or work team. Profits and productivity are not always increased in tandem, thus, gainsharing establishes a direct connection between worker productivity, and wages and bonuses. It is based on a formula which connects increased productivity of the individual or team to increased bonuses, independent of the company's performance. In short, gainsharing rewards those who make the improvements. It employs clear and concise criteria so employees have no doubt what they have to do to receive bonuses. Such criteria are four-fold: 1) increased final output; 2) decreased scrap; 3) increased quality; 4) decreased cost of labor.

Usually gainsharing bonuses are rewarded on the basis of team effort. This has proven effective because organizations have placed financial incentives and rewards to the lowest level of the organization. Gainsharing bonuses, unlike profit sharing, are allocated quarterly and sometimes monthly to reinforce behavior with reward. This connection between performance and financial reward has increased worker awareness of the financial situation of the company. Sharing such information with its employees often has a domino effect upon participation in other areas of the organization, and has flattened the organization's power and informational structure, by sharing the decision making and information with its employees. The Scanlon plan, the oldest and most popular gainsharing plan, originated in the 1930s when Joseph Scanlon, a local union president, attempted to prevent the shut down and massive layoffs of a steel mill. The Scanlon plan rests on the idea that participation in, and improvement of the firm must be financially rewarded if participation and improvement are to be sustained. Rewarding those who improve the organization is also the just thing to do. The Scanlon plan has been used as a framework for labor/management relations. It provides a context in which a common objective, organizational effectiveness, is achieved by participation as well as by compensation for achieving effectiveness. The Scanlon plan would define the costs of production in a given month, and if there were a savings, workers would receive a percentage of it. Today, the Scanlon plan distributes approximately 75% of corporate gains to employees and the other 25% to the organization. It is important to note the fundamental importance of participation and trust needed to have an effective gainsharing program. If workers are to improve the effectiveness of the organization, they need to be informed as to its workings, and must trust management to reward their work. In order to build this trust, the practice of equity needs to pervade the firm. This means the absence of executive dining rooms, special parking lots, executive health clubs, and so forth. Although they may be small gestures, and problematic in certain cases, they can in a small way symbolize the equitable nature of an organization.

Currently the Scanlon plan is in effect at Herman Miller, an office furniture manufacturer, where employees negotiate with management to determine goals in four areas: 1) customer service; 2) effective use of money; 3) effective use of materials; 4) effective use of labor. Once the workers exceed their goals they receive bonuses. The company spends one day a month informing the employees on the status of productivity,

profits, and employee suggestions. It also provides an ESOP as well as relatively strong job security. At Herman Miller, gainsharing is not merely a financial tool to motivate workers, but a way of working. Power and authority derive not from seniority or arbitrariness but from competence, knowledge, and skill. The implementation of a gainsharing program can help distribute compensation more equitably by distributing incentives, profits, information, and competence in their work. Herman Miller's wage structure provides incentives for workers to broaden their skills and knowledge and not only to accumulate more money. The dignity of work grows more out of workers' professional skills than out of the capital goods they attain from work. It is interesting to note that at Herman Miller, the gap in pay distribution among all employees cannot exceed twenty to one. That is, the highest paid employee, usually the CEO, cannot be paid more than twenty times the pre-tax income of its manufacturing employees.

A serious danger to employee needs, however, exists if pay is reduced only to performance. Certain theorists and consultants want to base wages and salaries entirely on the performance of productivity, efficiency, and profitability--a Taylorism revisited. For example, Boyett and Conn's book, *Workplace 2000*, implies that employees can be stripped of all benefits such as medical insurance, pension benefits, and the like so as to make the company "lean and mean." To reduce pay to compensation for productivity is to reduce the employee to an economic agent. Placing so much emphasis on productivity can also lead to employee burnout. In turn, this can pressure workers to unethical activities. Again a principle approach is needed to balance a purely strategic approach that can be determined by the competitive environment. Workers have fundamental rights when it comes to remuneration, namely, a family wage, which includes benefits such as medical insurance, short-term disability, and pension benefits. Employers have a duty of justice to do everything in their power to meet these needs.

4. *Process*: What are the processes used to design and operate a pay system? The process of compensation defines how pay is determined. Employee participation serves a dual role: a) *Expediency*: Involvement of the employees in compensation plans increases commitment, knowledge, and clarity to the plan which increases the successful execution of the plan. As Lawler points out a compensation plan cannot work simply "because it has the 'right' objective characteristics." Employee negativism over compensation occurs among employees often when they have been left out of the process of determining their pay even when they receive fair compensation. Of course, as Lawler points out, expediency is not always guaranteed. There are risks to participation such as self-interest, more time, sustainability of participation, and decentralization that leads to fragmentation.

According to Lawler, the issue of participation is determined largely by the strategic philosophy taken by the company, although Lawler himself seems to prefer less centralization and more participation. What does not get discussed in Lawler or for any compensation theorists for that matter is the formative role of participation. b) *Formation*: Participation is not only a matter of expediency, but it is also a necessary condition to the formation of human character and organizational community. also something fundamental to human nature. Many articles and textbooks understand participation only

in its strategic role as productivity and quality techniques. Very little attention is given to the formative importance of participation. As one Introduction to Business text states: "Although participative management does improve human relations, its major value is in improving productivity and quality while reducing costs." What is ironic about such a statement is that once the formative or moral dimension of human relations becomes subservient or secondary to the strategic or productivity dimension of participation, participation programs become perceived by employees as forms of manipulation which undermine the very effectiveness that originally was the case. Once productivity is considered the primary value for employee participation, participation becomes ineffective, since those involved see themselves as manipulating or being manipulated to corporate strategy. While employees must be productive and profitable and serve corporate strategy, it does not follow that participation ought to be understood simply as a means to enhance productivity. Participation is fundamentally an issue of being treated with dignity. Organizations that treat employees as ends in themselves ultimately attract and keep more employees and "win out on the bottom line" (Soloman). A strategy unrooted from principles has a detrimental effect on the process issue, since it is difficult to establish trust when employees are instrumentalized in relationship to the strategy that is simply economic.

Even though participation has a formative role in the human personality, participation has to be differentiated. One must first define the various degrees of participation and the limits to participation. As with all rights, there are limitations. Most employees do not enjoy the privilege of some CEOs who get to pick their compensation committees. Rather, there are degrees of participation that depending upon the industry, culture, and situation may be deemed appropriate. But to argue that employees should have no participation because it is not conducive to corporate strategy in determining compensation is failing to recognize the formative dimensions of participation.

Degrees of Participation

Shop Floor Managerial Executive

Joint Decisions			X
Consultation	X	X	X
Information	X	X	X

No Participation			
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According to the chart above, I have restricted shop floor and management participation on the process of pay to consultation and information. While information and consultation may lead to joint decisions, the final say on compensation does not rest with shop floor and management employees. All employees should have adequate information to how pay is determined. This may be seen as an innocuous point, but there is much debate over whether compensation systems should be secret or open (see Lawler, 17ff, and Wallace and Fay, 221ff). While many reasons exist why a company would keep its compensation information secret, a key reason is to hide inequity or at least perceptions of inequity. At minimum, information concerning pay ranges, job classification, and pay-increase budgets should be disclosed (see Lawler, 285).

Concerning consultation, Lawler provides some very helpful structures to involve employees. One in particular is the "diagonal slice task forces" which is made up of individuals from all levels and departments. In order for the task force to be effective Lawler points 4 essentials:

1. Individuals on the task force need to be opinion leaders who are credible with the rest of the organization so that "other employees feel that their interests have been well and fairly represented.

2. Provide a team building orientation for all task force members. Since pay related issues tends to bring out self-interest in a way that no other issue can, team approach within a task force is imperative.

3. Provide an substantive and extensive education on compensation systems. While this may be time consuming, in the long-run it is usually worth it.

4. Be sure to define the limits of the task force. This has two dimensions to it: a) Participation in the task force represent the degree of consultation not joint decision making. b) The task force should be informed of areas that are off limits and unacceptable by senior management. There is a serious

danger with consultation as a form of participation when senior management have issues decided before the consultation takes place.

Organizations also should provide avenues for due process where employees are allowed oppose and challenge performance reviews.

5. *Market Comparisons*: Market forces have always had a determining affect, both positive and negative, on levels of compensation. Market position addresses how a firm pays in comparison with other companies. Compensation must be determined in part by the market a company participates in order to remain competitive. Problems exist in paying below or above market wages. When compensation is above the market, the company finds itself at a competitive disadvantage of having high labor costs. Highly competitive markets make it difficult to increase pay, since passing pay increases to customers lead to higher prices which leads to decrease sales. Yet, higher wage rates may have the opposite effect. Organizations with higher pay rates tend to have more productive workers which in turn increase profits. "The improved productivity comes from three sources: reduced supervision costs, decreased turnover, and improved satisfaction and loyalty to the organization." If companies pay below market wages, they tend to lose their best people first which leads to short-term savings but long-term disaster.

Market comparisons tend to hold in check compensation decreasing to a point where workers are adversely affected and increasing to a point where customers and shareholders are adversely affected. But markets are not perfect mechanisms despite what certain economists say. Witness the obscene pay of some executives as well as the dismal pay of many teachers. Sometimes markets need to be challenged by certain organizations in which the organization becomes a leader in the market. Yet as a leader, the organization must be guided by principles that would impel them to risk in such a leadership role. The principles of need and order serve as a corrective in examining the market comparisons. And when organizations are unable or unwilling to lead in these areas, government has the responsibility regulate their activities.

Conclusion

While I have been particularly critical of Edward Lawler's book *Strategic Pay*, my criticisms should not underplay my great respect for Lawler's work and his project of better connecting compensation and strategy. My point throughout this paper is not a rejection of this connection but rather to further it so that compensation is also connected to the purpose of the company. Divorcing purpose from strategic principles in compensation practices is just as problematic as divorcing strategy from compensation. I have argued that strategy alone is inadequate since by itself strategy can easily violate the basic principles that connect pay to organizational purpose understood in terms of the common good. What happens to a person in a traditional, non-participative, excessively hierarchical organization? Is there something fundamentally problematic with a strategy

that is based in such a framework? And does the problem rest in terms of its purpose as a company? These are normative questions that cannot be answered only by a strategic view, but rather with a view of purpose.

What we have not examined in this paper, but which is essential to any connection of purpose and compensation, is virtue. Virtue is the implementation of the habitual action ordered to a good end. While the principles of good compensation illuminate what the end of compensation is, the virtues of justice, diligence, solidarity, honesty, courage, etc. bring us to attain such an end. In the pursuit of virtue toward the end of compensation, we not only transform society, but we transform ourselves. CEOs as well as all employees cannot view their compensation as something distinct from their own character, particularly the CEO who has more say in the termination of compensation in the organization. They must take seriously that compensation is an important part of the organizational and individual character.

Endnotes

Mick,

Attached is the paper. As you will see, it is a tad rough, and a tad long. As someone once said, "If I had more time, I would write less." Some parts need condensing and others need expansion. I look forward to your comments. Talk to you soon.

I take Lawler's insight of connecting strategy with compensation two steps further: 1) connect strategy to mission where you have a three item integration and 2) that the mission be evaluated normatively and not merely descriptively. The 4 principles of need, contribution, order and dignity are what I see to be the normative principles necessary for a adequate mission that must be incorporated into a compensation program that view the worker not simply as a means to a strategic end but

Lawler's fictitious company called Acme serves as a good example. He describes of a nonparticipative culture: does this present problems of looking at ESOPs merely as financial techniques. While the strategy of Acme indicates a nonparticipative approach, is this acceptable. There is a tension between a descriptive and normative view here. (Lawler 248-249). What happens to the employees at Acme? What is the mission of Acme? As in the case of Acme, a strategic contextualization of compensation tends to be capital driven at the expense of considering the human worker. This sometimes occurs

from the initial separation of a strategy from a company's mission or it occurs because the mission of a company is simply financially driven. The latter may be the case with Acme.

2. Virtue: end and mean.

3. Intermediate: stems from strategy which will differ from industry to industry (hi-tech, manufacturing, service, nonprofit, etc) This is where the differences between Hi Tech (which looks like EMD) and Acme begin to differ which will affect the structures and processes of compensation.

Lawler points out that compensation levels "must be driven by the kind of business an organization is in and the kind of management style it decides to adopt" (201). Management style stems from the mission and philosophy of the organization. paying the person (or skill and knowledge-base) vs the job. Principle of contribution is well served in paying the person, but if skill and knowledge base pay is not appropriate because of the industry, then other ways in the arena of pay for performance may be better. (need driven

However, this principle of contribution may be qualified at times by two additional factors: scarcity of resources and level of risk.

CONCLUSION: The Virtuous HR Manager

The integration of strategic and compensation principles provides the basis for prudential judgments in terms of compensation. But strategy does not provide the ends and purposes of an organization. This comes from the purpose of the organization. I have argued that if the organization avoids the instrumental relationship with employees, they

The principles of need, contribution, order and dignity define the end of compensation, that is, what is compensation for. In order for this end to get operationalized the company must have virtuous managers who desire this end and know how to implement the end. That is, they need to both just and prudent. They need to desire the end as well as know the means necessary to implement the end.

TWO PROBLEMS:

- a. Strategic principles alone tends toward a pragmatism which depersonalizes employees

- b. Compensation principles alone fail to take seriously the concrete situation and toward absolutizing concrete programs such as gainsharing, skill based pay, etc.

Problems of reducing wages to simply strategy:

DIFFERENT STRATEGIES: (Lawler 220)

- A. Entrepreneurial: high at risk comp.
- B. Participative/egalitarian: homogeneous approach, many choice
- C. Hierarchical/large/in many businesses: mix of compensation vary by level, function type of org., line of business, limited choices.
 - a. Mission and strategy may be different:
 - b. Strategy tends to be technical minded and economically driven--this tends to reduce employees to units of costs.

I. Generic Connections:

Mission/ Strategy/ Compensation: Different scenarios

1. Lawler's: inconsistency among strategy and compensation
2. Inconsistency between mission and strategy which leads to inconsistency between mission and compensation. (it is unlikely if strategy and mission are inconsistent that the link between mission and comp will be made). See Rosenbach on mission and strategy.

II. Normative Connections:

1. Socio-economic vs economic driven mission statement

a. Acme economic driven strategic view (Lawler 253-254): equity is not discussed in so-called economic driven systems--it is whatever the competitive market provides--if its 5 to 150 times more than production workers so be it.

Lawler is not interested in challenging Acme economically driven mission/strategic view. He is not interested in normative analysis, but rather a consistency of process between strategic and compensation. The only normative view he is holding is that there is a consistency between the two; however, he does not make a judgment on kind of consistency is maintained; hence, one is given Acme (nonparticipative, economic strategy) and Hi tech international (participative, socio-economic driven) which are considered adequate because their strategy drives their compensation system. Although he does wish to incorporate more participation and equity into Acme than its strategy and mission indicate (see pg 257)

Lawler's insight cannot be lost, namely, the connection between strategy and compensation. A mission of company is insufficient to drive a compensation policy, since mission statements lacks the specificity necessary to understand the particular situation which makes necessary the appropriate comp program. Lawler is very helpful on this point. Throughout his book he makes the point that comp programs must flexible to fit the particular situations. Lawler exudes a high level of practical wisdom. Programs and approaches are not always transferable to different situations no matter how good and ethical they sound. For skill based pay will not work in a non-skilled job (although some creative thinking may be done which can redesign nonskill jobs to skill jobs). It is precisely strategy that takes such situations into consideration.

The danger of Lawler's approach however is that he may at times be adapting to situations that are less than fully human.

Other human resource managers may answer the question from a market perspective: "the purpose of compensation is defined as that which assists in attracting, rewarding, retaining, and motivating high-caliber employees within the confines of current market rates." It is often argued that high ranking executives are paid 100-200 times more than

their employees because it takes that to retain their highly skilled services. While a certain element of truth exists in such a statement, although challenged by many according to degree, the statement is based on a particular notion of what compensation is for, namely, what benefits the tasks and goals of an organization. This is an important, however, limited goal. Many organizations define themselves not only in market terms but also in terms of purpose that go beyond market factors.

From a strictly market or organizational view point, It is often argued that high ranking executives are paid 100-200 times more than their employees because it takes that to retain their highly skilled services. While a certain element of truth exists in such a statement, although challenged by many according to degree, the statement is based on a particular notion of what compensation is for, namely, what benefits the tasks and goals of an organization. This is an important, however, limited goal.

From this point of view compensation is about motivation and nothing more. For example then, New Product Development Professionals are probably not motivated by extrinsic rewards as they are by intrinsic rewards (the satisfaction of seeing a product come to market and succeed). Now, if compensation was merely about motivation, we would stop there. Although I must say, I do not know many who are totally intrinsically motivated.

II. PRINCIPLE BASED

But compensation is more than just motivation, it is also about CONTRIBUTION (justice and equity). (as well as need, economic order in the organization and society, personal character)

Here compensation is understood not as incentives but as dividends. Contribution in relation to the equity provided.

The term "equity" to "justice" to tie the discussion of compensation more directly to its source, namely, what portion of the whole has been received in relation to the contribution of the worker. A wage based on "justice and equity" should derive not only from consumptive needs (commutative justice), but also from how the worker has

contributed to the expansion of these economies, namely, what equity have they contributed.

Equity is related to prudence to emphasize the concrete application of justice. Equity functions as a tool to evaluate the situation so as to bring out a fuller form of justice. Equity recognizes the dynamic change in an economy that is evaluated before justice can be applied, such as economic growth. The principles of justice are universally valid and true, but their degree of applicability to concrete cases cannot be determined without reference to the quantity and quality of available resources. Hence, his use of equity is an attempt to discover a more equitable distribution in reference to the specific amount to be distributed. In other words, how big is the pie, and does the slice correspond to each workers' contribution according to the available resources.

III. TEAM-WORK COMPENSATION:

Group incentive plans are defined as any variable pay program where dollars are awarded to employees based on the results of the unit to which they belong. This includes gainsharing programs, team incentives, and project-based incentives. Excluded from this definition are profit-sharing, special recognition awards, individual incentive plans and equity-based plans.

IV. GAINSHARING

4. Formula is not enough: *The authors of the book point out that a formula system is insufficient by itself.* For a team compensation program to work, an organization must have a culture that is characterized by

1. A Philosophy of Cooperation

2. An Involvement and Participation System

3. A Sense of Justice in terms of one's contribution.

In other words, virtues and principles.

Doyle and Doyle point this out in their book *GainManagement*. (Three steps 1. GainPlanning; 2. GainMaking 3. GainSharing; too much focus on #3 and not enough on 1 and 2 will undermine the whole enterprise.

VI. BENEFITS

Usually gainsharing bonuses are rewarded on the basis of team effort. This has proven effective because organizations have placed financial incentives and rewards to the lowest level of the organization. Gainsharing bonuses, unlike profit sharing, are allocated quarterly and sometimes monthly to reinforce behavior with reward. Sharing such information with its employees often has a domino effect upon participation in other areas of the organization, and has flattened the organization's power and informational structure, by sharing the decision making and information with its employees.

What is compensation for? Point out positives here (one needs to understand the industry (is it cyclical), the type of work, motivation,. Also point out shortfalls. Compensation also needs to be brought into context of a company's mission statement

"Relatively few organizations have done a good job of developing and stating core values, but those that have profited handsomely from doing so." (Lawler, 40)

In articulating the 4 principles give examples where companies comply with the principles see Milkovich and Newman, 18,

use image of body and soul. Integral relationship among compensation principles, compensation strategy, and compensation practices. What is the fit among the three? (see Mick and Phil in benchmarking project). Principles inform the strategy by placing limits on the economic pressures of the strategy as well as by infusing the strategy with a soul, with social meaning, etc. Strategy informs principles by concretizing their abstractness. See Robin and Riedenbach.

ORGANIZATIONAL PURPOSE

COMPENSATION PRINCIPLES

(these principles are extrapolated from the mission statement discussion of employees largely, but also customers, shareholders, etc.)

H/R COMPENSATION STRATEGY

What pay will meet the organization's strategy (e.g. variable pay). (see 3 types from Mick and Phil)

PAY STRUCTURES AND PRACTICES

Mission

Compensation Principles

Compensation Practices

Cases:

Conclusion: it must be more than strategic

Part I

1. Mission Statement: (Normative--base it on the 3 goods of management) (Nature of the organization, which includes personal and social presuppositions. (Workplace community; serve the community, return to shareholders

2. Strategy:

3. Relationship between mission and strategy

Part II

1. Compensation:

2. Relationship to Strategy

3. Relationship to Mission

4. Integration of Mission, Strategy, and Compensation.

("Allowing autonomy without ensuring that some team members have these skills is as foolish as training employees in them and then managing in a traditional, top-down way that does not use the skills." (Lawler, 156)

Conclusion: Possible misfit between I and II. again recipe for cynicism and poor morale.

% of variable pay to overall pay should not violate the principle of need. Distribution of programs: broadly distributed vs narrowly distributed vs a mix distribution.

It is sometimes argued that increased stock ownership by executives will result in better management and thus enhance corporate performance. A recent study reported in the *Wall Street Journal*, however, suggests strongly that significant stock ownership by executives has little effect on the economic order and health of the company. On the contrary, compared to companies where employees own more than 10% of the stock do far better. What may not be true of executive ownership may indeed be true if ownership is more broadly distributed, which would be quite consistent with Catholic social thought. (*Wall Street Journal* 23 March 1993, p 1.

Different levels of the organization: at lower levels gainsharing should provide higher payouts whereas higher in the organization profit sharing should provide higher payouts (note here the importance of understanding the hierarchy of the organization). See Lawler pg 130. "If a heavy commitment is made to gainsharing, profit sharing, and ownership, considerable education, communication, and power sharing need to occur in order for many of the potential advantages to be realized. . . . to be effective, paying for organizational performance must be more than a pay approach; it must be combined with a congruent management system." (131)

Problems: How to avoid the problems in the practices. INCENTIVE: Dividing workforce between incentive and nonincentive workers, costs, limiting behaviors, poor culture, (Lawler 61). These problems are acute when the performance or incentive is only economic--when performance and incentive are divorced from mission of the organization. MERIT: objective measurements of performance, given individually in team disrupts cooperation, and causes quality problems (Lawler, 77), rewarding individually increases competition and diverts from organizational systems such as information systems. Mistrust of the way rewards are allocated.

Lawler points out that when "jobs are designed such that people can do a whole piece of work, have responsibility for performing that task, and get feedback on the task, intrinsic motivation to perform is high." (93) The whole piece of work is key for appraisal

Example companies: Lincoln Electric, Herman Miller, Motorola, Nucor Steel, Chaparral Steel (Lawler 108)

Pay on the basis of organizational performance (Lawler, 193).--incentive pay or profit sharing.

Compensation at Risk based on performance: the cost flexibility of the total compensation, it can help focus individuals on organizational performance, and it fosters an entrepreneurial, performance-oriented culture." (Lawler 205) At risk compensation should probably be at a larger % on top. "The pay levels for these lower jobs are typically close to the minimum amount of money needed to maintain an acceptable life-style." (Lawler, 212) This is why need must serve as a foundation to equity.

Function will determine the type of award: sales--bonuses, engineers--technical awards and patent awards; production people--incentives (Lawler, 214); however, this is problematic when high degree of integration is necessary among the functions since competition may occur.

the use of these structures will depend upon the core and intermediate principles on which they are founded. For example, stock ownership options in Hi tech will be used to reinforce equity participation and (to a lesser degree) individual and team performance. Rather than giving across-the-board options to senior managers only, HiTech should give options throughout the organization to individuals and teams that have particularly outstanding years or accomplished singularly important breakthroughs." (Lawler, 256)

Multiple pay for performance systems at multiple levels: all levels (profit sharing); executive management (stock options and long-term incentives see Rosen on this) and lower level employees (gainsharing).

Lawler on Profit sharing *Strategic Pay* pg 123 1/3 of all organizations have profit sharing plans in the US. Of *Fortune* 1000 firms 15% cover all employees and 60% cover some employees. Some organizations have developed divisional profit sharing plans.

Chapt 11:

Individual performance may not be the same as organizational performance (214)

Problems of different compensation for different functions (214)

2. Pay for Performance: (profit sharing, stock ownership, gainsharing, recognition rewards, merit pay, bonuses, (These programs are variable pay elements which depend on the performance of the individual, group, division, and firms. % of variable pay to overall pay should not violate the principle of need. Distribution of programs: broadly distributed vs narrowly distributed vs a mix distribution.

Procedural Justice: Milkovich, 43. this can be manipulative see pg 44.

1. Participation:

2. Communication:

3. Hierarchy: Degree of Hierarchy: (this may belong in the process section) Lawler does not deal with this issue well; he has a poor understanding of hierarchy. See Milkovich, pg 32ff, 36 (egalitarian vs hierarchical structures. Milkovich 41 Degree of hierarchy will be partially determined by the industry--but no industry has justification for an oppressive hierarchy. Every organization has hierarchy.

Poor understanding of hierarchy and pits this notion against a egalitarian understanding of organization (Lawler, 211).

b. Relate to Dignity (explore participation)

c. Critique Lawler on Hierarchy

d. Strategist:

see Lawler pg 35-36: see Milkovich pg 184 -- according to ability to pay

see Lawler Chapt 10:

Disproportionate executive compensation is destructive of this community, creating cynicism and distrust.

(see chapter 5 employee burnout, competitive pressures, bottom of 101)

(Milkovich chaps 6 and 7 deal with competitiveness and pay

Conclusion: Possible misfit between I and II. again recipe for cynicism and poor morale.

This order should not simply be seen as chronological, since it is practices that principles can be born rather than in mission statements.

Eg. of GE which focused on internal equity at the expense of external market forces (Lawler 199-200).

Wrong understanding of hierarchy in the organization on the basis of perks see Lawler pg 210. see also pg 212.

Revenues/sales: how will it affect shareholder value, affect long-term stability,

see Milkovich on internal consistency pg 10. (comparisons among jobs or skill levels *inside* a single organization."

A. Focus on what is said about employees which gives us the basis to an organizations HR Philosophy; although what is said about employees must be contextualized with what is said about other stakeholders (customers--reasonable prices, shareholders--reasonable return, community--etc.)

1. Strategic limits and opportunities: (prospectors, analyzers, defenders, and reactors strategies) see Campbell and Nash, on IBM pg 13ff--they had a good but bad strategy.

key here is that the way one is paid must be related to one's philosophy of management and the strategic business orientation. Compensation must be related to the way one

thinks about work and organizes people. Compensation is an expression of a particular value system that supported by a philosophy of management. See Lawler pg 151 The starting place for any compensation system should be a set of core principles that drive particular pay practices and directly reflect the needs of the business." (Lawler 245) (this would include the role of labor costs, individual vs group performance effectiveness, motivation, relationship to the local and national market, nature of product in the marketplace, degree of training and information needed for workers, organizational structures (hierarchical vs flat)--see Acme as an eg.)

The fit between purpose and compensation will be affected by environmental factors which constantly change and are outside the control of an organization. (Miles and Snow, 22). The degree of environmental change will affect the degree of change in compensation structures and processes. A firm can view its employees in various ways: a means to the production of goods and services (employees are simply a market in which they are compensated in terms of supply and demand) so as to maximize shareholder wealth See tradition, paternal, or autonomous.

A mission statement is an organization's identity statement that defines its purpose--its reason for being: "Who are we as an organization and where are we going?" A mission statement is an attempt to articulate the culture of the organization. What are its beliefs, values, goals, processes, practices, etc. (see Walton on culture) Mission statements go under various titles: creed, statement of purpose, statement of philosophy, defining our business, etc. (Pearce and David, 109). Such statements set out the purpose of an organization by articulating its priorities, attitudes, and ends. Organizations reveal in their mission statements what businesses they are in, why they are in them, and how they will execute such businesses. The why question focuses on the user of the good and services. The customer is the end. The reasons they provide for producing such goods and services for particular markets are multiple: it is good for the customer, provides for the overall common good, furthers human development, serves needs, maximizes shareholder value, etc. The how question will focus on stakeholders who help produce the good or service such as suppliers, employees, communities, etc., which are intrinsically tied to the why question. For the purposes of this paper, I focus on how the organization pays its employees to produce the goods and services. This is not merely a matter of strategic techniques. Underlying the how to pay employees is an attitude or vision of the employee. How does the organization value the employee? The way the organization perceives its own employees contribute significantly to its own self-identity.

What the principles will look like are not automatically determined. Core Compensation Principles that stem from mission (need, contribution, order and dignity) Normative and Universal: the mission stems from a view of the person and society which eventually stem from a view of God and the world. These principles serve as a guide to the intermediate/strategic principles. Core principles reflect the nature of the organization and reflects those who work in it. The challenge for compensation managers is: "the efficient and equitable distribution of the returns for work." (Milkovich and Newman, 2).

This is where the differences between Hi Tech (which looks like EMD) and Acme begin to differ which will affect the structures and processes of compensation. An organization's strategy will affect the H/R compensation strategy. Egs. of compensation strategy is whether the company wishes to lead, meet or follow the industry in pay. Variable pay (low base but high bonus) so as to (traditional, paternal and empowerment strategies) Strategic or Intermediate Principles with Organization and Compensation: managers may believe they are paying for performance but employees may not--the gulf. peer evaluation evaluation of bosses secrecy (239)