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EXPLORING THE STRATEGIC POTENTIAL OF PAY: ARE WE EXPECTING TOO MUCH?

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Current theorizing emphasises the strategic potential of pay to enhance organizational performance and secure competitive advantage. Our understanding of how pay is managed effectively towards these ends is limited, however. When analysed at multiple-levels, an exploration of the management of pay within a sample of seven leading firms reveals that operationally pay practice is often not what is desired strategically or intended as policy. Despite corporate rhetoric, pay is non-strategic and attempts to use pay strategically may produce unintended consequences that destroy value. Flaws within current theorizing are identified and implications for pay theory, practice and future research discussed.

Keywords: reward and incentive systems, strategic control and reward systems, strategic HRM, institutional theory, multi-level analysis, qualitative orientation

In addition to being the single largest operating cost for many organizations, current theorizing emphasises the strategic potential of pay to enhance organizational performance and secure competitive advantage. Strategic pay[i], as it shall be termed here, has come very rapidly to represent the 'received wisdom' within practice, mirroring an equally rapid ascendancy in theory as the 'new orthodoxy' (Kessler 2001). Strategic pay refers to the predominantly financial measures through which organizations attract, retain and motivate employees to perform against strategic goals. Available trend data suggests that organizations, in the private sector especially, are attempting to use pay strategically (Milward et al 2000; Gerhart & Rynes 2003). Our understanding of how organizations are attempting to manage pay strategically is limited, however. Nor is it obvious how effective strategic pay systems are in practice and whether they fulfil the potential promised by advocates. Furthermore, a small but vocal body of critical commentary highlight tensions within strategic human resource management (HRM) theories – conceptual, normative and prescriptive, that one might expect to apply equally to theoretical approaches to pay (Legge 1995). In particular, many of the managerial assumptions upon which strategic theories of pay are predicated, such as that capacity of management to rationally choose the form and function of pay, are brought into question.

Through an exploratory study of the pay practices of seven leading multi-national firms operating in the global fast moving consumer goods (FMCG) sector, and using a multi-level framework to provide in-depth insights, this paper seeks to redress the dearth in our understanding of how effectively contemporary pay systems fulfill the strategic aspirations of proponents. Specifically, the study reviews the process through which contemporary pay systems are determined at multiple levels organizationally and attempts to answer three basic questions: *how* are firms attempting to use pay; *how* does this influence the form and function of contemporary pay systems; and, finally, *how well* are these systems perceived to work?

Consistent with strategic pay prescriptions, all firms within the sample are indeed attempting to use pay to secure employee and organizational outcomes of strategic value e.g. employee motivation, commitment and strategically desirable behaviours. Moreover, all use very similar forms of pay practice in order to do so. However, there is substantial variation within the sample in how those same pay practices are managed, with implications for their form, function and perceived effectiveness. The centralization corporately or decentralization to line management of authority for

[i] Strategic pay is referred to under a variety of terms, including (but not limited to) compensation management, remuneration, rewards, reward management, strategic rewards, total rewards and, functionally, compensation and benefits and pay and benefits

pay decisions is a key difference in approach to the management of pay within the sample. Where centralized, the findings indicate that standardized pay policies are rarely implemented as intended. Where decentralized, line management choose typically to continue to use pay in ways that are characteristic of traditional pay management, despite the aspirations of their superiors.

The net result of both is that, despite corporate rhetoric to the contrary, contemporary pay practice operationally is non-strategic. Strategic pay systems *fail* to achieve in practice what they are supposed to. Indeed, attempts to use pay strategically may produce instead a range of unintended and negative outcomes that destroy value. In seeking explanation for the phenomena observed, the manageability of strategic pay systems and the flaws of current theorizing are exposed and discussed. The findings challenge the notion that strategic pay systems can be effectively managed, and concludes that attempts to use pay strategically should be avoided. In light of the conclusions drawn, doubt is cast over the saliency of current theorizing on pay. In a theoretical development, the study also provides additional insights into the hitherto unacknowledged influence of a range of non-managerial determinants that shape pay practice as it is experienced at multiple levels of the organization. The combined recognition of the limits of current theorizing, the multiple levels of practice and the multiple determinants that shape pay practices and associated outcomes represents a distinctive contribution to our understanding of the organizational realities of contemporary pay practice and its potential as a strategic activity.

REVIEW OF THE LITERATURE

Fulfilling its strategic role, pay ceases to be simply the cost of hiring labour. It is instead a strategic management tool through which enhanced organizational performance may be secured (Milkovich and Newman 1999). Rationalist and managerialist accounts of strategic choice dominate current theorizing on pay. Where traditional forms of pay were characterised by pluralist employment relations and determined collectively through negotiation by management and employee representatives, strategic pay is characterised by the notion that management have the right to determine pay 'free from constraint' in the interests of securing competitiveness (Schuler & Jackson 1987, Barney 1995). Management, commentary espouses, choose rationally those pay systems, processes and practices that produce outcomes most closely aligned with strategic priorities (Lawler 1990). Strategy, above all else, is the principal consideration in strategic pay decisions (Schuster & Zingheim 2000).

Desirable employee behaviours within firms pursuing innovation based strategies include, for example, a high degree of creativity, a focus on long term performance and a willingness to take risks (Schuler & Jackson, 1987). Management attempting to use pay in support of such behaviours will typically place more emphasis on the use of long term incentives, offer enhanced employment security and extend to employees greater choice over their individual remuneration arrangements (Baird & Meshoulam 1988). By contrast, competitiveness achieved through cost containment focuses on the reduction of labour costs of which pay spend is often the largest element (Arthur 1992, Snell 1992). Organizations pursuing cost management strategies typically employ ‘administrative’ HR systems, ‘reducing cost and eliminating uncontrollable behaviour’, and focus on short term efficiency savings through flexible resourcing and paying the minimum necessary to secure productivity (Youndt et al 1996). Strategically, pay is a key element of the organization’s ability to attract, retain and mobilise its best source of sustainable competitive advantage – its people (Bergman and Scarpello 2002).

Strategic approaches to pay have found traction within practice. A survey by the Chartered Institute of Personnel and Development (CIPD), a professional body for human resources practitioners and the largest management association in Europe, reveals that by far the most common goal for contemporary pay practice is that of supporting the achievement of business goals (84 per cent), closely followed by rewarding high performers through performance differentiation (77 per cent) and the recruitment and retention of value talent (68 per cent). The emphasis on supporting business goals, through both attracting and retaining the necessary calibre of employee, but more importantly through rewarding high performance through employee differentiation, is indicative of the shift away from traditional pay to strategic pay.

Theoretical limitations and barriers to effectiveness? However, there are a number of apparent tensions within the strategic pay literature. For instance, contemporary theory assumes that pay interventions (incentives for example) sit in a value chain in which cause, the independent variable, results in the effect, the dependent variable. Thus, managerial choices determine practice, which in turn produce outcomes – cause and effect. Criticism has been levelled at the value chain model for not recognizing sufficiently the array of mediating variables that influence, say, employee or organizational performance as a dependent variable. An additional criticism is that it does not recognize the complex interactions that occur at different levels between the various elements of the value chain (Wright and Nishii 2004). Strategic pay interventions are, for example, typically formulated at the level of the organization. The behavioural outcomes elicited are exhibited at the level of the individual, however. In a relevant parallel, Kochan et al note that “existing industrial relations systems theory does not specifically address.... the apparent inconsistencies and internal contradictions in strategies occurring at different levels of industrial relations within the firm' (Kochan et al. 1986).

Fraught within the literature on strategic human resource management (HRM) is the tension between so-called universalistic 'best practices' and context specific contingent practices (Delery & Doty 1996). On the one hand, much empirical data supports the notion that there exist certain practices that have universal application and, when used, result in positive additive outcomes (Pfeffer, 1994; 1998). The notion of universality has gained much currency within the management literature and is pervasive in corporate discourse despite obvious differences between organisations (e.g. strategic orientation, characteristics of the internal and external operating environment). Conversely, contingency theory argues that opportunities for value creation are maximised when organizational activities such as pay are aligned to strategic priorities. Emphasising the importance of ‘fit’ between strategy and internal systems, practice(s) and processes, the firm’s human resources practices are used as a means of aligning employees to the goals and values of the organisation. Fit requires integration of human resources (HR) practices and the context in which they are applied. As each organization is different, HR practice(s) must be different too to be effective – idiosyncratic practice is an inevitable by-product. Indeed, it is the unique qualities of the firm’s human capital that permits sustained competitive advantage (Boxall 1992). Whilst intuitively appealing, the notion of fit and alignment is not on the whole well supported by existing empirical data (Delery & Doty 1996). Strategic pay theory is beset by the same tension, being characterised by both prescriptions advocating those best practices deemed to have universal application, and by prescriptions advocating the choice of pay practices that best fit the strategic priorities of the organization. Nevertheless, both represent a departure from the philosophical underpinnings of old pay and are characteristic of contemporary theorizing – that pay has the potential to yield organizational outcomes of strategic value (Bloom & Milkovich 1995).

In a further challenge to the hegemony of strategic and rationalist accounts of managerially determined pay, new-institutional theory represents a promising theoretical development and yet has received little or no application to pay (Kessler 2001). Deterministically, institutional pressures encourage conformity, or isomorphism, of practice between organizations (Hawley 1968, Meyer & Rowan 1991, Oliver 1997). Competition encourages conformity we understand, but so do the *social institutions* present within an organization's 'field' – its environment (DiMaggio & Powell 1983).

Coercive institutional pressures promote conformity of practice by requiring that organizations comply with universal and mandatory obligations. Laws are one such example, but it applies equally to external bodies upon which an organization is dependent (Oliver 1997). Financing bodies, for example, may retain control over the management of organizations in which they have invested. Professional associations provide accreditation upon the fulfilment of criteria of good governance and penalties in cases where performance against those criteria are found wanting. Through such mechanisms, coercive institutional pressures serve to encourage standardization of pay practice across fields as varied as executive compensation on the one hand, and the minimum wage on the other.

Normatively, organizations are prone to follow industry norms and trends (Oliver, 1997). Persistent norms become established as the standard against which all others are measured. Compared with other industries, for example, engineering firms exhibit many common characteristics of pay practice, moving 'like ships in a convoy' (Arrowsmith and Sisson, 1999). Other norms are more transient but no less compelling. Transparency of corporate performance highlights winners and losers, with winners regularly illustrated as 'best practice' organizations. The implicit assumption is that the practices that have led to their success may have application elsewhere. Winners become objects for aspiring others to emulate. Mimesis, then, is an additional institutional mechanism through which isomorphism occurs. Isomorphism binds organizations to the institutional structures pervasive within their environment in ways that are appreciable but also discreet. The net effect is that "after a certain point in the structuration of an organizational field, the aggregate effect of individual change is to lessen the extent of diversity within the field" (DiMaggio and Powell 1983).

Where institutional pressures encourage convergence at the inter-firm level, they potentially encourage divergence at the sub-firm level (Kessler 2001). Impeding the implementation of standardized pay policies, institutional pressures within the firm may potentially encourage the *emergence* of multiple and varying systems in place of corporately desired consistency. This notion finds traction in the literature: "Even if firms have a single HRM philosophy and a single set of HRM policies, these are likely to manifest themselves in different practices across subgroups of employees. By extension, the "same" HRM intervention should be expected to be differentially interpreted and received across these subgroups" (Jackson & Schuler 1995).

The influence of custom and practice, well documented in relation to traditional pay systems, is also largely neglected by current commentary but potentially highlight relevant. One such challenge to the effective use of strategic pay is collusion between managers and their subordinates and the adaptation of standardized pay systems to best suit their shared interests. These *emergent* patterns of behaviour referred to as 'transactional rules', bind management and the managed and give rise to custom and practice that over time acquires legitimacy (Brown 1973). Developing further the work of Brown (1973), two forms of custom and practice are potentially relevant to the effective management of pay systems: errors of commission and errors of omission. Errors of commission take the form of concessions made to workers which become cited as precedent informing future practice. Errors of omission are those which allow informal custom and practice to become established through negligence or ignorance on the part of management. Contemporary performance based pay systems are heavily reliant upon processes operated by line management e.g. objective setting and appraisal. Such dependency renders strategic pay systems highly vulnerable to poor management – either through wilful subversion, neglect or incompetence.

Similarly, operational line managers and senior management are not necessarily aligned in their interests. Williams et al (1990) observe that in practice, managerial activity is often characterized by "reacting to what seems to be real-time situational factors which pressure managers to respond almost immediately, sometimes in a remedial way and at other times in an opportunistic manner" (ibid). The implication is that emergent informal practice is likely to replace formal espoused practice in the interests of expediency as line management respond in real time to 'trigger information….gossip, hearsay and opinion' frustrating the careful planning and strategizing of their superiors (Mintzberg 1990). Given these potential barriers to effective implementation, and others, it is conceivable that enacted pay practice may deviate substantially from prescribed pay policy within organizations attempting to use pay strategically (Pfeffer & Sutton 1998).

From the review of the literature, it is apparent that strategic approaches dominate contemporary theorizing on pay. Is this reflected in practice? Are firms attempting to use pay strategically? If so, on what basis are strategic pay systems determined and what is their perceived effectiveness? How effective are strategic pay systems in producing employee and organizational outcomes of strategic value? Are there pay best practices, as Universalists might contend, or does strategic alignment inevitably result in bespoke pay strategies and contingent practice? Consideration of alternative theory suggests some fundamental tensions within our current theorizing on pay. Are pay systems determined solely as a result of managerial choice? Is pay determination not prone to institutional isomorphism as new-institutional theory would contend? Is it appropriate to conceive of pay in purely single level terms? Additional theory suggests that pay determination is influenced at multiple levels, a position largely neglected by strategic approaches which exclusively prescribe organization level interventions. If pay determination occurs at multiple levels, what is the relationship between levels and what are the implications for pay practice and performance? Moreover, how do we reconcile all of the different accounts - managerial, structural and institutional, acting at multiple levels - industry, organization and sub-organization, within our current theorizing on pay?

RESEARCH APPROACH AND METHODS

In light of these questions, and with the desire to avoid 'methodological myopia' (Kessler 2001), an exploratory research approach was adopted, utilising multiple-methods and conducting analysis of pay practice and related organizational phenomena at multiple-levels. A grounded interpretative approach was used to assess holistically the experience of those with responsibility for the management of strategic pay systems within seven sample firms. The interpretive approach permits the researcher to evaluate the management of strategic pay systems according to contextually bound values and links to existing theory, to develop further an emergent model that is grounded empirically.

Multi-level framework: The perspective adopted here was not to view pay practice in the single-level terms characteristic of most studies and theorizing on strategic pay. Equally, in a departure from traditional multi-level approaches focussing on multiple levels of the *organization*, this study uses a framework of multiple levels of *practice* through which to conduct an empirical investigation of companies' attempts to use pay strategically. The framework does not have a prior theoretical or conceptual grounding, nor did it inform the exploratory research in the first instance. However, through testing of the research design within a pilot sample firm, the emergence of multiple levels of pay practice and the relationships between levels constituting what we have to date, rather vaguely, defined as pay practice, became apparent. Thus, the framework informed the remaining research programme, providing a frame for theory, data collection, analysis, findings and the conclusions drawn.

The framework comprises three levels of analysis and each level of analysis represents one state of the *same* pay practice. Thus, it is proposed here that pay practice, like other functional activities presumably, is experienced as multiple states (or forms) by multiple stakeholders throughout the organization. This has implications for what we define as the unit of analysis in research terms. Within the multi-level framework that forms the basis for the analysis of pay practice in this study, the first level, the *pay approach*, reflects the implicit or espoused values, principles and aspirations that underpin pay practice. The second level, the *pay design*, reflects the technical content of the intended pay policy. The third and final level, the *pay operation*, reflects what is achieved operationally as pay practice.

Insert table 1 about here

In lay terms, the *approach* might be expressed as a formal pay strategy, or articulated vision, and represents what is desired strategically e.g. a performance driven culture. The *design* might be expressed formally as pay policy, being principally technical in content, and reflecting what is intended at the point of implementation. The pay *operation*, on the other hand, represents what is experienced as pay practice, and reflects the reality of what is achieved at the point of implementation.

These three levels of pay practice comprising the framework are not mutually exclusive nor are they necessarily hierarchical. Rather, they reflect three states of pay practice as they are *experienced* organizationally. By recognizing three distinct states of the same practice, it is possible to differentiate between the three levels conceptually and empirically: between the *approach* - those foundational principles underpinning pay expressed often as strategy; between the technical *design* of pay practice expressed often in the form of policy; and, finally, between pay practice achieved in operation.

The ability to distinguish between the three levels of practice permits the assessment of any potential disconnection. What is desired (the *approach*), and what is intended (the *design*), may not be reflected in what is achieved (the *operation*). The ability to draw such a distinction is largely absent from prescriptive and normative theory, which presume flawless execution as matter of course (Legge 1995). It also affords the researcher the flexibility to review multiple and varying aspects of the pay determination process holistically, and not in isolation. Whilst applied here specifically to pay, this framework has broader application and constitutes, it is hoped, a valuable contribution to multi-level research methodology. Following a review of the literature, it will be proposed that a combination of determinants, principally structural, managerial and institutional in nature, shape the form of pay practice at each of the three levels of analysis, with implications for pay practice effectiveness.

The multi-level framework is structured further using a processual model developed by Zbaracki (1998) but adapted specifically for the purposes of this study. The adapted model comprises four stages relevant to a multiple-level exploration of the pay determination process. The first stage, environment, refers to the conditions under which the determination process takes place. The second, variation, refers to the stage in the determination process where the stakeholders involved perceive the need for intervention in the form of, either, change or preservation of the status quo. The third stage, selection, refers to the conscious choice of ‘what’ the new or existing practice should reflect. The fourth and final stage, retention, refers to what is retained organizationally as pay practice. Data presented at each level and stage of the pay determination process reflects perceptions of both the rhetoric and reality of sample firm pay practices as they are experienced by the multiple stakeholders involved in the pay determination process. Reviewing the various stages of pay determination, at multiple levels, permits the exploration of the process of pay formation and the subsequent effectiveness of pay practice as it perceived within and between each of the sample firms.

Research Procedures and Data Sources

Data were gathered from seven multi-national firms operating in the global fast moving consumer goods market(s) (FMCG). Combined, the sample firms employed at the time of research almost 560,000 staff in a variety of occupations worldwide. Their combined annual sales were $160bn, with spend on pay constituting the single largest operating cost in nearly all cases. The sample firms are all house-hold name firms and market leading within the FMCG sector. They compete in some, or all, of the major consumer goods markets, including tobacco, food, confectionery, beverages (alcoholic and non-alcoholic), home care products and other non-durable consumables. In addition to their sustained high performance, the firms are also all highly reputable, and referenced frequently as examples of best practice, 'excellent', brand leading firms with the consumer goods sector and more broadly. All of the firms are very large, the smallest employing over 35,000 employees, and the largest employing slightly fewer than 200,000. The research was multi-level and multi-national in scope, reviewing pay practice at industry, organization, division and team levels. Primarily the fieldwork, which was conducted in the period 2004-2006, included quantitative analysis of industry trends in pay (in the UK and European FMCG labour market) and semi-structured interviews with relevant stakeholders in the seven sample firms described above.

Insert table 2 about here

Interviews: To secure representativeness within each sample firm, interviews were conducted with multiple constituent groups involved in the management of strategic pay systems, including senior managers, human resources directors, remuneration specialists, line managers, employees and specialist external advisors. Over 150 semi-structured interviews were conducted over an 18 month period in nine countries and over 20 business divisions of the seven sample companies. Interviewees had typically between 1 to 24 years experience as specialists within the pay function, or integrally involved within the pay determination process as generalist management. All interviewees, with the exception of some employee groups interviewed as 'end users' of the pay experience, were professional managers or consultants. Interviews with multiple respondents involved in all aspects of the pay determination process, from strategic conception through to implementation, across a range of management functions and operating at all levels of the firm (and the industry level in the case of commissioned consultants), provided the researcher with confidence that the issues raised in the interviews were representative of views within the wider organization.

The interviews lasted typically between one to two hours, with no interview falling under one hour. All interviews were recorded and comprehensive accompanying notes taken. Post-interview, further notes were recorded and key issues summarised and cross-checked against existing interview data. Interviews followed the same basic structure, being ordered thematically around key issues to emerge from a pilot sample firm (*Choc Co.*) and prior theorizing. However, interviews were sensitive to the experience and perspective of interviewees (e.g. specialist pay function versus generalist management opinion) and incorporate flexibility in scope as a result. In the very few cases where language prohibited direct dialogue (the native language of the researcher being English), a professional interpreter was used supplied typically by the sample firm being researched. The vast majority of interviews recorded were transcribed by a third party provider used standard conventions. Corrupted digital voice files prevented transcription in the case of four interviews, requiring the researcher to rely upon interviews notes. Following an initial analysis of interview data (transcribed in the form of verbatim scripts), any ambiguities were resolved through direct follow-up contact with the interview respondent by the researcher.

Observation and secondary data: Further complementing the interview data, the researcher was granted permission to observe, and in some cases participate, in pay determination meetings at each of the three levels of analysis (i.e. with senior management at the level of approach, with pay professionals at the level of design and with line management at the level of operation). The researcher also attended strategy sessions involving external advisors and consultants and employee 'town halls'.

A range of privileged firm-supplied information was gathered in the form of formal documentation about pay determination and pay management. Secondary data included firm memoranda, presentation materials, formal strategy and policy documentation, pay scheme rules, functional marketing material, internal briefings, brochures and, where available, quantitative data on pay distribution, employee turnover and so on. A large amount of public domain information on each of the sample companies was also collected, including published case studies, firm reports and accounts and business statistics regarding longitudinal financial performance. Archival data was collected in order to understand better the history of the sample firms, and the context in which pay is being determined.

Analytical Approach: The data were was inductively analysed using constant comparison techniques to ensure rigorous data collection and consistency in the application of qualitative methods (Nag, Corley, and Gioia 2004). Over time, consistent themes emergent from the qualitative data (both interview and secondary) were captured, informing future data collection, but also permitting the comparison of key event, phenomena and outcomes on a continual basis. Continual comparison of informant interview data and the coding of key words were conducted through specialist qualitative analysis computer software. Two software programmes were used. The first, NUDIST 5.0 provided limited functionality, and was replaced following the analysis of two sample firms with the more sophisticated package, NVivo 2.0. The software allowed for the cross-reference of codes throughout all of the interviews, and the construction of time and stakeholder sensitive event schematics. Issues and themes to emerge from the analysis of the qualitative data were characterized according to level and stakeholder perspective. Thus, the role of line management in the pay determination process, for example, could be assessed from multiple-perspectives dependent upon the stakeholder group interviewed (e.g. line management versus pay specialists) within each sample firm or across all.

FINDINGS

As market leading companies, might we presume that the sample firms are using pay strategically in support of their superior performance? Based upon a superficial assessment of company documentation and interviews with senior management and pay specialists, all of the sample firms do indeed claim to use pay strategically. Moreover, we observe very similar profiles of pay practice across the entire sample – these similar firms are attempting to use pay strategically in very similar ways. Consistent with strategic pay prescriptions, the espoused role of pay is, firstly, the attraction, retention and motivation of valued talent. Secondly, and most significantly, pay is commonly cited by senior managers as a decisive factor in their ability to secure strategically desirable employee behaviours.

In addition to market competitive basic pay, all seven firms deploy multiple forms of incentives on an all-employee basis (multiple occupations and at multiple levels throughout the organization), using one or more schemes at any one time depending upon the role and level of the employee. Incentive awards are contingent primarily upon individual performance, but moderated in all cases by overall firm performance. Opportunities for equity ownership at a discounted rate are also highly prevalent, taking the form of share options (made available on a restricted basis) and stock purchase plans. Six of the seven case firms also offer a comprehensive range of flexible benefits, or 'cafeteria benefits', emphasizing flexibility of provision and the ability of individuals to choose their benefits according to personal circumstances. The anomalous firm was planning to introduce a similar scheme at the time of research. Yearly referencing of the external labour market is universally the primary determinant of pay increases.

All seven case firms have dedicated pay professionals operating at the headquarters level forming a coherent group – the pay function. Interestingly, all of the case firms make extensive use of management consultants and professional services when formulating pay strategies. Not only do they use the same firms of advisors, but even the same high profile individuals within these firms in a number of cases. Indeed, if one were to include the seven market leading sample firms within a single respondent survey of pay practice, as has been the methodological norm in pay research to date, the results would indicate strikingly similar profiles of pay practice along a number of common dimensions.

The conformity observed is not surprising. The observed profiles of sample firm pay practice correspond with economy-wide trends in pay determination toward the adoption of strategic pay.

Proprietary consultancy data gathered from a sample of over one hundred Fortune 500 firms, operating globally, reveal that all (100 per cent) have had a global reward strategy in place for four or more years (Mercer Human Resource Consulting 2004). Global pay strategies are put in place for a number of reasons, the most important, however, being in support of global expansion. The main reasons for introducing global pay strategies include global expansion (29 per cent), improved governance structures (17 per cent), cost management (15 per cent), compliance and reporting (12 per cent) and mergers and acquisitions (5 per cent) (ibid). On a domestic, regional and global level, the survey data indicate that firms are embracing strategic pay for the achievement of competitive advantage.

Complementing those questions already raised, what explains the startling conformity of pay practice observed? Is the conformity evidence of the existence of pay best practices, and further evidence that management within the sample are purposefully (that is to say, rationally) choosing to adopt these practices? If so, what are the implications for the notion of pay practice contingent upon strategy? In short, is it best practice or best fit that matters in performance terms? Or, is it evidence institutional isomorphism? If so, can pay be described as being strategic in nature at all, being informed deterministically and not chosen voluntaristically? Irrespective, the findings confirm that firms within the sample are attempting to use pay strategically in the interests of securing employee and organizational outcomes of strategic value. Moreover, they are all market leading firms. As a crude correlation, the findings thus far present a compelling portrait of the efficacy of strategic pay and support for current theorizing.

A representative perspective on pay practice effectiveness

We know what the sample firms say they do, however, but do they do what they say? Drawing upon in-depth analysis of representative opinion from multiple actors involved in separate levels of the pay determination process, it is apparent that all is not as it seems superficially. Whilst all firms have attempted to use pay strategically, and use very similar pay practices as noted, there is wide variation of perceptions of how effectively pay is managed between the sample firms. Pay operationally is perceived in relatively few firms to be effective. In others, it is considered inconsequential. In others yet, it is seen as destructive. What are they doing differently and what are the implications for performance? A key difference is how sample firms attempt to manage pay and the degree to which authority for pay decisions is either centralized at the headquarters level or decentralized at divisional and / or business unit level and devolved to line management.

Decentralized pay determination: In the case of *Tobacco Co.*, pay is determined and managed locally within the overall guiding framework of the corporate pay strategy (the espoused approach to pay). The result is the deployment of pay systems that reinforce performance expectations, throughout the firm, with the additional perceived benefit of binding the fragmented organization (*Tobacco Co.* is a holding company) to the over-arching corporate identity and culture. Whilst a significant proportion of management and white collar employee pay is placed at risk, performance based pay systems are not viewed as incentives, but as rewards. Bonuses are determined post hoc and not according to a predetermined performance quantum or formula. Incentives are also, typically, bundled with above-market, median base pay, generous benefits and complementary non-financial rewards. These include, for example, career opportunities, training and development and a positive work environment.

Choc Co. bears a close resemblance to *Tobacco Co.* Variable pay systems are, again, managed as rewards and are complemented by generous base pay, benefits and non-financial rewards. Pay is viewed as a means of binding, culturally, the multiple subsidiary businesses that comprise the group organization overall: "For us, pay is just part of a wider, more holistic philosophy and approach, which is based on our belief that motivation and commitment, and thereby our ability to attract and retain talent, is driven by our culture and values, and not our pay…." (senior management presentation, *Choc Co.*). Given its history of growth through acquisition, this is considered an especially important outcome of pay by senior management. In the case of both firms, the locus of pay determination and the responsibility for effective management is devolved to line management. The role of the dedicated central reward function is to provide support and technical assistance to the line and to uphold the clearly articulated corporate approach to pay – the pay strategy.

Discretion over pay choices and responsibility for execution is purposefully devolved to line management reflecting a corporately held view that pay is best managed in the local context. The result is locally determined pay systems representing multiple variations on the same theme – the articulated pay approach. Pay for *Tobacco Co.* and *Choc Co.* is a core element of the overall employee proposition. In the hands of line management, it is not used as the strategic lever envisaged by proponents of strategic pay, nor is it used as a means of corporate control. Pay is used to support the achievement of local business objectives and not to drive them. There is a recognition that pay is something that, if mismanaged, can lead to negative outcomes in the form of conflict, and the associated organizational implications, and is therefore best managed almost as a matter of governance. More than getting it right strategically, the emphasis, within the three firms, is on not getting it wrong.

Drink Co. shares a similar philosophy about devolving primary responsibility for pay determination to line management. However, unlike *Tobacco Co.* and *Choc Co.*, *Drink Co.* fails to articulate and disseminate clearly the corporate approach to pay. The approach to pay adopted by *Drink Co.* senior management neither guides the determination of pay locally, nor does it communicate to the organization what senior management value in terms of performance expectations, values and behaviours. The central pay function provides merely the mandate that end-markets (business units) are required to incorporate pay at risk as part of employees' total pay, and provides basic minimum standards to which line management must comply when determining pay. Such standards include equal opportunities, for example. Whilst pay is locally determined, however, business unit performance targets (a measure of performance upon which performance pay is typically contingent) are centrally determined and do not, it is felt, represent practicable and achievable targets in the context of end market operations. As such, pay systems reinforce behaviours that are in some cases misaligned with local markets and result in conflict, dissatisfaction, and disengagement and employee disenfranchisement.

Centralized pay determination: Pay within *Candy Co.* and *Home Co.* is determined centrally at the regional level (Western Europe for example), within the overall framework of the corporately determined pay approach. Both firms have their headquarters in the USA, but the design and operation of the pay approach are managed differently. At *Candy Co.*, the emphasis remains on selecting pay systems which are in the interests of ensuring good governance and the best possible 'deal' for both employee and employer. This is consistent with their stated corporate value of mutuality and the paternalistic ethos that continues to pervade the firm, despite recent poor performance against competitors. *Home Co.*, on the other hand, desires conformity of the local organization to central planning, rules and checks in the interests of standardization and corporate control. Pay policy within *Candy Co.* is viewed by line management as operationally limiting, as a result of insufficient flexibility built in for the 'best fit' management of pay locally. Pay policies are disseminated regionally within *Home Co.* to business units in the form of a mandate, which is felt to constrain local leaders in attempting to manage their employees as they would otherwise wish. Even at a regional level, the tension between centrally determined policy, and decentralized pay execution, is a manifest challenge organizationally.

In the case of both firms, however, pay is intended to be, in principle, a measure that reinforces a broader employment proposition. Pay is intended to promote a sense of 'team' and corporate belonging and not the achievement specifically of corporate objectives. The performance based element of employees' total cash pay is, therefore, aligned to regional performance measures. However, the degree to which individual employees or teams are able to influence regional organizational performance is a perennial issue, with the frequent complaint being the limited line of sight between employees' individual contributions and the overall success of the firm. Arguably, as they are managed, the pay systems are of limited value and, by aligning employee pay to regional (geographic) performance, potentially demotivating.

Food Co. shares a similar pay approach to *Tobacco Co.* and *Choc Co*., but differs at the design stage by emphasizing the alignment of pay to the corporate organization over the local organization, in an effort to achieve levels of corporate fit. As such, the pay design takes the form of practice prescription and formal policy, informing the design and management of pay at the business unit/country level of the firm. However, acknowledging 'one size does not fit all', scope for local discretion is built in, allowing for some adaptation by local management to local business needs, thus resulting in pay systems that are aligned to both corporate and local performance targets. The result is a globally consistent pay system, emphasizing line of sight to both corporate and local targets that leads both performance and behaviours by placing a greater degree of employee pay at risk in comparison to the other two cases described above.

However, *Food Co.* fails, arguably, to support the process of local adaptation – and therefore the effective management of their pay systems – by not providing support on processual activities such as performance management, communication and other related areas of HR intervention. The linkage between performance management and pay systems is often not clearly understood, serving to undermine the much sought after 'line of sight' between individuals' performance and their pay. Moreover, contrary to what is intended, pay continues to be treated as a stand alone element, and not integrated with performance management and development for example, with the result that the employment offering often appears piecemeal when viewed from the perspective of the employee.

Grocery Co. differs by mandating pay systems corporately that are perceived to constrain local management when attempting to best manage their employees. By aligning pay systems to corporately determined targets, and placing significant levels of employee pay at risk, the findings suggest that the pay systems used direct employee interests and behaviours in ways contrary to the interests of their business unit operations. Moreover, the structure and management style of the firm is such that the negative aspects of the pay systems used are not communicated upwards, compounding the gap between the rhetoric of the approach, the intended *design* and the achieved operation. Not only does pay represent an obstacle to firm performance and value creation, but it also poses a risk, threatening to destroy value, unbeknownst to pay decision makers located centrally and operating corporately.

What are demonstrable and manifest, especially within three of the seven sample firms, are negative outcomes associated with attempts to use pay strategically. Contrary to expectations, it is apparent that pay systems can serve to diminish motivation, misdirect behaviours undesirably, consume managerial time and effort, misallocate pay spend, and produce various other negative outcomes that consume and destroy more value than is created. Illustrated by one senior business unit manager at Home Co.: 'People have worked their arses off against objectives which have been stretched and stretched and stretched by senior management who didn't want to accept the numbers. And therefore the workforce have now paid the price of not only being literally short changed versus the marketplace in terms of their overall net pay, but they actually feel like they're failing ……the stretch objectives set by senior management are potentially unobtainable, then that has a massively detrimental effect on morale.' (Home Co. Senior General Manager).

Considered overall, there is wide variation of perception of pay system effectiveness within and between the sample firms. In some sample firms, representative opinion holds that pay fulfils the stated aims of attracting, retaining and motivating valued talent. Pay also reinforces attempts to promote cultures of high performance. Pay is not used in these firms, however, as a means of leveraging behaviours – the function that is most characteristically strategic. Equally, pay in the remaining firms, a majority within the sample, is perceived to be of lesser value, and in some cases, a destroyer of value - pay systems do precisely the opposite of what they are supposed to. Why such variability of pay system effectiveness between firms that are superficially similar, aspire to use pay strategically and go about attempting to do so in very similar ways? The findings indicate that the most important differentiator is how the sample firms attempt to *manage* their pay systems, of which the choice to centralize or decentralize authority for pay decisions is an important aspect. Delving further into the data, analysis using the multi-level framework (of *approach*, *design* and *operation*) reveals a perspective on pay determination that is at odds with standard theory. The following sections attempt to explain why we observe such variability of perceived pay system effectiveness.

Pay determination at the level of APPROACH

Pay practice at the level of *approach* represents the principles and values that underpin pay practice philosophically and guide pay determination at subsequent levels within the framework. Articulated formally as pay strategy, typically, the pay *approach* is manifest of the strategic aspirations of senior management for role of pay in securing enhanced organizational performance and competitiveness. At this level, we observe a high degree of convergence of pay practice between the sample firms. All firms within the sample seek to align their pay systems to strategic priorities in support of organizational performance. All firms aspire to use pay to promote a culture of high performance throughout the organization and all the language of total rewards – a balance of both financial and non-financial rewards, to secure employee engagement and performance. There is some variation between firms in the role that the pay *approach*, as strategy, fulfils. In three of the seven sample firms, the pay approach serves as a guiding framework for decentralized pay determination. It communicates symbolically to employees what is valued by senior management in terms of behaviours, performance expectations and corporate values. To line management with responsibility for pay determination at lower levels of the organization, it establishes the broad umbrella principles which they are expected to observe. Within two of the sample firms, the approach takes the firm of a 'code of practice'; a set of espoused codes of governance to which those that manage pay are expected to comply. In both these cases, the pay approach is of symbolic importance. It is of primarily *rhetorical* value. In the final two sample firms, the pay approach, in whatever form, is not espoused nor communicated. Their philosophical approach to the use of pay, and their aspirations, is ambiguous as a result.

Insert figure 1 about here

Nevertheless, we observe a high degree of convergence of approaches to pay within the sample. Why? The process through which their approaches to pay are determined provides a compelling explanation. Prompted by concerns over competitor performance and the demands of interested stakeholders e.g. institutional investors, sample firm *senior management* seek to promote the use of pay as a strategic tool for enhancing performance. They are influenced by public stories and accounts of the effective pay practices of influential others (e.g. examples of best practice), prescriptive literature and industry standards, all highly pervasive at this level of decision making. Taking cues from these external standards of practice, and combined with the canvassing of opinion within the organization, senior management sanction the introduction of new pay practice(s) that are perceived to support best with evolving strategic priorities. In selecting what is most appropriate, however, senior management rely heavily on examples of external ‘best practice’. The result is the selection of an *approach* to the use of pay that is perceived to be both a best fit for the organization, based upon the limited information available to decision makers at this level, and best practice against external benchmarks. Indeed, extensive external referencing of pay practice against peer benchmarks within the sample was observed and acknowledged by respondents. Arguably, there is a greater abundance of information concerning legitimate external practice made available by external professional consultants and advisors than available internal information made available by the internal pay function due to resource limitations. The selected pay *approach* (a performance based approach, for example) becomes the retained pay strategy and is communicated as desired pay practice corporately.

As a result of the reliance upon external practice to guide the selection of the most appropriate *approach* to pay, the findings indicate that senior management, when determining pay, are heavily influenced by isomorphic institutional pressures – coercive, normative and mimetic. The phenomenon is seemingly industry wide (and beyond), as noted by a management consultant serving FMCG firms and others: ‘This happens so many times, you know, the CEO picks up Business Week or a magazine, calls up the SVP of HR and is like “we need to have pay for performance, it says in this article everybody else has pay for performance”, you know, and then the SVP of HR says to his reward director “okay, implement pay for performance because that’s what the CEO wants!”' (Management Consultant).

Normatively, a variety of institutional processes facilitate the referencing of external pay practice. These processes take the form of stories of success disseminated through prescriptive literature, the media, professional associations and academics. Mimetically, specialist management consultancies prescribe largely generic solutions when advising clients on pay related issues. Personnel within client firms are not unaware of the undue influence of consultants on shaping the form and function of pay to largely generic standards: 'They [consultants] are always looking for the next product to sell, they’re no different from any other industry and they will leap onto a bonus scheme design, or have a share incentive scheme, or have something like that, that they can hawk around us, as often willing victims. Because, yeah, we are all looking for the Holy Grail!' (laughs) (*Home Co. S*enior HR Practitioner). Coercively, interested stakeholders, including institutional shareholders, demand adherence to codes of practice in the interests of good governance. The result is convergence of pay practice between the sample firms at the level of *approach*. If we observe conformity of pay practices between peer organizations therefore, is it really evidence of best practice in performance terms? Are the gains of introducing strategic pay solely or even primarily economic? In light of the findings, it is perhaps more apt to cite such conformity of pay practice as evidence that the sample firms are converging isomorphically around *legitimate* norms of pay practice.

Why are pay professionals (and non-specialist senior management) driven to reference external standards of pay practice at all? In the face of uncertainty, institutionalists contend that institutions provide 'dependable and efficient frameworks for economic exchange', overcoming the uncertainty inherent in the transaction (North 1988). Institutions are therefore of benefit when determining pay, because they condition others to behave in a non-opportunistic manner and compensate for the uncertainty inherent within pay decisions by providing templates of established behaviours, codes and rules. Quite simply, institutions serve to reduce uncertainty in pay determination: 'It is quite inappropriate to conceive of firm behaviour in terms of deliberate choice from a broad menu of alternatives that some external observer considers to be ‘available’ opportunities for the organization. The menu is not broad, but narrow and idiosyncratic; it is built into the firm’s routines, and most of the ‘choosing’ is also accomplished automatically by these routines' (Nelson and Winter 1982). This resonates with the sentiments of a pay specialist at *Tobacco Co.*: 'This is what everybody is doing. This is what you should be doing [the norm]. The conventional wisdom is that you need to bonus people, whether it’s right, wrong or indifferent [for the firm] doesn’t matter. The conventional wisdom is you should be doing it.*'* (*Tobacco Co.* Senior Rewards Specialist). Institutions therefore exercise a great deal of influence over the determination of pay. Current theorizing on pay does not recognize the importance of the role of institutions in pay determination, nor the degree to which pay choices are informed by institutional forces, both consciously and in ways that are taken for granted (Kessler 2001). In practice, the greater the uncertainty under which decisions are made, the greater is the likelihood that decision makers are likely to reference practice externally and become by degree, prone to isomorphism. Providing the philosophical foundation for pay determination at lower levels, pay practice at the level of *approach* is selected for reasons other than for purely economic maximization.

Thus far in the multi-level analysis, the overall picture of sample firm pay practice is one of (a) a desire to use pay strategically, (b) the adoption of very similar approaches to pay and, related vein, (c) convergence around the prescriptive norms of advocates of strategic pay through (predominantly) a process of institutional isomorphism. Having chosen to use pay strategically, management within the sample firms must design pay systems that are fit fur purpose. How individual firms go about doing so varies considerably, with implications for pay system effectiveness.

Pay determination at the level of DESIGN

At the next level of analysis, the stage at which pay systems are designed through not yet implemented, the findings reveal an even more complex picture of pay determination. Despite sharing the same philosophical approach to the use of pay, *how* management within each of the sample firms attempt to design pay systems that are fit or purpose strategically varies, with implications for their perceived effectiveness. A key difference between the sample firms is the degree to which authority and responsibility for pay determination is centralized corporately or decentralized to business unit / divisional line management.

Insert figure 2 about here

Within three of the seven sample firms, responsibility for developing strategic pay systems is devolved to local management. Central pay function intervention is limited in the *design* process save for providing guidance when requested. Line management are also required to observe and comply with minimum standards in the interests of sound corporate governance. The perceived impact is that of the central pay function guiding the local determination of pay. In the context of their local operational environment, including localised pay custom and practice, line management reference the workings and the attitudes of their people and existing systems and structures and select component elements for change in line with the mandate articulated within the pay strategy. The focus typically is not on wholesale change, but on incremental improvement to existing practice in the interests of minimising disruption to ongoing work. An intention to change is communicated to the corporate pay function in the majority of cases, but not all, often being viewed as a 'courtesy call'. The retained design is further communicated to team leaders and employees in localised communications.

Due to their intimate involvement with operations, line management enjoy arguably a more complete understanding of their local organization when compared to pay specialists located centrally and operating corporately. Inevitably perhaps, decentralized pay systems are perceived typically as better aligned to the needs of the local organization by line management tasked with responsibility for the day to day management of their people. However, from a corporate perspective, decentralized pay design determination gives rise potentially to the emergence of myriad separate pay systems. Potentially inefficient and expensive in terms of duplication of administration; separate pay arrangements potentially inhibit employee mobility horizontally across the organization and reinforce divisions across the corporate whole. They also raise concerns over governance, practice being less transparent and less easy to monitor through controls and checks. Such concerns have encouraged a significant number of the sample firms to centralize authority for pay decision leading inevitably to standardization prescriptions for pay practice organizationally.

Where centralized, the environment in which pay systems are designed (for which pay function specialists are primarily responsible) is characterised by the prevailing organizational strategy, the espoused principles set fourth in the pay *approach*, and known internal structural and social contextual conditions of the organization overall. Centralization of pay determination is associated strongly with standardization of pay practice across the organization. Consequently, there is a greater likelihood of the pay *design* being aligned to centrally determined performance targets, and the form of the *design* itself, expressed as formal policy, being prescribed with little or scope for local adaptation. Disseminated throughout the organization in the form of formal mandated policy, such pay systems are perceived as constraining what local line management might otherwise do to remunerate their employees. The implication is that within these sample firms, local line management are obliged to implement pay systems that are not perceived to be fit for purpose locally – they are not considered effective. The perceived impact of such an approach to the determination of pay is one of constraint on the discretion of line management. The not uncommon emphasis placed on the development of the technical pay *design* by pay specialist operating centrally, perhaps at the exclusion of the development of effective plans and processes for implementation locally, is noted by one pay specialist at *Food Co.*: 'It comes back to the obsession that perhaps HR practitioners….. we are always seeking for the perfect reward system, the perfect appraisal system, what have you ….. we never give him [line manager] a perfect system.' (*Food Co.* Reward Function Manager).

Why are centrally determined pay systems viewed typically by local / line management as constraining - preventing them from how they would otherwise choose to remunerate their employees? Even from a reduced 'menu' of options, pay specialists operating corporately and located centrally are not necessarily able to discern what constitutes best fit for the wider organization. The findings, again, challenge the assumption that management is able to make informed pay decisions in the standard sense. The causal means-ends relationship between pay practice and pay outcomes is naturally discreet and difficult to measure, especially a priori (Wright and Gardner 2000). The ability to choose an optimal configuration of pay practice / system is further impaired by the cognitive limitations of decision makers operating centrally to comprehensively or accurately understand the sheer the complexity of the corporate operating environment in its entirety (Simon 1963). As a result, centralised pay decisions lack the necessary grounding to represent fit for purpose pay practice at the point of implementation.

The 'professionalization' of pay also has implications for the *design* of effective 'fit for purpose' pay systems. Pay specialists (pay function personnel) within all of the sample firms participate in invitation only industry peer clubs. Membership is restricted those working within FMCG and information and experiences are exchanged in an open forum. Industry peer clubs are designed to promote networking between pay specialists for the purpose of sharing best practice. An inevitable by-product is recruitment and 'job hopping'. They also help to foster a sense of professional status amongst the membership. Transparency of peer firm practice, combined with professional pride, encourage the development of ever more sophisticated pay practice that may or may not fit the needs of the organization. Recognized by a pay specialist at *Food Co.*: 'Within the remuneration function, probably by the way your peers in other remuneration functions react.... in other companies...... I think it just reflects the professional expertise, professional pride I think that there is about doing remuneration well. That is not necessarily a test of how well it serves the organization's purpose at all.' (*Food Co.* Country Reward Manager). The desire for enhanced professional legitimacy may supplant organizational effectiveness as the primary motivation in pay decisions. The result is technically sophisticated and institutionally legitimate pay practice that is organizationally a poor fit for purpose.

Pay determination at the level of OPERATION

Consistent with the findings of the two previous levels of analysis, variation in the operational effectiveness of pay systems is linked closely to the centralization or decentralization of authority and responsibility for pay determination. In the case of both approaches, line management are the primary management group involved, being responsible for pay system implementation and day to day people management. The environment in all cases is the sub-organization – business units or divisions of the larger organization. The sub-organization environment is characterised by local structural, social and cultural contextual conditions, such as employee attitudes, existing custom and practice, persistent pay norms and embedded management styles.

Insert figure 3 about here

Where pay systems are designed centrally, the intended pay design is communicated to line management as policy for which they have responsibility for implementation. Pay specialists remain involved to provide technical assistance to line management when dealing with issues arising from the proposed changes to existing pay arrangement e.g. contractual and grievance disputes. Pay specialist involvement is necessarily limited, however, due to resource constraint and limited availability. At the stage of selection, line managers review the intended pay design and operationally decide how proposed policy might be best implemented. This inevitably involves a degree of interpretation and adaptation, as line manager grapple with the challenges of replacing existing practice and attempt to integrate new pay practice with on-going work. If the implementation of centrally determined pay policy proves too taxing, or potentially too disruptive to workplace harmony (i.e. line managers and their relationship with subordinates) and ongoing work, there is abundant evidence within the sample firms of line management (a) adapting substantially the intended pay design, (b) subverting the intended pay design in favour of a locally developed system or (c) rejecting it entirely and continuing with existing practice. These acts of rebellion are for obvious reasons rarely communicated to corporate pay specialists or management located centrally. Advances in management information systems and information technology make such acts of noncompliance increasingly hard to hide. Nevertheless, numerous loop-holes exist within the corporate reporting structure(s) which line managers exploit to their advantage.

Such exploitation remains discreet often, as noted candidly by a divisional human resources manager with only a ‘dotted line’ responsibility to corporate HR function: 'Well, yeah, there’s sometimes people like me working with the line……..if I say collude that probably puts it too strongly. We will find ways around to help our business partners, because they will sit there and say things like, “Well, I really do need to help retain this guy, motivate him, but you know the reward team is saying that…….we can’t give a salary increase above a certain level…….it’s nonsense, dah-di-dah-di-dah, can you help me?”. So we will sit there and I will come up with a, hopefully, a solution which means that we can reward somebody in a different way, but it’s not via a salary increase, so it doesn’t come onto the radar screen of the reward team….' (*Home Co.* Line Unit HR Manager). Such rebelliousness may not be appreciable corporately and as a result, much operational pay practice might be classed as 'emergent’ and not the result of formal pay policy despite centralized prescriptions.

Responsibility for pay determination is decentralized within *Tobacco Co.* and *Choc Co.*. Pay systems in both are aligned to local organizational conditions and line management operate largely autonomously from corporate intervention, save for guidance from pay specialists when requested. Line management seek to implement the new pay design for which they have most likely had the responsibility for the development. Reforms to existing practice are in theory in line with the espoused maxims of the pay approach (e.g. principles and values). However, these principles and values are interpreted variably at each point of implementation, as line management in a myriad of operational sub-organizations respond to the corporate mandate for the strategic use of pay in support for corporate performance. The result is (a) the persistence of existing pay practice save for only minor revision or, more typically, (b) incremental revision to on-going pay practice. In both cases, line management attempt to limit as much as possible disruption arising from changes to employees’ pay arrangements.

Operationally, we observe that pay practices and their associated outcomes vary significantly both within and between sample firms as a result of these two separate approaches to the management of pay systems – centralized and decentralized pay determination. Critically, pay operationally in the case of both approaches is non-strategic. When given the discretion, the findings indicate that line management do not attempt to use pay strategically. Pay systems (including variable pay e.g. incentives) are used typically as post hoc rewards intended to reinforce additional non-managerial interventions (e.g. job enrichment and personal development) aimed at eliciting desirable behaviours such as employee job satisfaction, commitment, loyalty and performance. The role of pay is not to drive behaviours, but to reinforce workplace cultures of high involvement and harmony. Pay is viewed and managed as a factor of hygiene, and a great deal of managerial efforts is expended on limiting the potential of pay as a source of conflict and / or malcontent as a result of inequity between employees or processual failings e.g. poor performance management. The differentiation of employees' pay based upon individual performance is considered especially problematic and passed over often in favour of collective performance based measures e.g. division and team bonuses. Operationally, decentralized pay systems are arguably non-strategic in their scope, being more akin to traditional forms of pay. The view persists that pay is a cost of doing business, of hiring the necessary labour, and is less important than other managerial measures for eliciting employee performance. Pay remains important, but the emphasis is less on getting it right in line with strategic priorities, and rather more on not getting it wrong and thereby limiting it is as a risk.

Where pay determination is centralized, there is evidence that line management do not necessarily implement pay policies in their intended form. Corporately determined policies are perceived often to be a poor fit for the needs of the local organization, both in terms of their construction and the outcomes they are intended to elicit. As noted, standardized pay policy is rendered ineffective (to varying degrees) as a result of misinterpretation by line management and, in some cases, wilful subversion. Both these interventions by line management, one natural and the other calculated, limit the perceived negative consequences of implementing a poor fit for purpose centrally determined pay system. The enacted pay practice ceases operationally to be what was intended at the level of *design*. Rather, operational pay practice is emergent, in spite of the espoused pay approach and design and the best efforts of both senior management and pay specialists to use pay strategically. Where there are no such opportunities for revision to standardized pay prescriptions (in whatever form – adaptation or subversion, for example), there are numerous examples of pay systems producing negative outcomes. These may include incentivisation towards the wrong targets; encouragement of the wrong behaviours; financial penalties for failure to meet unachievable targets; low morale, employee disengagement and various other unintended consequences. Pay systems in this sense represent a risk to enhanced organizational performance. They achieve the opposite of what they are supposed to and destroy more value than they create.

A variety of reasons motivate the majority of sample firms to attempt to manage pay centrally. In the case of *Grocery Co.*, *Home Co.* and *Food Co.* is it a desire for corporate control arguably. In *Candy Co.*, the motivation is less one of control, but more one of a concern for effective governance, and the view of paternalistic senior management that the interests of employees are best served by a direct intervention, over their terms and conditions, by a professional pay function – 'mother knows best', in effect. Nevertheless, the centralized determination of pay creates operational difficulties for those for whom the arrangements are binding – both line managers and their employees. Centralization of authority for pay decisions requires that pay choices be based upon precise information about business conditions, the local labour market, the structure of work and performance management throughout the organization. Centrally located decision makers rarely enjoy exposure to such comprehensive or accurate information, with the result that their decisions reflect often (line management opinion would contend) a poor fit for the environment for which they are intended. As a result, formal pay policies are subject to willful misinterpretation by line management and employees at the point of execution, with the result that significant variations of the same policy between different operational business units are in evidence in the form of unendorsed emergent pay practice. To the frustration of one senior pay specialist at *Food Co*: 'I think the intent when this was done [the design] was quite clear. I think for a whole variety of reasons, and they are primarily, you know, sometimes people's rather malicious desire to interpret things differently, but because of a lot of these things, that's not what we ended up with.' (*Food Co:* Senior Reward Director – emphasis added). Such instances of line management rebelliousness, for whatever reason, are sometimes known to senior management and pay specialists operating corporately. Sometimes they are not.

The final level of analysis, the pay *operation*, reveals the operational reality of attempts to use pay strategically. Where locally determined, line management choose not to use pay strategically, despite the wishes of senior management. Where centrally determined, what is intended in the form of pay policy is, for a variety of reasons, rarely achieved as operational practice. Despite the corporate rhetoric, the reality of pay operationally within the sample firms is non-strategic.

DISCUSSION

This research programme sought to address a number of apparent tensions in current theorizing on pay. Specifically, the study sought to explore the process and basis upon which contemporary pay systems are determined at multiple levels organizationally and attempted to answer three basic questions: *how* are firms attempting to use pay; *how* does this influence the form and function of contemporary pay systems; and, finally, *how well* are these systems perceived to work? The insights gained through multi-level analysis afford us rich insights into the realities of pay practice within the sample firms. A number of conclusions are drawn and the implications for pay theory, practice and future research discussed.

Analysis of the determination of pay at multiple levels is especially fruitful. Current single-level theorizing on pay neglects many of the facets of what is a highly complex process that occurs at multiple levels and is prone to multiple influences producing multiple (and not necessarily complementary) outcomes. Pay practice at the level of approach, the philosophy underlying pay practice and articulated in the form of strategic aspirations, is primarily informed by institutional norms which encourage convergence between organizations. The outcome of pay determination at this level, articulated typically as pay strategy, is of primarily rhetorical value and secures legitimacy both for the organization and those with the responsibility for pay determination – senior management notably. Thus, superficially, pay practice is far more similar than it is different at this level, which has been interpreted perhaps as evidence of the existence of best practice by some. Rather, it is argued here that such convergence around specific pay related norms is evidence of common principles rather than tangible practice that has universal application and value independent of the context in which it is applied.

Pay practice at the level of design, the technical content underpinning practice and articulated as policy, reflects the most rational (by the standard definition of theory) portion of the pay determination process. At this level, pay specialists seek to devise pay practice that is best aligned to the pay *approach* and known internal organizational conditions. The retained design reflects the intended state of pay at the point of implementation. However, management are limited cognitively in their capacity to choose pay practice ideally fit for purpose. The complexity of both formal (structures, processes and systems), and informal (culture, norms and behaviours) aspects of the organization is such that securing alignment between the pay *approach* (strategy), *design* (policy) and *operation* (implementation) is largely unmanageable. Nevertheless, pay policy as a manifestation of the intended design, is primarily managerially determined. If managerially determined through a process of rational deliberation and preference ordering (i.e. selecting the optimal pay design given known conditions), does that render the pay design as strategic? Is pay strategic at the level of design? The question is moot. The value of pay policy is limited unless effectively implemented as intended. The findings indicate that policy is rarely implemented as intended. As has been illustrated, corporate control over the form and function of pay operationally is more perceived than real.

At the level of operation, the point of implementation, pay practice is shaped by myriad micro structural and institutional pressures pervasive within the host (localised) environment. Custom and practice is pervasive operationally at the ‘coal face’, and limit the effective implementation of standardized policy and / or encourages adaptation to the point that it ceases to resemble its original configuration. Whether pay determination is centralized or decentralized, pay custom and practice, manifest of persistent pay norms, is the primary determinant of pay operationally, and not corporate intervention. Combined, these pressures encourage extensive divergence between firms at the inter-firm level and between divisions and units within the same firm at the intra-firm level.

In the case of the sample firms there is a gap between the three levels of the pay *approach*, *design* and *operation* – between strategically what’s desired, intended as policy and achieved as pay practice operationally. The distinction between intended and actual practice is omitted from strategic management literature. Very little of the research underpinning standard theories of strategic pay recognize that 'not all intended HR practices are actually implemented, and those that are may often be implemented in ways that differ from the initial intention' (Wright and Nishii, 2004) and yet the findings are clear evidence of this. Despite rational planning at the design stage, selected pay systems are rarely perceived to be fit for purpose by line management responsible for implementation. Equally, when given full responsibility for the management of pay (both design and operation), they choose typically not to use pay in ways that would be characterized as strategic. They rely upon other managerial measures to secure desirable employee behaviours and performance. In the language of Gerhart and Rynes (2003), attempts to use strategic pay are neither ‘successfully implemented nor executed’. The findings raise serious doubts of the *manageability* of strategic pay systems. Whilst intuitively appealing, is attempting to use pay strategically even viable?

Moreover, in a significant number of cases, attempts to use pay strategically produce negative outcomes. Contrary to the promise of advocates, it is apparent that if poorly managed, strategic pay systems can diminish motivation, misdirect behaviours undesirably, consume managerial time and effort, misallocate pay spend, and produce various other outcomes that are quite the opposite of what is intended. Moreover, if pay is indeed a value-adding activity, then the value created is seemingly impossible to measure in the way that is most often desired – in financial terms. The inability to assess and measure quantitatively the financial value-added contribution of pay is a perennial frustration. All firms are struggling to get pay 'right', and some are failing to the degree that, arguably, they are getting it *wrong*. In practice, the experience of the sample firms would suggest that attempting to use pay strategically carries with it a number of risks, not least the possibility that strategic pay can achieve precisely the opposite of what it is supposed to.

Why the apparent disparity of effectiveness between centralised and decentralized pay determination? The findings indicate that centralization in authority for pay decisions invariably results in standardization of pay practice. Standardized pay policy, reflecting often a ‘one size fits all’ approach, is perceived by line management as a poor fit for the diverse needs and environments of the sub-organizations that comprise the organization as a whole – each operating potentially in different locations throughout the world, engaged in diversified product and service offerings, and employing different categories of employee. A recurring theme within the findings is the distance between pay specialists operating centrally and the environment (i.e. business and / or division) in which policy is to be enacted. Given the myriad diverse structural, social and micro-institutional pressures pervasive at the sub-organization level, the dominant environment at the point of implementation, could any standardized pay design ever be truly fit for purpose? Arguably, cognitive limitations inhibit a remote comprehensive understanding of the sub-organization and its environment. The implication is that the development of effective organization wide pay policy is inherently problematic and doomed to only partial success or, more likely, failure. Thus, there are limits on the capacity of organizations to effectively determine pay corporately, and the findings are perhaps a clarion call for democratic and devolved management within our most complex and important commercial organizations. Nevertheless, more organizations than not within the sample seek to centralize pay determination. Moreover, contrary to the stated intention, pay, along with other related interventions such as performance management, is used as a means of exerting organization level control. The rationale for seeking such centralized control is not necessarily malign – it can reflect a concern for good governance for example. Ultimately, however, the organization’s needs are often in conflict with the needs of the sub-organization, and pay has become the frontline (one of many perhaps) in the battle between the Centre and the Line.

The relationship between pay determination and value creation is also more nuanced that presumed by extant commentary on strategic approaches to pay. The findings further indicate that, in place of economic value creation, enhanced legitimacy is a value adding outcome of the adoption of strategic pay practices. Thus, the adoption of strategic pay practices confer upon the organization rhetorical value in the form of enhanced legitimacy, if not substantial value in the form of enhanced firm financial performance. Off-set by the costs of designing and implementing strategic pay systems, and given the potential for unintended consequences and negative outcomes, what is the rhetorical value of enhanced legitimacy worth to organizations? A great deal it seems, as all available trend data indicates that strategic pay practices are becoming increasingly widespread year on year (Watson Wyatt 2007). Despite the evidence to the contrary presented here, organizations are more and not less likely to attempt to use pay strategically in the interests of making a difference to the bottom line.

The sample firms are nevertheless successful in spite of their pay systems. Despite manifest variance in the effectiveness of their pay systems, and the associated outcomes – positive, neutral or negative experienced as a result, all of the case companies retain high levels of firm financial performance and are universally recognized as market leaders. Does pay matter therefore? Pay does matter, it is argued here, both in terms of its economics and social impact. However, the sample firms most likely experience superior firm financial performance as a result of numerous additional factors, and not pay. It is further argued here that the sample firms are successful *in spite* of the manifest negative outcomes associated with their attempts to use pay strategically. Presumably, they would have enjoyed even greater firm performance had their pay systems not produced unintended and negative outcomes in the form of employee disengagement and attrition. Whilst the valued added contribution of pay (like other human resources interventions) is notoriously hard to measure quantitatively, the negative consequences of attempts to use pay strategically and its subsequent mismanagement are all to obvious qualitatively.

Given the apparent ambiguity surrounding its manageability, why does strategic pay retain such appeal? Why, despite the manifest challenges involved, is the adoption of strategic pay increasingly more common and not less? In part, the promise of strategic pay is seductive and the commentary of advocates compelling. However, there may be other reasons too. Centrally determined pay systems are characteristically used as a means of driving the organizations towards the attainment of corporately determined performance targets. A consistent theme to emerge from the findings was the use of pay as a crutch for ineffective leadership. Have headquarters personnel lost confidence in local management within subsidiary businesses to drive performance? Are they using pay in an attempt to secure that performance directly? Has pay, in effect, become a panacea for effective management development? If so, the findings indicate that it is at best a placebo.

Implications for theory: The empirically grounded findings presented here challenge many of the *managerial* assumptions underpinning strategic theories of pay. Strategic theories of pay assume universally, for instance, rationality on the part of decision makers; that choice is the primary (if not sole) determinant of pay practice; that management are collectively united in their interests and intent; that conception and execution are indivisible; and that pay is an organization level intervention. On the contrary, pay is best conceived of as a multi-level phenomenon and not single level nor solely a strategic activity. Pay practice exists in multiple states at multiple levels and is influenced variably by a multitude of exogenous and endogenous non-managerial determinants. The findings indicate that at the organization level, pay is predominantly rhetorical in nature and produces outcome of rhetorical value e.g. the semblance of legitimacy. At the business unit level, the experience of operational pay practice is different again. To consider one level of pay practice solely, and not all, is to neglect much of the true nature of pay as it is experienced by multiple stakeholders throughout the organization and beyond.

Insert table 3 about here

In a contribution to more robust theorizing, the findings support the notion that pay determination outcomes are influenced deterministically by powerful institutional and social forces. The global and UK FMCG markets are two structured (and interrelated) organizational fields in which a variety of institutional mechanisms facilitate the dissemination of standardized pay practice between like firms. The sharing of 'best practice' is especially prevalent. Far from being best practice in *absolute* performance terms, the pay norms observed in the *approach*-level findings represent perceived best practice in institutional terms – they represent best *principles* of practice in effect, which resonates with the sentiments of Guest (1997). Such best practices do not confer enhanced financial performance on the adopting organization. Rather, they confer enhanced *legitimacy*. Whilst not necessarily effective at producing outcomes of strategic value, legitimate pay practice is still of value to management, especially given the need to justify pay decisions to both investors and employees (Boselie et al 2003). The net result is isomorphic convergence within the sample around legitimate pay norms. Moreover, the greater the uncertainty involved, it seems, the more likely pay decision makers are likely to reference external standards of practice and expose the organization to ever greater degrees of isomorphism as a result.

Indeed, management do not operate on the basis of comprehensive, much less perfect, information upon which pay decisions might be based. This problem is exacerbated within large complex organizations operating internationally (Jones 1999). Nor do pay decision makers have an accurate understanding of the likely outcomes of decisions they make a priori, as the complexity of the pay means – ends casual relationship defies prediction, and even probability of outcome, in many cases (Simon 1959). Pay decisions attempting to establish the optimal *form* of pay are often little more than elaborate guesswork, informed by past experience and what rudimentary data is available (Cyert & March 1963). In the face of such *uncertainty*, decision makers have little option but to reference practice externally - to consider the experiences of others who are perceived as legitimate and are therefore influential. Indeed, pay decision makers, particularly specialists operating corporately, are encouraged to reference externally by senior management, who seek affirmation in the form of benchmarks or peer comparisons (DiMaggio & Powell 1997).

In a further theoretical development, new-institutional theorizing appears to apply at not only the institutional level of analysis, but also sub-organizational levels of analysis in the form of workplace social and political norms that serve to shape the form and function of pay operationally. Theorizing on custom and practice is particularly relevant to the study of contemporary pay systems, and share many related themes with new-institutional theory. Both are almost entirely absent from contemporary commentary and merit further development and, indeed, conceptual integration.

Equally misguided is the assumption that management collectively are united in interest and intent – that of securing economic maximization principally. In place of unitarism, *pluralism* of interest continues to characterize not only the relationship between employer and employees, but also within the management structure itself[ii] (Fox 1971; Kochan et al. 1986). At the level of *approach*, for example, senior management principally desire alignment between pay and strategic priorities in the interests of securing enhanced performance and competitiveness. However, whilst alignment clearly influences the pay *design*, pay specialists are also driven by the need to establish functional legitimacy and personal credibility. The more sophisticated the pay *design*, the greater their status and standing with professional peers, or so the logic goes. At the level of *operation*, a desire for equity and workplace harmony encourages line management to limit the disruption of new pay systems by adapting them or, in the extreme, rejecting them entirely. Pay system effectiveness is

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[ii] Three distinct classifications of management involved in the pay determination process are used here. Principally senior management, pay specialists and line management.

contingent upon management at all levels of the organization acting coherently towards the attainment of a shared purpose – a rarity within the sample firms.

Despite the manifest challenges encountered by the sample firms, which extend to others outside of the sample presumably, the firms researched are more likely to attempt to use pay strategically than not. They do so within constraints, as noted, but the view persists generally that management is free to manage pay as they see best in the interests of securing competitiveness. The findings challenge this view and suggest that much of the freedom that management enjoy to determine pay unilaterally is more perceived than real. Pay decision makers are bound by institutional forces, some of which are consciously appreciable, but also indirectly by socially constructed norms, rules and scripts that are taken-for-granted. This resonates with the notion of *soft determinism*. Freedom is defined by soft-determinists as 'the power to do what one wants', even if one's desires are themselves wholly predetermined (de Rond and Thietart 2007). Pay practice is not formulated voluntaristically (i.e. as a result of free will), but *formed* in part deterministically.

Given this, what role for strategic choice? The findings suggest that standard theory overemphasises the role of strategic choice in determining pay at all levels, especially at the level of operation. Choice continues to feature in pay determination, especially at the level of design, but overall is one of many inputs and is potentially less influential than others. The notion of total choice, and managerial control over pay by extension, is an illusion. We should not assume by default that management are in control of pay. Summed up succinctly by Kessler, "How can rational, economic decisions be made if cause and effect remain uncertain, if actors and systems interact in complex ways, if organizations are drawn by histories of countless internal battles, allowances and compromises?" (Kessler 1995).

Given the tensions surrounding choice, and other assumptions, are we therefore overestimating the strategic potential of pay? Indeed, can pay be strategic in light of the findings? It is argued here that by the absolute terms of what has become standard theory, it cannot. Strategic approaches to pay are not sufficiently grounded in the complex and messy reality of organizations to be achievable by the pure terms of standard theory. As a result, many of the prescriptions of strategic pay theory, the 'received wisdom', are unachievable in practice. This may explain the limited success that organizations (even the leading sample companies) experience when attempting to use pay strategically. In attempting to do so, the sample companies have exposed themselves to a greater likelihood of failure than success and the risks associated with failure are significant in value terms. We are indeed overestimating the strategic potential of pay.

Limitations and future research: It is recognized that the findings and conclusions presented within this paper will not prove popular with large sections of the pay profession, remuneration and management consultants, academics, and others with a vested interest in the success of strategic pay conceptually and prescriptively. They will find it overly negative – pessimistic perhaps – and may challenge the conclusions drawn from the findings by citing numerous counter examples and stories of success. The methods used here, necessary to gain the 'deep' insights presented as findings, may also be criticised on those same grounds that relegate qualitative studies of pay secondary in terms of importance to dominant positivist quantitative studies – namely reflexivity, an inability to generalise and other such acknowledged limitations.

However, this study sought to understand better the management and effectiveness of strategic pay systems in practice and, in doing so, highlighted some of the weaknesses of what is now standard theory. The relevance of additional of theory were exposed, as well as a number of avenues of rich empirical research hitherto neglected, all of which merit further development academically. In attempting to move beyond the dominant logic of strategic pay, future research might best focus on exploring further the role new-institutional pressures play in shaping pay practice. Furthermore, little work known to the author has sought to integrate these new-institutional pressures with other powerful environmental forces that also serve to constrain and inform managerial choices, and understand therefore the dynamic interplay of forces that influence the shape and formation of firms' pay practices.

This study benefited from - indeed, would not have been possible without, the use of the multilevel framework. The segmenting of separate levels of pay practice within a hierarchical framework (*approach*, *design* and *operation*) has now a proven track record and would benefit future research aimed at investigating further pay and (potentially) other functional interventions. It is recommended that the framework be both developed further and deployed through future research. The methodological approach adopted here – in many ways a departure from mainstream approaches - has, it is hoped, proven its validity and its utility. In addition to the multi-level framework therefore, future research might seek to develop our understanding of pay related phenomena by deploying the same or similar methods. An obvious direct development of this study would be to combine the greater use of quantitative methods within the predominantly qualitative approach adopted here in the interests of yielding an even richer and sorely needed foil to the ‘received wisdom’.

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FIGURES AND TABLES

Table 1: The practice-centric multi-level framework

	FUNCTION	FORM	STATUS
APPROACH	Philosophy and values	Strategy and / or vision	Desired
DESIGN	Technical	Policy	Intended
OPERATION	Workable	Practice	Achieved

Table 2: Summary of key sample firm attributes

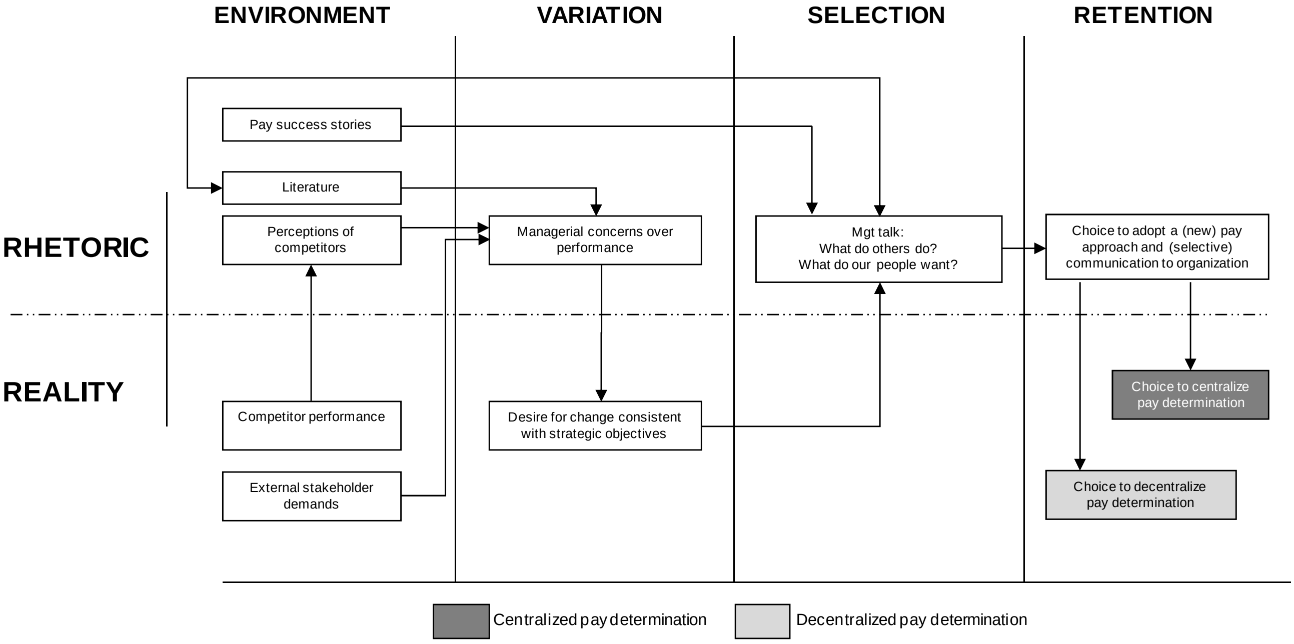
	Tobacco Co.	***Choc Co.***	***Drink Co.***	***House Co.***	***Grocery Co.***	***Candy Co.***	***Food Co.***
Industry	FMCG	FMCG	FMCG	FMCG	FMCG	FMCG	FMCG
Sub-industries	Tobacco	Confectionery & beverages	Alcoholic beverages	Home, health and hygiene	Confectionery food and beverages	Confectionery food and pet care	Home, personal care, food & beverages
Size (no. employees)	>90,000	>55,000	>45,000	>50,000	>90,000	>35,000	>200,000
Founded	>100 yrs	>150 yrs	>50 yrs	>50 yrs	>180 yrs	>75 yrs	>100 yrs
Life cycle	Mature	Mature	Mature	Mature	Mature	Mature	Mature
Ownership	Public	Public	Public	Public	Listed subsidiary	Private	Public
Org. structure	Holding Co / country structure	Business unit	Regional structure	Regional structure	Regional structure	Regional structure	Matrix
HQ	UK	UK	UK	USA	USA	USA	UK and Netherlands
Market Strategy	Brand led	Brand led	Brand led	Brand led and supplier	Brand led	Brand led	Brand led and supplier
Scope	Multi-national	Multinational	Multi-national	Multi-national	Multinational	Multinational	Multi-national
No. of facilities	54	48	21	36	95	65	100
Markets	160	135	180	150	155	120	150
Performance	Market leading	Market leading	Market leading	Market leading	Market leading	Market leading	Market leading

Source: Datamonitor (2004 - 2006) and sample firm company reports and accounts

Table 3: An integrated model of pay determination

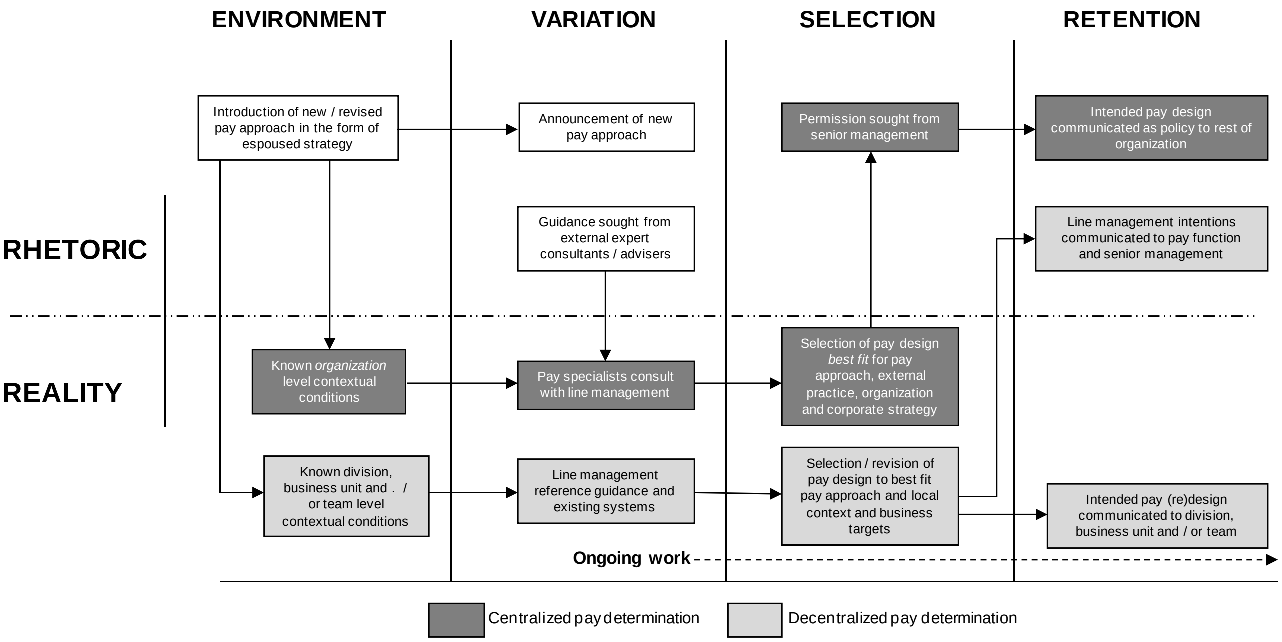
	FUNCTION	FORM	STATUS	DETERMINANT	OUTCOME
APPROACH	Philosophy and values	Strategy and / or vision	Desired	Institutional	Convergence
DESIGN	Technical	Policy	Intended	Managerial	Perceived choice
OPERATION	Workable	Practice	Achieved	Social	Divergence

Figure 1: the process of pay determination at the level of APPROACH



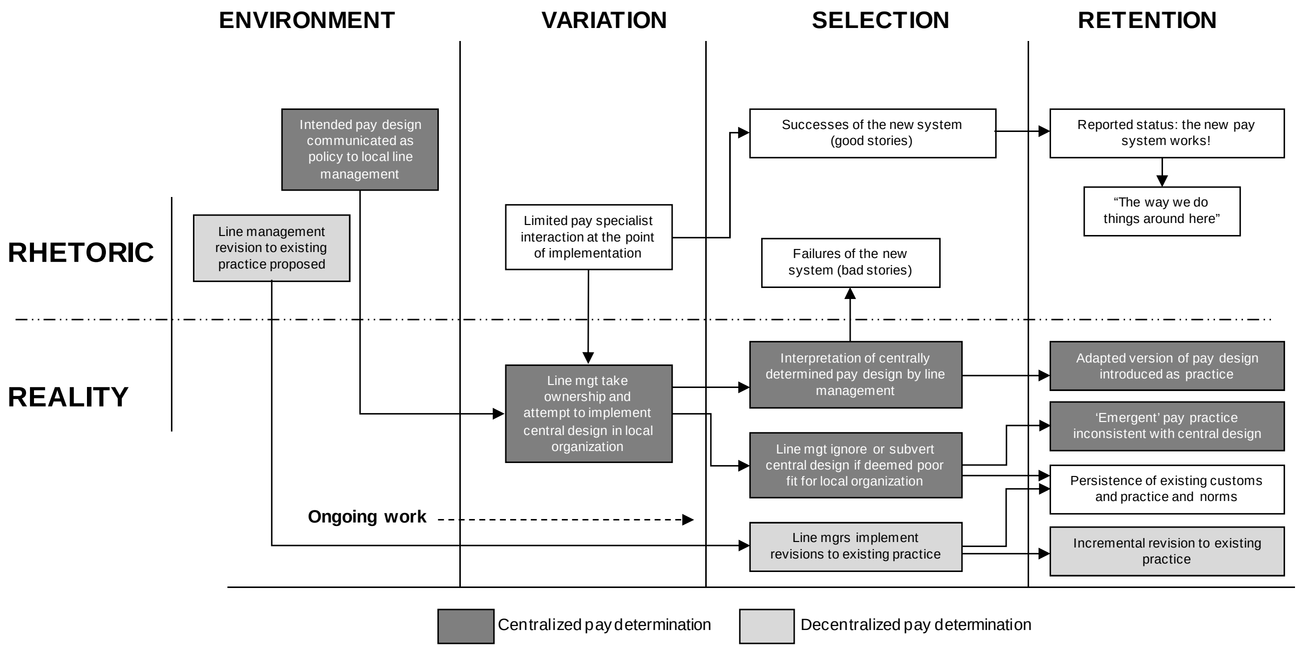
Adapted from Zbaracki (1998)

Figure 2: the process of pay determination at the level of DESIGN



Adapted from Zbaracki (1998)

Figure 3: the process of pay determination at the level of OPERATION



Adapted from Zbaracki (1998)