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Influences on reward mix determination: reward consultants' perspectives

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Abstract

Purpose – Reward research has focussed on level (what individuals are paid) and structure (relationship between different levels of reward). Less emphasis has been given to reward mix decisions, i.e. the relative proportions of each element making up overall reward. This paper seeks to examine the determinants of reward mix.

Design/methodology/approach – Interview based research with reward consultants as key organisational observers and participants in reward mix decision making.

Findings – Benchmarking has led to the development of reward mix norms. Organisations are under pressure to conform to these norms, moderated by leadership beliefs, the occurrence of events and the extent to which organisations' change capability can overcome strong institutional forces.

Research limitations/implications – The results question agency theory based explanations of reward mix determination and point towards resource dependence and institutional theory perspectives being more suitable theoretical frameworks.

Practical implications – The model developed allows reward managers to consider how the moderating variables, to the dominant mimetic pressure faced, could be manipulated for their firm to allow greater differentiation of the reward mix.

Originality/value – Academically the work contributes to a programme of research into reward determination from a constructionist perspective and aims to provide greater theoretical robustness to the subject. Practically, the findings may prompt practitioners to think more consciously about the drivers of their firm's reward mix. Policy makers may use the stronger theoretical base for understanding the determinants of reward mix choices and the extent to which organisational free choice and institutionally determined choice influence final choices in reward policy decision making.

Keywords Pay policies, Organizational theory, Consultants

Paper type Research paper

Introduction

The focus of the reward literature has largely been on a narrow definition of reward, examining pay, both fixed in the form of salaries and wages, and variable through schemes such as incentives and bonuses (Gerhart and Rynes, 2003). Reward mix has received less attention and measures used vary across different studies. Narrow definitions of reward mix have been conceptualised through the use of the ratio of base salary to short term bonus payments (e.g. Eisenhardt, 1988; Bloom and Milkovich, 1998). Alternatively, others have widened this simple ratio to examine the proportion of base pay to cash compensation i.e. including short and long term incentives (e.g. Tremblay *et al.*, 2003; Burke and Hsieh, 2006). Others have used the closely related area of bonus to cash compensation (e.g. Gomez-Mejia *et al.*, 1987; Elvira, 2001). These studies neglect the increased trend in practice where a "total reward" approach is increasingly common (World at Work, 2007). This research responds to this wider definition and call by some scholars that research should incorporate non wage

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compensation elements and look at the determinants of reward mix (Gerhart and Rynes, 2003; Heneman *et al.*, 2000).

2. Theoretical perspectives

Significant research has been conducted examining the factors that are proposed as determining an organisation's choice of reward systems (Cox, 2000). For example, Gerhart and Milkovich (1992) provided a compensation decision model portraying how both environmental and organisational factors, such as the organisation's business and HR strategy, directed the reward system. Following their work other scholars have conducted a large number of statistical studies examining potential "contingency" factors in reward determination including business strategy (Montemayor, 1996), firm size (Artz, 2008), ownership structure (Blasi *et al.*, 1996), unionization (Abraham *et al.*, 2008), economic variables (Christofides and Laporte, 2002), technological changes (Brown and Campbell, 2002), environmental uncertainty (Umanath *et al.*, 1996) and legal factors (Kaestner and Simon, 2002). Consequently a variety of causal relationships have been identified between different variables, but less has been learnt about why these factors may be influencing decisions (Gerhart and Rynes, 2003).

A range of theoretical explanations have been developed from the causal relationships established. Baeten (2008) identified 34 different theories used in reward research, a number of which examine reward mix determination. Therefore, although significant reward determination research has been carried out, we appear to know little about how reward mix is determined as there is no dominant paradigm (Gerhart and Rynes, 2003). Convergence around a smaller number of perspectives might therefore help direct future research (Pfeffer, 1993). Two commonly applied perspectives are now reviewed – agency and institutional theory – following previous research which showed that combining these approaches provided a more complete insight into reward mix determination (Eisenhardt, 1988).

Agency theory

Agency theory provides insight into what reward mix best aligns organisational and individual objectives. It outlines how the separation of organisational activities from ownership presents the problem of ensuring that owners' interests are aligned to those responsible for operating the business (Jensen and Meckling, 1976). Owners look to ensure that employees direct their work effort in line with the owners' interests. This can be achieved through adjusting the reward mix, in particular the balance between fixed and variable rewards, to ensure that appropriate incentives are in place for the employee to act in the owners' interest (Jensen and Meckling, 1976). The large body of research on agency theory generally supports its predictions that organisations can use incentives, alongside monitoring activity, to control employee effort (Eisenhardt, 1989; Prendergast, 1999).

Agency theory has emerged as the main theoretical explanation of reward mix. However, while the agency research tells us about the fixed to variable reward relationship, it does not incorporate benefits and relational returns. It has also been suggested that the approach overemphasises efficiency and rational drivers of reward mix determination and underestimates the institutional pressures that may also be relevant (Bartol and Locke, 2000). This led Barringer and Milkovich (1998, p. 71) to conclude that "agency theory presents a partial view of the world … that ignores a good bit of complexity of organizations". Institutional theory is now reviewed as an alternative perspective on this complexity.

Institutional theory

Institutional theory proposes that institutional forces create coercive, mimetic and normative pressures on firms to be similar in how they operate (DiMaggio and Powell, 1991). The extent to which these constraints operate for each organisation influences how much freedom of choice they have, including choice of reward mix (Carpenter and Wade, 2002).

Coercive isomorphism "results from both formal and informal pressures exerted on organizations by other organizations on which they are dependent" (DiMaggio and Powell, 1991, p. 67). These pressures can take a number of forms. First, legal, through laws and regulations set by government, or bodies acting on their behalf, such as tax authorities. Employment legislation in the UK has increased significantly since 1970 with, for example, minimum wage, working hours and holiday entitlements, share ownership and pension legislative requirements having been introduced (Perkins and White, 2008). These politically driven influences on reward mix, through the effect on benefit provision, may mean specific benefits are provided even though they are expensive (Festing *et al.*, 2007). Perkins and White (2008, p. 67) suggest that the legal context is so significant that "while employers may wish as far as possible to create reward strategies for their own particular circumstances, the starting point will always be what the law allows or requires.". Second, a major role for reward managers, as the tax system regarding pay and benefits changes, is the goal of tax efficiency, especially around the balance between benefits and cash wage payments (Perkins and White, 2008). The significance of tax has been emphasised by Long and Scott (1982, p. 218) who concluded that "taxation is a major determinant of the compensation mix".

Mimetic behaviour takes the form of organisations adopting policies that others have adopted in order to gain the security that conformity is perceived to bring (DiMaggio and Powell, 1991). Organisations look to avoid uncertainty and diverging from standard practice introduces a level of uncertainty in comparison to other organisations (Norman *et al.*, 2007). Mimetic pressures would appear to be commonplace in the reward field. First, organisational knowledge may be held by particular individuals and, through turnover, this knowledge may be spread across other organisations. Specifically, employees may be hired because of their knowledge of wider practice. Specific reward specialist recruitment agencies have been established (e.g. TotalRewardCareers), potentially indicating a specialist market in reward executives and a flow of their expertise across organisations.

Diffusion of standard reward mix practice may also occur through the activities of consulting firms and trade associations (DiMaggio and Powell, 1991). The use of consultants has been shown to have a legitimising effect (Main *et al.*, 2008). The reward consulting profession is well established in the UK. A Chartered Institute for Personnel Development survey (CIPD, 2008) found that 32 per cent of organisations had used a consultancy service to provide benchmarking data. Benchmarking has been identified as a key factor assisting the spread of isomorphism (Eisenhardt, 1988).

Finally, normative pressures stemming from "the collective struggle of members of an occupation to define the conditions and methods of their work . . . and legitimisation for their occupational autonomy" (DiMaggio and Powell, 1991, p. 70). For example the

"New Pay" prescriptions that pay should be linked to performance (Lawler, 1995), which have been widely adopted despite concern that they may not be appropriate prescriptions for all organisation (White, 1996). Eisenhardt (1988) found that the key driver in determining reward mix was acceptance of the practice within the sector, rather than the alignment with strategic goals. Support is also evident from research on executive reward. For example, Bender (2004, p. 521) concluded that "companies used performance-related pay because their peers did, and because that legitimised them in the eyes of the establishment".

What evidence do we have of isomorphism in reward mix situations? Institutional theory has been used to understand organisations' approaches to reward mix decisions in a variety of ways. Eisenhardt (1988) concluded that contextual conditions at the time the organisation was established were particularly significant on reward mix choice and, once chosen, the reward mix had longevity. Van der Stede (2003, p. 268) identified the presence of "intracorporate isomorphism", reflecting the strong influence of parent companies on business unit reward mix decisions. Segalla *et al.*'s (2006) examination of cross-national sales compensation practices concluded that culture influences reward mix determination through the effect it has on managers. This led them to question the applicability of institutional theory's prescriptions for effective reward mix decisions in all scenarios, in particular where national boundaries are concerned. Fernandez-Alles *et al.* (2006) found that reward mix policy incorporates popular trends and practices that will not necessarily increase organisational performance, but will increase legitimacy, stating that "variable compensation is sometimes designed to reward not those particular practices and procedures that rationally should enhance the performance of the company, but those that enhance its social standing and reputation in its institutional context" (Fernandez-Alles *et al.*, 2006, p. 963).

The review of empirical research on reward mix determination appears to show that institutional pressures do exist, and that they are often influential. However, while insightful, the theory does not appear to fully explain behaviour and differences in practices between organisations. Critics argue that institutional theory fails to fully incorporate individual organisational strategic and leadership goals (Oliver, 1991). Given that reward mix can be adjusted without increasing costs (Lazear, 1998)[1], then organisations may face less difficulty in differentiation themselves in this area. "[P]ay mix is where the action is in differentiating organisations" (Gerhart and Milkovich, 1992, p. 569).

Summary

If agency theory is to be believed then we might expect reward executives to discuss how monitoring of employees and efficiency considerations has influenced the mix of at least fixed and variable pay. However, it has little to say about benefits. Institutional theory identifies a societal dimension to reward mix determination as organisations seek to gain legitimacy. Reward mix decisions are therefore largely driven by fixed constraints, both legal and tax, alongside pressure to conform to the practice of other organisations or prescribed best practice formulas. These two perspectives are summarised in Table I.

The review of the literature has identified a number of areas where further reward mix research would appear warranted, with agency and institutional theories offering potentially useful perspectives for this research. We have seen how the

	Agency	Institutional
Purpose of reward mix decisions	Alignment of employee objectives to those of the organisational owners	Conformity with other organisations and market practice to gain legitimacy
Main assumptions	Rationale decisions People are self interested, risk averse Goal conflict and information asymmetry exists between owners and employees	Organisations seek legitimacy Organisations conform to norms
Organisational reaction	Rational active management	Passive conformity or rational legitimacy seeking
Implications for reward mix	Relative weight of incentives versus fixed reward will be managed to optimise the alignment of agent and owners' interests	Reward mix will be influenced by institutional norms and the extent to which operating within these norms confers legitimacy

Table I.
Summary of agency and institutional theory

conceptualisation of reward mix has typically been incomplete, neglecting significant components in benefit provision and less tangible non-financial rewards. Applying a wider definition would appear appropriate. Further, a large number of factors have been shown to influence reward mix decisions. This suggests that despite the research carried out, we in fact know little about how reward mix decisions are taken as no dominant paradigm has emerged. This may be an accurate reflection of reality, with this area of reward strategy determination being particularly complex. Alternatively, it may be that the "shopping list" of factors has muddied the field and after all this research we can conclude very little. Thus, research to provide greater clarity to the field of reward mix determination would appear to be needed.

3. Method

This research aims to deepen our understanding of how organisations determine their reward mix. Much of what we know about reward mix determination has been conducted through statistical review of archival or survey data. While relevant for a field of this nature, it has meant that little time has been spent with the reward policy decision makers to explore how they understand reward mix determination. Considering the area from a different research paradigm may add insight and potentially contribute to simplifying the field. This is in line with an emerging body of work looking to establish not only what is driving reward decisions, but also why these factors are important (Bender, 2007; Ogden and Watson, 2008).

The research reported here used reward consultants as informants for three reasons. First, they are acknowledged experts in their field. They have relationships with reward professionals and senior management in organisations and can play a significant role in reward decisions (Bender, 2008; Clark and Fincham, 2002). Second, the difficulties of researchers carrying out participant observation of organisational process have been noted with respect to entering the field, establishing a role and building a relationship (Luders, 2004). However, Rynes and Bono (2000) noted the excellent access that reward consultants have and suggested forming alliances with these individuals as a way of furthering reward research. Finally, their insights provide an alternative perspective to direct organisational responses.

Semi structured interviews, lasting between 30 and 80 minutes (an average of 45 minutes), were held with ten consultants from three global reward consultancies and one smaller independent consultant between December 2008 and October 2009. This was consistent with McCracken's (1988) contention that for much research a sample of eight was sufficient. An interview protocol was developed building on a comprehensive review of the literature with respect to reward mix determination.

With the permission of the respondents, all the interviews were recorded and transcribed resulting in 160 pages of single spaced transcript. The data was then coded with the support of NVIVO 8 software. This coding was initially done against a conceptual framework derived from the themes identified in the literature review, but after three interviews, this was amended with the addition of a resource dependency perspective (see discussion). The final conceptual framework applied to coding the interviews is shown in Figure 1.

This conceptual framework presents interests, forces, practices and resources as theoretical drivers of reward mix decisions.

All those interviewed had reward consulting backgrounds and wider experience in strategy consulting, actuarial science, research, graphic design as well as senior level experience in reward management in industry. Given the extent of their reward experience, they appeared well qualified to express views on reward mix determination. Initial concerns that the interviews would lead to the same "house" view of reward mix determination were unfounded.

4. Findings

This section outlines the research findings on how organisations determine reward mix. Findings on who is involved in reward mix determination are presented, followed by the factors that were identified as influencing these decisions in line with agency and institutional theory predictions that reward mix will be influenced by factors both within an organisation and pressures external to the organisation.

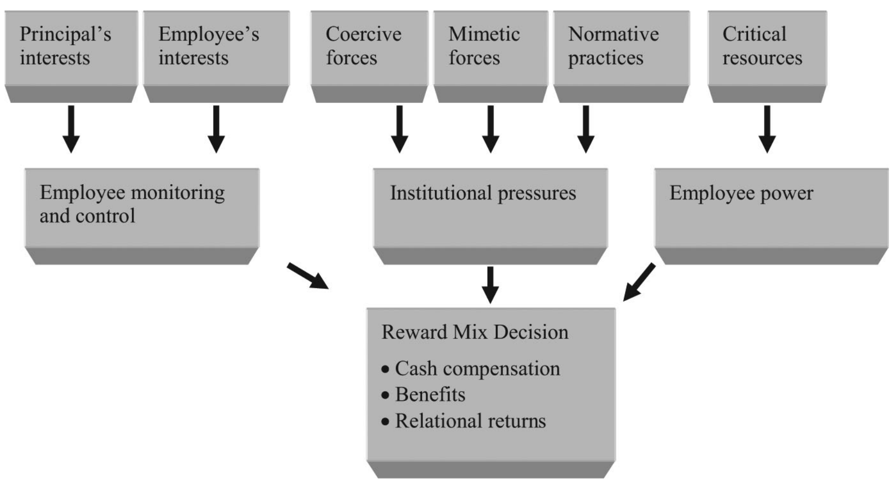

Figure 1.
Reward mix conceptual framework

Decision taking

The reward mix decision was identified as being influenced by four groups – The Board, the Executive, the HR Director/Head of Reward and the Finance Director (FD).

The interviews identified that some whole Board involvement occurred in all organisations. This typically focussed on the agreement of the overall reward budget, which tended to be dominated by base salary budgets, rather than detailed discussions of reward mix.

> Obviously the salary budget and the bonus and base increase proposals have to go through the board. If pay is 70% of your identifiable operating cost, it would be very surprising if it were any different [Consultant 3].

The extent to which the Board was involved in reward mix determination was seen as increasing, driven by two events. First, the increase in pension costs for those companies still operating defined benefit pensions. Boards were involved in decisions on whether the organisation should continue the scheme and shoulder the financial risk that this entails, or close the scheme and manage the employee unrest that may result. Second, the increased political and regulatory interest in the remuneration of employees below the executive level.

> REMCOs are being encouraged to look at coherence [of Executive reward schemes] with the rest of the organisation, so they are probably more interested than they used to be [3].

The extent to which decisions on reward mix were managed at the Board was believed by one interviewee to be related to the extent to which the HR Director had a role at Board level.

> The most sophisticated organisations will tend to be those where there is a HR contribution to the Board and where the leadership team itself . . . takes more of a transformation view of how you run an organisation than a transactional one [3].

The influence of the FD was also raised. The FD's interest was reported to be determined by the extent to which the organisation was driven by consideration of people as costs to be managed, as opposed to assets to be valued and developed. A number of the consultants emphasised the role of the FD, of which the following is representative.

> The Finance Director is going to be concerned just about the cost of things and they are going to look at that in a very material way [7].

The power of the FD over reward mix decisions was seen to have increased with the rising costs of defined benefit pensions and questions over the extent to which employees should be required to participate in organisational pensions schemes. This presented potentially conflicting objectives between the HR and Finance functions on pensions, with HR working to encourage employee participation in the pension scheme and finance focused on the overall cost of its provision. The FD's position was summed up by one consultant.

> I have had conversations with FDs who have dismissed the need to do anything about DC [defined contribution] engagement because they just don't see the point – its increased costs for the company, why do we care? [7]

Overall, the range of organisational decision makers with some role in determining the reward mix was diverse. No one individual or group was seen to dominate the decision. The following comment being representative.

> All I see is a horribly fractured approach to determining reward mix [5].

Competing pressures were seen to be potentially detrimental to the achievement of the most effective reward mix for that specific organisation. The effect of the competing interests was suggested as one reason why market benchmarking and mimetic behaviour tends to dominate the final mix decision.

> All of the strategic players are involved, in practice once you start doing that you end up with a committee and you end up with a principle or an idea that gradually gets shaved away until you get left with, well let's do what the market does [5].

Drivers of reward mix

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

Institutional pressures. The interviewees identified mimetic and coercive pressures as paramount in organisations' reward mix determination. No evidence was found of normative pressures.

Mimetic pressure – the market. The primacy of "the market", through the examination of the reward mix of other organisations, was uniformly identified as the main external influence on reward mix determination. Informants generally referred to labour market pressures and the extent to which labour was seen to be scarce, as opposed to the overall competitiveness of the product market within which organisations were operating. No explicit discussion occurred with respect of the influence product markets may have on reward mix, although one consultant did note that different sectors had differing mixes due to historically developed employee preferences, which were a legacy of the influence the sectors capital structure had on reward structures at the time they were established[2].

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

> There are organisations that actually say "I am not taking chances, and I am going do whatever the market does" and therefore they are prisoners of data in a way – and they can never have enough data [1].

Consequently, the market was seen as promoting reward mix inertia.

> [. . .] everybody is waiting for each other, the market is telling them nothing and it requires balls to go out and do something different [5].

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

> More sophisticated organisations now are looking at every detail of the reward mix and they are certainly basing that on market benchmarking . . . they will be looking at norm data with other employers to see whether they are different and why [3].

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

> We look for sameness, which we just wouldn't do with anything else that was either that costly or that strategically important to us [5].

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

> I don't think companies realise what they entering into at a cost is yet another zero sum game where you will find no competitive advantage because everybody will be doing it [5].

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

> Most organisations look at – well they say they look at - total remuneration in fact they don't, they look at element by element. What are our salaries like? What is our bonus like? What is our pension like? What are our cars like? [6].

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

> If you are running, say a shipping company, you won't care about a swing in the pension scheme funding because compared to the cost of owning all those ships and fuelling them and so on it's neither here nor there [6].

Coercive influences. In addition to these mimetic pressures a number of coercive influences were identified.

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

> It's all a bit influenced by things like the social security systems and what does the state think that the state has to provide . . . [which] tends to influence what the private sector has to pick up . . ., which is why we get different benefit practices in different countries [2].

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

> It's about encouraging employees to take more ownership of their financial future. So an employer is helping to mitigate the risk of lower potential guaranteed retirement benefits by making sure that people take more personal active interest [9].

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

> At the time it seemed very tax efficient to provide a car benefit, so all of a sudden car benefits become prevalent and then if you are going to compete in the market place you have to have a car benefit – at the time its tax advantageous to do it and here we still are trying to get ourselves out of tax driven benefits [2].

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

> So a lot of organisations have their share plans go quite a long way down the organisation and the reason for this is historically share options were tax favoured [6].

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

Agency interests.

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

> . . . getting people to understand what ownership represents [7].

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

> You need to understand what it is that motivates individual people and makes them want to perform and how different people perform in different ways [3].

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

> . . . by appearing to create a positive image or working environment, then they can afford not to have to pay top dollar [2].

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

> Firms see employees as a liability to be managed and the costs kept down . . . [treating] them as a transactional commodity, [rather than] as a business partner, or even customer, where you are going to be much more sensitive about your mix [3].

This approach has led to organisations focusing on base pay given, in one consultants words, "the multiplier effect it has on some of the other elements of mix" which are linked to this number (e.g. pension contribution, bonus, car allowance). This focus may have been at the expense of attention to other areas of significant cost, particularly around benefits.

> It can be really quite a drag on employment cost if you have a particularly generous benefit package. It might be much more generous than you need to give [4].

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

> The reward mix is taken for read and because we have had such good times the real decisions about what we should pay for and what the mix should be haven't had to be taken [5].

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

Resource perspective.

Talent and employee preferences. The relationship between the scarcity of key talent and the influence that gives to those staff to determine their own reward mix was raised by 8 of the 10 consultants. This was aptly put by one consultant:

> The scarcer they are the more employee expectations weigh in [1].

Nevertheless, sophisticated organisations assess all employee preferences in determining the right mix.

> If you talk about a research scientist then the opportunities to publish, the opportunities for professional recognition, the opportunities for learning and development and having a really state of the art lab are going to matter a lot to them . . . but if you thought about a call centre employee who was a student and who was doing this to keep the loan to a reasonable level, the drivers for them . . . might be having good kit, having a supervisor who didn't breathe down their neck and treated like a grown up [3].

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

> That [industry practice] has conditioned your expectations as you have grown up through your career, your expectation is market practice and your expectation becomes your preference . . . It's a conditioned response [3].

Explanations for inertia

Significant comment was made on the reasons why institutional pressures or, as termed by the consultants, inertia dominated reward mix determination. Two reasons were given for this – the quality of HR and the effect of organisational history and legacy arrangements.

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

> A lot of reward decision makers nod to strategy, but don't actually understand what it means and therefore what it means for reward [5].

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

> All of that spreadsheet based reward that we can look at is viewed as a different entity to the stuff about leadership and progression and the stuff about the kind of environment we work in . . . it requires quite a broad thinking HR director to weave those two things together [5].

A number of the consultants noted that there was a lack of understanding with regard to what reward mix was trying to achieve, with again the default position being market practice. This is illustrated below with reference to benefits.

> Do you know, I don't actually think a lot of people know why they offer benefits to be fair – you just do [2].

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

> It is a failure on the part of the HR community, the reward community and the consulting community to convince real decision makers that . . . reward levels and mix can genuinely have an effect that is causing this [5].

Organisational history. In addition, organisational history was identified as influencing inertia (raised by seven consultants).

> Organisations are always to some degree hostages of their history and you do find organisations where there are taboo words and taboo practices [3].

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

> In truth at executive level making changes . . . is reasonably easy to do because you have got a small population of people who are not going to rock the boat in a dysfunctional way . . . taking stuff further down into organisations is much harder to do because you can have serious industrial relations problems if what you are doing is, or is perceived to be, a worse deal [6].

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

Breaking down the inertia – the role of events. Six interviewees noted that although inertia was strong, events could break this down. A number of examples were quoted of clients that were reviewing their reward mix to manage costs down in the economic conditions present at the time of the interviews. This was viewed as an opportunity to make the reward mix more effective, through differentiating the offering from competitors and breaking free of the isomorphic pressures that were perceived to exist.

> You have to follow the crowd when everything is going fine. When things are a little different that is when you can be more different from other organisations [4].

Alongside the economic downturn, mergers were also suggested as catalytic events.

> If you are in crisis, if you have been taken over, if you are merging, you have cover to tackle those things [6].

Although pressures to maintain the status quo are strong, organisations have used events to catalyse change in their reward mix. However, these were seen as exceptions to the wider practice of conforming to industry norms.

5. Discussion and conclusions

This paper has examined reward consultants' perspectives on the determinants of reward mix policy decisions. With agency and institutional theory as theoretical background, this research examined who is involved in reward mix determination, the factors that are deemed to influence decisions and the explanations for why change has not been more forthcoming in this area. Patterns in the findings are now discussed and related back to the literature.

The interviewees did not, on the whole, give accounts aligned to the prescriptions of agency theory. The institutional theory proposition that mimetic and coercive elements have an influence on mix was more generally supported, with examples given of organisational isomorphism with respect to market benchmarking and the development of industry norms. Little evidence was found of normative isomorphism.

Presented in Figure 2 is a schematic model of reward mix determination developed from the findings (using the methodology proposed by Whetton (2002)). The main constructs are market forces and reward mix, mediated by industry norms. The industry norms were seen to emerge from the specific market forces faced.

The constructs shown above and below the main sequential association are considered moderators in the relationships shown. That is, the presence of these factors may change the main relationship. The influence market forces may have on industry norms is moderated by legal factors, such as minimum wage legislation, tax changes such as changes to pension legislation, or regulatory changes, such as that being debated in the financial services industry at the time of the research. In addition, the transmission of industry norms to organisational reward mix policy may be influenced by a number of variables. First, leadership belief's about reward mix and how it influences employee behaviour. Second, the overall strategy of the organisation and how its execution is affected by specific talent needs and cost pressures. Finally, the

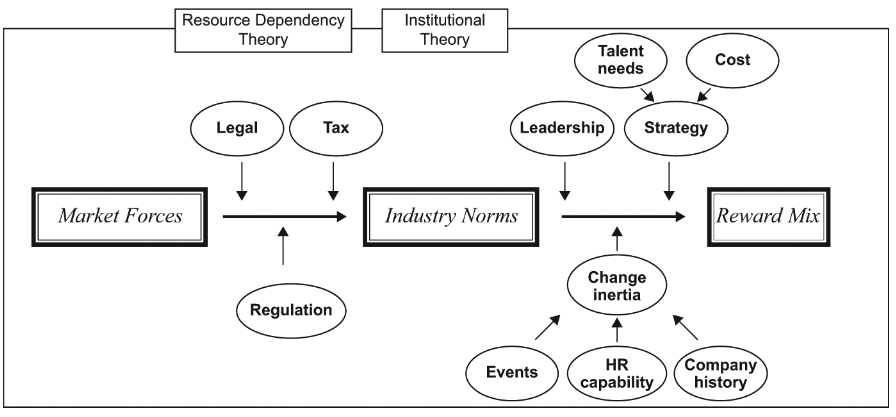

Figure 2.
Model of reward mix determination

extent to which change inertia exists. This inertia depends on the capability of the HR function in leading reward mix reform. In addition, company history and legacy arrangements further inhibit reform. However, the occurrence of events, such as mergers, can act as catalysts breaking down established practices.

The model developed challenges agency theory as the dominant paradigm for understanding reward mix decisions. The theoretical assumptions underpinning the model are resource dependency and institutional theory. The significant role of the labour market highlighted in the interviews and the relationship between market pressures and talent shortages are consistent with the main premise of resource dependency, which contends that groups holding critical jobs are able to exercise higher levels of power derived from the control they have (Pfeffer and Salancik, 2003). This power can then be used to influence the reward mix given to these individuals based on their own, rather than the organisations' preferences, which then may become established as industry norms (Tremblay *et al.*, 2003). The extent of the balance of power in the relationship between employer and employee (or their representatives through trade unions) has been extensively examined by Brown (2008), in the context of product market competitiveness and its influence on labour rates. He notes that "the labor market is of great importance to the relative power of employees and unions, but that they do battle on a field delineated by the employers' product market" (Brown, 2008, p. 121). However, the interviews only provided evidence on the importance of labour markets and the scarcity of key skills and not the interplay between product market competitiveness and labour markets.

Institutional factors seem to be endemic in the decision making process. In this context it is not surprising that path dependency emerges from the accounts provided given its similarities with institutional theory (Scott, 2008). While this perspective has traditionally been employed to explain technological developments, North (1990) argues that it applies to any institutional change given that when historically significant effort has been advanced there will be a preference for the status quo.

However, in addition the findings suggest a further theoretical perspective may provide insight into the dynamics of the reward mix decision. The leadership team was identified as significant through the influence their beliefs and values had on the HR team's consideration of appropriate reward decisions and confidence the leadership instilled within HR to break free of the "iron cage". This suggests that upper echelon theory and its contention that organisational decisions are heavily influenced by the mental models held by executives would be worthy of further consideration (Hambrick, 2007).

The research has contributed to knowledge in a number of ways. First, it takes forward previous work examining reward mix at the employee level and through this challenged the dominance of the agency perspective. Further, the research begins a programme of research intended to contribute to the call for research to "uncover the mental models used by real executives and compensation specialists in designing pay programs" (Gerhart and Rynes, 2003, p. 78), through the use of a qualitative approach to the research design which, while not unique, is unusual in the reward field. For practitioners, it brings greater transparency to the context and constraints under which they are operating and, through this, greater consciousness of these constraints. Finally, for policy makers a better appreciation of the extent to which institutional factors influence reward mix decisions. If, as suggested, labour market and institutional factors dominate and significantly constrain organisational decision making, this may suggest that formal regulatory policy interventions would be required to change reward mix practice (if this is desired for social or political reasons).

6. Limitations and suggestions for future research

The interviews have provided an insight into organisational practice through the perspective of an observer rather than the perspectives of those directly involved in the practice. An organisational perspective on reward mix determination through discussion with those directly involved in the process, would also be informative in developing understanding. In addition the consultants identified employee preferences as a significant influence in reward mix determination. Research which examines the employee perspective would be a worthwhile line of investigation.

A range of factors that were raised in the agency and institutional theory literature were not raised by the interviewees. Concluding that they are not factors in reward mix determination would be premature. For example, further exploration of the extent to which product market forces may be the driving force behind labour market pressures would appear to be warranted given the earlier conclusions of Brown (2008) on their significance.

Despite Rynes and Bono's (2000) observation that alliances with reward consultants may be productive, collaborations have been relatively limited. Given the insights gained in this work, further research ascertaining consultants' perspectives on this and other reward related research areas, would appear to be fruitful.

Notes

1. The extent to which adjustment is possible may be constrained by the ability of the organisation to lower base pay (many thanks to the anonymous reviewer for this point).
2. Brown (2008) notes the significance of product market competition on reward level determination. This argument focuses on the extent to which competitive pressures on organisations influence their ability to extract economic rents for their activities which can then, through negotiation, be shared with employees.

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