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From New Pay to the *New*, New Pay?

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Alignment is a central concept within the established logic of strategic HR management. Human resource management (HRM) systems and processes create value by closely aligning valuable human capital to the strategic direction of the firm. The outcome is a workforce that is both capable and motivated to execute the strategy of the organization, in whatever form that may take. Pay is central to establishing and maintaining alignment between what matters to employees and what matters to their employer. The emphasis traditionally has been to attempt to limit the risk of potential conflict over pay. More recently the focus has shifted to view pay as a strategic lever by which management can generate enhanced employee commitment, loyalty, motivation and positive behaviors for superior firm performance.

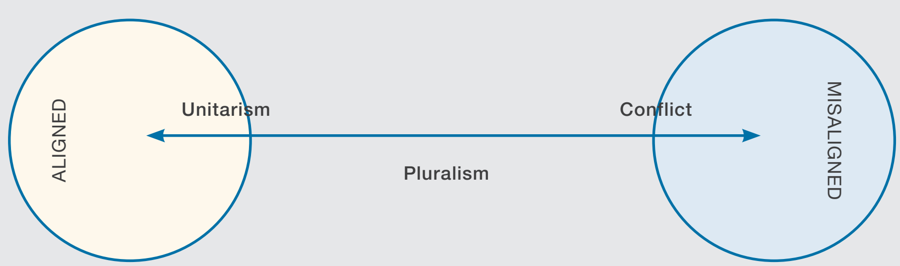
This article discusses how contemporary pay systems often fail in this role due to unavoidable barriers to their effective design and implementation. Research by the author indicates that attempts to use pay strategically produce unintended consequences, many of which result in unnecessary conflict. The consequence is most obviously to limit employee engagement, motivation and commitment. But worse yet, enhanced conflict reduces the likelihood of employee discretionary contribution and produces instead negative and damaging behaviors. Difficult to get right and easy to get wrong, this article argues that it is time for a *new*, New Pay. It concludes by proposing that pay should be managed as a risk with a clear focus on protecting value, while enabling effective leadership as the best means of securing employee alignment.

EFFECTIVE ORGANIZATION IS A POLITICAL PROCESS

An organization is classically defined as a collection of individuals and groups working toward a common purpose. Critical to organizational effectiveness therefore, is the degree to which individuals and groups — whether individual employees, teams or business units — are working toward a singular corporate purpose in the form of shared strategic priorities. Senior managers focus, rightly so, on determining the firm's strategy in line with perceived opportunity and challenge within the operating environment. And yet beyond this, organizational alignment is often assumed or overlooked despite being critical to organizational effectiveness. If not aligned to the corporate vision, mission and values, to what end are employees working? And whose responsibility is it to ensure alignment of interest, effort and behavior, and how is it best achieved? It is the essential and never-ending challenge of effective organization: Within the context of what we wish to achieve, how do we get employees to do the right thing? It is to this end we expend the vast majority of organizational spend over and above pay itself, including job design, culture management, leadership, communications and development.

To better understand this phenomenon within complex work organizations, political science offers us a useful framework by which we might organizationally diagnose the state of employee alignment. Expressed in terms of conflict — the absence of shared interest or purpose — there exist three broad states at any one time. At the right-hand extreme of the continuum, as shown in Figure 1, there exists a "conflict" state in which there is little or no alignment of interest between employer and employee. At the opposite extreme, there exists a state of "unitarism" in which there are high levels of alignment of purpose between employer and employee. In between, by degree, there exists a state of "pluralism,"

FIGURE 1 A Spectrum of Conflict



in which employees are more or less aligned. The framework can be applied at the overall organization level, e.g., group level, or at the sub-organizational level, e.g., individual departments, functions, divisions, business units or teams. For the organization as a whole to be more than the mere sum of its parts, all elements of sub-organization must be aligned at the corporate level to make possible innovation through synergies and/or efficiencies through economies of scale.

To organizationally achieve a state of unitarism is the overriding goal behind HRM. HR practices, such as performance and reward, are instrumental to generating organizational alignment. Alignment is important along numerous performance dimensions. In terms of efficiency, if there is lack of conflict because employees have internalized the goals of the organization as their own, then fewer managers are required through which conflict would otherwise have to be contained. For innovation too, alignment is critical. Innovation capability is a function of the possession of high levels of organizational intellectual capital. More practically, this means investing in our human capital to develop deep knowledge, often requiring individuals to specialize and become experts. Information asymmetry between the manager and the managed becomes highly problematic in situations where the managed are more knowledgeable than their superior. In the absence of effective monitoring, we can only empower staff in the presence of high levels of trust. How can we trust them if we don't have confidence that they are working in the interests of the organization? Equally, unless aligned, why would employees wish to exhibit discretionary effort, not simply going the extra mile, but fundamentally defining the terms of their own contribution and expertise above and beyond the traditional capacity of management to achieve such outcomes? While unitarism is the key architectural principle behind HRM, and the desired organizational end state, the reality of organizational life can be very different.

Conflict represents a grave risk to organizational effectiveness. At the extreme, in situations where there is no alignment to a common purpose, there is literally no organization in a functional sense. Individuals and groups, teams or business units, are working to different goals on varying trajectories. Beyond mere inefficiency, the manifestation of conflict within the employment relationship is varied and often abundant, from striking workers, picket lines and in some cases, throwing a monkey wrench into the works. More discreetly, conflict might result in elevated employee turnover as individuals seek better employment opportunities elsewhere. Worse still, disenfranchised and disengaged employees in conflict with their employer over potentially any number of issues might stay, the infectious conflict becoming a permanent feature of work for them and those around them. Conflict might also result in the withholding of employee discretionary effort and contribution, a key condition for effective knowledge work, as we rely upon employees to determine how their knowledge and talent is best deployed in the interests of the firm. Worryingly, discreet conflict is much more difficult to identify and remedy than overt conflict. It is potentially ever present and an invisible brake on organizational performance and attempts to introduce change.

Patterns of conflict need to be placed within historical context, as do the ways by which we remunerate our staff, either as the cause of much workplace conflict or, more recently, as the means through which we attempt to secure unity of organizational purpose. Many would argue that we are undergoing an epochal shift in the organization of work, with far-reaching implications for how we seek to reduce conflict and promote alignment. What are the prospects for pay?

CHANGING PATTERNS OF WORK ORGANIZATION

Unitarism was not in our industrial past a requirement of effective work organization when work was characterized by a requirement for busy hands on, say, the production line. Emotion, and associated features of work engagement, esteem, commitment and pride, had no place in the Taylorist workplace of the early 20th century, which was characterized by programmable and routine behaviors developed according to time and motion studies and "scientific" work planning (Taylor 1947). Around the world, this still persists in work environments involving routine manual labor, especially in low-skill production. The key organizational priority in such environments is no different from the profit imperative of 200 years ago in industrializing Britain, Europe and the United States, namely, maximum productivity for the least possible cost. The HR priority is to secure worker compliance to prescribed objectives and in doing so limit the potential for conflict that Karl Marx would say is inevitable as a result of worker exploitation and alienation (the estrangement of workers from each other and the results of their labor). In this highly structured and rule-bound environment, conflict can result only in inefficiency, whether mild or severe. This model of industrial work organization, and the imperative for conflict avoidance through collective structures, such as industry-wide collective bargaining, has served us well; it is why we enjoy all the benefits of mass production, mass consumption and mass employment today.

But our organizations are changing, in the developed world at least; because some would claim that we are at a tipping point between the Industrial Age and the Information Age. For better or worse, complexity within the operating environment is forcing a revision to the dominant model of bureaucratic organization; we must adapt if we wish to have a future. The bureaucratic organization is giving way to an emerging model of post-bureaucratic work organization (Hecksher and Donellon 1994). In place of formal structures, organizations will in the future be characterized by informal networks, in which knowledge is widely distributed and not centralized in a hierarchical manner. Existing research and work by the author offers some broad indicators of the direction of travel:

- Flexible specialization and the ability to connect knowledge and creativity simultaneously across multiple boundaries will feature as core organizational competencies (Hamel and Prahalad 1994).

- Crucial for the organization of work, alignment will be secured through the propagation of shared values, manifest in strong cultures, not in rules, policies and procedures characteristic of the bureaucratic organization.
- No longer concerned with manual labor, future organizations will be knowledge intensive, and the employment imperative being one of hearts and minds. The future networked organization will rely more than ever on its people as both the key repositories of knowledge and the means through which knowledge is collaboratively exchanged (Kang and Snell 2009).
- There will still be segmentation of staff, but it will be much less rigid than in the past, and mobility between occupations, and perhaps even employers, will be much greater too (Trevor and Kilduff 2012).
- Expect portfolio working by highly connected individuals and groups leveraging multiple networks simultaneously. Within these networks there will be broad categories of contribution, just as there are in our existing organizations, but movement between these categories will be far more fluid and short term, as agents respond rapidly to quickening patterns of demand for their expertise and utility (Sidhu 2010).
- In place of purely functional or hierarchical segmentation, e.g., finance manager level 7, of human capital within organizational structures, two broad categories are increasingly emerging as the demands on our organization evolve in step with an environment that demands simultaneous optimization of performance *and* change (Trevor and Hill 2012).

What pay looks like in this complex and dynamic future organization is not clear. However, such fundamental change to working practice and organization will necessitate equal change to the way in we remunerate employees. Where are we and where do we go from here?

IN WITH THE NEW PAY

The New Pay has risen dramatically to become the dominant logic of pay management across virtually all sectors and geographies of the world. It is referred to by numerous titles including strategic pay (Lawler 1990), strategic compensation (Hurwich 1986), and strategic reward (Armstrong and Brown 2001) to name just a few (Schuster and Zingheim 2000). Under New Pay, unlike "old pay," management has the right to determine pay free from constraint, whether trade unions or government, and purely in the interests of enhancing firm performance and shareholder value (Milovich and Newman 1999). The New Pay movement also fundamentally assumes that management has the ability to design and implement pay systems effectively for value (Devanna et al. 1984). Pay is no longer merely the cost of hiring labor, strategic HRM emphasizes its potential to secure strategically desirable employee outcomes for the employer (Lawler 1984 and 1990). Desired employee outcomes, so the theory goes, will tend to vary between firms as they seek to differentiate themselves from their competitors (Youndt et al., 1996). When aligned to competitive strategies, strategic pay systems should vary in form and function if they are to be fit for purpose (Schuler and Jackson 1987).

The evidence is that employers have embraced New Pay principles. For example, large private sector firms in the United Kingdom are attempting to use pay strategically following the decline of collective bargaining as the dominant mode of pay determination (Cully et al., 1999). More widely, Towers Watson (then Watson Wyatt) reveals a similar global trend toward the use of pay systems in support of strategic goals (Watson Wyatt 2007).

However, is pay the right lever to pull? Research on employee motivation, engagement and commitment consistently rank pay lower in influence than the quality of the relationship between the manager and the employees, interesting work and respected leadership. Moreover, while there has been a dramatic decline in collectivized industrial action over the past 30 years, in most Western economies at least, it is not necessarily evidence of unitism, but perhaps merely a reflection of the removal of the apparatus through which conflict was traditionally expressed. There is conflict in every corner of the globe over claims of excessive pay for executives, reckless bonuses for bankers and general perceptions of unfairness and inequity in the distribution of income. Is the New Pay really working for us?

OUT WITH THE NEW PAY?

There is growing evidence that the reality of New Pay systems may be far removed from the promise. Research by the author reveals that New Pay systems often do not succeed because there are unavoidable barriers to strategic alignment (Trevor and Brown 2012). More than merely infectious, in many cases New Pay systems consume or destroy more value than they create, often unbeknown to decision makers (Trevor 2011). Unlike in the past, conflict arising from pay is discreet, and therefore potentially more difficult to remedy. Within a sample of seven leading multinational consumer goods firms, the research indicated a high degree of conformity between firms regarding the role of pay and choice of pay practices. All firms were attempting to use pay as a tool to drive behaviors in support of strategic priorities and used the same individual and collective performance-based pay systems to do so. However, how these same pay systems were managed differed significantly between firms, with implications for their perceived effectiveness outside the HR function (Trevor and Brown 2012).

Pay decision makers faced high uncertainty when attempting to select the best fit for the pay system given the strategic goals and priorities of the firm. To compensate, the tendency in all cases was to extensively reference external practice, the logic being "if it worked for them, it will work for us". Despite the drive toward strategic distinctiveness, this explains why we see more similarities of pay practice across firms than we see differences. Competition has a normalizing effect, but social institutions do too — on a scale that is unappreciable to those operating within a highly structured field such as compensation (DiMaggio and Powell 1983). The result is to impede attempts to generate authentic alignment between pay design and the firm's distinctive competitive proposition to market. Despite the rhetoric, the reality of many pay systems is that they are not organizationally aligned to the strategic drivers of value, but to externally-perceived best practices (Trevor and Brown 2012). The desire for legitimacy takes precedence over all other considerations in compensation decision-making, including firm performance (Boselie et al., 2003). In the words of one remuneration director, "This is what everybody is doing. This is what you should be doing. The conventional wisdom is that you need to bonus people, whether it's right, wrong or indifferent doesn't matter. The conventional wisdom is you should be doing it" (Trevor and Brown 2012).

The research also revealed that the greater the degree of centralization of pay decision making, the less likely line managers were to implement pay systems in line with stated policy. Passively or otherwise, they resisted attempts to impose centrally determined pay policies if they were perceived to be a poor fit for the local context. The overriding concern of line managers was to maintain harmony within their teams and business units. Pay systems that introduce a performance element, for example, risk undermining local perceptions of fairness and equity. Line managers in numerous instances significantly adapted or rejected the introduction of new pay systems to avoid the risk of workplace conflict, often unbeknown to senior management or pay decision makers within the HR department. Line managers are key to the successful implementation of pay systems, because they represent the front-line relationship with employees and exercise the greatest influence over the messages the employee receives from his/her employer about what is valued (Trevor 2011).

The complexity of attempting to strategically use pay prevents both effective design and effective implementation. While intuitively appealing in principle, the research highlights a range of challenges surrounding the manageability of new pay systems, which render them largely ineffective. Further, there is evidence that pay practices destroyed value. In cases of significant unintended consequences, there were many examples of employee disengagement, disenfranchisement and demotivation. Quite opposite to the intention, new pay systems within these organizations produced conflict in place of alignment, with much of the conflict being discreet and, therefore, difficult to remedy. In trying to promote unity through pay are we, in fact, creating conflict? Difficult to get right, and easy to get wrong, is attempting to strategically use pay worth the risk?

THE *NEW*, NEW PAY?

It is time for a fresh approach to the management of pay. In place of using pay as a lever to promote value, we should approach it as a risk and focus on protecting value. To provoke discussion throughout the HR and business community, following are some potential axioms for a *new*, New Pay:

- **Pay is an enabler, not a driver, of performance.** Organizational measures, and especially leadership, are more effective at eliciting the outcomes we overly rely upon pay to produce — outcomes such as employee motivation, commitment, loyalty and behaviors. In place of escalating the financial value of rewards, we should invest instead in enhancing the quality of people management across our organizations.
- **Pay is like plumbing.** It should only matter when it goes wrong. Job enrichment should replace wealth creation as the primary means of attraction and retention of talent. Every employer should articulate their value as a vehicle through which talent might maximize their potential and make a positive difference in line with their intrinsic interests and passion.

And specifically in relation to the management of pay:

- **Ignore what everybody else is doing.** Due to increased complexity and change, the business environment is only going to become more uncertain and the temptation to emulate influential others (e.g. prestigious companies) all the greater. Best practice confers enhanced legitimacy, but does not lead necessarily to enhanced performance. Distinctiveness is rewarded strategically, and pay is no different when it comes to the tough choices about how much we should pay our employees and in what manner.
- **Keep it simple and keep it local.** Responsibility for pay strategies and policies should be delegated as much as possible to line managers to ensure meaningful alignment around the needs of localized business and employee interests. The trade-off is corporate-wide transparency and control, but one-size-fits-all approaches to pay will not be able to effectively differentiate between the diverse needs of employees and groups in the highly complex and dynamic future organization.
- **Pay needs to be managed as risk.** Pay is merely one element of the employment relationship and has greater potential to produce conflict than it does alignment in the strategic sense. Beyond market competitiveness, pay should be removed from the employment equation as much as possible. Pay should also be treated as a risk-management activity with the associated focus on governance, controls and checks.

Pay remains central to the employment relationship, but conflict arising from pay is a greater risk than ever because it is discreet, disaggregated and far more difficult to remedy. As governments, employers and employees, we embraced collective measures in the past to mitigate the risk posed by elevated conflict, but we have eschewed such measures to instead rely on purely managerial structures in the expectation of superior firm performance. In the words of Schuster and Zingheim, the focus of the dominant logic of New Pay is to "Pay people right," (2000). Mounting evidence suggests that contemporary pay systems are difficult to get right in the strategic sense. They are likely to generate harmful outcomes in the form of conflict and misalignment of interest. Perhaps the focus should be on "not getting it wrong."

Productive behaviors are better secured through effective leadership, an appeal to community and the design of work that is intrinsically meaningful. Perhaps the appeal of contemporary pay systems is that they seem to offer a silver bullet through which we might avoid having to grapple with the leadership challenge; and everybody else is doing it. The reality is that pay is no substitute for poor leadership, or a crutch to support weak leaders. Alignment of purpose is best secured as it always has been — by providing a clear vision of contribution to positive progress that appeals to our better nature.

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