

## *When Executives Rake in Millions: Meanness in Organizations*

Sreedhari Desai (Harvard University)  
Arthur Brief (University of Utah)  
Jennifer George (Rice University)

Paper Presented at the  
23<sup>rd</sup> Annual International Association of Conflict Management Conference  
Boston, Massachusetts  
June 24 – 27, 2010

### Abstract:

The topic of executive compensation has received tremendous attention over the years from both the research community and popular media. In this paper, we examine a heretofore ignored consequence of rising executive compensation. Specifically, we claim that higher income inequality between executives and ordinary workers results in executives perceiving themselves as being all-powerful and this perception of power leads them to maltreat rank and file workers. We present findings from two studies—an archival study and a laboratory experiment—that show that increasing executive compensation results in executives behaving meanly toward those lower down the hierarchy. We discuss the implications of our findings for organizations and offer some solutions to the problem.

### **Abstract**

The topic of executive compensation has received tremendous attention over the years from both the research community and popular media. In this paper, we examine a heretofore ignored consequence of rising executive compensation. Specifically, we claim that higher income inequality between executives and ordinary workers results in executives perceiving themselves as being all-powerful and this perception of power leads them to maltreat rank and file workers. We present findings from two studies—an archival study and a laboratory experiment—that show that increasing wage disparity results in executives behaving meanly toward those lower down the hierarchy. We discuss the implications of our findings for organizations and offer some solutions to the problem.

### **When executives rake in millions: Meanness in organizations**

It is well known that the compensation of Chief Executive Officers (CEOs) has sky-rocketed with the Fortune 500 CEOs' average compensation having increased by 300 percent over the last decade (Dovrak, 2007; Frank, 2007). Debate about the appropriateness of such compensation has been multi-faceted and heated (for a review, see Gerhart, Rynes, & Fulmer, 2009). Our aim is to add another dimension to this debate. Simply put, we will argue and empirically demonstrate that as the disparity between CEOs' compensation and ordinary workers' income increases, the former become meaner toward the latter.

The rest of the paper unfolds as follows. First, we examine how increased compensation and concomitant increase in wealth relative to rank and file workers leads CEOs to experience enhanced perceptions of power. Then, we present existing theories on how an increased sense of power causes top managers to objectify lower level employees and view them as mere instruments to be used and discarded. We present a study wherein we analyzed archival data and found that the higher the compensation received by CEOs, the more poorly employees in their organizations are treated. In a second study conducted in the laboratory, we examined one possible underlying mechanism responsible for the increase in managers' mean behavior, namely, an exaggeration in the power perceived by managers with relatively higher income compared to their employees. We conclude by discussing the implications of our work for organizations and offer some remedies to the problem of poor employee treatment by executives who receive very high compensation relative to organizational employees at lower tiers.

### **CEO Wealth—Power**

From 1990 to 2005, the average CEO's pay increased almost 300 percent after adjusting for inflation, with the CEO of a Standard and Poor 500 company now earning \$10.9 million per year (Dovrak, 2007; Frank, 2007). As CEO compensation has escalated, so have journal articles exploring the pros and cons of offering executives extreme compensation packages. For the most part, this debate has been centered on whether increased pay leads to increased firm performance. An exception to this is recent work by Desai, Brief, and George (2009) in which they addressed issues pertaining to CEO compensation and human rights concern. Here, we build upon their effort and focus on how increasing disparity between CEO compensation and wages of ordinary workers leads to excessive power accumulation at the top and resulting in unethical treatment of employees lower down the hierarchy.

We employ an umbrella definition of power and define it broadly as the capacity to influence or control other people or advance one's own goals (Keltner, Gruenfeld, & Anderson, 2003). That wealth leads to power is no big surprise. Wealth manifests itself as power in numerous ways (Ackerman, Goodwin, Dougherty, & Gallagher, 2000). First, it leads to economic power. Having deeply lined pockets ensures that the rich are protected from stochastic shocks to their income flow as well as any other temporary economic setbacks. It is also easier for the well-off to raise economic capital since banks and other lenders are more favorably disposed to those who can put up large collaterals. The wealthy also have enormous purchasing power, and as such, their spending habits can dictate what goods are produced in a market economy (Ackerman et al., 2000). Wealth also translates into political power. By contributing to the election campaign of a

favored party, the wealthy can help their preferred party win. Those with more money can also lobby for reforms that either benefit them directly or support causes that they endorse. CEOs have been known to lobby for tax reforms that work to their advantage (Bebchuk & Fried, 2003). For instance, whereas the effective federal tax rate for the average family in the U.S. has been almost static since 1980, there has been a lowering of the tax rate for millionaires and the top one percent of the richest households—the income bracket to which CEOs belong (Phillips, 2002). In addition to economic and political power, CEOs can also wield corporate power and determine where to open new factories, make decisions pertaining to how environmental wastes are disposed off, which charities are supported, and more generally, stimulate local economies and influence the quality of lives that people in those economies lead (Ackman et al., 2000).

The literature on executive compensation has also identified CEO pay as being a key indicator of CEO power. Simon (1957) was one of the early scholars to propose that pay differences are set by management as a way of symbolically distinguishing between different ranks within the organization. The higher the pay of the employee, the higher is his rank, and more is the power wielded by him. Similarly, Lazear and Rosen (1981) put forth the notion that CEO compensation can be viewed as the prize in a tournament competition, with the amount of the prize signifying the rank, and therefore, power of the winner. Finkelstein (1992) and Hambrick and D’Aveni (1992) have also asserted that compensation is an important metric of the formal power wielded by CEOs. According to the “managerial power” perspective prevalent in the domain of corporate governance, the power wielded by CEOs as a consequence of the wealth accrued to them causes them to be in a better position subsequently to negotiate even higher pay rises, leading to a

never ending pay-power cycle (Bebchuk & Fried, 2004). Financial economists have also commented on how executive pay translates into power that results in undesirable CEO practices such as using managerial discretion to benefit themselves personally, engaging in empire building (Jensen, 1986; Williamson, 1964), and entrenching themselves into their positions so that it is difficult to fire them when they underperform.

According to the “CEO as a figurehead” perspective, the board of directors uses the CEO’s wage to signal to people not only within but also *across* organizations that the CEO is powerful (Steers & Ungson, 1987). To quote Henderson and Frederickson (1996), “CEO compensation may be used to send a powerful symbolic message to organizational stakeholders.” (p. 801). They claim that the compensation of the CEO is used as an impression management tool and is designed to suggest how powerful he is. This impression of a powerful CEO consequently inspires suppliers, customers, and rival organizations to cooperate with him.

The relationship between CEOs’ remuneration and power has been empirically recorded in many studies (Finkelstein & Hambrick, 1988). Most notably, across an array of publicly traded firms, Lambert, Larcker and Weigelt (1993) found support for their “managerial power model” by demonstrating that higher executive compensation was associated with more perceived power. An increase in structural power as a consequence of increased compensation is also accompanied by social recognition of the CEO’s power. What the CEO is paid is often publicly available information. When CEOs earn, for example, 400 times the amount earned by rank and file workers, these workers’ perceptions of the power of the CEO are likely affected. Thus, we suggest that increasing compensation not only increases CEOs’ perception of how powerful they are

but also affects the perceptions of the workers they manage. Subsequently, when workers witness CEOs behaving as if they are powerful, the workers react as if this is indeed the case. When social understanding and social consensus develops to accept the distribution of power, CEO power becomes institutionalized and legitimized and this gives birth to a consensually accepted status system. Workers' response to the CEO's behavior perpetuates the CEO's belief in his or her increased power. Previous research indicates that social beliefs can act in a self-fulfilling manner, affecting responses to individuals and thereby encouraging these individuals to behave in ways that confirm attitudes about them. Thus, when workers acknowledge the dominance of CEOs, CEOs' perceptions that they are all-powerful are strengthened. Such power may become institutionalized over time such that in due course organizational members may become even more accepting of the power wielded by executives, and in turn, this may feed into the executives' perception of their legitimate power.

Whether it is through economic, political or social domains, higher compensation leads to larger perception of power. We argue that this increased perception of power in both work related domains (e.g., power over suppliers) and work unrelated domains (e.g., lobbying power) leads CEOs to experience power within their organizations. Research by Galinsky, Gruenfeld, and Magee (2003) has demonstrated that priming feelings of power by having participants recollect an instance wherein they felt powerful, leads them to feel powerful subsequently in an *unrelated* task. Likewise, experiencing power while interacting with stakeholders such as consumers and suppliers may lead CEOs to experience power while formulating policies concerning lower organizational members.

In the next section, we will elaborate on how this experience of power influences CEOs' cognitions and behavior toward rank and file workers.

### **CEO Power-Meanness**

There is a plethora of examples of those in power behaving meanly toward lower level employees. One of the most notorious examples is that of executives at Wal-mart, the largest retailer and private employer in the U.S. Wal-Mart continues to make headlines year after year for violating wage laws, failing to provide adequate health care to employees, exploiting workers, taking an anti-union stance, and violating human rights in foreign countries. Some of the gory details involving its overseas operations include denying workers minimum wage, compulsory overtime, failing to provide adequate safety equipment to workers, and hiring child labor. Back in the U.S., Wal-Mart's executives' behavior toward their employees has been just as mean. For example, in California, Wal-Mart denied an unpaid thirty minutes of lunch break to workers who worked six hours or more, in direct violation of Californian labor laws. In another instance, in an attempt to force full-time workers to switch to a part-time schedule, Wal-Mart came up with an innovative "flexible scheduling" policy requiring workers to shift rotations instead of working in steady shifts. Equally shocking was an internal memo published by the *New York Times*. In this memo, a Wal-Mart executive detailed various unethical ways of reducing health care benefits for employees and increasing company profits by \$1 billion by the year 2011.

Findings from systematic laboratory and field research also support anecdotal evidence such as that presented above, and taken together, attest to the popular notion that power corrupts. The perception of power has been shown to have a variety of



negative effects on power-holders (but see Handgraaf et al., 2008; and see Study 2 of Magee & Langner, 2008). For instance, power has been shown to lead to selfish and corrupt behavior (Galinsky, Gruenfeld, & Magee, 2003; Kipnis, 1972), reduced empathy and less openness to the perspectives, emotions, and attitudes of others, a tendency to objectify and stereotype others, sexually harass those with low power, and in general, behave in socially inappropriate ways. Within the negotiation contexts as well, researchers have found that high-power disputants are less in tune with their opponents' underlying interests and are less likely to come up with integrative solutions that are advantageous to both parties.

Why does power have such detrimental effect on power-holders? According to Kipnis' (1972) classic power-holding theory, being in a position of power changes people's cognitions, motivations, and behaviors in significant ways. First, power becomes an end in itself, such that retaining or enhancing one's power becomes a strong motivating force. Second, with power, comes the desire to influence and control subordinates. The exertion of influence in turn causes power-holders to undermine their subordinates' agency, such that they attribute their subordinates' performance to good management and not their efforts. Denying subordinates agency facilitates in perceiving them as subhuman entities that can be used and discarded. This view of how power corrupts is also in keeping with philosophical perspectives on the instrumental nature of power according to which, the experience of power results in viewing those with less power as instruments or means to an end. Such a perspective has been used to explain a variety of mean behavior, from economic objectification of workers to sexual harassment of female employees.

Within the ethics literature, the failure to recognize the moral worth of other people and empathize with them is referred to as a “moral disengagement” process that subsequently enables the self-sanctioning of mean behavior (Bandura, 1999).

Dispossessing subordinates of human qualities and thinking of them as inferior beings may make powerful executives feel that it is permissible to treat them merely as a business expense and deny them decent working conditions, health coverage, lunch breaks and so forth. Even normal, well-adjusted people are susceptible to the negative effects of power. For instance, in a simulated prison experiment, college students who were randomly assigned to play the part of the prison authority and given absolute power over inmates tended to devalue prisoners and treat them in degrading ways. Zimbardo (2007) argued that as a result of objectification and dehumanization, an environment with exaggerated power asymmetry can cause even normal people without any apparent prior psychological problems to become brutal and abusive towards those with low power.

Recent research on nonconscious processes has documented that people with high power are more likely to engage in automatic processing of social information as compared to those with less power, who are more likely to engage in careful, systematic processing of information (Keltner, Gruenfeld, & Anderson, 2003). As such, superiors are more likely to take cognitive shortcuts and stereotype subordinates. They are unlikely to take into consideration the needs and aspirations of those lower down in the organizational hierarchy unless such attention can somehow better enable them to reach their overarching goals. Along similar lines, the “power as control” theory suggests that those in positions of power are in control over resources and do not perceive themselves as being interdependent on those with less power. Consequently, they tend to pay less

attention to their distinguishing features and traits. In a human resource decision making context, Goodwin and Fiske (1993) found that power-holders paid less attention to those with less power. College students were given the authority to assess high school applicants for a summer job. When the college students were accorded more say, and thus more power in the decision making process, they paid less attention to the applicants. When power-holders pay less attention to subordinates' individuating features, they resort to stereotypes, and this, in turn, can result in discrimination in the workplace.

According to the "power as threat" perspective, those with high power perceive a constant threat to their position and feel the need to justify why they are in a position of power. They imagine that others are contriving to take their power away from them and that most people, including those with low power, can not be trusted. This kind of "leader paranoia" translates into power-holders exercising their power and degrading those with less power to ensure that they are kept in their place (Kramer & Gavrieli, 2004). Stereotyping subordinates and thinking of them as being less capable and less human justifies existing power differentials and helps minimize threats to power roles. Actively denigrating subordinates can then serve to remind other employees who is in power. Fast and Chen (2009) found that such aggressive tendencies are exacerbated when the perception of power is coupled with a perception of being incompetent, when the ego of the power-holder is likely to feel threatened. Other researchers have documented that certain personality types, such as those with an exchange-relationship orientation are even more likely to abuse their power than others, such as those with a communal-relationship orientation. A meta-analytical study examining the effects of

power asymmetry within organizations found that increasing power differentials resulted in superiors evaluating subordinates more unfavorably, after controlling for other factors (Georges & Harris, 1998). All in all, the theoretical arguments presented above support the stance that more power leads managers to mistreat subordinates more and evaluate them more unfavorably.

To summarize, we have argued that increasing executive compensation leads to executives experiencing a sense of immense power and that such a perception of power causes them to behave meanly towards those at the bottom of the organization. Below, we present two studies. In the first study, we use archival cross-sectional data to establish that higher CEO compensation results in poorer employee relations. In the second study conducted in the laboratory, we examine how disparity in the compensation handed out to managers versus employees results in the former perceiving more power, and consequently, treating the latter more meanly in a subsequent economic game by firing employees despite adequate performance.

### **Study 1**

#### **METHODS**

The unit of analysis for our study was the organization. We investigated the relationship between the total compensation of an organization's CEO and the organization's relationship with its employees. The sample of organizations was drawn from Kinder, Lydenberg, Domini & Co. (KLD) Company Profiles, a database that has been used by several researchers in the past (e.g., Kane, Velury, & Ruf, 2005) and is currently being used by approximately 150 investment firms to evaluate stakeholder performance for social choice funds. For each year starting from 1991, KLD has

evaluated approximately 650 firms on key stakeholder issues through publicly available information and interviews with key personnel. KLD conducts an annual evaluation of each company on an indicator relevant to this study, employee relations. As past researchers have noted, there are several advantages of using the KLD database: an objective set of multiple criteria that are applied consistently across companies, comprehensive coverage of multiple stakeholder groups (both within and outside the U.S.), and longitudinal assessments on an annual basis.

In our study, we focused on the year 2007, the year for which most recent data on organizations' scores on employee relations was available through KLD. This list was compiled by KLD after screening approximately 650 companies that comprised the S&P Index, the Domini 400 Social Index, the Russell 1000, and the Russell 3000 for the year 2007. In our sample, we included only those firms that were listed in the KLD data set, and for whom secondary data regarding executive compensation, firm details, and executive gender were available in the Compustat database. Our final sample size was 261 firms.

### **Measures**

**Meanness.** In the KLD database, each firm receives a rating of its strengths and weaknesses with respect to its relations with its employees, as well as other stakeholder issues. To capture mean behavior, we chose to focus on employee relations because taken together, these items are a proxy for how lower participants may be treated in the organization (see Appendix A for a description of the criteria). We first standardized the data and then computed a composite score for meanness by adding the weaknesses and subtracting strengths (Kane, Velury, & Ruf, 2005).

**Compensation.** Since most studies on executive pay, for example, those included in a meta-analysis by Tosi, Werner, Katz, and Gomez-Meija (2000), have measured CEO compensation as salary plus bonus, we followed suit. Compensation was measured for the lag year since we expected wealth effects to take time to set in.

**Control variables.** To control for the differing circumstances facing firms, we include a number of firm and industry-level covariates in our analyses. Specifically, in our regressions, we controlled for a variety of firm specific characteristics such as firm size, age, performance, risk, as well as the type of industry since they may arguably have a bearing on human resource practices. We also controlled for the gender of the CEO since researchers have demonstrated that men and women respond differently when they experience power. Below, we detail the operationalization of each of these variables.

*Firm age.* We controlled for firm age, that is, the number of years since incorporation, because firms may perform differently at different stages of development and this may influence employee relations.

*Firm size.* Firm size was operationalized as the log of total market value of equity and was measured for the lag year (Kane et al., 2005).

*Firm performance.* In our analysis we used a market-based measure of performance, that is, a proxy for Tobin's Q, as well as an accounting measure, return on assets (ROA). Both of these variables are widely used in the finance literature as measures of a firm's financial performance. Our proxy for Tobin's Q was the ratio of the firm's market assets to its book value. ROA was computed as the ratio of net income before extraordinary items and discontinued operations to the book value of assets.

*Firm risk.* Our measure of firm risk was the variance in stock returns, a widely-used market-based indicator of a firm's volatility-related risk, computed as the standard deviation of the underlying stock price's daily logarithmic returns, for the previous 60 months.

*Industry dummy.* Since extant research has found different pay-performance relationships for high versus low technology firms, we controlled for industry type by creating a dummy variable that was coded 1 for high technology firms and 0 otherwise.

*Gender of CEO.* Gender of the CEO was a dichotomous variable that was coded as 0 for male and 1 for female CEOs.

## RESULTS

Sample means, standard deviations, and correlations for the indicator and dependent variables are presented in Table 1. To examine if CEO compensation affected subsequent meanness, we conducted step-wise regression analysis on meanness, including only the controls in Step (i) and introducing the indicator variable of interest, that is, CEO compensation, in Step (ii). The results are presented in Table 2. As can be seen from the table, firm age and ROA had a positive, significant influence on meanness whereas firm size had a negative influence. Of greatest importance, the hypothesized main effect of CEO compensation was significant ( $\beta = .14, t = 2.13, p < .05$ ). Our finding suggests that the higher the level of CEO compensation, the meaner the behavior of the organization toward lower level participants.

One of the shortcomings of our study was that we were unable to test the mediating role of perceived power on the relationship between executive compensation and meanness. To this end, we designed a second study using experimental techniques.

## Study 2

### METHODS

*Sample.* Sixty two students (41 men and 21 women) enrolled in undergraduate organizational behavior classes at a university in the U.S. participated in the experiment and received course credit for their participation. Based on the number of points accumulated during the experiment, one participant out of every ten received \$10.

*Design.* This experiment employed a single factor between participants design with two levels of the manipulated variable (relative compensation of manager: low vs. high).

*Procedure.* On arrival at the laboratory, participants were told that they were going to participate anonymously in a game with participants at another university. They were told that there were 3 parts to the game. In Part 1, they would be asked to solve some simple anagrams. Their performance on the anagram task would be compared with that of a participant at the other university, and based on their relative performance participants at each university would be given some points and assigned the role of either a manager or an employee to be played out in Parts 2 and 3 of the game. Together, a manager and an employee would comprise an organization. Participants then solved anagrams for 5 minutes. Unknown to the participants, they were always assigned the role of managers but were randomly assigned to either the low or high relative compensation of manager condition. Those in the high relative compensation of manager condition were told that they had earned 65 points and been assigned the role of manager, whereas the participant at the other university had earned 15 points and been assigned the role of employee; those in the low relative compensation of manager condition were told that



they had earned 65 points and been assigned the role of manager, whereas the participant at the other university had earned 60 points and been assigned the role of employee.

Next, participants were told that in order to simulate the conditions in real world organizations, in Parts 2 and 3 of the experiment, the “manager” would perform managerial tasks whereas the “employee” would perform non-managerial tasks.

Specifically, they were told that the employee would solve some simple mazes for 10 minutes and based on the performance of the employee on the maze task, the organization would make profits as per the profit matrix illustrated in Appendix B.

Participants were also informed that solving mazes required a different set of skills compared to solving anagrams, and that performance on one task was uncorrelated with that on the other. The purpose of doing so was to ensure that those in the high relative compensation of manager condition did not form any apriori expectations regarding employees’ performance in the subsequent task.

Participants further were told that after the performance of the employee and the associated profits of the organization would be determined, the results would be communicated to the manager. The manager would receive 20 percent of company profits while the employee would receive 10 percent of the profits. The manager would then have to decide whether or not to retain the employee for the third part of the experiment. If a manager decided to not retain the employee, the experimenter would randomly assign a new employee to the manager. This new employee then would solve mazes for 10 minutes and based on the matrix described previously, the organization once again would make profits. If the manager decided to retain the employee, the same employee would work for the organization in the third part of the game. They were

specifically instructed that if an employee was not retained for Part 3 of the game, that employee would not take any further part in the game. In other words, he/she would neither have an opportunity to solve any more mazes nor make any more points.

Participants were then told that those playing the part of employees would solve mazes for 10 minutes. After 10 minutes passed, participants (managers) were told that their employee's performance was average and that the organization's profit was a hundred points. At this point, managers decided whether they wanted to retain their employee or not. Their decision not to retain the employee was coded as 1 and was a measure of their meanness. Part 3 of the game took place subsequently. At the end of Part 3, participants were asked to fill out a brief questionnaire that contained two items designed to tap into perceptions of power (Schubert, 2005) and a few filler items. The two items measuring perceptions of power were "I felt powerful in my role" and "I felt weak in my role" [reverse coded]. Responses to these items ranged from 1 = strongly disagree to 7 = strongly agree ( $r = .54$ ).

## **Results and Discussion**

Table 3 provides the means, standard deviations, and correlations among the key variables.

**Meanness.** The dependent variable, meanness, was a categorical variable which was coded as 1 if the manager chose *not* to retain the employee and 0 otherwise.

To examine whether perceptions of power mediated the relationship between relative compensation of manager and meanness, we conducted mediational analysis. First, we conducted an Analysis of Variance with perceived power as the dependent variable and relative compensation of manager and sex as the independent variables

(overall  $F(3, 59) = 11.11, p < .001, adjusted R^2 = .33$ ). Gender had a significant main effect on power such that men perceived higher levels of power ( $M = 11.20, SD = .28$ ) as compared to women ( $M = 9.80, SD = .38$ ). More importantly, as predicted, higher relative compensation of manager resulted in greater perceptions of power ( $M = 11.47, SD = .35$ ) compared to low relative compensation of manager ( $M = 9.52, SD = .32$ ). We then conducted a hierarchical, logistic regression analysis on meanness, entering the predictor variables in the following order: (i) control variable – sex<sup>1</sup>, independent variable – relative compensation; and (ii) mediator – perceived power. The results of this 2-step regression are provided in Table 4. As reported in the table, in Step (i), we found the hypothesized direct effect of relative compensation of manager on meanness ( $Exp[b] = 3.11, p < .05$ ) such that higher relative compensation of manager lead to more meanness (see Figure 1). On introducing the mediator in Step (ii), the direct effect of relative compensation of manager became considerably smaller and insignificant ( $Exp[b] = 1.33, p = .67$ ), whereas indirect effect of perceived power was significant ( $Exp[b] = 1.58, p < .05$ ), thereby suggesting the perceived power fully mediated the relationship between relative compensation of manager and meanness.

The results from Study 2 provide support for our argument that increasing relative compensation of manager results in an increase in the perception of power which leads to those in positions of authority behaving meanly.

### General Discussion

The appropriateness of the amount of pay an executive typically makes is a hotly debated topic both within academia and in popular media. Whereas traditionally,

---

<sup>1</sup> Researchers have demonstrated that men and women respond differently when primed with power (e.g., Bugental, Beaulieu, Schwartz, & Dragosits, 2009).

researchers tended to focus on whether higher executive pay leads to superior firm performance, a burgeoning research topic is the ethics of executive compensation. Within this domain, researchers chiefly have concentrated their efforts on issues such as conflict of interest in the way that executive pay is determined, how executives are susceptible to temptations such as inflating short term gains in order to reap quick rewards, or how the widening income disparity between executives and average workers fuels perceptions of inequity among the latter and demotivates them. We have introduced to this conversation a fresh perspective linking excess executive compensation to subsequent mean behavior toward lower organizational constituents.

We have proposed in this paper that increasing executive compensation has implications for the way that executives treat employees lower down in the organizational hierarchy. We believe we are amongst the first to examine both theoretically and empirically, the link between high compensation and power. We argued that rising pay leads executives to experience high levels of power over other organizational members and consequently causes them to objectify lower level employees and behave meanly toward them. Across an archival study and a laboratory experiment we found converging evidence that lent empirical support to our hypothesis. By doing so, we have brought to light an as yet unexplored dimension to the debate on the pros and cons of executive compensation. We have argued that in addition to examining the links between executive pay and a firm's financial success, it is important to consider a thus far unreported ethical implication of high executive compensation—that executives with higher income treat employees more meanly.

### **Some remedies**

Below, we have compiled some solutions suggested by philosophers, political economists and social scientists to remedy the situation of executives behaving meanly. Most of these solutions focus on ways in which executive excess may be curbed, and some suggest ways of empowering lower level organizational members.

*Disentangling board and executive interests*

The literature on executive compensation has identified that the relationship between the CEO of a company and its board of directors tends to be somewhat symbiotic, with the board participating in the CEO selection and wage determination process and the CEO subsequently exerting control over not only whether directors get re-nominated to the board but also over perks received by board members. Making matters more complicated, board members and CEOs often belong to the same social network, with CEOs sometimes sitting in on the boards of other organizations along with board members of their own companies. Such a level of interdependence naturally raises doubts about the board of directors' ability to assess and monitor objectively CEOs' performance and consequently estimate appropriate levels of their pay. Indeed, Young and Buchholtz (2002) found that compensation committee directors with close ties to the CEOs made more biased decisions favoring CEOs than did those with distant relationships. Likewise, Core, Haultausen, and Larcker (1999) found that when outside board directors are appointed by the CEO, subsequently they are more likely to approve higher compensation for the CEO. Thus, one proposed corporate governance solution is to include more outside members in the board, or better still, to have only independent directors participate in the nomination and selection processes of both the board and the CEO. This way, executive compensation levels may become less inflated.

*Need to divorce remuneration consultants and auditors from CEOs*

Moore, Cain, Bazerman, and Lowenstein (2005) have brought to attention a fundamental flaw in the way independent consulting firms arrive at expert judgments such as those regarding CEOs' performance and appropriate remuneration. On the premise of standard agency theory, they argue that to the extent that such consulting firms are retained by the CEOs of the very firms they are auditing or making a recommendation to, they have no incentive to suggest lower compensation packages. Rather, to ensure that they are hired a second time, and to avoid a reputation for suggesting low executive compensations, they might be motivated to present large sums as appropriate remuneration. Likewise, auditors who are retained by CEOs have minimal incentives to disagree with the performance reports put together by the CEO's aides. All in all, unless remuneration consultants are made accountable to shareholders instead of CEOs, their recommendations for suitable executive pay will continue to be inflated.

#### *Increased disclosure and shareholder rights*

To encourage shareholder participation in determining CEO wages, the Securities and Exchange Commission (SEC) has recommended that not only should companies disclose the amount of compensation paid to executives, they should also explain to shareholders precisely how the board of directors has arrived at a specific figure for CEO compensation. The basic premise behind this proposal is that shareholders who feel that a firm is wasting valuable resources on unproductive CEOs can withdraw their funds from that firm's stocks and invest elsewhere. Though theoretically this proposal seems sound, due to practical constraints faced by investors such as limited time, bounded rationality, and transaction costs, monitoring CEO pay for individual firms and switching funds from one firm to another may not be as simple as imagined. Other criticism levied

against the efficacy of increased disclosure is that clearer data related to executive performance and compensation may cause CEOs to exploit such data to build a favorable case for why their high pay, in fact, is justified. In addition to improving the clarity of information provided to shareholders, legislature such as the Shareholder Vote on Executive Compensation Act suggests that shareholders should also be given the right to vote on the amount of compensation given to executives. Indeed, in many countries except the U.S., shareholders have such voting rights but their vote is often non-binding. To be meaningful, shareholders' vote should be binding. However, the administrative complexity of such an endeavor may make it a very challenging proposal to implement.

### *Capping the excess*

Plato is known to have remarked that the highest paid worker in an economy ought not to make than five times the pay earned by the lowest paid worker. Aristotle thought likewise and cautioned that inequality, if not reigned in, will cause lower members of the economy to revolt. Within organizations in the US, the income inequality between top executives and lower level workers is currently at an unprecedented high. Taking his cue from Plato, J. P. Morgan declared that top executives' compensation should be capped at twenty times the wage of an average worker. However, unless all organizations adopt this rule, capping an executive's wage will put a firm at a competitive disadvantage. For instance, consider the case of Whole Foods Market Inc. In the 1980s, the salary of its CEO was pegged at 8 times the pay of the average worker. However, when its executives were persistently made strong offers by its competitors, Whole Foods Market relented and raise the cap on executive compensation to 19 times that of the average worker. Other firms, such as Ben & Jerry's,

Herman Miller Inc., and Costco Wholesale Corp., that have tried to implement similar strategies of capping executive excess have also had limited success. That said, it is worth noting that the success that many major baseball and other sports leagues have had in imposing a limit on their teams' salaries is impressive. If businesses were to emulate them and simultaneously adopt such a policy, they may be more successful at limiting executive pay.

### *Progressive taxation*

If market forces prevent organizations from capping executive compensation, perhaps it is time for a tax reform. At present, whereas ordinary employees have only 401(k) plans available to them if they want to defer their taxes, CEOs enjoy limitless tax deferrals in the form of executive deferred pay-plans. Imposing an upper limit on such deferrals for high earning executives will constrain CEO wealth to some extent. Also, at present, managers of private equity and hedge funds are required to pay 15 percent capital gains rate on their income as opposed to the usual 35 percent rate that would be applicable if their income were treated as ordinary earnings. Legislation that eliminates such tax loopholes or increases the marginal tax rate on incomes in the very top bracket would also reduce disparity in top managers' and ordinary workers' net income. Furthermore, tax loopholes that permit organizations to treat massive pay packages as a "business expense" should be modified if corporations are to be persuaded to lower CEO compensation.

### *Linking pay to charity*

A radical alternative might be that executives be required to donate earnings above and beyond a pre-set level to a public charity of their choosing (Desai et al., 2009).



Such a strategy has been previously tried at the investment bank, Bear Sterns, which required its top earners to donate 4 percent of their salaries to charity and enforced the requirement by checking employees' tax returns. More recently, Goldman Sachs is making news for considering a similar charity requirement plan. Such a requirement would allow for organizations like Goldman Sachs to continue showing their appreciation of the fine work done by CEOs and motivate them extrinsically while simultaneously curbing the power they could have enjoyed due to excessive accretion of wealth.

### *Empowering lower level employees*

CEO decisions to outsource jobs, lay off employees by the hundreds under the guise of reorganization strategies, lower health benefits, and reduce retirement benefits have been accompanied in the past by a decline in the power of trade unions. One way to check mean behavior by top executives might be to strengthen labor unions. In fact, over two thirds of U.S. adults believe that to protect workers, labor unions must be made stronger. Despite widespread recognition (e.g., the United Nations' well known Declaration of Universal Human Rights) that it is people's fundamental right to join and form a trade union for the protection of their rights, corporations such as Wal-Mart continue to take an anti-union stance aimed at suppressing labor demands. Legislature must be passed to protect those workers who attempt to unionize members and strict action should be taken against corporations that penalize workers for forming a union. After several failed attempts to form a union, workers at Wal-Mart used a creative approach whereby they formulated a group called Wal-Mart Workers Association. This association is not a labor union, rather a body of all current and past workers of Wal-Mart

which pursues the motto of fair wages and decent working conditions for all workers. This way, workers attempted to escape the wrath of management.

*Public outcry and media attention*

Negative media attention may be able to accomplish what regulation and corporate self-governance may fail to do. Johnson, Porter, and Shackell-Dowell (1997) documented that CEOs of companies that received bad publicity related to their executive compensation practices were likely to pay their CEOs less in subsequent years and likely to increase the pay-performance sensitivity of their compensation. Media coverage of public outcry at exorbitant pay packages and outrage at CEOs behaving badly may serve to bear down on organizations to reduce CEO compensation by making socially responsible investors become reluctant to invest in firms with unethical practices and also, possibly, by bringing about regulatory reform. The existence of firms such as KLD that regularly monitor firms for any issues pertaining to employee relations, adherence to human rights, and more generally, the practice of corporate social responsibility, is evidence that there is a formidable and ever growing market force willing to penalize firms with bad corporate governance and mean policies.

In closing, we have presented a case against rising executive compensation. We have argued that rising CEO pay results in power asymmetries in the workplace such that top executives come to view lower level workers as dispensable objects not worthy of human dignity. We presented the results from an archival study that show that high CEO compensation subsequently results in poor employee treatment, despite controlling for various and firm and industry specific variables. We also presented results from a laboratory study that show that increasing income disparities between managers and

workers results in managers perceiving greater power, and treating workers meanly.

Taken together, the evidence from the two studies is compelling. We have offered some solutions to remedy the problem of meanness in corporations. At a time when business leadership has come to be synonymous with worker exploitation, both internal organizational policies and government legislation need to be reformulated to protect workers, lest the moral outrage at the indignities suffered by them lead to a rebellion against corporate America.

## References

- Ackerman, F., Goodwin, N. R., Dougherty, L., & Gallagher, K. (2000). *The political economy of inequality*. Covelo, CA: Island Press.
- Bandura, A. (1999). Moral disengagement in the perpetration of inhumanities. *Personality and Social Psychology Review*, 3, 193–209.
- Bebchuk, L. A., & Fried, J. M. (2003). Executive compensation as an agency problem. *Journal of Economic Perspectives*, 17, 71–92.
- Desai, S. D., Brief, A. P., & George, J. (2009). Meaner managers: A consequence of income inequality. In R. Kramer, M. Bazerman, & A. Tenbrunsel (Eds.), *Social decision making: Social dilemmas, social values, and ethical judgments* (pp. 315-334). NY: Taylor & Francis.
- Dvorak, P. (2007). Theory and practice – Limits on executive pay: Easy to set, hard to keep. *Wall Street Journal (Eastern edition)*. New York, N.Y.: Apr 9, 2007. p. B.1
- Fast, N. J., & Chen, S. (2009). When the boss feels inadequate: Power, incompetence, and aggression. *Psychological Science*, 20, 1406-1413.
- Finkelstein, S., & Hambrick, D. C. (1988). Chief executive compensation: A synthesis and reconciliation. *Strategic Management Journal*, 9, 543-558.
- Finkelstein, S., & Hambrick, D. C. (1989). Chief executive compensation: A study of the intersection of markets and political processes. *Strategic Management Journal*, 10, 121-134.
- Frank, R. H. (2007). *Falling behind: How rising inequality harms the middle class*. Berkeley, CA: University of California Press.

- Galinsky, A. D., Gruenfeld, D. H., & Magee, J. C. (2003). From Power to Action. *Journal of Personality and Social Psychology, 85*, 453-466.
- Georgesesen, J. C., & Harris, M. J. (1998). Why's my boss always holding me down? A meta-analysis of power effects on performance evaluations. *Personality and Social Psychology Review, 2*, 184-195.
- Goodwin, S. A., & Fiske, S. T. (1993). *Impression formation in asymmetrical power relationships: Does power corrupt absolutely?* Unpublished manuscript. University of Massachusetts at Amherst. CITED IN FISKE 1993 POWER AS CONTROL
- Handgraaf, M. J. J., Van Dijk, E., Vermunt, R. C., Wilke, H. A. M. & De Dreu, C. K. W. (2008). Less Power or Powerless? Egocentric Empathy Gaps and the Irony of Having Little versus No Power in Social Decision Making. *Journal of Personality and Social Psychology, 95*, 1136-1149.
- Johnson, M., Porter, S., & Shackell-Dowell, M. (1997). Stakeholder pressure and the structure of executive compensation. *University of Michigan Working Paper.*
- Kane, G. D., Velury, U., & Ruf, B.M. (2005). Employee relations and the likelihood of occurrence of corporate financial distress. *Journal of Business Finance & Accounting, 32*, 1083-1105.
- Kasser, T., Cohn, S., Kanner, A. D., & Ryan, R.M. (2007). Some costs of American Corporate Capitalism: A psychological exploration of value and goal conflicts. *Psychological Inquiry, 18*, 1-22.
- Kelman, H. C. (1973). Violence without moral restraint: Reflections on the dehumanization of victims and victimizers. *Journal of Social Issues, 29*, 25-61.

Keltner, D., Gruenfeld, D. H., & Anderson, C. (2003). Power, approach, and inhibition. *Psychological Review*, *110*, 265-284.

Kipnis, D. (1972). Does power corrupt? *Journal of Personality and Social Psychology*, *24*, 33-41.

Kramer, R. M. & Gavrieli, D. A. (2004). The exaggerated perception of conspiracy: Leader paranoia as adaptive cognition. In D. M. Messick and R. M. Kramer (Eds.), *The Psychology of Leadership: New Perspectives and Research*. Mahwah, NJ: Lawrence Erlbaum.

Lambert, R. A., & Larcker, D. F., & Weigelt, K. (1993). The Structure of Organizational Incentives. *Administrative Science Quarterly*, *38*, 438-461.

Magee, J. C., & Langner, M. A. (2008). How personalized and socialized power motivation facilitate antisocial and prosocial decision making. *Journal of Research in Personality*, *42*, 1547-1559.

Martin, K. J., & Thomas, R. S. (1999). The effect of shareholder proposals on executive compensation (March 12, 1999). Available at SSRN:  
<http://ssrn.com/abstract=160188> or doi:10.2139/ssrn.160188

Moore, D. A., Cain, D. M., Loewenstein, G., & Bazerman, M. H. (Editors). (2005). *Conflicts of interest*. New York: Cambridge University Press.

Phillips, K. (2002). *Wealth and Democracy*. New York: Broadway Books.

Schubert, T. W. (2005). Your highness: Vertical positions as perceptual symbols of power. *Journal of Personality and Social Psychology*, *89*, 1-21.

Simon, H. (1957). *Models of man, social and rational: Mathematical essays on rational human behavior in a social setting*. New York: Wiley.

Steers, R., & Ungson, G. R. (1987). Strategic issues in executive compensation decisions.

In Balkin D. B., Gomez-Mejia L. R. (eds), *New Perspectives on Compensation*

(pp. 315-327). Englewood Cliffs, NJ: Prentice-Hall.

Tosi, H. L., Werner, S., Katz, J. P., & Gomez-Mejia, L. R. (2000). How much does

performance matter? A meta-analysis of CEO pay studies. *Journal of Management*,

26, 301-339.

Young, M. N., & Buchholtz, A. K. (2002). Firm performance and CEO pay: Relational

demography as a moderator. *Journal of Managerial Issues*, 14, 296–313.

Zimbardo, P. (2007). *The Lucifer effect: Understanding how good people turn evil*. New

York: Random House.

## Appendix A

### Weakness Criteria for Employee Relations

1. The company has a history of notably poor union relations.
2. The company recently has either paid substantial fines or civil penalties for willful violations of employee health and safety standards, or has been otherwise involved in major health and safety controversies.
3. The company has made significant reductions in its workforce in recent years.
4. The company has either a substantially under funded defined benefit pension plan, or an inadequate retirement benefits program. In 2004, KLD renamed this concern from Pension/Benefits Concern.
5. The company is involved in an employee relations controversy that is not covered by other KLD ratings.

### Strength Criteria for Employee Relations

1. The company has taken exceptional steps to treat its unionized workforce fairly.
2. The company has a cash profit-sharing program through which it has recently made distributions to a majority of its workforce.
3. The company strongly encourages worker involvement and/or ownership through stock options available to a majority of its employees; gain sharing, stock ownership, sharing of financial information, or participation in management decision-making.
4. The company has a notably strong retirement benefits program.
5. The company has strong health and safety programs.
6. The company has strong employee relations initiatives not covered by other KLD ratings.

## Appendix B

### Profit matrix

Performance of employee	Profit earned by the organization (in points)
Below average (4 mazes and below)	10 points
Slightly below average (5 to 10 mazes)	70 points
Average (11 to 20 mazes)	100 points
Slightly above average (21 to 26 mazes)	130 points
Above average (26 mazes and above)	190 points



**Table 1**

Correlational analysis of included variables (Study 1).

	Mean	SD	1	2	3	4	5	6	7	8
1. Meanness	0.03	1.42								
2. Firm age	11.55	4.90	0.12							
3. Firm size	5.81	0.82	-0.15**	-0.01						
4. ROA	0.47	0.27	0.13*	-0.10 <sup>†</sup>	0.04					
5. Tobin's Q	0.05	0.10	0.00	0.16*	-0.35**	-0.05				
6. Firm risk	184.00	570.56	0.04	-0.07	-0.13*	-0.06	0.02			
7. Industry dummy	0.20	0.40	0.01	0.06	-0.02	0.00	-0.02	0.20***		
8. CEO gender	0.04	0.19	-0.01	-0.13*	-0.13*	0.04	-0.03	-0.02	-0.10 <sup>†</sup>	
9. CEO compensation (in thousands of 2007 USD)	777.48	649.55	0.07	-0.02	0.28***	-0.01	-0.03	-0.09 <sup>†</sup>	-0.12*	0.06

Note. All tests of variables are two-tailed (N = 261).

<sup>†</sup>p ≤ .10; \* p ≤ .05, \*\* p ≤ .01, \*\*\* p ≤ .001

**Table 2**Summary of hierarchical regression analysis<sup>a</sup> of meanness (Study 1).

Main effects	Step 1	Step 2
Firm age	0.14*	0.14*
Firm size	-0.18**	-0.22**
ROA	0.15*	0.15*
Tobin's Q	-0.08	-0.09
Firm risk	0.04	0.04
Industry dummy	-0.02	0.00
CEO gender	-0.03	-0.02
CEO compensation		0.14*
Model F	2.48*	2.77*
ΔF		4.52**
R <sup>2</sup> (%)	6.40*	8.10*
ΔR <sup>2</sup> (%)		1.70**
Adjusted R <sup>2</sup> (%)	3.80*	5.20*

Note. All tests of variables are two-tailed (N = 261).

<sup>a</sup>Beta coefficients are standardized.

\* p ≤ .05; \*\* p ≤ .01.

**Table 3**  
Summary Statistics and Correlations (Study 2)

	Mean	SD	1	2	3
1. Sex	0.65	0.48	-		
2. Income inequality	-	-	0.14	-	
3. Perceived power	10.71	2.09	0.38**	0.49***	
4. Meanness	0.22	0.42	0.25*	0.29*	0.52***

*Note.* All tests of variables are one-tailed (N = 62).  
†p ≤ .10; \*p ≤ .05; \*\*p ≤ .01

**Table 4**  
Summary of hierarchical logistic regression analysis of meanness (Study 2)

Predictors	Step 1						Step 2					
	<i>B</i>	SE <i>B</i>	Wald's $\chi^2$	<i>df</i>	<i>p</i>	<i>e<sup>B</sup></i> (Odds ratio)	<i>B</i>	SE <i>B</i>	Wald's $\chi^2$	<i>df</i>	<i>p</i>	<i>e<sup>B</sup></i> (Odds ratio)
Constant	-1.063	0.528	4.050	1	0.044	0.345	-5.167	1.714	9.093	1	0.003	0.006
Sex	0.988	0.571	2.988	1	0.084	2.685	0.438	0.637	0.473	1	0.492	1.550
Income inequality	1.135	0.546	4.316	1	0.038	3.111	0.282	0.667	0.179	1	0.673	1.326
Perceived power							0.457	0.178	6.622	1	0.010	1.580
Goodness-of-fit test			$\chi^2$	<i>df</i>	<i>p</i>				$\chi^2$	<i>df</i>	<i>p</i>	
Hosmer and Lemeshow test			0.573	2	0.751				5.982	7	0.542	
Cox and Snell $R^2$	= 0.127						Cox and Snell $R^2$ = 0.228					
Nagelkerke $R^2$	= 0.169						Nagelkerke $R^2$ = 0.304					

*Note.* All statistics reported herein use 3 decimal places in order to maintain statistical precision. N = 62.

**Figure 1**

Effect of income inequality of manager on meanness (Study 2)

