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Americanization as a driver of CEO pay in Europe: The moderating role of CEO power

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ABSTRACT

This paper examines the relationship between Americanization and CEO pay levels in Europe and how this relationship is moderated by CEO power. Based on neo-institutional theory, our study provides empirical support for a link between Americanization and CEO pay levels. Drawing on a sample of large listed European firms, our results suggest that various dimensions of Americanization, i.e., Americanization of the CEO, of the firm and of the industry, can be associated with higher CEO pay. Combining neo-institutional approaches with managerial power perspectives, we show that Americanization can have an even stronger effect on pay when the CEO is powerful.

1. Introduction

CEO pay is a topic that has received considerable attention by scholarly research and by the general public over the last few years (Devers, Cannella, Reilly, & Yoder, 2007; Finkelstein, Cannella, & Hambrick, 2009; Kumar & Zattoni, 2016). While there are significant differences in CEO pay practices between countries, the United States is usually viewed as ‘setting the tone’ in worldwide CEO compensation (Abowd & Bognanno, 1995; Berrone & Otten, 2008; Cheffins & Thomas, 2004). Clearly, US CEOs receive significantly higher pay than CEOs anywhere else in the world (Gerakos, Piotroski, & Srinivasan, 2013; Murphy, 1999). Previous literature has stressed that CEO compensation practices from the US might be adopted by firms in other countries, for example by firms in Europe (Cheffins, 2003; Fiss & Zajac, 2004; Zattoni & Minichilli, 2009). As a report in the New York Times put it: “Along with hip-hop and Hollywood movies, Europeans are eagerly importing another American phenomenon: soaring pay packages for chief executives” (Fabrikant, 2006).

However, in this paper, we argue that not all European firms are equally prone to adopt US pay practices (Bruce, Buck, & Main, 2005; Cheffins, 2003; Sanders & Tuschke, 2007). Our assumption is that firms such as SAP, a German software firm headed by an American CEO and operating in a US-dominated industry, are under greater pressure to offer US-style CEO pay packages than other firms that are less exposed to the US. Anecdotal evidence supports our assumption: in 2016, SAP’s CEO Bill McDermott was the highest-paid CEO in Germany (Ricadela,

2017). But is there more than anecdotal evidence to be found? Our study has the objective to systematically examine whether Americanization is related to CEO compensation levels in European firms. Whereas firms themselves may be ‘Americanized’, we also consider the Americanization of individuals and industries. We define Americanization as exposure to the US institutional environment, and we investigate this exposure at the level of individuals, firms and industries to analyse the association with CEO compensation levels.

Previous studies in the international business (IB) and corporate governance field have already started to investigate the link between Americanization and the adoption of governance practices in general. From this literature we know that Americanization can be linked to the adoption of governance practices such as greater information disclosure or board monitoring by independent directors (e.g., Desender, Aguilera, López-Puertas Lamy, & Crespi, 2016; Khanna, Palepu, & Srinivasan, 2004). In addition, some studies have analysed the relationships between Americanization and compensation; these studies provide robust evidence for an association between Americanization and the adoption of equity-based pay components, such as stock options (e.g., Buck & Chizema, 2008; Chizema, 2010; Geng, Yoshikawa, & Colpan, 2016; Sanders & Tuschke, 2007). However, prior research on the link between Americanization and the level of executive compensation is relatively rare, with only a handful of studies indicating that Americanization might be related to higher levels of CEO pay (Carter, Lynch, & Zamora, 2009; Fernandes, Ferreira, Matos, & Murphy, 2013; Gerakos et al., 2013; Oxelheim & Randøy, 2005).

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While existing studies provide valuable insights, they mostly employ a conceptualization of Americanization that is restricted to the *firm*. Yet, the broader literature on the determinants of CEO compensation suggests that it is not only firm characteristics that can influence CEO pay practices but also characteristics of the *CEO* and of *industry peers* (Finkelstein et al., 2009; Geng et al., 2016; Gomez-Mejia, Berrone, & Franco-Santos, 2010; Sanders & Tuschke, 2007). Thus, our study attempts to fill a gap and establish a broader framework by conceptualizing Americanization as comprising three dimensions, i.e., Americanization of the CEO, Americanization of the firm and Americanization of the industry. The framework is based on neo-institutional approaches and, hence, addresses calls for a socialized view of corporate governance (Aguilera & Jackson, 2003; Chizema, 2010).

Furthermore, because previous research has focused primarily on the direct relationship between Americanization and CEO pay, there is relatively little knowledge about contextual factors that play a contingent role in this relationship. Therefore, we go beyond investigating the direct effect of Americanization on CEO pay levels by exploring the role of CEO power in the Americanization–CEO compensation nexus. We base our reasoning on related literature emphasizing the importance of power relations among corporate governance actors in the adoption of governance practices in general and compensation practices in particular (Aguilera & Jackson, 2010; Buck & Chizema, 2008; Greenwood & Hinings, 1996). Thus, we extend our theoretical framework grounded in neo-institutionalism by integrating managerial power theory.

Based on a sample of the largest multinational enterprises (MNEs) in Europe, our study uses regression analysis to test the relationship between Americanization and CEO compensation as well as the moderating effects of CEO power. Our results provide support for our hypothesized direct relationships, demonstrating that all three dimensions of Americanization (i.e., CEO, firm and industry) are positively associated with CEO compensation levels. Our findings also show evidence for a positive moderating effect of CEO power for the individual and the industry dimension. In other words, an Americanized CEO or a CEO in an Americanized industry can actually magnify the positive effect of Americanization if he or she is powerful. Hence, it is not solely coercive, normative and mimetic pressures that lead European firms to employ US-style compensation practices; it is also powerful CEOs strengthening Americanization processes.

What are the main contributions that our study makes to IB and corporate governance literature? First, we broaden our understanding of the link between Americanization and CEO compensation levels by examining multiple dimensions of Americanization. Based on neo-institutional perspectives, our approach offers a more comprehensive view of Americanization, since we move beyond the firm level. Second, we contribute to our knowledge about how firms respond to exposure to multiple institutional environments. Combining neo-institutional perspectives with managerial power perspectives, we demonstrate how CEO power influences the adoption of practices from foreign institutional environments. Third, our study provides novel insights into the mechanisms through which managerial power leads to higher executive compensation. We find that powerful CEOs can espouse specific institutional logics that have a positive impact on their pay levels. Fourth, we shed light on the role that powerful CEOs play in the adoption of governance practices and other organizational practices that stem from the US context. The findings of our study suggest that powerful CEOs' self-interest can be an influencing factor in the adoption of practices. Overall, our study follows a recent call by Aguilera, Judge and Terjesen (2018) that "[f]uture research could help us to better understand how multinational firms pursue distinctive governance practices and how transnational pressures shape these decisions." We aim to respond to this call by showing that in European MNEs, CEO compensation practices are shaped by Americanization in connection with CEO power.

2. Theory and hypotheses

2.1. Corporate governance and multi-institutional embeddedness

While many studies on CEO compensation are based on agency theory (Bebchuk & Fried, 2003; Cuevas-Rodríguez, Gomez-Mejia, & Wiseman, 2012; Schmid & Wurster, 2016), we investigate the Americanization of compensation through the lens of neo-institutional theory. This theory's basic tenet is that organizational success depends not only on technical efficiency but also on conformity with the demands of the institutional environment in which the organization is embedded (Meyer & Rowan, 1977). In particular, organizations are confronted with the institutional logics of their institutional environment that help to interpret organizational reality and that provide guidance on what is appropriate and successful (Thornton, 2004). According to neo-institutional theory, organizations are under pressure to employ practices that are prescribed and legitimated by the prevailing institutional logic (Greenwood, Raynard, Kodeih, Micelotta, & Lounsbury, 2011). However, MNEs (unlike some other types of organizations) are very specific with regard to the institutional environments to which they are exposed. Because MNEs operate in various countries, they are simultaneously embedded in multiple institutional environments and, hence, are exposed to various institutional logics (Collings & Dick, 2011; Marano & Kostova, 2016; Saka-Helmhout, Deeg, & Greenwood, 2016). This 'cross-border condition' results in diverse and possibly conflicting institutional pressures. Striving for legitimacy, MNEs must reconcile and outweigh various institutional pressures, depending upon their relative salience (Aguilera, Judge et al., 2018; Greenwood & Hinings, 1996; Durand, Hawn, & Ioannou, 2017).

There are three main types of institutional pressures, i.e., coercive, normative and mimetic pressures (Chizema 2010; DiMaggio & Powell, 1983; Judge, Li, & Pinsker, 2010). Coercive pressures are imposed on organizations by other actors upon which they are dependent and by cultural expectations prevailing in the society within which organizations function. Normative pressures result primarily from professionalization, i.e., the development of a shared understanding of appropriate practices amongst members of an occupation. Organizations and individuals in the field, such as consultancy firms, universities and analysts, act as disseminators of these practices. Finally, mimetic pressures occur when organizations respond to uncertainty by modelling themselves on other organizations perceived as successful (Chizema, 2010; DiMaggio & Powell, 1983; Scott, 2014). As a function of these pressures, MNEs can be compelled to employ organizational practices that differ from those prevailing in their home environment (Kostova & Zaheer, 1999; Marano & Kostova, 2016; Sanders & Tuschke, 2007). In our study, we focus on MNEs that are based in the European institutional environment and are exposed to the US institutional environment.

Corporate governance, which is often defined as "the structure of rights and responsibilities among the parties with a stake in the firm" (Aoki, 2000: 11), is shaped by the institutional environment in which the organization is embedded (Aguilera & Jackson, 2010; Geng et al., 2016; Kumar & Zattoni, 2016). Firms that are exposed to various institutional environments are under multiple institutional pressures to employ appropriate governance practices (Desender et al., 2016; Judge, Douglas, & Kutan, 2008; Yoshikawa & Rasheed, 2009). It has been further argued that governance practices developed in one national environment can diffuse to another, as recent studies in international corporate governance research have documented (Bezemer, Zajac, Naumovska, Van den Bosch, & Volberda, 2015; Cuomo, Mallin, & Zattoni, 2016; Fiss & Zajac, 2004; Geng et al., 2016; Haxhi & Van Ees, 2010; Yoshikawa, Tsui-Auch, & McGuire, 2007; Zattoni & Cuomo, 2008). While practices may diffuse from one country to another country in general, the MNE context is a particularly rich setting for such diffusion: the relationships, links and flows among various MNE units

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