

WHARTON ON

Human Resources



The HR Contribution

FROM ADDRESSING DAY-TO-DAY EMPLOYEE ISSUES like hiring, promotion, and compensation to handling larger potential crises such as layoffs and restructuring during a merger, Human Resources plays a critical role in the life of a company. As the workplace evolves, so do the needs of managers and employees; and HR departments need to stay ahead of that curve. How can companies retain talent in an increasingly competitive global business environment? What factors contribute to employee burnout? How can companies make use of an aging workforce with little means for retirement? And how does the rising tide of M&A activity ultimately affect employee morale? The following *Knowledge@Wharton* stories examine these issues.

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Critics say HR departments are needlessly bureaucratic, obstructionist, and too closely aligned with the interests of senior managers. Others note that HR plays a key strategic role, providing direct input into major business transactions such as mergers and acquisitions and restructurings, and improving organizational effectiveness. The truth is probably somewhere in between—a reflection of workplace evolution, the new global economy, and changing expectations on the part of employees and managers.

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David Sirota, co-author of *The Enthusiastic Employee: How Companies Profit by Giving Workers What They Want* (Wharton School Publishing), believes far too many managers stifle employee enthusiasm across the board by using bureaucratic or punitive techniques that should be reserved for a troublesome few. In an interview with *Knowledge@Wharton*, Sirota talks about employees' three basic goals, how to deal with employees who are "allergic" to work, and how managers can inspire greater loyalty and productivity from their workforce.

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One of the biggest complaints employees have, according to Wharton Management Professor Sigal Barsade, is that "they are not sufficiently recognized by their organizations for the work they do." Barsade and doctoral student Lakshmi Ramarajan look at the role of respect in a paper entitled "What Makes the Job Tough? The Influence of Organizational Respect on Burnout in Human Services."

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The days when an executive could look forward to a leisurely retirement out on the golf course are over, thanks to a possible looming job shortage, a graying population, low savings rates, and an insecure Social Security system. The impact of these factors on both workers and companies was the subject of a Symposium on Older Workers, co-sponsored by the AARP Global Aging Program along with Wharton's Center for Human Resources and Boettner Center for Pensions and Retirement Research.

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The initial headlines announcing mega-corporate mergers and acquisitions typically focus on Wall Street's appreciation for improved finances, less duplication of services and staff, the ability to grow faster, and the anticipation of higher returns for shareholders. Yet, as Wharton professors point out, companies that fail to factor in the costs of layoffs, declining morale, and the chaos that comes from restructuring are headed for trouble.

Is Your HR Department Friend or Foe? Depends on Who's Asking the Question

TALK TO HUMAN RESOURCES professionals, consultants, and scholars who study the workplace, and you will find two different views of HR.

According to its critics, HR departments can be needlessly bureaucratic, obstructionist, stuck in the “comfort zone” of filling out forms and explaining company benefits, and too closely aligned with the interests of management yet lacking the business knowledge to be effective strategic partners. Dealing with these types of HR departments “is like going to the dentist,” says David Sirota, author of *The Enthusiastic Employee: How Companies Profit by Giving Workers What They Want* (Wharton School Publishing). When people are asked to rate the quality of different functions within their company, he adds, “IT and HR are repeatedly rated the lowest.”

The more positive view of HR is that it works directly with senior management, providing crucial input into major business transactions such as mergers and acquisitions and restructurings. In this scenario, HR departments have moved away from the traditional role of administrators—many of those responsibilities are now outsourced—to a more creative focus on their prime role, which includes recruiting talent, promoting mobility and career development, and improving organizational effectiveness. “I would not choose HR as a career if we couldn’t be a strategic partner with the business,” says Kathy Gubanich, managing director of HR at The Vanguard Group. “HR is fortunate to report to the CEO of Vanguard... If we didn’t, it would mean HR’s priorities are being set differently.”

Peter Cappelli, director of Wharton’s Center for Human Resources, recently led a discussion at the Center focused on the question: “What is the role of HR now?” From the 1920s on, Cappelli says, HR was seen as a way to advocate for, and protect, employees—an orientation that became “quite explicit in the 1950s and beyond as part of an effort by management to



prevent unionization.” But more recently, and especially over the past decade, the threat of unionization is much less widespread even as technological advances have made employees more expendable. The “social contract” between employee and employer—in which companies provided lifetime employment to its workers in return for loyalty and commitment to company goals—has ended.

These days, employees are afraid to quit because of the tight labor market and reluctant to complain about increased work loads for fear of being laid off, says Cappelli. “Companies are pushing more and more work onto employees, and HR departments are becoming the mechanism for doing that. As a result, the idea that HR people are there to represent workers—or at least deal objectively with their concerns—is pretty much gone.” In addition, with companies continuing to cut back employee benefits such as healthcare and pensions, HR departments have found themselves “increasingly the bearer of bad news to employees.”

Meanwhile, HR issues are very much a part of the press’s business coverage, whether it’s Hewlett-Packard’s recent announcement that it is laying off 14,500 employees (including a number of HR positions) or the breakdown of talks between Citigroup chairman Sandy Weill and Citigroup’s board over the retirement perks available to him under his contract. Weill, who

is reportedly interested in starting a private equity fund, had earlier committed to staying on as chairman until April 2006.

Strategy-Driven HR: Reality or Goal?

If you look at the history of HR, says James Walker, a consultant on strategic human resources based in La Jolla, CA, trends in HR—such as outsourcing, the establishment of call centers and service centers, and the integration of work-life balance issues—usually require about a decade to take hold.

For example, “most of us would like to see HR be transformed more rapidly into a business partner, with less emphasis on administrative functions that can now be outsourced,” Walker says. “To achieve that, it’s vital to help key HR individuals accelerate their development of business skills. I think many companies are, in fact, doing this, but not as fast as I would like. There is still a tremendous attraction within HR to the comfort zone of more traditional and functional support-service kinds of relationships.”

The classic area where HR leaders can provide strategic input is “anticipating a merger,” says Walker. “A very well-defined set of opportunities and experiences exists, including assistance in valuing the merger, developing the integration plan, communicating with employees, matching talent, and so forth. Some company HR departments play a key role here. In others, they are still observers, cleaning up the mess afterwards.” HR executives who serve as business partners, he adds, are more likely to be in strategy-driven organizations—professional services firms, financial services firms, high-tech companies, and “to some extent pharmaceuticals, the opposite end of the continuum from healthcare companies and manufacturers.” The most talented HR leaders, he says, tend to work “in pockets within a business. They have established a relationship with their client executive in which they are able to have a dialogue and push back as appropriate.”

Over the last 10 to 15 years, HR has begun to have a much bigger impact on how a company operates, says J. Steele Alphin, global personnel executive at Bank of America. “To put this in perspective: At Bank of America, we have \$28 billion of noninterest expenses. Of that, \$15 billion is related to personnel”—everything from salaries, incentive plans, and fringe benefits to

talent retention programs and risk management strategies. “If you can effectively manage those dollars, trying to get as high a return on investment as possible, then you approach the opportunity a lot differently.”

To fulfill his mandate of growing revenue, increasing productivity, and developing leadership in the company, Alphin, who reports directly to CEO Ken Lewis, has assembled an HR team that includes managers with degrees in business, HR, psychology, and engineering. “Our team looks very similar to any other high-level team in Bank of America,” he says. So when HR sits around the table with other departments, “we don’t talk HR; we talk about the business.”

Lewis, he adds, “looks to us to be business leaders, business partners, the person at the table who will always bring up the critical fact that no one else does.” Alphin, who has 10 direct reports, says that most of those 10 people show up “on replacement charts for other areas of the company. One of our goals is to be a net supplier of talent to Bank of America. We have had personnel executives move into running real estate, branding, and transition on acquisitions.”

According to Mark Bieler, a human resources consultant who was executive vice president of HR at Bankers Trust from 1985 to 1999, “without the direct tie to strategy, there is no context for HR work. You have to be completely focused on aligning HR practice, policies, and procedures to the overall strategy of the organization.” In the mid-1980s, when Bieler was at Bankers Trust, chairman Charles Sanford converted the company from a commercial bank to an investment bank—“about as radical a cultural shift as one could imagine,” says Bieler. “My role was taking a set of HR practices that I had inherited and making sure they were consistent with where we were trying to take the firm. At the simplest level, that means redesigning pay systems, not so much to pay people more—although investment bankers do tend to make more—but to restructure the system to include smaller amounts of fixed compensation and to put more of people’s pay at risk.

“In addition, we became the first bank in the mid-1980s to offer a cafeteria-style benefits approach because we wanted people to take charge of their lives, to be more

entrepreneurial. Cafeteria benefits were more suited to the type of organization we wanted to be... We shifted our recruiting goals, changed the way new employees were socialized...and bit by bit, brick by brick, aligned what we did from the people point of view with the strategy of the company."

Jack Welch, former CEO of General Electric and author of a book entitled *Winning*, noted in a recent interview that "outside of the CEO, HR is the most critical function in any company. Development of leaders is the ultimate responsibility of every CEO and thus is an integral part of HR. I saw my job as allocating people and dollars to opportunities. I wasn't designing products. I was putting people where I thought they were right for the job. I did that with my partners in HR." HR evaluation systems, he says, "should be rigorous and nonbureaucratic" and monitored as closely as financial reporting is now monitored under Sarbanes-Oxley.

While many HR professionals say their role is to be a strategic partner with senior management, critics question whether this is possible given that HR people often lack the business skills to understand strategy or their role in implementing it. Furthermore, some senior managers aren't interested in having HR as a strategic partner; they just want the department to go out and hire the people they (the managers) want.

"If top management doesn't see value in having HR as a strategic partner—and if HR can't think out of the box in that role—then the partnership is probably not going to happen," says Wharton Management Professor Nancy Rothbard. She cites the case of a woman who heads HR at an in-house call center for a large financial services firm who is "constantly experimenting with new ways to help the company achieve its overall goals," such as trying out new tools to better select employees and sitting through hours of training sessions to test their effectiveness. Overall, says Rothbard, such an approach "means committing resources—in terms of top management's time, as well as the time of managers a level below." The effort, she says, "took guts on HR's part because it wasn't clear there was going to be a definite payoff."

Of course becoming a "partner" with senior management doesn't always happen. At

Vanguard, says Gubanich, "you have to earn your way to the table. I might also say that rather than a strategic partner, we are more of a strategic enabler. We need to understand the business deeply—where it is now and where it wants to go. This is important because sometimes I think we get caught up in, 'What is the coolest program?' or 'Should we be designing something new?' The key question has to be: 'Was HR successful at moving the company in the direction it wanted to go?'"

HR departments have moved away from the traditional role of administrators to a more creative focus on recruiting talent, promoting mobility and career development, and improving organizational effectiveness.

HR at Vanguard has a number of strategic imperatives, Gubanich adds, "such as hiring the right people in the right place in the right time, looking for breadth and depth of leadership talent, maintaining the right culture for the organization, risk mitigation and operational excellence... For example, if someone at Vanguard wants to create a new business, we talk about the people and programs needed to get there. Do you have the leadership necessary for that? Do you have the training programs? Do you know how to take a group and say, 'We are now going to do things this way instead of that way'? What do you want to accomplish? Will you be sales oriented or service oriented? What are the competencies required for the job? Will you focus on external or internal hiring or a combination of the two? And so forth."

The same orientation exists at Air Products, an \$8 billion industrial gas, chemical, and home healthcare company headquartered outside of Allentown, PA. Vince Kraft, director of industrial relations, reports to the vice president of human resources. "When people say HR is nonstrategic and does not understand the business, here it is just the opposite," Kraft says. "We are imbedded in a variety of operational issues especially in the field. We are out there among the employees, customers, and the distribution network; and we are seen by senior management as very valuable, especially when

it comes to areas like professional development and succession plans.”

In some companies, HR’s influence extends beyond their own departments. “Outside of the marketing function,” notes Bank of America’s Alphin, “the personnel function at Bank of America has one of the biggest responsibilities relating to brand. For example, every year we hire about 40,000 people externally. Each time we interview someone, we are looking for talent. That person, in turn, has a chance to see our company. That’s a branding opportunity. If you interview people, even if you do not hire them, the experience should be such that they would want to bank with us.”

A Two-Tiered System

Critics of the way HR has developed over the past decade suggest that HR has become a “handmaiden of management,” more concerned with carrying out directives from above than supporting the needs of employees.

Bieler sees “some truth” to that claim but says it’s “largely because of the decentralization of the functions. The most common model today in large corporations is a smaller, highly expert central staff and then masses of HR people in distributed HR organizations throughout the company. Their reporting relationship may either be dual—to the head of the line operating office and to the head of HR—or may be direct. But at the end of the day, the power dynamic seems to favor HR’s relationship to their senior line executive. This distribution of the HR function has many advantages, but one of the downsides is a decrease in the view of HR as playing an ombudsperson role in the organization.”

The “social contract” between employee and employer—in which companies provided lifetime employment to its workers in return for loyalty and commitment to company goals—has ended.

According to Air Products’ Kraft, “the climate change” toward HR being perceived as pro-management “began when we started to outsource what is generally described as administrative duties, but what are generally

regarded by employees as positive employee relations—such as help with medical insurance, leave, and vacation issues. The day-to-day contract between employees and management of keeping each other informed has been relegated to either voicemail or e-mail as opposed to conversations. HR began to be perceived by the employee base as a necessary evil.”

Kraft also notes a tendency to treat people as “numbers rather than as individuals, which is not the fault of the company but really the fault of financial pressure from Wall Street. It’s very hard not to feel the pressure to cut costs...”

When Leon Cornelius, a director of GM’s labor relations staff, first started at a GM plant in 1978, “all the HR issues were handled right there, in the plant,” he says. Employees could ask questions about benefits, compensation, and “if you were sick or somebody passed away, there were people who you could talk to about it and find a sympathetic ear. It wasn’t strategic; it was more transactional, but it had that personal touch. Now it’s all about going to the web and calling 1-800.”

The system could be better if it were two-tiered, Kraft suggests. “Somebody has to develop an alternative dispute resolution system or some mechanism that allows employees a voice... I still view that as a part of the HR function, although it doesn’t seem to be happening.”

Kevin Sullivan, an employee relations consultant at IBM, acknowledges allegations of HR bias towards management, but points to the company’s appeals process as an effort to “maintain the integrity of the system.” Once employees exercise their right to challenge a performance appraisal, salary decision, or other personnel matter, that challenge is handled in one of two ways—either through the appointment of an investigator, assigned by management, to look into the complaint, or through a panel review. The panel, which is available to U.S.-based employees, consists of five individuals—three employees and two managers, all of them randomly selected—who hear the case and make a decision. “That system gets used. Our employees are not shy about coming forward.”

In many companies, Sullivan adds, employees feel that the social contract between the company and its workforce no longer exists

and that “employees are on their own. What companies must do is offer a compelling case to the individual as to why he or she would want to work there. In our case, we emphasize our skills training, our workplace flexibility options (including work-at-home), our commitment to diversity, our focus on performance differentiation, our leading-edge technology, and our leadership development... You have to show employees that opportunities exist.”

For Mark Bieler, the bottom line is that “the quality of HR functions correlates more than anything to the quality of culture and management they are supporting. If you put me in an environment as head of HR in a company that fundamentally doesn’t respect people and has a short-term orientation toward them, I would have a difficult time either championing the needs of the people or furthering the objectives of the organization through HR policy or practice.”

Seeing the Employee as Customer

According to the August 2005 cover story in *Fast Company* magazine, entitled “Why We Hate HR,” HR people are not interested in an “open-minded approach” when it comes to making exceptions to company policies, including pay schedules. “Instead, they pursue standardization and uniformity in the face of a workforce that is heterogeneous and complex... Bureaucrats everywhere abhor exceptions—not just because they open up the company to charges of bias but because they require more than rote solutions.”

Rather than sending the message that the company values “high-performing employees and is focused on rewarding and retaining them,” the article says, “HR departments benchmark salaries, function by function and job by job, against industry standards, keeping pay—even that of the stars—within a narrow band determined by competitors. HR, in other words, forfeits long-term value for short-term cost efficiency.” The article poses this question: “Who does your company’s vice president of human resources report to? If it’s the CFO—and chances are good it is—then HR is headed in the wrong direction.”

Sirota has a different way of getting at the same issue: If you think of HR as having three roles, says Sirota, the first is to carry

out administrative functions. The second is to serve as strategic partner, and the third is to see the employee as customer. The most important part of that customer-centric view involves “working with management to develop policies, practices, and philosophies geared toward creating a truly motivated and dedicated workforce,” says Sirota. Generally speaking, “in many organizations, that role is more notable by its absence.”

When HR managers “say they want to be business partners,” suggests Sirota, “what they mean is they want to work for management. Most companies say employees are our greatest asset, but what they really mean is they are our biggest cost.” HR should “be proactive. Walk around the company, find out the issues, just as you would do with customers. External customers are surveyed regularly. HR should be surveying their internal customers as well.”

GM’s Cornelius agrees that “what’s missing in today’s workplace is the view that HR is there for the employees. When younger people in the organization come to me for advice I say, ‘Have you talked to anybody in HR about this?’ and they roll their eyes and say, ‘Why should I bother to do that?’” But it doesn’t have to be that way, Cornelius adds. “An HR person can handle a hard conversation with an employee about what he or she needs to do to improve, but that employee can still walk away thinking: ‘If I do these things, I will have somebody there who will help me move around the company or get me positioned for a promotion.’”

According to Mark Bieler, a human resources consultant, “without the direct tie to strategy, there is no context for HR work.”

HR also tends to push onto managers a number of functions that could be done by HR staff, such as finding and downloading the forms needed when an employee retires. “HR has dumped a number of jobs on other functions that they used to do themselves,” Cornelius says. But he also has praise for specific HR policies, including, for example, those dealing with layoffs. “I give GM credit in situations where there is a downsizing. They stand tall

when it comes to the employees. The situation is handled in a very humane way.” And where major long-term issues are involved, such as restructurings and joint ventures, “HR is actively a part of those strategic discussions, along with labor relations. HR brings value” to the table.

Bank of America is taking the idea of serving employees one step further. The company just opened a facility near Charlotte, NC, which provides a flexible work environment and allows people who live in nearby communities to spend a day or two every week at that location, rather than commuting an hour or more each way into the city. “It’s a new concept, and we have gotten very good response to it,” says Alphin. “In addition, we are already seeing increases in productivity among employees who use this option.” Alphin points to another initiative at Bank of America instituted this year—a broad-based incentive plan that will pay out between \$500 and \$3,000 to eligible employees from mid-level managers to their associates, in addition to existing incentive programs already in place.

He predicts that some companies will start insourcing HR functions that they previously outsourced. “We have about 1,200 people in HR now, but that number will soon grow to 1,500 because we are bringing some staffing back in-house—including recruiting—that we had outsourced. We liked the pricing, but we didn’t like the quality,” Alphin says. “You always have to look at that tradeoff.”

Performance-Based Pay

Given the recent controversies over huge compensation packages at public companies, pay-for-performance continues to be a hot-button issue for everyone from CEOs down to lower-level employees. According to Walker, “the leading-edge thinking now is much more on segmenting work across the company and also segmenting the work force” in ways that let differences be defined and valued. “This allows HR to move away from a system of ‘everyone is treated the same’ to one where people can be treated differently according to business needs, individual preferences, and performance. That’s a trend, starting with IBM and working through a lot of companies.”

IBM’s Sullivan would agree. The philosophy of the company toward its 330,000 employees “is

to pay our best people like the best people in the industry are paid. The rest of our employees get paid competitively. We also have a performance appraisal system in which we hold people accountable. That’s the underpinning of the system, whether it is pay, promotions, or the opportunity for stock options and other awards and recognition. It is all based on performance.”

At Vanguard, with its 11,000 employees, “we describe ourselves as a pay-for-performance organization,” adds Gubanich. “As such, we believe that the top performers should be rewarded more. We do all kinds of analysis on pay and total compensation—where it should fall on the individual level as well as the job aggregate level. In addition, it can’t just be all about the individuals. It is valuable to also have team and company incentives.”

Issues of pay and performance are now reaching boards of directors as well, says Bieler. “One key factor in the evolution of HR departments has been Sarbanes-Oxley. At least for the head of HR, this has radically changed the relationship with the board’s compensation committee. Recently, as part of my work redesigning two companies’ compensation systems, I dealt with consultants hired by the compensation committee. That hadn’t happened before. So issues around pay—including sensitivity to full disclosure of executive perks, for example—are in the forefront these days, as are issues of management development and succession. Sarbanes-Oxley has had a profound effect on the relationship between the board and the company, in which the HR function plays a key role.”

The question arises, adds Walker, as to where a board gets guidance on matters of corporate pay, perks, etc. “Is it from corporate HR, or does the board hire its own consultants directly?” With regard to compensation, “HR executives should be doing the analysis and bringing information and advice to the board. If you want HR to be a strategic partner, it can’t be just with the CEO; it has to be with the board as well.”

But pay issues are not always easy to administer, especially at places like universities and hospitals, where, as Bieler says, “there are numerous constituencies, all of whom think they are in charge. It is hard to get your arms around a clear-cut strategy.” Cappelli suggests that one approach to setting pay, “left over

from this idea of looking out for employees, is to have a model of equality: Treat everyone roughly the same, especially in issues of pay. Of course places that do this get complaints from top managers saying, 'I lost these people because HR wouldn't let me pay them enough.' Top managers, who for the most part are high achievers, believe people should be paid based on their own performance."

The problem, says Cappelli, "is that perceived inequities drive people crazy. It's one thing

to say, 'This person is a star, pay him or her more, or he might quit.' What happens next? People who discover this person is being paid more [within an equal pay system] start to complain. So you move to a model where everyone is paid based on performance. But this approach requires an objective assessment of performance that everyone must be willing to buy into. That's the hard part." ■

Giving Employees What They Want: The Returns Are Huge

DAVID SIROTA, CO-AUTHOR of *The Enthusiastic Employee: How Companies Profit by Giving Workers What They Want* (Wharton School Publishing), believes far too many managers stifle employee enthusiasm across the board by using bureaucratic or punitive techniques that should be reserved for a troublesome few.

Yet his book, written with Louis A. Mischkind and Michael Irwin Meltzer, finds that firms where employee morale is high—such as Intuit and Barron’s—tend to outperform competitors. The authors’ research is based on the results of 2.5 million employee surveys taken since 1994.

For example, out of 28 companies employing 920,000 studied by Sirota Consulting, the share price of 14 companies—those considered to have high morale—increased an average 16 percent in 2004. Those prices were then compared to the companies’ industry averages, where the increase was just 6 percent. Six “low-morale” companies saw their prices increase, on average, by 3 percent, as against an overall industry average of 16 percent. Industry comparisons were based on data from 9,240 companies.

In an interview with *Knowledge@Wharton*, Sirota says managers should rely on common sense principles that allow workers to take pride in their work. He urges them to reject trendy, get-tough tactics that were promoted in the late 1990s, such as trimming staff even at healthy companies in order to improve shareholder value.

KNOWLEDGE@WHARTON: *What do employees want?*

SIROTA: We find there are three basic goals of people at work. First, to be treated fairly. We call that equity. Employees want to know they are getting fair pay, which is normally defined as competitive pay. They want benefits and job security. These days, employees especially need medical benefits, so those have become significant. On the nonfinancial side, employees want to be treated respectfully, not as children



or criminals. Equity is basic. Unless you satisfy those needs, not much else you do is going to help. If I feel underpaid and if I feel that the company is nickeling and diming me, or wants to pay as little as possible, there is not much else an organization can do to boost my morale. This runs contrary to what a lot of people in my field say—that pay is not that relevant. Baloney. It’s terribly, terribly important.

Second, employees want a sense of achievement from work. The key element is to be proud of what you do and proud of the organization for which you are doing it. People don’t want to work for an organization that’s run by a bunch of crooks. The third element is camaraderie. This is also not mentioned much in our field, but it’s key—not only in the sense of having a friend, but working well together as a team. That is a tremendous source of satisfaction for people.

KNOWLEDGE@WHARTON: *Do you see a difference in attitudes among different kinds of employees or organizations?*

SIROTA: We find these three elements are nearly universal. There is all this talk of new generations—for example, that Generation X does not care about job security. We find absolutely no evidence of that. We find no difference across countries, between men and women, or in the new economy versus

the old economy. One reason a lot of these new economy companies imploded is they forgot about basic management. Our research indicates you don't tamper with some of the basics. All this talk about flattening the organization to eliminate hierarchy is nonsense. There are certain traditional management principles that are important and valid. There are also traditional management principles that are very disruptive, like not giving people a say in the way they do their jobs.

KNOWLEDGE@WHARTON: *Your research shows most workers are happy at a new job for about 6 months before the honeymoon ends. What goes wrong?*

SIROTA: We are often asked how to motivate employees. Our response is, that's a silly question. The real question is: "How do you keep management from destroying motivation?" When we look at the data, we find that people coming to a new job are quite enthusiastic. Most of them are very happy to be there and looking forward to meeting their new coworkers. But as you study the data, you find morale, or enthusiasm, declines precipitously after 5 or 6 months. One theory is that there is a natural honeymoon that is bound to end. And yet we find that in 10 percent of companies, the honeymoon continues throughout a worker's entire career. So there are organizations that are able to maintain enthusiasm.

As a general proposition, it is hard to be enthusiastic about an organization that is not enthusiastic about you. Let's look at a few specific things. One is job security. We expect employees to be enthusiastic, loyal, and engaged in an organization, but with the slightest downturn or prospective downturn, we get rid of them. They are expendable. They are treated like paperclips. How can you be loyal and committed to an organization that seems to have absolutely no concern about your job?

According to one of the trendiest notions so popular during the booming 1990s, job security is not important to people, particularly young people in high tech, because if they lost a job in tech, they could just walk across the street and get another one. But with the collapse of the high-tech companies, surveys found that job security went to the top of the list. Take a high-morale company—Southwest Airlines. After 9/11, it said: "We will take a hit in our stock

price and not lay off anybody." That's putting your money where your mouth is.

Other things that suppress enthusiasm are obstacles to performance, such as insufficient training, poor equipment, or findings that fit under the general heading of "bureaucracy." These include useless paperwork and the inability to get a decision made, or a decision made on time.

Conflicts across the organization are another obstacle. Some of the most negative findings were between IT and their internal customers, the employees. [The two sides] often find themselves in a battle. Conflict between functions is debilitating. People don't come to work to fight.

Out of 28 companies studied by Sirota, the share price of 14 companies—those considered to have high morale—increased an average 16 percent in 2004.

Finally, there is the status structure of companies that treat employees as second-class citizens. Consider, for example, the distinction between hourly and salaried workers, as if two different categories of human beings exist. Salaried are professional, the thinking goes, and hourly are the ones you have to watch out for. There are status symbols, such as the parking lot. At large factories in the Midwest, salaried employees have one set of parking spaces, and God knows how far away the parking lot is for the hourly workers. The high-morale companies have eliminated a lot of this stuff, which has nothing to do with conducting business. All it does is feed the egos of some people at the expense of the self-esteem of the bulk of the workforce.

KNOWLEDGE@WHARTON: *You acknowledge that some employees are "allergic" to work. How should managers deal with them?*

SIROTA: About 5 percent of every workforce is allergic to work. These employees are shirkers. But managers in many companies, especially where there are large numbers of blue-collar workers or back-office operations such as call centers, treat the entire workforce as if it is the 5 percent. They set up rules and punitive

measures for taking too long a rest break, etc. There is close supervision, so people who come in wanting to work, and hoping to take pride in their work, find themselves treated as if they are children or criminals.

About 16 percent of the companies we deal with have a hostile workforce. But the bulk of the problem is not hostility. It is that people have become indifferent. That is the silent killer. There are people who just don't want to work for whatever reason. They become troublemakers, and you have to deal with them in a very tough way. You have to focus on them. But you don't then generalize from them to the rest of the workforce. The mistake we make is we feel we have to be consistent, that we have to have the same rules for everybody. So companies are consistent in treating everybody as a child or a criminal. That's very, very destructive.

KNOWLEDGE@WHARTON: *Workers indicate to you that immediate managers are not the problem. Who is?*

SIROTA: The conventional wisdom is that if there is a problem, it occurs on the front line. Our data shows that large percentages of employees are quite positive about their immediate bosses. The biggest problem is not the first level of supervision. It tends to come from the middle. Workers see the problem at the levels above the immediate manager. They often consider their own bosses as buffers to middle management. Workers say, "I like my boss." Morale goes down when it comes to middle management, then goes up again at the senior level. The top guy can do no wrong. That's a fairly common response. What workers don't realize is that all the pressure is coming from the top. They are the ones telling the middle what to do. The villain is viewed as middle management, but the real villain is senior management.

KNOWLEDGE@WHARTON: *What happens when workers have top managers who are dishonest and greedy?*

SIROTA: The employees at Enron are not only out of a job, but also out of their pensions and IRAs. Yet what we find in the analysis of the data and in focus groups is concern not just about the hanky-panky we have seen in the last 3 or 4 years, but also about cheating the customer. Employees want to be proud of the

quality of the work they and their company do. When I was in the auto industry in the 1970s, the unions and the workers were blamed for poor quality. When we interviewed them, they said they felt terrible about the garbage they were producing. They said all management wanted was to get the cars out the door. Workers have a strong need to feel they have done something and done it well.

KNOWLEDGE@WHARTON: *What can managers do to boost enthusiasm?*

SIROTA: First, provide security. Laying off people should be the last resort, not the first thing you do. Some companies use a ring of defense. If the business is having difficulties, they retrain workers or bring work inside from subcontractors. There are a number of steps you can take before laying people off.

Second, where there are difficulties in getting work done, we talk about self-managed teams. Toyota, which has been an incredibly successful company, is an example. In the 1970s, Toyota wanted to know how to enrich the job of assembly workers and thought about having groups of employees build an entire car. But that would have been so inefficient. Toyota said instead it could have a team of workers manage part of the assembly line. The team could look at quality and at what kind of maintenance and support were needed, and it could decide how to rotate workers. As opposed to the usual top-down management, this approach is tremendously satisfying for workers, reducing the need for bureaucracy because the people essentially are managing themselves.

"We are often asked how to motivate employees," Sirota says. "The real question is: 'How do you keep management from destroying motivation?'"

Recognition is also important. Employees do not have to be told that you love them, but you want to be appreciative of good work. It sounds very corny, but people are corny. People need this kind of feedback. A lot of rewards don't work, including the employee-of-the-month one. Organization-wide awards should be like the Nobel Prize, where peers are involved in the selection of the individuals who receive

the award for outstanding achievement, not day-to-day work. Some things are so basic it's embarrassing to talk about, but in many focus groups, workers—when evaluating management—will say, "He comes in, and he doesn't even say hello to me." That's the kind of comment we get.

As for systems, we find the traditional merit pay systems with an appraisal and pay increase are quite negative. Workers feel no relation between what they do and their pay increase. A reward has to be felt as a reward. Research has verified a system such as 'gain sharing' in which a group of workers judges its performance over time. If productivity goes up 20 percent and the workforce increases 10 percent, then that means there is greater efficiency. That result should be shared with the workers 50 percent and management 50 percent. This has a tremendous impact on productivity and morale.

KNOWLEDGE@WHARTON: *All of these recommendations seem so soft-hearted. Are you ever criticized for being naïve?*

SIROTA: Yes, all the time, mostly by hard-line managers and human resource managers. They are cynical about workers. But there are

managers and CEOs who look at this and really run with it. They tend to be optimists and give people the benefit of the doubt.

KNOWLEDGE@WHARTON: *Given the evidence, why do managers continue to choke off enthusiasm?*

SIROTA: What I think happened is that in the 1980s and 1990s we had a reaction to particular forms of management. We talk about four kinds: First there is paternalism, where workers are treated as children. Then there is adversarial, where workers are the enemy. Then there is transactional, where workers are like ciphers. Management does not know what they are like as individuals. The attitude is, "We paid you, now we are even. We don't owe you anything." That's where most companies have gone today. Loyalty is dead.

The fourth is what we have been talking about, which is the partnership organization. It does not mean that because I paid you, we are now even. You don't treat partners that way because you might need them to help you out sometime, and they might need you. It's more like a relationship between mature adults—not like children or enemies, but allies. ■

More Than Job Demands or Personality, Lack of Organizational Respect Fuels Employee Burnout

WHEN LAKSHMI RAMARAJAN worked for a nonprofit organization several years ago, she noticed a high turnover rate among the employees. It wasn't because of the work itself, but because of the organization's management. "Employees were passionate about their jobs but felt disrespected by their managers," says Ramarajan. "The employees were belittled and patronized and often publicly chastised for challenging the status-quo." Complaints about the negative work environment "were met with inertia or rejected out of hand. Eventually, a lot of employees left."

That experience led to a research paper co-authored by Ramarajan, now a doctoral student in the Wharton Management Department, and Wharton Management Professor Sigal Barsade entitled "What Makes the Job Tough? The Influence of Organizational Respect on Burnout in Human Services."

According to Barsade, "One of the biggest complaints employees have is they are not sufficiently recognized by their organizations for the work that they do. Respect is a component of recognition. When employees don't feel that the organization respects and values them, they tend to experience higher levels of burnout."

Or, as Ramarajan puts it, "it is often not the job that burns you out, but the organization."

A Sense of Identification

While the researchers' paper focuses on the health care industry—specifically on certified nursing assistants (CNAs) in a large, long-term care facility—their findings apply to a broader range of industries and individuals. Barsade, for example, cites a project she did for the real estate, accounting, and legal departments of a large financial services agency. "The people in these departments were known as 'nonproducers.' That wasn't their formal title, but it was what they were called because they were not revenue generators. Not only did they not have as much power as the people who brought in the money," but their contributions



in terms of helping streamline and improve the company's operations were not acknowledged. "This does not suggest a culture of respect," Barsade says.

She also cites physicians allied with HMOs who are often told how many patients they must see each day, how long they can spend with the patients, and what diagnostic questions they must ask. "Doctors can't offer customized care under these circumstances. They feel disrespected and are more prone to burnout" than doctors who work more autonomously, she suggests.

A company's culture—which, for the purposes of the study, is defined as "the unwritten norms and values surrounding how employees are valued as individuals"—plays an important role in burnout, the researchers say. "We know that employees start identifying with an organization as soon as they join it," says Ramarajan. "The more they feel respected as a member of the group, the more likely they are to have that sense of identification. Respect is a way in which employees get entrenched into the workplace and feel that what they do is meaningful. Conversely, if they observe that people around them are disrespected, they come to a consensus that the organization doesn't treat people well."

The researchers cite several ways in which the perception of organizational respect or disrespect can influence employee burnout. For example, “in situations where employees perceive that the organization does not treat employees with respect or dignity, burnout can occur from employee demoralization. Disrespected employees may need to mask their true emotional reaction regarding how their organization treats them while they assist their clients. This masking and suppressing could increase emotional exhaustion, a major component of burnout studied in the human services industry.”

Conversely, the researchers say, “individuals who feel respected by their organizations are more likely to expend effort on behalf of the organization” and are thus less likely to experience burnout.

“Negative Affectivity”

Barsade and Ramarajan were especially interested in health care because many of the lower-level jobs in that industry tend to be difficult and because a lot of research has been done on the industry’s burnout rate, says Barsade. “In the existing literature, there are two factors that have predicted burnout and why it occurs. The first factor is the job itself. The second is the personality of the employees and the presence of ‘negative affectivity’—someone’s propensity to be high energy in their negative emotions, such as anger, irritability, anxiety, or frustration. It’s not that people are always feeling that way but that they are feeling that way more so than people who have less negative affectivity. We focused on those two factors.”

Within health care, Barsade adds, the CNA job was especially interesting because the work is so hard. “There are tough physical components involved in helping patients, such as lifting them, bathing and feeding them, cleaning up after them, and so forth. And there are also emotionally taxing components, such as when the CNA gets attached to a patient who dies, or when patients demand constant attention and care. So what better place to see what impact the organization has on the burnout levels of its employees and what they can do about it?” In addition, she says, burnout can affect the quality of patient care.

One approach an organization can take to try and decrease burnout and reduce turnover is to hire people who aren’t going to be stressed out by the job. That, of course, is not only difficult to predict with complete accuracy but is often not feasible given the labor market supply. Organizations can also try to change the job to make it less demanding; but, at least in the case of CNA positions, the ability to do that is limited because of the nature of the job. A third approach—one not addressed by the existing research on burnout—is to consider the organizational culture of the company, says Barsade. “Can the values of the company—including whether you treat employees with respect or with disrespect—influence how people do their work and whether or not they will feel burned out?” Although burnout can lead to higher turnover costs in any industry, health care is especially interesting because the nature of its work is more likely to result in burnout. “As our country ages, this will become a bigger and bigger issue,” Barsade says.

A company’s culture—the unwritten norms and values surrounding how employees are valued as individuals—plays an important role in burnout, the researchers say.

In conducting their study—which looked at CNAs from 13 units across three sites of a long-term care facility during two different time periods, 2003 and 2005—the researchers measured several aspects of participants’ jobs. Under the heading “organizational respect,” for example, participants were asked to rank how characteristic, or how uncharacteristic, the following five statements were of their organization: “Staff members respect each other;” “Staff members are treated with dignity;” “Cultural diversity of the staff is valued;” “Supervisors pay attention to staff members’ ideas;” and “Staff members are encouraged to be creative when solving problems.” These were the characteristics that a committee of senior managers and employees thought best illustrated how organizational respect would be demonstrated in their organization.

Under the heading of “autonomy,” participants were asked to respond to the following

statements: “In general, how much say or influence do you feel you have in what goes on in your unit?” “Do you feel that you can influence decision making...regarding things about which you are concerned?” “Does your supervisor ask your opinion when a problem comes up which involves your work?”

Under the heading “trait negative affectivity,” employees rated their general tendency to feel irritable, upset, nervous, afraid, and guilty. “Burnout” was measured by participants’ reactions to four statements: “I feel emotionally drained from my work;” “I feel used up at the end of the workday;” “I feel fatigued when I get up in the morning and have to face another day on the job;” and “I feel burned out from my work.”

Among the Study’s Findings

■ Organizational respect influences burnout above and beyond the effects of job demands and negative affectivity. Because existing studies conceptualize burnout as stemming from the job or the individual, rather than the organization, “the ‘problem’ from a managerial perspective is the person,” the authors note. “Succumbing to burnout becomes a private affair of the employee and not something of concern to the organization as a whole... This ignores the contextual sources of the problem.”

Furthermore, the researchers say, “by conceptualizing job demands as a primary cause of emotional exhaustion,” the nature of the work is seen as the culprit, rather than “the multiple sources of an employees’ work experience.” Human services jobs—such as caring for elderly sick patients or working with mentally ill individuals—may be difficult, the researchers add, but the “presumption that the demands are due to client interaction means that very little can be done about changing the negative parts of the experience.” In fact, the researchers suggest, companies can take a number of steps to change the organizational culture.

■ The impact of organizational respect on burnout is felt most strongly when job autonomy is low. This finding confirms the researchers’ hypothesis going into the study about the importance of autonomy, which they define as “the discretion that one has to determine the processes and schedules involved in completing a task.” Autonomy,

the researchers note, can act as a buffer on stress—and actually decrease job burnout—if autonomy is high, but not if it is low.

■ The respect with which an organization treats its employees “is a pervasive organizational-level phenomenon that employees can recognize and agree upon,” the researchers note.

By conceptualizing job demands as a primary cause of emotional exhaustion, the nature of the work is seen as the culprit, rather than the multiple sources of an employees’ work experience.

In addition, “respect can be a powerful signal to individuals regarding their standing not only as employees but as people... As information comes from a variety of sources, one’s perceptions of respect and disrespect are not only based on how one views one’s own treatment but also by how others are treated. For example, when team members see someone else on the team being treated unfairly, they alter their own perceptions of the fairness of the team. Likewise, the extent to which others, not just the self, are treated...can influence an individual’s own perceptions of respect.”

Ramarajan and Barsade carry this point further: Given the increasing importance of health care providers in aging societies, one aspect of burnout is especially crucial—the phenomenon of human services workers mentally “turning over” but remaining physically present. “In our study, we found that being a longer-tenured employee was significantly correlated with higher burnout. From a managerial perspective, withdrawal behaviors are perhaps more important to human services organizations than turnover because withdrawal may be the response taken by employees who do not have high-quality job alternatives,” they write.

In the worst-case scenario, the researchers add, “disrespectful organizations can be left with neglected and neglectful individuals who have figured out how to cope or survive by mentally turning over, while those with better job alternatives—or more commitment to their professions rather than the organization—end up leaving.”

Putting Work in a Broader Context

The authors' research has a number of implications for managers. While it is likely, the authors note, "that disrespect is experienced across industries, disrespect for individuals may be particularly problematic in the helping professions where concern for individuals is supposedly paramount." Because it is not just the demands of the job, or the personality of the employee, that drive burnout in human services jobs, but is also the organizational environment, "then there is a point of entry for human resource management. Good versus poor management, in the form of organizational respect, may therefore have a clear and critical role in stemming burnout in human service organizations."

For example, Barsade suggests that HR departments make it clear they respect and value the work employees do and recognize the difficulty of that work. "Employees understand that internally their work is very significant to how well the organization achieves its goals." Companies like Mary Kay, Inc., are based on the idea of "rewarding people to success," she says. "Mary Kay rewards for everything. It uses respect as a powerful motivator for its sales force of independent contractors."

Employers can also highlight to their employees how important their work is to society as a whole, Barsade adds. "Very often, caretaking

work is not all that valued, but if employees in a daycare center, for example, understand that they are involved in early childhood education," this puts their work in a broader context. In addition, she suggests that for people in jobs that don't pay very well (and won't in the future), managers can at least compliment employees, hold awards dinners, and so forth, "just so long as these shows of respect are authentic."

This doesn't mean that managers "can't look at employees' performance or can't disagree with suggestions and demands that employees might put forward," Ramarajan adds. "It just means that everything is done with an attitude of respect." This approach won't just make employees feel better. "It will help them stay with the organization and do a better job. So it's not just about keeping your employees happy but actually doing the job the organization exists to do."

Does Ramarajan think employees would be surprised to learn that job burnout is not always "their fault," but can also reflect the way the organization treats them? "I don't think employees would be surprised, but I do think managers and/or corporate executives might be. And I think employees would be surprised to find out how widely shared this experience is." ■

Older Workers: Untapped Assets for Creating Value

THE DAYS WHEN AN EXECUTIVE could look forward to a leisurely retirement out on the golf course are over, thanks to a possible looming job shortage, low savings rates, and an insecure Social Security system. The impact of these factors on both workers and companies was the subject of the Symposium on Older Workers, co-sponsored recently by the AARP Global Aging Program along with Wharton's Center for Human Resources and Boettner Center for Pensions and Retirement Research. Speakers included AARP CEO William D. Novelli; Olivia Mitchell, executive director of Wharton's Pension Research Council; and Thomas Dowd, a deputy assistant secretary at the U.S. Department of Labor.

In his keynote address to the symposium, Novelli argued that recent shifts in the demographic makeup of the workforce—including, for example, the fact that by the year 2010, 20 percent of the workforce will be over age 55—represent a tremendous opportunity for the business community because of the collective knowledge and experience offered by this group of older workers—if only companies are able to adjust their concept of what older workers can learn and accomplish later in their careers. “In many businesses, people in their late 50s are considered at the top of their game, ripe for the best assignments, ready for the corner office,” Novelli said. “I seriously wonder about the value of involuntary retirement in any field, except perhaps those that require strenuous physical performance.”

The Graying of the Workforce

There is no doubt that the composition of the workforce is skewing older, as the baby boom generation rapidly approaches the “traditional” retirement age of 65—but the meaning of that milestone is shifting just as quickly, said Novelli. “Today, less than 2 percent of American workers are in agriculture, and manufacturing employs only about 13 percent of American workers,” he noted, adding that as the economy has shifted away from hard, physical labor and



agriculture, “brains and learned skills have dominated, if not completely replaced, brawn and endurance.” The result? A move to the knowledge economy, to which older workers with their added experience and wisdom are ideally suited and which increasingly makes the notion of a set “retirement age” obsolete. “Since work has changed, our ideas about workers must change accordingly,” Novelli said.

This demographic shift that Novelli described is more than just theoretical. According to the Census Bureau, between 1998 and 2000 the number of workers between the ages of 65 and 74 increased by one-seventh, to nearly four million. In 2002, the total workforce in the U.S. increased in size by 720,000 workers, and workers over the age of 55 accounted for nearly all of that increase. And according to the Bureau of Labor Statistics, by the end of the current decade 20 percent of the workforce will be over 55.

Some argue that it is less a case of demographics and more a case of older employees working later into life due to poor savings rates and the realization by boomers that they simply can't afford to retire. But Novelli emphasized that regardless of its cause, the graying workforce is a reality. In

recognition of more Americans extending their working lives, the Social Security Administration responded by raising the age of full benefits to 67 from 65. Novelli called on corporations to similarly adjust their notions of the work that older workers are capable of performing.

He outlined a “10-year social impact plan” aimed at altering the way companies view, re-train, and compensate their older workers. Broadly, Novelli’s plan seeks to reduce age discrimination in the workplace, encourage employers to adopt human resources policies with multiple options to meet the needs of older workers, and aid workers in remaining on the job or returning to the workforce by offering them more learning opportunities.

Novelli argued that these goals can be reached through, for example, the provision of part-time or alternative work schedules to allow older workers more flexibility in their work life as they age. “We are learning that work after retirement age can take new, more interesting or less stressful forms,” he said. This can mean shifting to part-time or flex-schedule work at an existing job or undertaking a career shift and moving to a job that is less demanding. For example, Novelli highlighted a joint project that the AARP sponsors along with Home Depot to train older workers for employment in Home Depot stores.

By the year 2010, 20 percent of the work-force will be over age 55.

Novelli also suggested that companies provide technology training courses tailored to older workers’ skill gaps in order to keep them current with new equipment: “Older workers can learn new things, although it appears that they do not learn them via the same training approaches as are applied to younger employees,” he said. Companies that allow older workers to learn at their own pace, or to take alternative classes from those offered to younger employees, would reap the rewards of a better-trained and higher-performing older cohort on staff, he said.

Most simply, however, Novelli stressed the alteration of the public perception that must take place—changing the expectation that reaching a certain age must equal “retirement” or idleness. “We should promote the idea to

employers that turning away older workers is a waste of human capital. We will gain ground as employers realize that discrimination is wrong, not just for legal or moral reasons, but for business reasons as well.”

Changing Universe of Benefits

When Professor Olivia Mitchell suggested to the symposium that they “just don’t get old, don’t get sick, don’t retire...and you’ll be fine,” she had everyone’s attention. Mitchell, executive director of Wharton’s Pension Research Council and director of the school’s Boettner Center for Pensions and Retirement Research, talked about benefit plans for older employees and the restrictions in store for these plans as the workforce ages.

Once known as “fringe benefits,” employer-provided benefits include health insurance, life and disability insurance, paid time off, and pensions and medical benefits for retired former employees. As Mitchell explained, however, these benefits are now far from “fringe.” “In the U.S. and other countries, employers are the nexus for the whole insurance picture—healthcare and pensions, specifically.” In the U.S., the cost of providing these benefits to employees now amounts to nearly 30 percent of companies’ labor costs.

Some of this cost is due to legally required benefits, including the taxes paid by corporations to cover workers’ compensation and unemployment insurance, as well as Social Security and Medicare taxes. But the lion’s share of the tab is filled by voluntarily provided benefits, which come to 20 percent of total payroll costs, said Mitchell. As of now, and despite dramatic cost increases, nearly all companies continue to offer these voluntary benefits: 76 percent of employees were offered health insurance by their employers in 1987; 74 percent were provided coverage in 2001. As the workforce ages, the cost of providing health coverage in particular is expected to rise sharply.

Since these benefits are “voluntarily provided,” companies are under no legal pressure to continue offering them, but they have certainly become a social expectation, said Mitchell. In fact, because providing health insurance to groups of people (which spreads the risk for the insurer) is so much less expensive than providing coverage to individuals, it is often

very difficult for individuals to obtain insurance coverage if it is not through their employers. As a result, rather than discontinue benefits as costs rise, companies are instead passing more of these costs along to their employees.

Why Provide Benefits, Anyway?

As Mitchell pointed out, 100 years ago, the American economy was primarily agricultural, with most workers self-employed or working in family-run farms or businesses. There were few wage-based jobs and therefore, few “benefits” in the sense that we know them now. This employment picture began to change following World War II with the “golden age” of benefits emerging from the 1950s through the mid-1980s as the economy shifted to industrial and urban wage-based jobs. “Initially, the effort focused mainly on protecting workers against income loss in the event of workplace accident and illness—which led to insurance coverage for disability and premature death,” Mitchell explained. Later, pension programs were added.

The benefits “menu” approach allows employees a high degree of choice—but Wharton’s Olivia Mitchell says choice isn’t necessarily all it’s cracked up to be.

Companies were able to provide these benefits at a relatively low cost; they received significant tax breaks for doing so, and economies of scale allowed them to receive a cost break for pooling their employees into a lower-risk group for insurance coverage. “It was also a big part of attracting top candidates, part of an overall attract-retain-motivate strategy,” Mitchell said. “Then, on the other end, defined benefit pensions were retirement inducing. They were in place to get you to leave when you were past your prime.”

A lot has happened since the corporate benefits system first emerged, and the changes continue to advance more rapidly now than ever. First, few people today stay at one job for anywhere near as long as they did in the previous generation. “There are no 20-, 30- or 40-year careers anymore,” Mitchell said, which means that traditional pension benefits do not carry the same incentive value as in years past. Instead,

“employees want benefits that can be tailored to their needs and their lifestyles at the particular point in time that they are with a company.”

These changes have translated to a demand from employees of all ages for flexible spending options for health insurance and medical care, as well as a move towards defined contribution pension plans—such as 401(k)s—over the traditional defined benefit plans of earlier years. Added to these shifts is the reality of the graying workforce, which has greater need for medical care, and simultaneous increases in healthcare costs generally, which have combined to make the provision of benefits to employees an extremely expensive proposition for employers.

To address the realities of providing benefits to a changed workforce, companies have shifted to what Mitchell calls a “disintermediated” benefits system, or an “a la carte” menu of benefits from which employees choose and are then partially charged for their participation. In practice, this means that companies no longer select a one-size-fits-all healthcare program, but rather provide several insurance options to employees for health insurance, dental insurance, even vision and prescription coverage. Employees choose what level and type of coverage they would like—or may opt not to participate at all. Similarly, rather than enrolling everyone in the same pension program that pays out a set amount at retirement (defined benefit), companies now provide programs such as 401(k)s for which employees must choose to enroll, then choose how much of their earnings to contribute (defined contribution pension plans), then also choose what funds to invest their retirement savings in.

Even though the menu approach has for the most part been welcomed—even demanded—by employees, Mitchell noted that as the cost of healthcare options rise, participation rates have dropped: “89 percent of employees who were offered healthcare coverage took it in 1987, but the figure dropped to 82 percent by 2001.” And the same effects can be seen in the pension programs: Rather than 100-percent employee enrollment in traditional defined benefit pension programs, Mitchell said that in 1987, only 38 percent elected to contribute to their voluntary retirement funds, and in 2001 that number had risen to just 43 percent.

The menu approach allows employees a high degree of “choice” in what their benefits package actually looks like. But according to Mitchell, “choice” isn’t necessarily all it’s cracked up to be. Many employees, overwhelmed by the financial choices available in their pension funds, for example, are “overinvested in their own employers’ stock, despite several high-profile flameouts that we have seen over the last few years,” simply because it’s easiest for them to choose to invest their pension monies in their own company’s stock. “Menu construction seriously affects choices as well,” she added. “Most people focus on the top of a list of fund choices and stop reading after the first three or four. They are not choosing the best options; they are just overwhelmed by how much choice there is.”

In addition, many people simply aren’t saving enough to ever cover their costs in retirement. And others have opted out altogether, completely paralyzed by the overwhelming number of choices presented to them. “Employees have to answer: Do I want a particular benefit? Which one do I want? How much will it cost? How much do I need to spend on a benefit such as this? How do I annuitize this spending?” said Mitchell, who recently edited a book entitled, *Benefits for the Future Workplace*. “All of these are complicated questions—and they are a lot to ask from people” who generally are not sophisticated when it comes to making investment decisions.

So, What Next?

According to Mitchell, as the current crop of near-retirees age, they will be faced with the cumulative effect of these challenges to their benefits picture. Most have not saved nearly enough, or their savings have been hit by the recent fluctuations in the financial markets. They will likely not have healthcare provided in retirement by their former employers, and healthcare costs will only continue to rise. Those “lucky” enough to still be recipients of defined benefit pensions may be surprised when they discover how underfunded most corporate pension funds are. For example, “the unfunded portion of DuPont’s pension program is equal to the company’s global assets,” Mitchell said. And Social Security certainly won’t be the answer, either. “Social Security benefits payouts are dramatically increasing because of the baby

boomers aging. By 2018 the system will be taking in less in tax contributions than it will be paying out,” she added.

The result? Mitchell predicts, as conference attendees heard from nearly every other speaker at the symposium, that baby boomers will need to remain in the workforce far longer than employees in the last generation, and much longer than they themselves may have anticipated. She returned to her earlier comment: “Like I said, just don’t get old, don’t get sick, don’t retire...and you’ll be fine.” Still, Mitchell did offer some advice for future generations of employers and employees. “We need to financially educate our citizens more and earlier, outside of the company-based benefits environment, because companies will not be the nexus of benefits and pensions in the future. Clearly, this is not a good model going forward. As it changes, people will need to consult financial professionals more and will need to understand the financial choices they are faced with in order to operate in this complex environment.”

Looming Retirements, Across the Board

To close the symposium, Thomas Dowd, deputy assistant secretary, employment and training administration, at the U.S. Department of Labor, discussed how the country and the labor force are entering a period of unprecedented change. For example, more than 25 percent of all U.S. Postal Service workers who were employed in 1998 will be retired by 2008, he said, arguing that figures like that are representative of what we will see across many industries in the years to come: “Most of our clergy will be pensioned off, the federal workforce will be drastically cut, and the demand for skilled workers will outpace supply.” To further complicate matters, Dowd pointed to scientific projections that “people aged 65 today will live to an average age of 83, which is significantly longer than in generations past.”

Dowd said a new perspective on what older members of society can bring to the workplace is required. “We must change the mindset we have about older workers. Don’t put an age category on who’s eligible to work. Older workers bring knowledge, experience, and wisdom—something that is not taught in schools.” According to Dowd, knowledge workers now comprise about two-thirds of the labor force, outpacing factory

workers by a ratio of two to one. To ignore the knowledge and wisdom offered by older workers is to leave American companies in the lurch, in need of skilled employees without being able to find them. This is one reason, he added, why so many companies are offshoring jobs. “When companies don’t find the talent needed, they seek it abroad. We must recognize that we are in global competition for workers.”

Finding Creative Workforce Solutions

Dowd said the current administration has invested \$15 billion each year in workforce development programs under the umbrella name of the “Public Workforce System.” “It’s not a social service system; it’s an economic development system—a system that creates opportunities for future, ongoing growth.”

Included in this rubric were such programs as the High Growth Job Training Initiative, which identifies industries with a high demand for workers and provides funding to train workers in those fields. Relevant industries include healthcare, biotechnology, geo-space, hospitality, and retail. “Solutions focused on older workers are important. We call it ‘E3’—employment, education, and economic development—which together form a strategy to use this untapped labor pool. We need every available, willing individual to work, and we must equip him or her with the skills necessary to do it,” Dowd said. He highlighted the job retraining efforts underway at the Forsythe Technical Community College in Winston-Salem, NC, which is currently helping workers at all age levels transition to working in the biotechnology industry, as an example of one such successful initiative.

During the question-and-answer period, Dowd took questions regarding what programs the government has developed to allocate training dollars specifically for older workers. Many government training programs are youth oriented, the questioner said, and many don’t specify a target group at all. “We have one specific program for older workers, the Senior Community Service Employment Program,” answered Dowd. The program is contracted to the AARP Foundation to run employment placement for seniors who fall below the federal poverty line. These seniors are placed in nonprofit community organizations and are provided whatever training they require to

perform their new jobs. “Our other programs, minus the youth-specific programs, serve all age segments,” Dowd said.

Another audience member asked Dowd about the rising healthcare costs facing older workers, especially since many seniors end up taking temporary employment or seasonal positions that do not offer health benefits. “As big corporations move towards employing millions of temp workers with no benefits, where does the government stand on providing a gradual subsidizing of healthcare costs?” she asked. Dowd replied that the issue did not fall under his department’s jurisdiction.

Dowd was also asked whether the government has plans to support more model programs that demonstrate how to reintegrate older workers into the labor force in both the public and private sectors, citing the National Older Worker Career Center as an example. He responded that although proposals for such programs exist in the 2005 fiscal year budget, he was unable to disclose them to the audience. “We fund demonstrations of best practices all the time,” Dowd added, “but I have yet to see anyone doing any of them after the demonstrations. It seems like it’s more for getting conference speaking opportunities. We should be going out and finding great practices that are already in use and funding those instead.”

At one point, Wharton Professor Peter Cappelli, director of the school’s Center for Human Resources, challenged Dowd’s premise that there would indeed be a labor shortage at all. Noting that there is still upwards of 5 percent unemployment in the United States today, Cappelli asked Dowd, “How can we have a shortage of workers if there is unemployment? It’s impossible.” Dowd replied, “The fact of the matter is, even if we have some unemployment, we still need to train people; we still need their skills to sync up with the skills that are in demand.”

And bringing the conversation full circle, back to the subject of the aging labor force, Dowd added, “The important thing to remember is that we need to recalibrate our notion of ‘Best By’ dates for American workers. Age is only an indicator of years spent acquiring and developing human capital assets—not a date at which you must retire.” ■

The Human Side of Mergers: Those Laid Off and Those Left Aboard

THE INITIAL HEADLINES announcing mega-corporate mergers and acquisitions typically focus on Wall Street's appreciation for improved finances, less duplication of services and staff, the ability to grow a company faster, and the anticipation of higher returns for shareholders when the two companies merge into one.

But what about low morale and decreased productivity among the rank-and-file, a by-product of many corporate mergers that attempt to slam together two diverse corporate cultures? Or the impact on employees who lose their jobs, and the employees left behind after layoffs are announced? How will these so-called survivors deal with the loss of institutional knowledge, increased workloads, and a sense of uncertainty about their own futures?

The story of what happens to the rank-and-file employees after these corporate weddings is rarely headline-grabbing news. When Procter & Gamble announced in January 2005 that it would buy Gillette for \$57 billion, the fact that 6,000 people would lose their jobs was all but buried in the details of a deal that would link some of the world's most well-known household brands.

The reasons why, many say, are simple. "The investment community focuses on costs. They generally always like the idea that you can cut workers" and save money when mergers and acquisitions are announced, says Peter Cappelli, director of Wharton's Center for Human Resources. "But it's difficult for them to factor in the associated costs of layoffs, declining morale, and the chaos" that comes from restructuring. Because the investment community can't easily measure these costs, "they don't factor them in, and that's one reason why mergers rarely work out."

Also, mergers of large corporations rarely consider the effects of layoffs on local communities because "they are such a small part of the overall global economy, and their effect on it is tiny," says Cappelli. Corporate boards used "to care about the local economy,



but the change in governance of corporations means that they focus primarily on the concerns of the shareholders." When it comes to the well-being of the employees, he says, "they don't care."

Perhaps they should. Mergers that result in layoffs can be a "devastating experience, both psychologically and physically" for those who lose their jobs, says Sigal Barsade, a professor of management. People who are fired or laid off often get sick and develop stress-based illnesses. Recent studies have even shown that "being laid off and then rehired is associated with more work-related injuries and days off than just receiving a warning notice or, of course, not being laid off at all. So even if you rehire employees, there can be damage."

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Furthermore, says Cappelli, companies typically "don't pay attention" to the potential loss of institutional knowledge when there are layoffs. Why? Because on paper, the merger of two corporations means "an opportunity for some companies to increase their quality of talent—two people for every position—so they pick the best one. But the process through which

this happens is messy. Some companies that do this are good at it—particularly when they are making small acquisitions, for example, or acquiring smaller companies. But when big mergers are involved, I think they are just as bad at it” as the others.

Management Professor Nancy P. Rothbard points out that institutional knowledge can “have two meanings. One is the idea of skills and knowledge of information that is relevant. But another is the knowledge of the way things are done in the company. Often, that changes with the merger. It’s not clear, but sometimes retaining the people who are wedded to the old ways might be problematic if they are not able to adapt. It might become a hindrance if it creates a barrier to change.”

Another way to look at institutional knowledge is to view its retention as a competitive advantage, says John Paul MacDuffie, co-director of Wharton’s Reginald H. Jones Center for Management Policy, Strategy, and Organization. “Companies that pay attention to these human factors, who retain and keep the right people and do it better than other companies have a competitive advantage, not just on the deal-making side, but the human resources, merging-of-cultures side. And it’s not as common as you would think.”

Violating a Psychological Contract

Companies should pay attention to how they treat the people who are leaving for several reasons: namely, the survivors, the people who are left behind to keep the show going. Both Barsade and Rothbard agree that one of the key factors in predicting how corporate survivors and those who get laid off respond is each individual’s perception of “procedural justice.”

“Were fair standards and clear guidelines applied? Or were the layoffs done in an unfair or ambiguous manner?” asks Rothbard. “It’s usually important for the company to use consistency and clarity (in making the announcements) and explain what the criteria are for the people who are losing their jobs.” What the literature has found, adds Barsade, “is that the best way to help survivors get through this period—as well as help the people who are laid off—is if there is the perception of procedural justice. Is the layoff process fair and transparent and recognized as such?”

MacDuffie suggests that employees respond better to layoffs if the process “does not violate the sense of a psychological contract” between the employee and the company. It’s important that the employer turned to layoffs as a “last resort, not a first resort. If mismanagement from the top causes the layoffs, then obviously it is going to produce a very different feeling. If there is a scenario where managers imperiled the employment of a lot of people who placed their trust and faith and retirement savings with them, that has a different feeling too.”

A way to look at institutional knowledge is to view its retention as a competitive advantage, says Wharton’s John Paul MacDuffie.

The P&G and Gillette merger, MacDuffie says, “is two successful companies coming together, a merger that is trying to take advantage of economies of scale and better use of distribution networks, that is going to end up with redundancies and layoffs. But if the growth prospects overall are high, people may take a relatively positive feeling into the merger. If they are not in a place where the redundancies are, their jobs will be safe, and prospects for the company’s future are enhanced.”

For those who “survive” and keep their jobs after a restructuring, the results can vary. For instance, people who are resilient by nature tend to do better, and if survivors are surrounded by positive, resilient people, everyone tends to perform better. Both survivors and those who lost their jobs tend to go through a natural phase of grieving—similar to the steps of grieving that occur after a death, as outlined by author and physician Elizabeth Kubler-Ross, says Barsade. “They are mourning the loss of friends, the loss of the organization. Once you have undergone a layoff, it jolts you. It is a feeling of betrayal. And you have to manage that.”

How? “If you are a line manager, your ability to bring in a therapist for everyone is extremely low. So you have to let people vent, you have to let them be angry... Many managers feel uncomfortable dealing with sadness, fear, and anxiety—and they are feeling it themselves, too.” More often than not, the situation is

particularly “sticky for middle managers—who didn’t decide that this (layoffs) should happen but are in the position where they have to carry it out for the organization.”

The Push for “Employability”

Mergers and acquisitions offer another challenge—keeping the survivors who are “acquired” and clearly bring value to the new company. MacDuffie notes that companies that do this successfully “work hard to communicate to the employees that they match the new company values and culture. They put a lot of careful attention into the human factors that would make them inclined to stay”—factors ranging from e-mail availability on the first day of work to future stock options. Otherwise, talented employees “are primed to be picked off by other firms” after a merger.

The ubiquitous nature of layoffs and the changing perspective on employment may also play a role in how people respond to mergers and acquisitions that result in layoffs. “I don’t think there is ever a way to be comfortable with (layoffs), because it introduces an element of risk to anyone’s employment,” says MacDuffie. “But the fact that it’s more common today means that there’s no stigma to being laid off. You are not as likely to see it as your fault. It’s the result of organizational change. The new word is ‘restructuring.’ It’s a fact of life in our economy.” Cappelli agrees. When it comes to layoffs, “there is a clear message that it’s not about individual performance, particularly with mergers and acquisitions, when it’s due to duplication of jobs.”

MacDuffie admits that young workers today are much more reluctant to embrace a job for life and have adapted to today’s push for what many call “employability.” “Companies today offer employees ‘employability’—which means that ‘we promise you wonderful training and experiences, so even if we have to lay you off, you could sail out and get a new job.’” Though he knows it exists, MacDuffie questions many aspects of this changing employment contract. “Will people adjust to a new reality and be willing to take the view that, ‘Oh, I’m here to get skills; I’ll have many more jobs in my lifetime?’ Will that actually prevail, or will the reaction be cynicism, mistrust, withdrawal of effort and

commitment, a lot of things that are negative for the company and the individuals involved?”

MacDuffie points to a recent survey of American workers aged 18 and over that shows that only 45 percent of workers say they are satisfied with their jobs; only 20 percent feel very passionate about their jobs; less than 15 percent feel strongly energized by their work; and only 31 percent believe that their employer inspires the best in them. The “New Employer/Employee Equation Survey”—conducted by Harris Interactive, Inc., for Age Wave, an independent think tank, and The Concours Group, a global consultancy advising senior executives—points to a somewhat ironic consequence of the so-called “employability” model for workers.

“If you begin to embrace the notion of employability, you are getting less commitment,” MacDuffie says. “I’m not sure why. One view is that people are very committed to the job they are doing, to the projects that they are on, but they are not caught up in loyalty to the company. Maybe this is an acceptable loss. But the other view is that people are not just less committed, but they are cynical, they are suspicious, they are always kind of calculating ‘What is in it for me?’”

The importance of taking the human factor into account, however, may be slowly gaining respect in the world of corporate mergers, for one simple reason: When these multibillion-dollar adventures begin to fail—and statistics show that at least half of them do—the accusatory fingers begin to point to the possibility that layoffs are not as successful a strategy for organizational change and increased performance as previously thought. MacDuffie suspects that in time, the typical Wall Street “old knee-jerk response—‘Oh there are layoffs, let’s raise the stock price’—may be replaced by the need for more assessment.” Layoffs or restructurings that are announced in the absence of any articulated plan for the future might actually bring the stock price down, he says. ■