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LOOKING AT HRM THROUGH THE LENS OF AGENCY THEORY – ARE SUBOPTIMAL HRM PRACTICES A CONSEQUENCE OF MORAL HAZARD?

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Abstract

The aim of the paper is to provide theoretical evidence that agency problems do exist and could cause under-performance in the HRM area, but as well to systematize and elaborate HRM control systems which reduce agents' moral hazard in general, and especially when making HRM decisions. A substantial quantity of the literature indirectly connected to the field, as focused literature on the agency theory implications for HRM so far is scarce, is analysed. The organisation of the existing knowledge in the following areas is provided: (1) introduction to agency problem and moral hazard, (2) agency problems related to managing employees, (3) HRM control mechanisms for managing agents, and (4) HRM control mechanisms for reducing agents' suboptimal HRM decisions.

Keywords*: human resource management (HRM), agency theory, agency problem, moral hazard, HRM decisions, HRM control mechanisms*

1. INTRODUCTION

Agency theory has been used by scholars mostly in corporate governance, economics, and finance (Eisenhardt, 1989; Gomez-Mejia & Balkin, 1992; Lan & Heracleous, 2010), but as well in accounting, marketing, organizational behaviour, human resource management (HRM), family business, political science, and sociology (Caza, 2011; De Kok, Uhlaner & Thurik, 2006; Eisenhardt, 1989). Although it has been recognized as a potentially valuable perspective for HRM research, it has received little attention in the strategic HRM literature (Caza, 2011; Krausert, 2014). Moreover, the agency theory has been criticized because its overly simplistic assumptions do not reflect the real-world business environment, and because empirical research has failed to support its basic tenets (Miles, 2012), but it was found to support HRM-related practices in contemporary organizations (Welbourne & Cry, 1996).

Nevertheless, HRM studies were predominantly focused on agency theory implications related to agents' compensation (remuneration schemes, incentives and stock sharing). Only sporadic studies dealing with other HRM issues concerning agents can be found, such as selection (e.g. Yu & To, 2011) or subsidiary staffing (e.g. Gong, 2003; Harvey, Speier & Novecevic, 2001).

However, agency problems related to HRM are not only those considering agents. Principal-agent issues facing firms occur as well when agents do not encourage or adopt best HRM practices, despite the fact that proficient HRM practices contribute to organizational performance by improving productivity, financial performance, social outcomes, and reducing turnover (Arthur, 1994; Collins & Clark, 2003; Huselid, 1995; Ichniowski, Shaw & Prennushi, 1997), which is obviously a first principals' goal.

HRM decisions that serve managers' own interests and not the interest of the principal are many. Some agents are not excited about implementing high performance HRM practices, as those practices require considerable budgets but impact the company performance only in the long run. Agents could as well be interested in securing private benefits though employing people from their personal social networks instead of best candidates, or in recruiting unproductive subordinates to protect their positions and career prospects. As well, in order to favour their devotees, many demonstrate favouritism in performance evaluation or promotion decisions, as well as non-transparency when rewarding and deciding on additional training and development (T&D).

The aim of the paper is to provide theoretical evidence that agency problems do exist and could cause under-performance in the HRM area, but as well to systematize and elaborate HRM control systems which reduce agents' moral hazard in general, and especially when making HRM decisions. A substantial quantity of the literature indirectly connected to the field, as focused literature on the agency theory implications for HRM so far is scarce, is analysed. In the following sections the organisation of the existing knowledge in the following areas is provided: (1) introduction to agency problem and moral hazard, (2) agency problems related to managing employees, (3) HRM control mechanisms for managing agents, (4) HRM control mechanisms for reducing agents' suboptimal HRM decisions.

2. INTRODUCTION TO AGENCY PROBLEM AND MORAL HAZARD

Agency theory assumes that the principal/owner employs the agent/manager to perform some service on behalf of the principal (Jensen & Meckling, 1976), under a contract determining compensation for achieving desired outcomes (Miles, 2012). The principal delegates work to the agent (Eisenhardt, 1989), as the agent possesses specialized knowledge and skills (Gomez-Mejia & Balkin, 1992), with the interest that the agent will perform in a manner that maximizes stockholder wealth and satisfaction (Harrell-Cook & Ferris, 1997).

However, managers of other people's money cannot be expected to watch over it with the same zeal as the owner (Smith, 1776/1952 as cited in Miles, 2012). So, if both parties to the relationship are utility maximizers, there is good reason to believe that the agent will not always act in the best interests of the principal (Jensen & Meckling, 1976). It is assumed that the agent is opportunistic and pursues personal interests which are highly unlikely to be identical, and are even typically not fully compatible with those of the principal (Ellis & Johnson, 1993; Harrell-Cook & Ferris, 1997). The divergence between agents' and principals' interests, goals and risk preferences arises conflicts (Eisenhardt, 1989; Miles, 2012; Yu & To,

2011) and potential mischief (Dalton, Hitt, Cert & Dalton, 2008; Lan & Heracleous, 2010) – so-called agency problem, as well as necessary expenditures to overcome it – so-called agency costs (Jensen & Meckling, 1976; Pereira & Esperança, 2015).

The **agency problem** arises because (a) the principal and the agent have different goals and (b) the principal cannot determine if the agent has behaved appropriately (Eisenhardt, 1989). Concerning the latter, as the principal tends to have imperfect information with which to evaluate the agent, the information asymmetry exists (Miles, 2012; Yu & To, 2011). In other words, the agent has more information than the principal about his characteristics and the decisions and actions he pursues, and it becomes convenient for him to act in his own interests at the expense of the shareholders (Fama & Jensen, 1983 as cited in Supangco, 2006).

Agency costs come from many sources, from agents' recruitment and adverse selection costs, through costs associated with regulating and monitoring agents, to self-serving motivations costs – so-called moral hazard costs. A **moral hazard** exists when the agent takes undue advantage of the entrusted authority, and incurs undesirable costs for the principal (Harrell-Cook & Ferris, 1997). By making decisions deviating from the firm's best interest, managers secure private benefits for themselves. Self-serving behaviours which arise as a consequence of agency problem are, for example, using work time and organizational resources for personal gains, perquisites, earnings manipulations, shirking/laziness, favouritism, pet projects, professional status related to empire building, side deals, corporate riding, stealing, but as well greenmail, golden parachutes and managerial myopia (Chng, Rodgers, Shih & Song, 2012; Eisenhardt, 1989; Eisenhardt, 2009; Gomez-Mejia & Balkin, 1992; Shapiro, 2005 as cited in Miles, 2012; Pereira & Esperança, 2015; Ponzo & Scoppa, 2010; Shleifer & Vishny, 1997).

All those consequence of managerial discretion reduce performance (Caza, 2011). Therefore, in order to align agents' interest with those of the principals, and reduce agency costs, different mechanisms are put in place to manage agents' behavior. As agency theory assumes that everyone is naturally inclined to perform detrimental behaviors at work and will therefore behave opportunistically if given the chance (Kidder, 2005), it is vital to establish mechanisms which discipline agents who abuse their agency roles.

3. AGENCY PROBLEMS RELATED TO MANAGING EMPLOYEES

Although human capital is considered to represent the only sustainable source of competitive advantage (Hamel & Prahalad, 1994; Pfeffer, 1994), and therefore investment in these resources should be a strategic competitive priority (Harrell-Cook & Ferris, 1997), the adoption of effective HRM systems is oftentimes hindered by short-term performance pressures and private benefits of managers (Krausert, 2014).

The evidence suggests that although high performance HRM practices increase financial performance through increased human resources productivity (Mitchell, Obeidat & Bray, 2013), they incur considerable implementation costs, while the manifestation of benefits lags behind their implementation for years (Krausert, 2014). Therefore, even if an agent believes that human capital investment improves

long-term value for the above reasons, he/she may still under-invest in it, because

the results are intangible and difficult for the market to verify in the short-term (Edmans, 2008).

Namely, the only immediately-observable effect from such an investment is reduced earnings, and since low profits may signal that the firm is of poor quality, its stock price may fall (Edmans, 2008). Fearing such a decline, managers whose pay and reputation are tied to the stock price may choose to forgo such investment (Edmans, 2008), supporting claims of 'managerial myopia' – sacrificing of investments required to sustain performance in the longer term in order to bolster near-term performance (Krausert, 2014). More to it, risk-aversion on the part of the agent and a bias toward short-term efficiency could be created by short-term performance pressures (Hoskisson & Hitt, 1994 as cited in Harrell-Cook & Ferris, 1997; Krausert, 2014). Therefore, given the vulnerability of agents' positions and the competition for top management jobs, managers realize it is to their advantage to maintain an outstanding track record of profitability (Borcherding, 1978 as cited in Harrell-Cook & Ferris, 1997). This shift in perspective may result in reduced management support (Krausert, 2014), and decreased investment in activities that contribute to long-term organizational welfare (Harrell-Cook & Ferris, 1997), such as high performance HRM systems.

Finally, the non-adoption of high performance HRM practices could be entailed by private agent's costs, as its implementation requires changes in behavioral routines and power relations (Krausert, 2014). Among other, high performance HRM practices hinder favoritism, the second major moral hazard related to managing employees.

3.2. Favouritism

Favouritism, as a preferential treatment of an employee on the basis of factors that do not directly relate to a person's ability to perform his or her job function (Tyler, 2012), such as person's background/ideology or social/family connections with the agent, leads to substantial agency costs as it was found to be a morale killer and detrimental for the firm's overall performance (Bandiera, Barankay & Rasul, 2009; Tyler, 2012). In the same time, it generates value for those who exercise it (Prendergast & Topel, 1996). As such, supervisors derive utility from exercising bias when making decisions on selection, performance appraisal, remuneration, promotion, etc.

Favouritism in recruitment is a form of moral hazard in an agency framework in which a manager obtains private benefits by hiring connected people of lower abilities (Ponzo & Scoppa, 2010). Relatives, friends and individuals belonging to "old boy networks" are preferred for reasons unrelated to productivity – family ties, social connections, clanship, exchange of favours or even bribes, over more competent workers for access to good jobs (Ponzo & Scoppa, 2009, 2010). By recruiting low quality workers, agents impose a cost on the principal and on other, more competent job applicants (Ponzo & Scoppa, 2010). As it affects the quality of staffing decisions, it has an overall negative impact on the performance of the organization (Bandiera et al., 2009; Ponzo & Scoppa, 2009). Favouritism in recruitment was shown to be associated with agents' low powered incentives, strong family ties, low

educational levels, low productivity jobs, small firm size, high unemployment areas, and less developed regions (Bandiera et al., 2009; Ponzo & Scoppa, 2009).

An agent may derive private benefits as well from **favoritism in performance evaluation**, by favorably evaluating performance of those he/she has social connections with, because they receive utility if his/her preferred subordinates' wages are higher (Krausert, 2014; Prendergast & Topell, 1996). The door to favoritism is opened by subjectivity in measuring employee's performance, as evaluators can use their power to misreport their evaluations to accord with their preferences, and reward favored subordinates beyond their true performance (Prendergast & Topel, 1996). However, distorted performance appraisals may cause problems not only in incentive systems, but could harm placement decisions (Prendergast & Topel, 1996). The worst case scenarios are bribing and wasting valuable productive time on lobbying superiors to obtain desirable performance evaluations (Prendergast & Topel, 1996).

Furthermore, agents may derive private benefits from raising preferred subordinates' compensation (Edmans, 2011). Firms must balance the costs of **favouritism in remuneration** (Prendergast & Topel, 1996), as arbitrary rewards, undeserved pay rises and benefits which are not merit-based are direct financial costs. Rampant **favouritism in promotion decisions** is the next form of favouritism, detected to be a widely-spread phenomena in the contemporary business (Tyler, 2012). When members of families, friends or other socially connected people are appointed to valuable jobs because of their connections rather than their merits (Ponzo & Scoppa, 2010), so-called bad promotions occur (Tyler, 2012). Finally, **favoritism** could happen **in training and development decisions**, when it is invested in the development of favored employees, and not in facilitating learning of job-related or future-needed knowledge and skills of most talented employees.

Favoritism was found to be prevalent when the intensity of family ties is strong, when agents suppose that the exchange of favors within the group can be repeated over time, when the uncertainty of connection process is low, in jobs paying high wage rents, in organizations in which managers face low-powered incentives, and when it is easier to make hidden payments (Bramoullé & Goyal, 2009 as cited in Ponzo & Scoppa, 2010; Ponzo & Scoppa, 2010).

3.3. Recruitment of unproductive subordinates

Agents who fear being replaced by more productive subordinates have an incentive to deliberately recruit lower ability, less dangerous candidates in order to protect their own positions and career prospects in the firm (Friebel & Raith, 2004; Krausert, 2014; Ponzo & Scoppa, 2010). As well, they are induced to abuse their personnel authority in other ways to protect their status when they see their subordinates as threatening, such as retain from developing employees under their purview (Friebel & Raith, 2004).

Aforementioned behaviours directly decrease the productivity of the workforce and jeopardize the function of internal labour markets as a screening device for talent, implying substantial costs (Friebel & Raith, 2004). However, although such behaviours hide substandard agents' performance (South & Matejka, 1990), they hurt the agent too, as hiring unproductive subordinates reduces the performance of

the manager's unit reflecting badly on the manager's ability (Friebel & Raith, 2004).

4. HRM CONTROL MECHANISMS FOR MANAGING AGENTS

To minimize the agency problem – to counter the agent's propensity to engage in self-serving, counter-productive behaviour and limit divergences from principal's interests, the literature advocates three control mechanisms: (1) monitoring agents' behaviour through boards of directors, (2) establishing appropriate remuneration systems for rewarding agents, and (3) market control.

Boards of directors can monitor managers and assure that their interests do not diverge substantially from those of principals, as they are supposed to be independent of management (Dalton et al., 2008; Jensen & Meckling, 1976). However, when an agent has high autonomy, and highly specialized knowledge, monitoring becomes very difficult and expensive, so principals rely on incentives to reward agents for appropriate outcomes (Gomez-Mejia & Balkin, 1992; Tosi & Gomez-Mejia, 1989). They principally rely on equity ownership – the idea that agents which are equity holders direct the firm in their joint (principals' and agents') interests (Dalton et al., 2008; Jensen & Meckling, 1976), but tying agent's rewards to the outcome of the action is another option (Petersen, 1993). Lastly, based on the efficient market hypothesis, capital markets may operate to discipline agents, as self-serving executives may subject the firm's assets to be devalued (stock price declines), which makes the firm vulnerable to a hostile takeover (Dalton et al., 2008; Fama, 1980 as cited in Pereira & Esperança, 2015).

Additionally, agents' opportunism could be curbed by information systems (budgeting systems, reporting procedures, etc.) (Eisenhardt, 1989) or electronic monitoring which limits the agent to deceive the principal (Kidder, 2005), as well as by different HRM-based mechanisms.

There are many HRM control mechanisms which enable to align agents' and principals' interest. Already mentioned compensation alignment is one of the most effective ones, and therefore elaborated independently.

4.1. Compensation alignment

Looking through an agency theory lens, one of the primary functions of HRM is to structure agents' pay to align agents' actions with the needs of principals, i.e. to create incentives that reduce agent's self-interests (Bender, 2007; Caza, 2011; Jensen & Meckling, 1976; Petersen, 1993). The issue at hand is how the principal should compensate its agent for the work performed (Ellis & Johnson, 1993). Various compensation plans/contracts are put forward to compensate agents, while the most important element is to determine the optimal contract – to predict the conditions under which particular types of compensation strategies (e.g. fixed vs. variable pay; behaviour vs. outcome contracts) are most appropriate (Eisenhardt, 1989; Gomez-Mejia & Balkin, 1992; Miles, 2012).

Agency theory identifies two types of compensation schemes – behaviour-based and outcome-based compensation, that facilitate two forms of control – behaviour

and output control. A behaviour-based system compensates the agent strictly on the basis of its activities (typically through straight salary), while outcome-based compensation is calculated on performance against stated objectives (such as commission or stock options) (Ellis & Johnson, 1993). Principals prefer to base agent's pay on non-contingent compensation (behaviour contacts) when agent's behaviour can be observed, and on financial returns (incentive contracts) when agent's behaviour cannot be adequately monitored or assessed (Eisenhardt, 1989; Gomez-Mejia & Balkin, 1992; McLean Parks & Conlon, 1995; Stroh, Brett, Baumann & Reilly, 1996).

Behaviour-based compensation result in agents behaving in a compliant manner because it is in their best interests (e.g. do what's in your job description, and you get a raise) (Welbourne & Cyr, 1996). They imply that the behaviour of agents is closely controlled through policies and procedures, standardization of work, adherence to rules, explicit monitoring of routines, and adequate information regarding cause-effect relations, consequently resulting in rigid and cautious behaviour (Welbourne & Cyr, 1996; Yu & To, 2011).

Agents' compensation contingent on company performance – **output-based compensation**, are associated with desirable managerial behaviours that can contribute to firm performance, including greater perseverance, greater focus on key organizational tasks, higher risk taking, willingness to assume responsibility for a longer-term orientation, and even enhanced ethical behaviours (Chng et al., 2012; Schuler, 1987 as cited in Welbourne & Cyr, 1996). Implicit in the agency theory approach is the assumption that linking pay to performance will not only mitigate moral hazard (Eisenhardt, 1989; Kalmi, Pendleton & Poutsma, 2005; Kidder, 2005), but will motivate agents to perform better and act as owners (Bender, 2007; Becker & Olson, 1989 as cited in Welbourne & Cyr, 1996). The underlying premise is that increasing employee ownership in the firm (both true ownership through possessing stocks, and psychological ownership through participating in firm's results) coaligns the preferences of agents with those of the principal because the rewards for both depend on the same actions/behaviours (Eisenhardt, 1989; Jensen & Meckling, 1976; Krausert, 2014; Welbourne & Cyr, 1996). More to it, a greater link between pay and performance implies greater alignment (Bender, 2007). Incentive compensation is therefore common in practice (Shleifer & Vishny, 1997), and comes in many forms – variable pay, commissions, short-term and long-term bonuses, profit-sharing, stock-based compensation, etc.

In recent years, the popularity of equity-based compensation, particularly **stock options**, as a device for linking principals' and agent's interests has gained importance (Conyon, 2006 as cited in Dalton et al., 2008; Dalton et al., 2008; Souder & Shaver, 2010). Through the use of stock option plans, agents are encouraged to not only think like owners, but to behave as owners (Welbourne & Cyr, 1996). As well, stock options are useful incentive to overcome managerial reluctance to make long horizon investments (Souder & Shaver, 2010), and hence ensure the long-term success of companies (Dalton et al., 2008; Welbourne & Cyr, 1996). Namely, managers are often overly focused on short payoff horizons as their compensation historically came from salaries and bonuses tied to short-term performance feedback, and because they may be concerned about dismissal for low performance during the period before the

value of long horizon investments is realized (Souder & Shaver, 2010).

A positive relationship between firm performance and the proportion of equity-based executive compensation was found (Mehran, 1995 as cited in Dalton et al., 2008; Li, Yang & Yu, 2015; Welbourne & Cyr, 1996). However, companies should be aware of differences between unexercisable and exercisable stock options. As unexercisable options only have value in the future, they provide managers with an incentive to make longer horizon investments, while the value of exercisable options can be obtained immediately, and therefore deters long horizon investments and encourages managers to favor short horizon investments instead (Souder & Shaver, 2010). More to it, it has been demonstrated that high powered incentive contracts, and especially stock options, can actually motivate dishonest managerial behaviors, such as self-dealing and criterion manipulation, manipulating with accounting numbers and investment policies, and earnings manipulations (Chng et al., 2012; Shleifer & Vishny, 1997; Gomez-Mejia & Balkin, 1992).

Apart from the easiness of monitoring agents, other arguments for using behavior- or performance-contingent compensation exist, as exhibited in Table 1. What is, however, provoking is that the majority of academics present the two systems as alternatives, although they could be mutually reinforcing. There are already empirical proofs that some firms, such as technology-intensive ones, perform better when they adopt both output and behavior control (Makri, Lane & Gomez-Mejia, 2006 as cited in Yu & To, 2011).

4.2. Other HRM control mechanisms for managing agents

Previously elaborated forms of control systems – behavior and output control, are as well in the origin of different HRM control mechanisms organizations could use to control agents' harmful behavior. However, the third form of formal control system – input control, is as well an option (Snell, 1992 as cited in Yu & To, 2011; Yu & To 2011). Namely, all three formal control systems affect work performance (Yu & To, 2011). The implication is, consequently, that organizations should use a combination of HRM practices which assures the control on all three levels. Table 2 exhibits HRM-based mechanisms for diminishing moral hazard, indicating whether a practice is input-, behavior- or output-oriented.

Table 1: HRM control mechanisms for managing agents

HRM activities	HRM control mechanisms
HRM philosophy	Administrative/bureaucratic HRM – formalizing policies and procedures, controlling costs, performing human resource audits, etc. in order to standardize and control employee behavior to minimize uncertainty (BC). Usage of different codes (e.g. ethical, diversity) that inculcate the agents not to take unfair advantage of the principals (BC)
HR planning	Dismissing an agent (OC)
Recruitment	Rigorous selection that ensures that the agent possesses required knowledge, skills and abilities in order to avoid adverse selection (IC) Looking for specific personality traits (e.g. trustworthiness, honesty) and values (e.g. morality) by using identity tests or similar to screen out potentially unsuitable job applicants (IC) Looking for person-organization (P-O) fit (including shared values), as well as person-job (P-J) fit when hiring agents (IC) Selecting managers that match the compensation arrangement already in place (fixed vs. incentive compensation) (IC)
Performance management	Standardized responsibilities with an overriding concern for procedures and methods enabling the accountability for actions (BC) Performance appraisal based on results (accomplishing performance targets) (OC)
Remuneration	Behavior-based compensation contracts, such as salaries (BC) Monetary rewards closely linked to performance outcomes (pay for performance) – incentive compensation, such as variable pay, commissions, short-term and long-term performance-based bonuses, profit-sharing, equity ownership (e.g. stock options), golden parachutes (OC) Group incentives which relate agent's pay with his/her co-workers' performance, as it might elicit more effort at the same cost to the principal (OC) Benefits that motivate desirable managerial behaviors, such as loyalty rewards (BC)
Training and development	Training for newly employed (a part of socialization) with the purpose of organizational identification (aligning the goals of agents with those of the firm) (IC) Investments in T&D as it signals to agents that the firm expects to maintain a long-term relationship (IC)
Career management	Clear promotion ladders as it signals to agents that the firm expects to maintain a long-term relationship (IC)
Working atmosphere	Fostering job satisfaction, employee engagement, organizational commitment and loyalty as they eliminate divergent interests and create an environment of cooperation (IC) Developing favorable socio-emotional climate and culture (IC) Developing trust as even normally honest and ethical employees may resort to deviant behaviors if they feel that they work in an unjust environment and that their trust has been violated (IC)

Note: IC = input control; BC = behaviour control; OC = output control

Source: Bandiera, Barankay & Rasul, 2005; Caza, 2011; Chng et al., 2012; De Kok et al., 2006; Eisenhardt, 1989; Gong, 2003; Kidder, 2005; Tucker, 1993 as cited in Kidder, 2005; Krausert, 2014; Lan & Heracleous, 2010; Miles, 2012; Petersen, 1993; Pereira & Esperança, 2015; Welbourne & Cyr, 1996; Yu & To, 2011

5. HRM CONTROL MECHANISMS FOR REDUCING AGENTS' SUBOPTIMAL HRM DECISIONS

In response to the managers' tendency to make HRM decisions that serve their own rather than the firm's interests, organizations can formalize, they can monitor, or they can centralize those decision. First, agents' suboptimal HRM decision could be reduced by prescribing HRM policies and procedures. Unfortunately, the majority of companies do have procedures to avoid favouritism and other suboptimal HRM decisions, but they are found not to be effective (Tyler, 2012).

Monitoring and centralizing those decisions implies that HRM professionals are an objective third party (Tyler, 2012). HRM decision are thus shifted to a centralized HRM department (Friebel & Raith, 2004), but managers should stay involved as it is vital that they participate actively in various HRM activities, such as final employment or promotion decisions, performance appraisal, subordinates T&D, etc.

Table 3 exhibits potential HRM control mechanisms for reducing agents' suboptimal HRM decisions, by specifying which particular suboptimal decision (see chapter 3) could be therewith resolved.

Table 2: HRM control mechanisms for reducing agents' suboptimal HRM decisions

HRM activities	HRM control mechanisms	Suboptimal HRM decisions resolved
Recruitment	Prescribed selection criteria (bureaucratic rules in selection decisions), such as required educational qualifications, knowledge or skills, minimum number of years of experience	Favouritism in recruitment
	Rigorous selection based on competences	Favouritism in recruitment
Performance management	Clear performance criteria, such as more quantitative criteria and more quantified development criteria	Favouritism in performance evaluation
Remuneration	Clear remuneration systems (bureaucratic rules of awarding compensation) less sensitive to supervisor evaluations	Favouritism in remuneration
	Less merit-pay	Favouritism in recruitment
	Incentives for mentors	Non-investing in younger workers T&D
Career management	Clear promotion criteria	Favouritism in promotion decision, recruitment of unproductive subordinates
	Promotion decisions based on competences	Favouritism in promotion decision, recruitment of unproductive subordinates
	Promotions done by committees	Favouritism in promotion decision, recruitment of unproductive subordinates
	Nonreplacement rules – never promoting an employee to the position of his/her immediate superior	Recruitment of unproductive subordinates, non-investing in younger workers T&D

Source: Friebel & Raith, 2004; Krausert, 2014; Ponzo & Scoppa, 2004; Prendergast & Topel, 1996; Tyler, 2012

6. CONCLUSION

It is believed that the agency framework is an unusually rich and relevant framework for studying behavior in organizations (Petersen, 1993), including behaviors related to HRM.

Not only that HRM practitioners should be proactive in detecting existing/potential HRM agency tensions in their organizations associated with managing employees, but they have to devise HRM control mechanisms both for managing agents' behavior and for reducing agents' suboptimal HRM decisions. The paper lists three main agency problems related to managing employees: (1) the non-adoption of effective HRM systems, (2) favouritism, and (3) recruitment of unproductive subordinates. As well, HRM mechanisms for managing agents' behavior and reducing agent's suboptimal HRM decisions, that minimize agency costs and result in maximization of firm performance, are systematized. Namely, as agency theory reminds us that much of organizational life, whether we like it or not, is based on self-interest (Eisenhardt, 1989; Gong, 2003), one of the solutions to the agency problem could be the design of appropriate HRM systems for controlling agents behaviors and their decisions in the HRM area.

EXTENDED SUMMARY / IZVLEČEK

Cilj članka je predstaviti teoretično ozadje problema dvojnosti v razmerju lastnik manager, ki lahko pripomore k nedoseganju zadostne uspešnosti področja kadrovskega managementa znotraj združb.

Poleg tega članek predstavi sistematizacijo in dodatno pojasni sisteme nadzora za področje kadrovskega management, ki lahko zmanjšajo moralno tveganje agentov, še posebej ob sprejemanju odločitev, povezanih s kadri.

Literature, ki bi (posredno ali neposredno) povezovala področji kadrovskega management ter teorijo principal-agent, je zelo malo. Prav ta povezava predstavlja področje teoretične analize članka, in sicer z metodo pregleda literature ter teoretične konceptualizacije.

Rezultat je sistematiziranje do sedaj dostopnega znanja iz naslednjih področij: (1) uvod v kadrovske izzive, povezane s teorijo principal-agent; (2) izzivi, ki izhajajo iz teorije principal-agent in so povezani z ravnanji z zaposlenimi; (3) kadrovski mehanizmi nadzora managerjev ter; (4) kadrovski mehanizmi nadzora za zmanjševanje neoptimalnih odločitev managerjev, povezanih s kadrovskim področjem.

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APPENDICES

Appendix 1: Guidelines for using behavior- or output-based compensation

Behavior-based compensations	Output-based compensations
• when more information about an agent's behavior is available (when agents can be monitored) • when actions are easy and cheap to observe and measure • when outcomes are either difficult to measure or difficult to measure within a practical amount of time • when principals and agents are involved in long-term relationships/transactions, as principals are better-informed about the agents' behavior and the goals of the principal and the agent are aligned • when agent's job is programmable (routine tasks) • when the environment in stable • when the expected length of an agency relationship is longer (when it is preferred that agents stay longer in a company and that they are committed/loyal to the company) • when a company wishes to retain talented agents during times of high levels of turbulence • when outcome uncertainty is high, as it is expensive to shift risk to the agent despite the motivational benefits of outcome-based contracts • when agents have a lower core self-evaluation, as the greater uncertainty presented by incentive compensation may overwhelm their meagre self-belief and reduce their propensity to respond to incentive compensation in the desired manner • when an agent is more risk averse, as in that situation it is increasingly expensive to pass risk to the agent • in companies with less ambitious and difficult strategies	• when direct supervision is infeasible or counterproductive because of information asymmetries • when outcomes are easy to observe, measure and assess in terms of their value • when the information asymmetry between principal and agent is likely to be greater because of the short-term agency relationships • when agent's job is less programmable, because when task programmability is low an agent's behavior is difficult to monitor • when accomplishing the task entails risks for the agent • when principals want to motivate agents to engage in risk-taking behavior that enhance long-run firm performance • when a company is undergoing significant/rapid change/growth, experiencing high degrees of uncertainty/turbulence in the environment, or is a high-risk company, as compliant behavior curtails actions that are needed for quick response to unknown problems • when outcome uncertainty is low, as the costs of shifting risk to the agent are low • when high levels of turnover, for example for "bring in new blood", are preferred • when agents have a higher core self-evaluation, as they are more comfortable with the increased uncertainty associated with incentive compensation, and more confident in their ability to achieve the stated performance goals and earn the promised rewards • when principals want to reduce favouritism, as agents target high ability workers irrespective whether they are socially connected to them or not when they are paid performance bonuses • when an agent is increasingly less risk averse (e.g. a wealthy agent), as in that situation it becomes more attractive to pass risk to the agent • when the principal is more risk averse, as in that situation it is increasingly attractive to pass risk to the agent • in companies that adopted more ambitious and difficult strategies (risk-taking organizations)

Source: Bandiera et al., 2009; Chng et al., 2012; Eisenhardt, 1989; Gomez-Mejia & Balkin, 1992; McLean Parks & Conlon, 1995; Dow & Raposo, 2005 as cited in Pereira & Esperança, 2015; Pereira & Esperança, 2015; Petersen, 1993, Stroh et al., 1996; Jensen & Murphy, 1990 as cited in Welbourne & Cyr, 1996; Welbourne & Cyr, 1996; Yu & To, 2011