

SIM 2017 / 14th International Symposium in Management

## Managerial Opportunism in Modern Russian Corporations

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### Abstract

The sustainable development of the corporation in unstable economic conditions is largely determined not only by the current situation of the market, but also by competent actions of management personnel. In the negative economic situation in the country and the world, the interaction between the subjects of the corporation at different levels is characterized by a high degree of managerial opportunism. This article deals with the structure of the top managers' remuneration in Russian corporations. There is a rating of the dependence of the level of wages due to the results of manager's activity. The average wage dispersion within manager and staff worker groups of the corporations is estimated. The presented results show that the existence of problems of managerial opportunism are common for all companies in the world and require the development of effective mechanisms for its limitation.

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Peer-review under responsibility of SIM 2017 / 14th International Symposium in Management.

*Keywords:* opportunism, managers, shareholders, corporation, bonuses

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### 1. Introduction

Managerial opportunism negatively influences the efficiency and the development of corporations. Therefore, a study of how managerial opportunism manifests and proposals for its restriction is necessary for the most effective management of the corporation. The removal of the owner from corporate management led to the problem of asymmetric distribution of information in favor of the manager. Having delegated their powers to the manager, the shareholders were not always able to observe what efforts the manager makes to fulfill his duties. Further, the shareholders are unlikely to receive complete and reliable information about the current state of the affairs of the firm. This situation leads to the premises for managerial opportunism. The aim of such behavior is to directly benefit at the expense of the shareholders.

### 2. Literature Review

In the second half of the twentieth century, an American economist named O. Williamson identified three levels of selfish behavior in individuals. Opportunism is its strongest form; its semi-strong form is a simple following of

personal interests and a weak form of selfishness (in fact its total lack) is obedience. (Williamson, 1985). According to his definition, opportunism is a persecution of the personal interest with the use of insidiousness. This behavior includes more overt forms such as lies, theft, and fraud, but it is hardly limited to them. Opportunism can be manifested at different stages of contractual relationships. O. Williamson denoted ex-ante and ex-post ones. Pre-contract (ex-ante) opportunism occurs before the contract making, when one of the parties of the contract deliberately misleads another party. The parties show post-contractual (ex-post) opportunism, by only partially following or breaking the contract's terms.

Managerial opportunism comes in many forms, here are several prevalent ones beginning with crude opportunism. This form of opportunism denotes a deliberate, conscious violation of the contract terms to achieve one's interests. Strategic opportunism includes the asymmetric distribution of information that makes it possible to hide the part of the actions of one side from the other. Natural opportunism is deviation from the terms of a previously concluded contract due to changes in circumstances. At the heart of opportunistic behavior, there is a mismatch between the economic interests of economic agents, due to the limited resources as well as uncertainty.

In recent years, the problem of opportunism has been a popular topic of scientific research. Todorova & Vasilev, (2017) showed the possibilities of opportunism reduction and overall, the transaction costs in firms that use an authoritarian management style. They recognize the special importance of this kind of power model in the firm for the countries of Eastern Europe, in which opportunism is restrained not by the economic motivation of managers, but by strict control and hierarchy. Kolev, Wiseman & Gomez-Mejia (2017) considered the process of disposing of residual rights in corporations as a problem of bargaining among a firm's top managers and the board of directors, as well as its influence on the performance of corporations. Their study showed ample opportunities for the manifestation of managerial opportunism under these circumstances.

In the articles by Albanese, Navarra, & Tortia, (2015) and Navarra, & Tortia, (2014), the differences in the possibilities of opportunism manifestation appear in relation to the level of wages in companies of different ownership structures. It has been established that firms owned by investors have more opportunities and willingness to manifest opportunism in terms of labor remuneration than companies owned by employees. It has also been pointed out that the power of firms in setting wage rigidity is negative for labor productivity and stable employment. The studies by Zhang, Li & Huang (2017) showed that the repeated and ongoing interactions of the firms' agents reduce the level of opportunism in them. The authors propose to move from a formalized to a socialized interaction of subjects in a corporation. This is based on the diagnostic of exchange interruption types in the firm. Kundakchyan & Grigoryeva (2016) studied the impact of contractual relations on the level of behavioral opportunism in organizations. The authors exposed a significant influence of the level of specificity of assets, as well as incompleteness of the contracts on the possibility of agents for opportunism manifestation in modern companies.

Special attention was drawn to the problem of differences in the level of wages of staff workers and managers, as well as its impact on the firms' performance. Ding, Akhtar & Ge (2009) proved that the inter-hierarchy wage dispersion between managers and staff workers is positively related to firm performance, but intra-hierarchy wage dispersion within manager and worker groups is negatively related to firm performance. The study of Gerlach & Hübler (1998) considered various factors explaining the differences in the level of wages in big and small German firms, including those typical for management personnel. In general, for big companies with the same level of responsibility and the same qualifications, the level of pay was higher than for small companies. In the later study of the correlation between the level of wages and the size of American firms (Majumdar, 2010) a negative relationship was discovered between these factors.

The comparative analysis of wage policy and its differentiation Grund (2005) showed some significant differences between American and German companies owned by one owner (the American level of differentiation was significantly higher). Mion & Opromolla (2014) proved the positive influence of the previous experience on the level of payment for the company's managers, in particular, the experience of export activity at the previous place of work. The phenomenon of the high-wage firms was considered by Abowd, Kramarz & Margolis in their study from 1999. They found that paying more in comparison with the high-wage market positively affects the productivity and profitability of the firms. At the same time, hiring highly paid employees is positive for productivity, but negative for the company's profitability. However, the empirical studies of the managerial opportunism and its relationship with the efficiency of the companies is still not enough to make a definitive conclusion about the nature of this relationship.

### 3. Methodology

This article is based on institutional methodology derived from O. Williamson, A. Alchian, G. Demsets, O. Hart, B. Holmstrom. The corporation is considered a complex system in which there are many different agents with different interests. Each entity, pursuing its goals and its benefits, in relations with others, orients to the same behavior on their part. In this context, the problem of opportunism inevitably arises as a result of following its interests within the framework of contractual relations between interacting agents. The problem of opportunism arising in the relationship of owners and hired top managers of Russian companies deserves separate attention. To assess the opportunism of managers, the current system of their remuneration is used in conjunction with various aspects of the company's activities.

The study of the efficiency of remuneration systems shows that the applied evaluation criteria and indicators are not sufficiently developed. The problem of an adequate evaluation of the results of work and the proportionality of wages, typical for both ordinary employees and top management personnel, has been discussed in economic literature for a long time. The existing systems for assessing the contribution of each employee to the overall result of a corporation, despite the different approaches, indicators, and criteria underlying them, are equally ineffective. Most of the known approaches are based on the comparison of the planned amount of work (or the value of a particular indicator i.e. profit as an example) with the actual one. Reaching a given level and exceeding it, employees receive remuneration in the form of bonuses or compensations. It reflects the efficiency of the whole corporation in the specified period without taking into account the individual contribution. The approaches that provide a score or rating evaluation of the employee's work are highly subjective and not always able to make an adequate assessment of the work.

The payment of the compensation, disproportionate to the spent efforts, leads to the de-motivation of the employees to start. Moving onwards, it causes an orientation to the personal gain in the short period of time, the lack of reliable links within the corporation, etc. The formation of the average employee's wage, as a rule, is quite transparent. The employment contract specifies the terms of reference, establishes the limits of labor productivity, according to which the basic part is calculated, and the amount of incentive payments or bonuses based on the results of work is fixed. However, the majority of companies do not disclose the same amount of information for the same process of management personnel. In the last few years, a number of the largest Russian companies published a methodology of the remuneration systems used by top managers at various enterprises. The efficiency of a corporation is understood to mean its activity, which not only fixes a stable growth of the main indicators (for example revenue or profits), or they achieve a specified value, but also ensures the receipt of income by its subjects (for example dividends or capitalization growth). It is worth noting that some corporations also take into account other characteristics such as retention or increase in market share, competitiveness, growth of the customer base, and so on.

### 4. Managerial Opportunism

One of the negative trends in modern corporations is a significant gap in the growth rate of wages of employees and management personnel. For the first time, this problem received wide coverage in the media during the crisis of 2008-2009 which, in turn, attracted increased public attention. Despite a sharp decline in corporate profits, top management positions received bonuses and compensations at the end of the year in full, and in some cases, the amount of compensation had even increased.

The problem of a significant difference in the wages of managers and average workers is denoted all over the world. In Great Britain, for example, the salary of the top manager is 172 times higher than that of a hospital nurse or it is 145 times higher than the average salary of a teacher (Independent, 2017). In the Russian Federation, 1% of the highest paid employees earn 63% more than 1% of staff workers with the lowest salaries. A similar trend is observed in China, where the difference is 70 times, and in Europe, this figure reaches a 22-fold difference on average (Global Wage Report)

Certainly, the differences in wages may be due to the various factors – work experience, the level of education, the degree of responsibility for decision making etc. The importance of such factors is without doubt. However, these factors explain only a part of the rising inequality. The more employees there are in the company, the more

complex structure it has. It is likely that the emergence of each new level of management leads to the 2-3 times gap in wages.

Nevertheless, the wage gap of more than 100 times within one company is a common practice for the biggest Russian corporations (Tab. 1). As a measure of the average wage, the ratio of the fund of accrued wages and the average number of employees of the enterprise were used (Commersant).

Table 1. The average annual income of members of the board and employees of the company in 2016 (mln. p.), Commersant, (2017)

Company	The average income of a member of the board	The average income of an employee
Gazprom	144,1	1,7
Rosneft	369,7	6,7
Aeroflot	54,4	0,3
Sberbank	299,3	0,9
RZD	99,8	0,6

It should be noted that in addition to the ordinary employees, the shareholders remain dissatisfied with the constant growth of managers' salaries. The inevitable consequence of the development and growth of the corporation is the emergence of a more complex management structure. At a certain stage, this leads to the need to transfer the management functions to a certain group of people - managers. As a result, there are two formed groups: the owners who have transferred the management function, and managers who directly manage the corporation.

Top management should manage the company, guided primarily by the interests of the owners, namely, maximizing their income. However, practice shows that this is not always true. The study conducted by CFA (CFA UK, 2016) showed that the level of wages of CEOs of FTSE 350 increased by 82% in the period between 2003 and 2015. While the income of investors of these companies increased, on average, by only 1%, and in some companies it had even decreased. There has also been a steady growth in the remuneration of managers in Russian corporations (Figure1). For example, over the past 10 years, the total remuneration of Aeroflot managers has increased by more than 30 times.

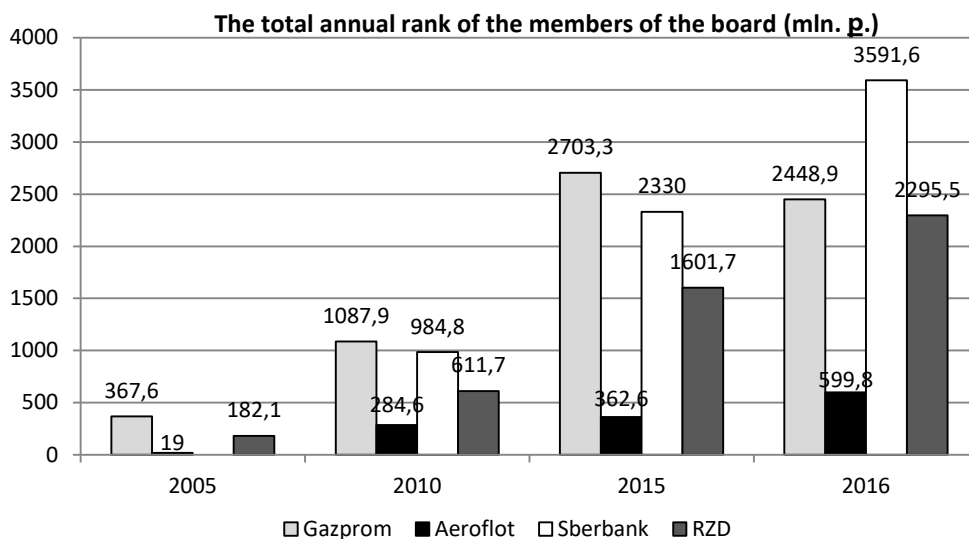


Fig.1. The dynamic of the total annual rank of the members of the board of Russian companies

Despite the fact that the average wage of corporate employees in Russia is significantly lower than in Europe and the United States, the remuneration of some Russian top managers is comparable to those of the largest foreign companies (Table 2) (Commersant, 2017). Table 2 presents the data on the level of managers’ compensations, included in the top-10 highest-paid top managers of the largest US companies, as well as top managers of Russian companies.

Table 2, The data of the level of compensation to the top managers in 2015, Commersant, (2017)

Name	Company	The total level of compensation (\$ mln.)
Jeff Immel	General Electric	26,4
Bhavesh Patel	LyondellBasell Industries	24,5
Randall Stevenson	AT&T	22,4
Indira Nuui	PepsiCo	22,2
James Gorman	Morgan Stanley	22
Alexey Miller	Gazprom	17,7
Igor Sechin	Rosneft	13
German Gref	Sberbank	11
Boris Kovalchuk	Inter RAO	3,5
Nikolai Tokarev	Transneft	3

Managerial opportunism begins when the manager’s personal interests and the interests of owners cease to coincide. The shareholders are primarily interested in receiving income from the capital invested by them in the corporation, while the main goal of managers' activity is personal enrichment. Obviously, information transparency can reduce the losses of shareholders caused by the opportunistic behavior of managers. However, in reality, to prevent and limit managers’ opportunism, it is necessary to incur costs not only to reduce information asymmetry, but also to stimulate managers by paying them various bonuses and compensations.

The efficiency of the company's activities largely depends on top management’s interest in the results of their work. There is a problem of determining the degree of interrelation between the intensity of the work of managers and wages, the intensity of their work, and the efficiency of the firm as a whole. It is quite difficult to find the optimal balance between the constant (wages) and the variable part of the manager's pay. Figure 2 shows the compensation structure of top managers of two Russian companies. As we can see, there is no similar compensation structure in companies. Depending upon the goals that shareholders set for the managers, not only key performance indicators (KPIs) are determined, but also part of the remuneration of labor aimed at achieving them.

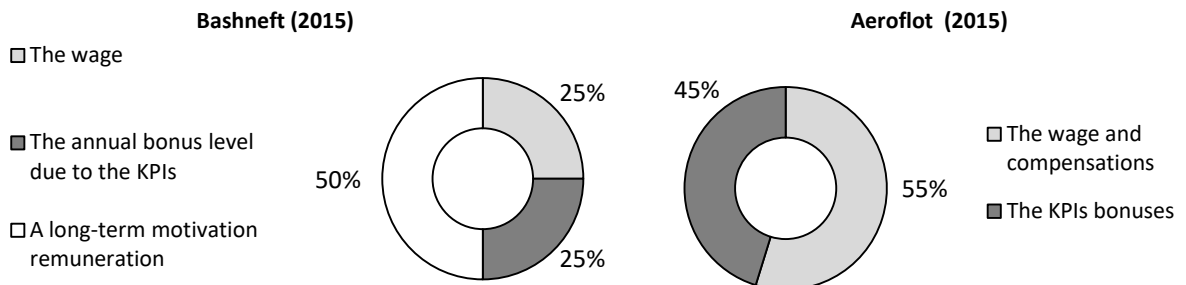


Fig. 2. The structure of wages in Russian companies Bashneft and Aeroflot in 2015, Annual Report «Bashneft» and «Aeroflot», 2015

Increasingly, managers are paid bonuses according to the results of the firm's activity for a certain period of time.

However, due to the lack of transparency in the financial systems of some companies, it is often difficult to measure the true financial result. After all, the result of the company's activity depends on various external factors. The owner is not always able to determine by what means certain indicators are achieved, to what extent they depend on the efforts exerted by the managers, and to what extent they are provoked by the influence of external factors.

The determination of remuneration depending on the amount of profit is also ineffective. Low profit indicators can be a consequence of reinvestment in the development of the organization. Such investments will only yield returns after a few years. Consequently, the dependence of the bonus on the size of profit forces managers to focus on short-term planning and maximizing the immediate benefits. Nevertheless, from 60 to 80% of managers' salaries are tied to any indicators of the company, for example, revenue, stock quotes, etc. (Harvard Business Review, 2016). As it was shown earlier in Russian companies, the part of the remuneration is also tied to achieving the set values of key performance indicators. At the same time, the analysis of the relationship between the growth rates of manager payments and the growth rates of revenue and net profit did not reveal a close interrelation between these indicators. The table presents data obtained as a result of the comparison of the indicators in 2015 and 2016.

Table 3, Growth rates of indicators in 2016 in comparison with 2015

Company	Tw (Proceeds)	Tw (Net profit)	Tw (Remuneration)
Gazprom	-0,092	0,02	0,906
Bashneft	-0,087	-0,136	2,587
RZD	0,044	19,44	1,433
Rosneft	0,026	-0,586	1,004
Alrosa	0,347	6,041	1,141
Rostelecom	-0,002	-0,497	0,968

As it is shown in Table 3, the amount of remuneration is practically independent of the values of key indicators achieved in the current period. The obtained values of the correlation coefficients indicate a weak relationship between the growth rates of managers' payments and the growth rates of revenue and net profit. Orientation to obtain a given result in the short term significantly hinders the development of the company. As a result, the refusal to implement long-term projects and investments in new developments can lead to the loss of some competitive advantages.

### 5. Opportunism limit

It is an important aspect of the success of a modern corporation to limit and prevent managerial opportunism. Managerial opportunism is a special phenomenon, which negatively affects the functioning and development of any enterprise. Weakening control over the behavior of managers threatens the corporation with significant losses, so it is necessary to carry out a set of measures to limit and prevent opportunism. Effectively motivating the top managers is necessary both for the owners of companies and for the managers themselves. It is required to determine the size and structure of the managers' remuneration, capable of creating the necessary motivation and ensuring achievement of the set goals. Rethinking the approach to determining the size of bonuses led to the development of mechanisms for limiting opportunism of managers, among which options remain the most popular. The world practice of long-term motivation is built on the pooling of the interests of shareholders and managers, namely, the growth of the corporation's capitalization. The option involves a close relationship between the size of the remuneration and the company's capitalization. The motivation mechanism for the option program is based on a certain delay in the payment of compensation. It is from the receipt of the option to the possibility of its implementation. If the manager in a given period of time goes to another company, he or she, as a rule, loses the opportunity to receive this bonus. An obvious drawback to the option programs is the possibility of a depreciation of the company's shares for reasons beyond their immediate control (crisis, negative political situation in the country, sectoral factors, etc.). In this case, the motivational effect of the option is significantly reduced. It should be noted that, despite a certain motivational function, options for company managers are rather just a complement to other incentive mechanisms.

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