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**A QUESTION OF VALUE(S): POLITICAL CONNECTEDNESS  
AND EXECUTIVE COMPENSATION IN PUBLIC SECTOR  
ORGANIZATIONS**

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**Abstract.** While the de-politicization of public sector management was a core objective of past reform initiatives, more recent debates urge the state to act as a strong principal when it comes to public sector unity and policy coherence – and consequently make a case for reinvigorating links between the political and managerial sphere. Using data from Austrian public sector organizations, we test and confirm the causal relationship of political connectedness of board members and executive compensation. Differentiating between value-based and interest-based in-groups, we suggest that only value-based political connectedness has the potential to restore patronage as a control instrument and governance tool. Self-interested and reward-driven patronage, on the other hand, indicated by a strong association of political connectedness and executive pay, refers to the type of politicization that previous public sector reforms promised to abolish.

**Keywords.** Public management; public governance; corporate governance; executive compensation; (de-)politicization; patronage; Austria

## **Introduction**

After a substantial period of disaggregation and ‘quangocratization’ (Hood 1991), political-administrative systems worldwide are facing a paradoxical situation: On the one hand, and very much in the spirit of New Public Management’s central credo to ‘let the managers manage’, the establishment of autonomous public sector organizations (PSOs) was tied to the promise of de-politicization and managerial autonomy in the delivery of public services (McLaughlin and Osborne 2002; Pollitt and Bouckaert 2011; van Thiel et al. 2012). As a consequence, politicians have been criticized for retaining positions and responsibilities in such organizations (Flinders and Matthews 2010). On the other hand, decentralization and increased autonomy in decision-making have led to serious policy fragmentation within the public sector (Christensen et al. 2007). As a result, a reinvigoration of links between the political sphere of the state and its

decentralized units has been called for (Flinders 2010; Flinders and Matthews 2010; Kitschelt 2000; Kopecký and Mair 2012) as a potential remedy to regain policy coherence, as well as to reinforce accountability.

In public debate, however, it is mostly the bitter flavor of favoritism that dominates when it comes to political connectedness and patronage. De-politicization – described by Burnham (2001, 128) as “the process of placing at one remove the political character of decision-making” – is not seen as being achieved through decentralization and agencification. Autonomous PSOs are perceived as organizational arrangements in which politicians install boards of directors more or less at will, as a means of rewarding political ‘minions’ – high social prestige and attractive compensation included. As a consequence, the nomination of managers of PSOs and their financial compensation has been under close scrutiny by public audit courts, the media, and critical voices from civil society. The Austrian Court of Audit has repeatedly detected a lack of transparency and comprehensibility, missing standards, and inconsistency (Rechnungshof 2011), and has found support in *Transparency International* (2009, 313) which criticizes the “arrangement of close ties” between representatives of PSOs and political parties.

In our article, we tackle the question of whether the political connectedness of PSO board members is a manifestation of democratically legitimated control and, thus, a signal of responsible state ownership, or whether it is a manifestation of undue favoritism that should be thwarted. In other words: Is it possible to distinguish empirically between these two ‘types’ of political connectedness to address the paradoxical claim that the state should, at the same time, actively exercise its ownership functions *and* refrain from political interference (OECD 2005, 3; see also OECD 2010)? Drawing on existing literature on board composition and executive pay (Bebchuk and Fried 2006; Belliveau et al. 1996; Ennsner-Jedenastik 2014; O’Reilly and Main 2010; Westphal and Zajac 1995), we test a number of hypotheses on the relationship

between political connectedness and board compensation with data from Austrian PSOs. In more detail, we collected data from corporatized organizations with 100 percent direct ownership by the federal state, comprising a set of variables that describe a total of 724 board members in 72 organizations. Estimating several statistical models, we find that political connectedness has high explanatory power, and accounts for more of the variance in executive compensation than other factors that have previously been discussed in the literature, such as size or industry (Finkelstein et al. 2009).

On the basis of our findings, we argue that the very character of political connectedness – either as a governance tool or as favoritism – is dependent on the specific type of ‘in-group’ that serves as the linking pin between polity and PSOs. Consequently, and building on the foundational work of Lazarsfeld and Merton (1954), we propose a differentiation between two different types of political connectedness: (public) value orientation of in-groups, on the one hand, and politicization that is grounded in self-interest of a circle’s members, on the other. Drawing on Granovetter (1985) and Zukin and DiMaggio (1990), we argue that only the former has the potential to re-establish coherence and unity of the current highly fragmented landscape of PSOs – the ‘control’ dimension of political connectedness – while the latter type of in-group accounts for the reward-oriented version of patronage (Kopecký et al. 2008, 2012).

### **Conceptual Orientation and Hypotheses**

For private sector firms, board composition and compensation are ‘classic’ issues within *corporate* governance literature. For PSOs, however, conceptual and empirical research on board composition and compensation is surprisingly limited – despite increasing interest in, and lively debate on, the performance of agencies and corporatized organizations (Bilodeau et al. 2007; Boyne et al. 2006; Nelson and Nikolakis 2012; Pollitt 2006) and issues of *public corporate* governance (Papenfuß 2014; Schedler et al. 2007). In particular, the role of directors’

political connectedness and its influence on executive compensation has not yet received adequate attention in the scholarly domain of public management research. By investigating the impact of political connectedness of top managers in PSOs on executive compensation, our article tackles this question and explores the conceptual integration of these hitherto disparate phenomena.

### **Political Connectedness as a Potential Means of Political Re-embedding?**

PSOs are not at all a new phenomenon. However, during recent decades, the trend towards disaggregation – boosted by what has been aptly described as ‘agency fever’ (Pollitt et al. 2001) – surpassed prior endeavors in this direction both in terms of quantity and quality. It also laid the basis for institutionalizing ‘public managers’ as appointed leaders in such newly created organizations. In the discussion of dysfunctions and negative effects of organizational disaggregation (Boyne et al. 2003; Christensen and Lægreid 2006; Pollitt et al. 2004), two aspects seem to be of particular significance for our purpose: fragmentation through policy autonomy, and (de-)politicization.

One of the core conceptual tenets of past reforms demanded separation of policy formulation from policy execution (Gray and Jenkins 1995; Peters and Pierre 1998). Apart from efficiency gains through professional management, such separation was also seen to push back favoritism and undue political influence. In practice, however, a low level of policy specification, steering, and performance control was found to be the norm, and increasingly, agencies and corporatized organizations acquired policy autonomy *in addition to* their managerial autonomy. The unavoidable consequences were steering deficits and policy fragmentation (Kolbe 2006; Lægreid and Christensen 2006, 2007; van Thiel et al. 2012). Instead of praise for de-politicization, political decision-makers saw themselves criticized not only for “freeing organizations from the perceived burdens of political control” (Bovens 2005,

201), but, more importantly, for “remov[ing] themselves from direct responsibility for policy implementation” (Flinders and Skelcher 2012, 327). Flinders (2010, 319) even portrays de-politicization as a “dangerous trend” and a “threat to democratic politics, not its savior”.

To remedy this development, some scholars recently proposed an “unfashionable defense of patronage” (Flinders and Matthews 2010, 640). Drawing on a basic distinction between political patronage as an instrument of control and as an instrument of reward (Kopecký et al. 2008; see also Eschenburg 1960), such defense focuses on the former and aims at re-conceptualizing political connectedness as a control-oriented tool and resource of modern governance (Flinders and Matthews 2010; Kopecký et al. 2012). In such a vein, political connectedness is interpreted as a valid means to re-link citizens, politicians, and public administration (Kitschelt 2000), and as having the potential to establish policy coherence in an otherwise increasingly dis-embedded organizational landscape. Reward-based political patronage, on the other hand, is regarded simply as a means of favoritism used to reward political minions. However, how is it possible to precisely distinguish political patronage as control from political patronage as reward?

### **Social Similarity as a Key Factor for Board Composition and Compensation**

Questions concerning the political connectedness of corporate boards address the issue of board composition – a field that is relatively well researched for the private sector (Burris 2005; Mizruchi 1996). Some more recent publications in this scholarly domain focus on the political connectedness of firms (Niessen and Ruenzi 2009) and other personalized ties of CEOs and directors (Pina-Stranger and Lazega 2011), showing how such connectedness and enhanced social capital may result in added value and/or competitive advantage for the company (Finkelstein et al. 2009) which may, in turn, legitimize a higher level of executive compensation.

Board composition is also closely associated with the mechanisms of board appointments. Westphal and Zajac (1995), drawing on social-psychological effects, stress that board members who are involved in the selection and appointment process of new members tend to choose candidates that are similar to themselves with regard to certain biographic and demographic characteristics (and privilege these also in terms of higher compensation). More generally, similarity is a well-established social mechanism for the establishment of connections between people. The underlying principle, denoted as ‘homophily’ by Lazarsfeld and Merton (1954), is also expressed in the proverb ‘birds of a feather flock together’. Empirical and conceptual research has indicated that the creation of social ties is favored by similarity among individuals (McPherson et al. 2001). In line with this argument, similarity is thought to be a salient basis<sup>7</sup> for group membership; in addition, it increases influence, mutual trust, and interaction (Tsui and O’Reilly 1989; Westphal 1999). For Westphal and Zajac (1995), homophily and self-categorization are powerful mechanisms that produce evaluation bias and, subsequently, support. Consequently, various kinds of “resources are likely to be distributed preferentially when the members of a group share a common identity [...], are friends [...], perform interdependent tasks [...], and share demographic or other similarities” (Belliveau et al. 1996, 1571).

Building on such insights, extant research on CEO compensation in private sector firms has recently shifted away from mere economic explanations to include more social accounts, especially as empirical evidence of a direct association between pay and organizational determinants, with the exception of size and industry, has remained scarce (Finkelstein et al. 2009; Malsch et al. 2012; O’Reilly et al. 1988; O’Reilly and Main 2010). In particular, the link between executive compensation and organizational performance – a prominent assumption from a principal-agent perspective (Shleifer and Vishny 1997; van Essen 2012) – has been challenged by scholarly work (Bebchuk and Fried 2006; Jensen and Murphy 1990; Rost and



Osterloh 2009; Tosi et al. 2000). For the case of PSOs, compared to private sector firms where shareholder wealth may serve as a performance measure, respective performance measures are more complex (see also the ‘performance paradox in the public sector’; van Thiel and Leeuw 2002). In addition, such information is mostly not available to political decision-makers who, despite growing policy autonomy of decentralized PSOs, have retained the discretion to appoint top-management. Thus, for the public sector it seems to hold especially true that noneconomic factors play an important role in the determination of executive salaries (O’Reilly et al. 1988). Recent perspectives therefore draw on social-psychological aspects that focus on processes within the boardroom (O’Reilly and Main 2010), or include factors from outside of the organization such as political reasons for agency termination (Park 2013). Given the relevance of social similarity as a mechanism and the role of the individuals or groups that actually nominate board members and set their salary level (Belliveau et al. 1996; Daily et al. 1998), political connectedness is a focal factor precisely because it embodies both shared similarities and the specific type of relation employed.

### **Hypotheses**

In our hypotheses, we propose a number of links between social similarity (via political connectedness) and executive compensation. In doing so, we follow the popular assumption that political connectedness is reward-driven.

Potential influences of political connectedness on executive compensation in public sector corporatizations may unfold on two levels: The first level concerns questions of board composition – the degree of political connectedness of board members in general and its influence on executive compensation. On the second level, political proximity of the executive board and the line minister under whose control the organization operates may influence executive compensation. For empirical reasons, we have formulated our hypotheses for a two-

tier corporate governance system. In two-tier systems, the functions of executive (or inside) and non-executive (or outside) directors are divided into two separate boards – an executive and a supervisory board. However, we do not expect this to influence our results as boundaries between the monistic and the dualistic board system have widely dissolved (Davies 2001; Spindler 2014). In a two-tier system, members of the supervisory board basically have the same rights and duties as non-executive directors in a one-tier system, and the executive (or managing) board fulfills the tasks of executive directors. In addition, such noticeable convergence tendencies have been promoted by good governance standards (e.g., the Cadbury Code of Best Practice in the UK). According to such standards, non-executive officials should perform the principal functions of board nomination and remuneration.

#### Delegates from the core public administration on the supervisory board

The Weberian ideal of a public servant serves as a point of departure for our investigation; with the underlying values of independence, objectivity, and a *sine ira et studio* approach, the image of public sector employees is “one of a law-abiding and objective civil servant with a great sense of duty, combining expertise, stability and continuity with a special professional ethos as ‘bearer of state sovereignty’” (Hammerschmid and Meyer 2005, 630). Adequate compensation comes with such a position; however, it does not seem to be a significant motive for working in the public sector, where salaries are generally inferior to those of private sector employees with equivalent qualifications.

We expect that a higher proportion of administrative representation in the supervisory board (e.g., from the line ministry or other core administration bodies) will lead to a lower level of executive board compensation. Our reasoning is – in line with the above – twofold. On the one hand, public officials will understand themselves as committed to the public interest in the way that they feel responsible for taxpayer’s money, and therefore act in a more expense-conscious

manner when it comes to executive compensation. On the other hand, and more importantly, we draw on social comparison theory of compensation (Belliveau et al. 1996; Daily et al. 1998; O'Reilly and Main 2010): Public officials who sit on supervisory boards compare the compensation they grant with their own remuneration. As pay levels even of senior public officials are rather low compared to private-sector managerial salaries, we expect these representatives on the supervisory board to set a below-average executive compensation.

H1: A high degree of administrative involvement in the supervisory board is negatively related to the level of the executive board's compensation.

#### Political connectedness of the supervisory and the executive board

We further assume – building on our considerations above – that executive compensation is driven by the political connectedness of board members. Politically connected actors<sup>1</sup> in general, and independent of their respective political party affiliation, share certain ‘insider’ features that make them ‘socially similar’ to some extent: They know the formal and informal ‘rules of the game’ and have been socialized in (or close to) political cadres. Therefore, they have privileged access to socio-political players and decision-makers, and perform the key bridging task of an ‘interpreter’ between the rationalities of politics and public administration, on the one hand, and business, on the other (Schedler and Rüegg-Stürm 2014). Depending on a country's administrative system, such politically connected actors may take advantage of intersectoral mobility between the public and the private sector, and make use of ‘revolving doors’ to switch between them. In this respect, being politically connected provides a vital

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<sup>1</sup> Note that the term ‘politically connected actors’ does not mean ‘politicians’: Commonly, active politicians do not hold directorships in boards of PSOs.

source of social capital, and is a characteristic prerequisite for appointments at the interface of these social spheres.

Distinct group affiliations represent someone's personal network and elite institutional affiliations (Belliveau et al. 1996). In turn, social circles provide social status (D'Aveni and Kesner 1993) and the opportunity of better career outcomes (Ibarra 1992) in a 'top-down' way. Generally, it is assumed that politically connected supervisory board members preferably elect other politically connected actors as executive boards members, since they value that the latter "[bring] personalized ties back in" (Pina-Stranger and Lazega 2011) for their mutual benefit. Building on the argument that such patronage embodies an elite-oriented means of reward and serves to pay-off loyalty (Kopecký 2012; for 'service patronage': Eschenburg 1960; Müller 2006), we hypothesize that high political connectedness of the supervisory board has – via board composition – a significant influence on the compensation of the executive board.

H2a: A high degree of political connectedness of the supervisory board is positively related to the level of the executive board's compensation.

In logical consequence, the argument holds true – in a modified form – when seen from the perspective of the executive board: Managers who are politically connected are more likely to be appointed, as they share the distinct features of an 'insider'. For appointees, the appointment certainly has the character of a reward: We expect those members of executive boards who are politically connected to be beneficiaries of patronage and rewarded by higher compensation; they are, in such a way, able to realize and 'cash in' their specific social capital.

H2b: A high degree of political connectedness of the executive board is positively related to the level of the executive board's compensation.

## Political proximity between the executive board and the line ministry

In addition to political connectedness as such, issues of political ‘color’ and party membership are thought of as playing a vital role in both: the appointment of executives in agencies and corporatized organizations (e.g., political partisan affiliation was found to be a predictor for managerial survival in SOEs; Ennsner-Jedenastik 2014) as well as in setting the level of their compensation. In this respect, Kopecký et al. (2008, 4) conceptualize party patronage “as the power of a party to appoint people to positions in public and semi-public life, considering the scope of patronage to be the range of positions so distributed”. Supervisory boards, which formally make executive appointment decisions, are themselves elected delegates, and it is part of their control agenda to ‘appoint the right people’. In many cases, this question of fit is defined via the catalogue of values as documented by political party membership or otherwise strong ties with a specific political party. Frequently, it is the minister’s privilege to decide whom to delegate as a member of a supervisory board; or, depending on the legal structure of the specific organization, in some cases ministers are directly in charge of appointing executive directors of an organization. This gives them considerable power to influence appointment decisions. PSOs, in the words of Flinders and Skelcher (2012, 331), “are a hardy breed of administrative animal and are simply too useful to politicians as tools of governance to be lightly discarded”. Politicians, thus, are often found to distribute positions among ‘allies’ who share their political preferences (Bendor et al. 2001) in order not to end up with “a government of strangers” (Hecló 1977). Such patronage is criticized for neglecting the abilities and experience of the politically connected protégé: “It does not depend on what the protégé can do for the office, but on the advantages the office brings for him” (Eschenburg 1960, 3; translation by the authors). For appointees, board positions have a rewarding character as they come, in any case, with high prestige and corresponding monetary remuneration. We expect this effect to be even stronger when social similarity between patron

and protégé is not only restricted to political connectedness as such (see Hypotheses 2 and 3) but also entails proximity in the sense of party affiliation (for the same effect on management turnover see Boyne et al. 2010; Ennsner-Jedenastik 2014). As a consequence, we assume that minister and executive board members sharing the same political ideology have a significant influence on executive board compensation.

H3: A high degree of political proximity between executive board and controlling line ministry is positively related to the level of the executive board's compensation.

### **Empirical Setting: The Austrian Case**

The composition and compensation of the top management of state owned enterprises (SOEs) is under close scrutiny by the general public in Austria. The constant critique of the Austrian Court of Audit (*Rechnungshof*, e.g., 2011) has been echoed by organizations like *Transparency International* (e.g., 2009), as well as by the yellow press – albeit condensed in a more simple message: Public managers earn too much (“64 public managers earn more money than the Austrian Federal Chancellor”, *Neue Kronen Zeitung*; or “Public managers rake in cash during years of crisis”; *Der Standard*; both on December 28, 2011; all translations by the authors).

Austria is, for several reasons, an interesting case in examining empirically the core conceptual topics outlined above more closely. Although a federal state, it is nonetheless characterized by a strongly centralized system and by exceptional political stability (i.e., by predominantly grand coalition governments) since WWII. The country has had a great number of SOEs as a consequence of broad-scale nationalization in 1946 and 1947; due to their substantial role during Austria's post-war economic resurrection, privatization only began in the late 1980s, with the state remaining a major shareholder in many of these organizations. As

a consequence, public entities, as well as leading banks under considerable state influence, have controlled many of the relevant industries, and the country has developed a characteristic doctrine of party patronage (Ennser-Jedenastik 2014, Müller 1989, Treib 2012). Following the ‘Proporz’ logic, the control of the public sector was divided in proportion to the votes won in the general elections, initially more or less exclusively between the Social Democratic Party of Austria (*SPÖ*) and the conservative Austrian People’s Party (*ÖVP*). By the mid-1980s, this practice became increasingly problematic, and a major scandal that made obvious how the extent that public enterprises had to be subsidized with public funds marked the beginning of a wave of broad-scale privatizations. The trend may have been accelerated by Austria’s accession to the European Union in 1995, due to the union’s underlying skepticism towards state ownership (Alfonso and Papadopoulos 2013), and finally peaked in the early 2000s under a conservative-liberal government (Hammerschmid and Meyer 2005). While many of the formerly SOEs disappeared from the public sector due to such privatization, numerous others emerged as autonomous organizations in the wake of organizational decentralization. In fact, organizational autonomization and disaggregation (*‘Ausgliederung’* as agencification and corporatization) has been a core element of the public sector reform in Austria (Hammerschmid et al. 2012; Leixnering et al. forthcoming).

Austria is a highly embedded system with close links between the economic, social, and political elites (Höllner 2013). With the continued influence of political parties, Austria has been characterized as “the country of corporatism” (Traxler 1998), and has been portrayed, in Gourevitch and Shinn’s (2007) comparative study, as the opposite of the United States in terms of measures of institutional complementarity. Policy-making in a corporatist system is not so much based on pluralistic interest groups’ efforts to lobby and/or pressure the government as it is on actually integrating these groups in the policy-making process (Alfonso and Papadopoulos 2013).

Similar to Germany, Austria has a distinct continental European administrative tradition with an overriding legalistic *Rechtsstaat* philosophy, characterized by a strong public administration, a dominating legal logic (as exemplified by the legal background of many public sector executives), and a strongly hierarchical system with directives as the central principle governance mechanism (Baraldi 2014; Meyer and Hammerschmid 2010). Political party involvement in PSO directorates is generally taken for granted, and board positions are usually distributed between the governing parties not only across but also within different organizations (Ennsner-Jedenastik 2014).

### **Data and Method**

Our empirical sample consists of the full population of corporatized organizations – both under public and private corporate law – with 100 percent direct ownership by the federal state as of 2008 (N = 72). These organizations operate in a variety of policy fields (infrastructure, culture, tertiary education, agriculture/environment, regulation/control, or shared services) and are as diverse as the *Schönbrunn Zoo* or the Federal Debt Management Office. All organizations were either incorporated into the administrative apparatus prior to being granted the status of legal independence, or established anew. No nationalized, formerly private business organizations are included. In total, 724 board members (165 in executive boards, 559 in supervisory boards) are affiliated with these organizations. In addition to organizational-level data which were retrieved through analysis of corporate documents and publicly available reports and statistics (the Compass database, Commercial Register, Austrian Federal Ministry of Finance, or Austrian Court of Audit), we collected data on individual board members through extensive online and media research on their biographies and careers.

In order to test our hypotheses, we estimated a number of linear regression models using computation techniques in STATA. The dependent variable – *Compensation of the Executive*



*Board* – was constructed as the natural log of the average salary of an executive board member in the respective organization. We had to use the average pay per organization, as the only reliable source for this measure –the Austrian Court of Audit – only publishes these data in such an aggregate form. Average annual salaries per executive board member in 2009 range between € 63,900.00 and € 715,400.00 (mean = € 177,453.00, SD = € 93,486.00).<sup>2</sup>

A number of independent variables are employed in hypotheses testing. In a first step, the *Involvement of Core Administration* in the supervisory board was binary coded on the personal level (23.8 percent of the supervisory board members are delegates from the core administration, mostly from federal ministries). In a second step, it was aggregated on the organizational level (i.e., expressed as a percentage of the respective supervisory board). Similarly, the *Political Connectedness of the Supervisory Board* was first measured as a categorical variable (denoting the specific political party) on the personal level and then expressed as a percentage of the respective supervisory board. Employing a conservative coding approach<sup>3</sup>, we found political connectedness for 49.6 percent of supervisory board members.<sup>4</sup>

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<sup>2</sup> Full data on compensation to supervisory board members (i.e. the non-executive directors) of Austrian PSOs were not available. Supervisory board members are not involved in executive tasks, hence, this data is not relevant for studying executive compensation in our empirical context.

<sup>3</sup> Several definitions of political connectedness exist in the literature (for an overview, see Faccio 2006). Our approach was characterized by a step-by-step coding from formal to informal attributes of board members, including past or present activity in the political arena as represented by a political mandate, the membership in a political party, or the candidacy for election; well documented but ‘unofficial’ connections; or affiliations in the social partnership characteristic for the Austrian empirical context (e.g., Austrian Trade Union Federation, or Austrian Federal Economic Chamber).

<sup>4</sup> Note that directors in the supervisory board (i.e., the non-executive directors) can be both politically and administratively connected. In our data, 11.5 percent of delegates from the core administration are also politically connected.

TABLE 1: Descriptive Statistics

	Mean	SD	1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.
1. Legal Form	0.530	0.503	1.0000										
2. Policy Area: Infrastructure	0.130	0.333	0.3575	1.0000									
3. Organizational Size	5.354	1.744	-0.5488	-0.1210	1.0000								
4. Average Salary of Employees	3.772	0.306	0.2122	0.2699	-0.1488	1.0000							
5. Size of the Executive Board	0.653	0.606	-0.4877	-0.0916	0.6231	0.1171	1.0000						
6. Gender of the Executive Board	0.778	0.305	0.2464	0.2772	-0.0769	0.0533	-0.0858	1.0000					
7. Age of the Executive Board	3.951	0.134	-0.3995	-0.0552	0.2061	0.0384	0.1058	0.0152	1.0000				
8. Involvement of Core Administration in the Supervisory Board	0.256	0.263	0.4881	0.0546	-0.5254	-0.0468	-0.4962	-0.0614	-0.1827	1.0000			
9. Political Connectedness of the Supervisory Board	0.465	0.241	0.1157	0.2567	0.0799	0.0218	0.0221	0.1917	-0.2804	-0.1755	1.0000		
10. Political Connectedness of the Executive Board	0.404	0.426	0.3056	0.1354	-0.3852	0.2959	-0.3388	0.1354	-0.1852	0.1654	0.3317	1.0000	
11. Political Proximity between the Executive Board and the Line Ministry	0.227	0.366	0.3467	-0.0435	-0.2102	0.3227	-0.2155	0.2748	-0.1752	0.0385	0.2680	0.6665	1.0000

We reproduced this procedure for the operationalization of *Political Connectedness of the Executive Board*, indicating political connectedness for 33.3 percent of executive board members. Finally, in order to assess the *Political Proximity between the Executive Board and the Line Ministry*, we measured similarity as the percentage of executive board members that are affiliated with the same political party as the respective line minister in charge of controlling the organization.

In order to provide a more robust examination of our hypotheses, several control variables were included: We predict a positive association of *Legal Form* (binary coded, 0 = public law, 1 = private corporate law) and executive compensation, as the legal form can be perceived as a proxy for the marketization of an organization and the services it provides. Empirical evidence from the private sector (as discussed above) also suggests a positive association with the *Policy Area*; we therefore controlled for *Infrastructure* (binary coded, 0 = other policy area, 1 = infrastructure), a policy area in which a considerable number of private-sector firms is active. Scholarly literature as discussed above refers to *Organizational Size* (natural log of staff number) as a determinant that (positively) affects executive compensation. We also predict the *Average Salary of Employees* (natural log of average employee salary) to positively influence executive pay, since we expect an organization's overall compensation level to equally affect both top-management and employees. As the *Size of the Executive Board* (natural log of number of seats in the executive board) lowers the responsibility of individual executive board members, we predict this to be also mirrored by their compensation: For larger boards, we expect the overall expenditures for board compensation to increase, but the average sums paid to decrease. Evidence shows that *Gender of the Executive Board* (in percent of board members of the respective organization; 0 = all female, 1 = all male) affects pay in the sense that women's compensation is expected to be lower than men's ('gender compensation gap': Bertrand and Hallock 2001). Eventually, we predict *Age of the Executive Board* (natural log of average age

of executive board member of the respective organization) to positively influence executive compensation, since in the public sector, seniority can be expected to be mirrored in salary. Table 1 gives basic descriptive statistics and correlations for the variables employed. No multicollinearity issues were detected (mean VIF 1.93; highest individual VIF 2.64; condition number 4.16).

## Results

Table 2 displays the six linear regression models we employed to test our hypotheses. Model I shows results for control variables (i.e., the base model). Models II through V, then, individually examine the arguments set out in our four hypotheses, while model VI represents a full model. *Political Proximity between the Executive Board and the Line Ministry* is a special case of *Political Connectedness of the Executive Board*. Thus, in the full model, we run only the variable with the higher impact on the dependent variable.

All independent variables add explanatory value at a significant level during individual testing; our hypotheses, thus, are confirmed. In particular, the political similarity between executive board and line ministry, as well as the political connectedness of the supervisory board best explain high executive compensation. Moreover, representation of the core administration has a negative impact on executive pay.

In addition, results for a number of control variables complete the picture (see models I through VI). In particular, and as predicted, activity in the policy area of infrastructure, organizational size, and the overall salary level of employees prove to be predictors for higher executive compensation, while the number of executive directors is negatively associated with

TABLE 2: Linear Regression Models

	Model I	Model II	Model III	Model IV	Model V	Model VI
1. Legal Form	0.128 (0.123)					
2. Policy Area: Infrastructure	0.298* (0.141)	0.357** (0.126)	0.233† (0.123)	0.352** (0.124)	0.452*** (0.117)	0.359** (0.118)
3. Organizational Size	0.079* (0.034)	0.047 (0.033)	0.060* (0.029)	0.083** (0.030)	0.070* (0.028)	0.048† (0.028)
4. Average Salary of Employees	0.390* (0.153)	0.398** (0.144)	0.440** (0.135)	0.303* (0.147)	0.186 (0.141)	0.230† (0.136)
5. Size of the Executive Board	-0.258** (0.097)	-0.336*** (0.091)	-0.285** (0.083)	-0.238** (0.089)	-0.208* (0.083)	-0.253** (0.081)
6. Gender of the Executive Board	0.049 (0.146)					
7. Age of the Executive Board	0.210 (0.352)					
8. Involvement of Core Administration in the Supervisory Board		-0.405* (0.186)				-0.280† (0.163)
9. Political Connectedness of the Supervisory Board			0.606*** (0.163)			0.363* (0.162)
10. Political Connectedness of the Executive Board				0.293** (0.106)		
11. Political Proximity between the Executive Board and the Line Ministry					0.495*** (0.111)	0.384** (0.113)
Constant	2.393† (1.439)	3.610*** (0.604)	2.984*** (0.552)	3.493*** (0.576)	3.979*** (0.552)	3.901*** (0.560)
R <sup>2</sup>	0.315	0.346	0.420	0.372	0.461	0.530
Adjusted R <sup>2</sup>	0.240	0.297	0.376	0.324	0.420	0.478
N	72	72	72	72	72	72

† p < 0.1 \* p < 0.05 \*\* p < 0.01 \*\*\* p < 0.001 (two-tailed test)  
Standard errors in parentheses

above-average compensation. The legal form of the corporation as well as gender and age of the executive board members do not have a significant effect on compensation.<sup>5</sup>

### **Discussion of Findings and Implications**

We started this article with the question of whether political connectedness may serve as a governance tool to re-install the democratic legitimation and accountability and counteract policy fragmentation (Flinders and Matthews 2010; Kopecký et al. 2012). We have contrasted this positive view of political patronage to the more popular assumption that patronage serves as reward for political minions, and have argued that a close look at executive compensation may help to distinguish between the two types of political connectedness. In our empirical study, we not only find a highly significant positive relationship between political connectedness and executive compensation, but also that social similarity in terms of shared political party affiliation even exceeds political connectedness as an explanatory factor. Our study also shows that representation of members from the public administration on the supervisory board has a significant negative effect on executive compensation. Below, we discuss conceptual implications of these findings and conclude with some considerations for public sector management.

#### **Political Connectedness via Different Forms of Social Similarity**

According to the seminal work by Lazarsfeld and Merton (1954), connectedness can be grounded on ‘value-homophily’ or on ‘status-homophily’. While the former is built on the

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<sup>5</sup> Although conveying the full population, the relatively small N might be of statistical concern. In order to build a parsimonious model, we keep the degrees of freedom available as large as possible. Consequently, we drop control variables with no significant impact in Model I (they also show no significant effect when added in Models II through VI).

consensus of ideas and beliefs among members of a circle, the latter is ‘value-heterophilous’ and based on utilitarian considerations. Here, the linking mechanism is the pursuit of interests, and the very aim of such status-based circles is the maximization of its members’ benefits. Building on this distinction, social similarity can be either value-based or interest-based.

From an ‘idealist’ standpoint, political parties display all relevant characteristics of value-based groups, such as a distinct and explicit set of fundamental values, ideological beliefs, and ideas about a preferred social and political order. However, given their access to power and opportunities to position their members in attractive positions, political connectedness does not necessarily imply the adherence to a party’s fundamental set of values, but may simply embody an appropriate strategy to find privileged access to all kinds of opportunities. This inherent ambiguity of political connectedness holds especially true for board appointments in SOEs: On one hand, it may serve as a politically re-embedding governance tool that ensures policy coherence, as it puts members of an in-group in executive roles who represent values and ideological beliefs which are legitimated by representative democracy. On the other hand, political connectedness may simply mean that profit-oriented in-groups distribute offices and directorates among their clientele in order to maximize their social prestige and income and to secure loyalty. Following Lazarsfeld and Merton’s (1954) insight that value-homophily and value-heterophily have to be treated as matters of a degree of (dis-)similarity, we suggest that the impact of political connectedness on executive compensation actually serves as an indicator of the type of the underlying politically connected in-group: The stronger the impact of political connectedness on the monetary compensation, the higher the degree of status homophily, and the lower the degree of value homophily.

In our empirical study, we found political connectedness to be an essential explanatory variable for the level of executive remuneration. Building on the discussion above, we interpret

this as a strong indicator for the reward component of patronage being at work. Underlining this interpretation, when testing Hypothesis 4 we find that this effect is even stronger when similarity is not restricted to political connectedness as such, but also entails consensus in terms of proximity to a specific political party. This is in line with Ennser-Jedenastik's (2014) study in which he finds that party affiliation of PSO managers with government, opposition, or line minister determines the length of their tenure.

We find a reverse effect – negative impact on compensation – for public administration representation in supervisory boards. Given the fact that officials may – notwithstanding their specific public servant ethos – also display personal ties to party networks, our results suggest that public administration constitutes an in-group relying strongly enough on shared values (Byrkjeflot and du Gay 2012; du Gay 2000; Meyer et al. 2014) that this kind of homophily outweighs status-related elements that may arise from the political connectedness of some of its members (i.e., self-interest).

In order to answer our initial question whether political connectedness of PSO board members is a manifestation of democratically legitimated control and, thus, a signal of responsible state ownership, or whether it is rather a manifestation of undue favoritism, we have argued that it is necessary to distinguish between the two types of connectedness: Value-based connectedness and interest-based connectedness. We have further proposed to take the link between politicization and executive compensation as an indicator for the type of political connectedness at work in a particular case. Political connectedness has the potential to serve as governance tool when it is predominantly value-based: In this case, it may contribute to the political embeddedness of the respective organization through the involved individuals' social ties (Granovetter 1985; Zukin and DiMaggio 1990). But when, as in our empirical study,



interest-based connectedness outweighs the value-based, political connectedness manifests reward-driven patronage.

### **Implications for Public Sector Governance**

Despite all attempts to de-politicize and ‘marketize’ PSOs, the formal right to nominate boards of directors and, consequently, to set their level of compensation has remained with the political sphere. De-politicization has, thus, been more an ‘arena shifting’ (Flinders and Buller 2006). However, organizational disaggregation and the emergence of legally independent and more business-like, corporatized organizations have resulted in a multiplication of such board positions that need to be filled. In addition, through corporatization, the former compensation limits were removed, since legal qualification requirements and formal remuneration schemes valid for the public administration were no longer applicable to such positions.

Board members are not nominated by parties, but by individual political actors. The role of political parties in controlling patronage is declining (Kopecký and Mair 2012). Political networks that are no longer primarily ideological, but are tied together by personal allegiances: politically driven appointments usually “take place through personal networks rather than the party hierarchy or party apparatus” (Kristinsson 2012). Recent research (Ennsner-Jedenastik 2014; van Thiel and Yesilkagit 2011; Yesilkagit and van Thiel 2008) has suggested conceiving PSO executives as part of a delegation chain or cascade that runs from the citizen as the democratic principal via parliament, government, and the individual minister to the respective acting official or manager. The greater the distance from the chain’s top (i.e., the more extended the delegation is), the weaker the formal control and the more leeway for personalized reward-driven patronage. Scholars may have recently linked party patronage more closely to the control component of patronage (Treib 2012) and construed the reward component as its by-product at best (Kopecký 2012). However, and despite the emerging significance of individual political

actors in patronage (rather than political parties), our findings strongly suggest not to think of the reward component as an outdated phenomenon at all. In a similar vein, Ennser-Jedenastik (2014, 138) concludes that “attempts at diminishing the influence of party politicians over the public sector through the introduction of new public management reforms may even have contributed to a rise in politicization.”

What measures could be taken to reduce interest-driven patronage? One option would be to reduce discretion around compensation, either through the re-introduction of remuneration schemes and upper limits – comparable to the remuneration schemes of top civil servants, politicians, or remuneration in private sector companies –, or by linking compensation to performance indicators. The former, more in line with a ‘rediscovery’ of the virtues of bureaucracy (Byrkjeflot and du Gay 2012; du Gay 2000; Olsen 2008), would re-align corporatized units with those units that are not legally independent and, thus, run under the public sector regime. The second – performance-based remuneration schemes – has proven difficult to implement in PSOs, although the mediating effect of performance on politicized directors’ fortune has been called “a strength rather than a weakness of a system of democratic government“ (Boyne et al. 2010, 151). Notwithstanding recent empirical evidence for positive effects of corporatization on organizational performance (Bilodeau et al. 2006; Kang and Kim 2012; Nelson and Nikolakis 2012), and the negative influence of politicization (Lewis 2007; Menozzi et al. 2011; Vining 2011), the limitations of such a perspective must not be neglected. Facing skepticism that the ‘performance paradox’ (Meyer and Gupta 1994; van Thiel and Leeuw 2002) can be overcome, even its advocates had to admit that such evidence is mostly confined to operational efficiency, as well as to economic and market performance, and does not include effectiveness or impact measures. In the public sector, due to its character as a political construct, ‘good’ or ‘bad’ performance may though be perceived differently by various stakeholders (Andrews et al. 2010; Boyne and Dahya 2002). A managerialist performance-

dominated approach may also reinforce self-interested tendencies among PSO managers and crowd out the culture of public service honesty (Christensen et al. 2013). In addition, a focus “on managerial performance rather than on political responsiveness” may let managers implement strategies that are politically undesirable, as some political programs can be more easily realized in an economically efficient way than others (Peters and Pierre 2004, 285). Taking into account the immense diversity of PSOs (e.g., in terms of relevant stakeholders, forms, functions, or profit orientation), the development of suitable and multi-dimensional performance indicators (and related incentives) will remain a highly complex endeavor (Boyne et al. 2006).

### **Concluding Remarks**

This article adds to recent strands in public (corporate) governance literature that aim at explaining executive compensation, party patronage, and political connectedness as a governance tool. Our study makes a threefold contribution: First, we contribute to executive compensation literature in general, as we provide empirical evidence for the importance of social/psychological aspects rather than economic/rational determinants to explain executive compensation. In doing so, we also shed light on the under-researched field of management pay in PSOs. Second, we contribute to recent literature on party patronage: Our study clearly demonstrates that the reward component of party patronage has not at all disappeared. Third, we contribute to public governance literature that has recently brought forward the idea that political connectedness and patronage may serve as a governance tool. Building on work on value-homophily and status-homophily, going back to Lazarsfeld and Merton (1954), we argue that the close link between political connectedness and executive compensation points rather at the latter being at work. This makes it doubtful as to whether politicization is able to re-align

decentralized units with the democratically legitimated and accountable representatives and reinstall policy coherence.

There are, obviously, boundary conditions and limitations to our empirical study that, at the very same time, create opportunities for future research. The Austrian empirical context provides both an excellent setting for the study of politicization as well as a constraint in terms of generalizability of results; comparative empirical research designs could add robustness to our findings. It would be also particularly insightful to see studies where no link between political connectedness on executive compensation can be shown. Due to data access restrictions on executive remuneration in Austria's public sector, the unit of analysis in statistical testing has been the organization, and not the individual board member; this fact might weaken the claims we can make in our discussion, and again calls for studies in fields where this restriction does not apply.

In closing, we return to our point of departure: the unsolved dilemma of the call for de-politicization of public sector management versus the demand that nation states adequately perform their role as principal and 'public shareholder'. The question remains in what way the paradox of honoring both – the promise of de-politicization *and* recent attempts to overcome policy fragmentation – can be resolved. How can the major challenge be met “to find a balance between the state's responsibility for actively exercising its ownership functions, such as the nomination and election of the board, while at the same time refraining from imposing undue political interference in the management of the company” (OECD 2005, 3; see also OECD 2010)? Or, in other words: How can the re-vitalization of politics be achieved when, at the same time, favoritism has to be minimized? On a conceptual level, our study provides an approach to distinguish between the two types of political connectedness by modeling the association of political connectedness and executive compensation. On a more practical level, it prompts the

problematization of such an association where present, and the consideration of means that are able to reduce it.

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