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## WE'RE ALL IN THE SAME BOAT, BUT I HAVE A BETTER SEAT: THE PERFORMANCE IMPACT OF PAY GAPS IN NEW VENTURES (SUMMARY)

David Gras

*Texas Christian University, USA, d.gras@tcu.edu*

Luisa Delgado-Márquez

*IE Business School, Spain*

Garry Bruton

*Texas Christian University, USA*

Julio de Castro

*IE Business School, Spain*

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≈ SUMMARY ≈

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*David Gras, Texas Christian University, USA*  
*Luisa Delgado-Márquez, IE Business School, Spain*  
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*Julio de Castro, IE Business School, Spain*

### Principle Topic

A key set of decisions in the new venture formation process revolves around how to establish appropriate and motivational pay levels for members of the business (Wasserman, 2006). New ventures must decide whether the organization should adopt a relatively flat rewards structure wherein there are small differences in pay between those making the most in the organization and those making the least, or a more hierarchical structure wherein there are substantial pay gaps between top-earners and bottom-earners (Henderson & Fredrickson, 2001). Extant research provides equivocal guidance on the topic. In particular, behavioral theories of deprivation and tournament theory are at odds when it comes to the performance effects of pay gaps. With this study, we bring these contrasting theoretical perspectives more into alignment through the examination of their boundary conditions. Specifically, we argue that new venture organizational forms which inherently engender cooperation may reap the benefits of pay gaps without compromising cohesion and functionality in new ventures. We further argue, based on distributive justice literature (Forsyth, 2005), that this positive relationship between pay gaps and performance in cooperation-oriented new ventures will be moderated by the following factors: 1) business informality, 2) the business's involvement in larger social movements, and 3) size of the business. Specifically, organizational members in new ventures will view pay gaps as less fair in informal (those not registered with the government) businesses, those heavily involved in broader social movements, and smaller businesses. Perceived injustice in organizations with these characteristics is expected to dampen the positive effects of pay gaps on cooperative new venture performance.

### Methods

We test our hypotheses in the context of highly cooperative organizational forms; namely businesses in the solidarity economy. In 2009 and 2010, the Brazilian government conducted a study on 20,000 solidarity organizations, and our sample consists of new ventures in the resulting database. Our performance variable is captured by profit, the pay gap variable is the difference between the highest and lowest paid members, and the moderators reflect extant measures of similar concepts. We employ instrumental variable regression to test out hypotheses.

### Results and Implications

Results indicate support for our hypotheses on the positive effect of pay gaps on new solidarity business performance, as well as the predicted moderating effects of informality and size. The hypothesized social movement moderator is in the direction predicted, and partially significant. Our study has implications for both theory and practice. Regarding theory, extant behavioral theory suggests that pay gaps are detrimental for team and firm performance (Martin, 1998). We demonstrate that this prediction does not hold for cooperative new ventures. Specifically, we provide evidence for a substitution-effect whereby teams may retain cohesion and functionality in the face of pay gaps if alternate factors, such a cooperation-oriented mission, motivate members. Moreover, we identify new contingencies in this relationship. Regarding practice, we provide guidance to entrepreneurs on structuring their reward systems to maximize performance, and the conditions under which these reward systems are applicable. Moreover we set the stage for a wealth of potential future research on the antecedents of performance for an impactful, prevalent, and understudied organizational form.

**CONTACT:** David Gras; d.gras@tcu.edu; (T) +1-817-257-4267; Neeley School of Business, TCU Box 298530, Fort Worth, TX, 76129, USA.