

Messing with corporate heads? Psychological contracts and leadership integrity.

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Introduction

Now, more than ever, corporate leaders need to demonstrate the leadership required to successfully lead their organisations, practice the high levels of corporate ethics expected, and empower every employee to achieve the extraordinary. With an unsettled socio-economic environment, as well as uncertainty and leadership crises in both business and the community at large, it's critical to forge a better understanding of the factors that impact leaders and their constituencies. This article offers senior and middle managers, HR professionals, consultants and academics a new way of thinking about leadership and how to achieve extraordinary outcomes by using an actionable research-based model based on the psychological contract.

Organisational leaders face complex situations with inherent conflicts. Coupled with these challenges is growing concern that we are experiencing a leadership crisis, with leaders exhibiting corrupt, self-indulgent, and even evil behaviours. Increasingly, leaders appointed to resolve problems are engaging in practices that contribute to societal problems. Some leaders will seek leadership roles to fulfil a psychological desire to control or to manipulate. Others simply don't care about the ethical implications of leadership decisions. Now, more than ever before, ethical and extraordinary leadership is required.

Researchers have promoted several approaches in response to these complexities. This paper presents a leadership model to fulfil existing needs: the Leadership Psychological Contract (LPC) in which leader's relationship with all stakeholders is paramount. The psychological contract (PC) has been recognised as one of the most promising areas in organisational research. However, its contribution to the leadership domain remains under-investigated. This paper targets this deficiency by reviewing and integrating the best approaches of contemporary leadership and PC literatures. Further, the model presented in this paper addresses two major deficiencies of previous approaches: (1) the scarce leadership research conducted at the unit/team level and (2) the impact of leaders on followers' emotions and extra motivational behaviours.

This article aims to improve the practice of extraordinary and ethical leadership for the 21st Century by contributing a leadership psychological contract model of thought leadership. In a nutshell, by focusing on the relational exchange between leaders and followers, as the true nature of leadership, our LPC is a predictive model made up of seven critical measures: fulfilment of expectations, trust and fairness (which constitute the 'health' of the contract – the leader's credibility), commitment, satisfaction, discretionary effort, and innovation (which constitute the 'consequences' of the contract – the leader's impact).

Contemporary Leadership Approaches

Leadership is one of the most discussed and researched topics in management, across a wide range of disciplines. Not surprisingly, leadership research has produced more models than any other behavioural science. In the past 20 years, several distinct leadership approaches have emerged to address the current leadership crisis, including authentic leadership, transformational leadership, servant leadership, and ethical leadership. Key similarities underlying these positive forms of leadership are “concern for others” (altruism) and “integrity”. The similarities among servant leadership, transformational leadership, charismatic leadership, spiritual leadership and authentic leadership, include a “positive moral perspective” and “positive social exchanges”, and “leaders’ self-awareness of values, thoughts and emotions”.

Two further major similarities emerge when examining positive leadership approaches. The first is that the relationships leaders have with their followers are critically important in demonstrating concern and establishing trust. The second is that the leader demonstrates integrity. It stands to reason that positive leadership approaches could benefit from an understanding of the psychological contract between leaders and followers, seeing that it focuses on positive social exchanges and integrity.

Contemporary Leadership Approaches and the Psychological Contract

A central element of contemporary leadership approaches is the relationship between leaders and followers. Yet, despite the recent recognition that promoting psychological contracts through leadership is the missing link between HR strategy and organisational performance (McDermott *et al.*, 2013), to date, no contemporary approach to leadership has explicitly considered using the psychological contract as a framework to fully understand this leader-follower relationship.

The concept of psychological contracts (PC) has received considerable attention in the last 20 years. In this paper, we define and assess the validity of a leadership psychological contract model believing that it promotes positive and ethical leadership, and incorporates measures of leader credibility, integrity, and influence. This model is based on Guest’s (1998) causal model of the psychological contract. It is predictive in nature and includes antecedents, mediating and outcomes variables.

The term ‘psychological work contract’ was first coined by Argyris (1960) to explain the implicit agreement between employers and employees. This includes the mutual obligations, values, expectations, and aspirations, beyond those set out in a formal written employment contract. Evolving from social exchange theory (Blau, 1964), the PC is an implicit understanding of social expectations between individuals. Rousseau (1989) defines the PC as a reciprocal understanding between an individual and organisation encapsulating unexpressed beliefs, promises, expectations, responsibilities, and obligations of employees with regard to a fair employment relationship. Although some of these elements can be stated clearly in formal written contracts, it is more common for them to be implied.

There are two main types of PC contracts: transactional and relational. Transactional contracts relate to expectations or obligations that are quantifiable, objective, and generally shorter-term and static in nature. These often focus on financial agreements and compensation issues. Relational contracts imply an exchange of socio-emotional factors, such as support or loyalty, as opposed to a financial exchange. The obligations and expectations are intrinsic and emotional in nature. Relational contracts are often subjective, less tangible, longer-term, and dynamic.

Relational and transactional PCs are not mutually exclusive. A single PC can include elements of both types of contract. The terms psychological contract breach or violation (PCV), which are used interchangeably, refer to employees' beliefs that the organisation has failed to uphold promises or obligations. In turn, this fosters negative work attitudes, emotions and behaviours. Conversely, PCs are intact when individuals perceive their employer has upheld their promises or obligations. In such cases, employees have relatively strong and generally fulfilled PCs, and it is expected they will be highly committed, satisfied and engaged (Rousseau, 1995).

A recent review of leadership research spanning 25 years (Hiller *et al.*, 2011) identifies transformational leadership and leader-member exchange (LMX) theory as the most common approaches directly investigating the relationship between leadership and performance. Transformational leadership aims to inspire followers to achieve results beyond expectations and involves four sets of behaviours: (1) idealised influence (charisma); (2) inspirational motivation (vision); (3) intellectual stimulation (e.g. encouraging creativity and innovation); and (4) individualized consideration (e.g. demonstrating concern for follower well-being). Transformational leadership works via relational contracts, which imply a social exchange beyond financial rewards or contractual relationship agreements. In contrast, transactional leadership focuses on the materialistic aspects of the exchange relationship between the leader and follower.

LMX theory enriches this leader-follower discourse by expressing that leaders could develop relationships of varying quality with followers through various practices and reward systems. LMX, like psychological contract theory, is based on social exchange theory. The first stage of LMX starts with followers taking roles where the relationship is scripted and of a low-quality. The second stage is role-making, in which the leader and follower begin to negotiate roles and expectations. The third stage, routinization, occurs when the follower has earned the leader's trust. Roles are flexible, and the leader can rely on the follower. Working through these three phases is referred to as "leadership making." The latter represents the highest quality LMX relationship. High quality LMX is associated with followers having greater satisfaction with their jobs and lower turnover intentions.

Worthy of note is the fact that researchers have not explicitly considered the role of the psychological contract within each of these approaches. This paper addresses this gap. Firstly, it extends past research of LMX, transactional leadership and the PC in investigating their link to follower performance. Secondly, it provides a new framework to better understand and manage

effective leader-follower relationships. Thirdly, it addresses various criticisms and recommendations made in the literature, including Hiller *et al.*'s (2011) call for more varied approaches in investigating leadership outcomes, and to study the impact of leaders and leadership on emotional constructs.

The Leadership Psychological Contract

Psychological contracts (PCs) provide an analytical framework for studying relationships within organisations. However, they present an inherent 'agency problem' (Guest, 1998). A traditional employment contract is usually signed between the employee and an 'agent' or 'representative' of the organisation. The PC literature, however, refers to the contract between the employee (an individual) and the organisation itself. The problem with this is that PCs can then be projected onto multiple members within the organisation (senior and middle managers, supervisors, HR officers, colleagues) who do not necessarily communicate a consistent or uniform set of expectations. This leads to uneven or mixed expectations from the different parties involved. Some authors (e.g. Rousseau, 1995) have attempted to deal with this problem by 'humanising' the organisation, which is then treated as 'individual'. To our thinking, however, this does not solve the 'agency problem', since employees still can choose from a range of representatives when thinking about their relationship with the organisation. The LPC solves this agency problem by clearly identifying the employee's immediate leader as the key contract maker and individual with whom the PC is actually held.

Further, the LPC adds value to the leadership literature by integrating LMX, transactional leadership and other contemporary leadership approaches (positive, ethical and authentic leadership). Positive leadership approaches, such as authentic leadership, emphasise the relationship between leaders and followers. As positive leadership approaches continue to evolve, the LPC model provides a useful analytical cause-effect framework that enhances theoretical developments. This paper seeks to present a deeper understanding of positive and ethical leadership by establishing a compatible model of leadership - the leadership psychological contract. The LPC model is based on Guest's (1998) causal model of the PC, which claims to have some predictive power.

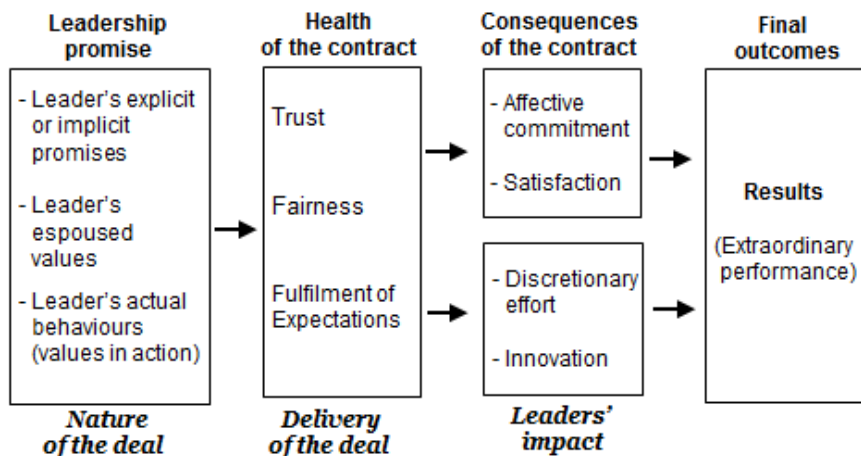
Given that leaders represent their organisation in the employer-employee relationship, when applying the LPC model to the leader-follower relationship, the following components need to be appreciated:

- The leadership promise includes the leader's explicit or implicit promises, principles and espoused values, as well as the leader's actual behaviours or values in action. This component constitutes the contract makers of the LPC (or the nature of the deal offered by the leader), as shapes the followers' expectations and establishes the leader's obligations. This first component provides the assessment criteria against which followers will make judgments, in order to ascertain the health of the contract or delivery of the deal (the leader's integrity and credibility) – the next component of the LPC.

- The health of the contract, or delivery of the deal, reflects the extent to which the leadership promise has been fulfilled or the contract has been delivered. This includes the followers' assessment (a cognitive response) to the leader's behaviour, when compared to their expectations or perceived obligations of the leader. That is the followers' perceptions of the leader's delivery of promises, expectations and/or perceived obligations. This component constitutes the leader's integrity and credibility which is operationalised by measuring three independent variables: the follower's perception of the extent to which the leader has fulfilled the obligations, levels of trust and fairness.
- The third component of the LPC constitutes the consequence of the contract or *the leadership impact* of the leader. It refers to followers' emotional and behavioural responses to the health of the contract or delivery of the deal. The followers' emotional response is operationalised by measuring two mediating variables: affective commitment and satisfaction. The followers' behavioural response is measured using two outcome variables: discretionary effort and innovation.
- The fourth and final component refers to results that take the form of extraordinary performance, as opposed to ordinary, mediocre, average or expected. They are also referred to as game breaking results within certain industries and relate to accomplishing results that are unprecedented.

Figure 1 diagrammatically summarizes these components.

Figure 1. Theoretical Framework for the Leadership Psychological Contract (LPC)



As the LPC integrates these key measures into a predictive 'cause and effect' model, it enables valid and reliable measurement, diagnosis and reporting of leader-follower relationships. Results provide a clear indication of any deficiency areas and clarity in recommending corrective action.

The LPC incorporates the unexpressed beliefs, promises, expectations, responsibilities, and perceived obligations of leaders towards their followers. These drivers of the LPC have two main components: the leaders' espoused values or principles; and the leaders' actual behaviours (values in action) when measured against the leader's espoused values or principles. Michie and Gooty (2005), for example, suggest that authentic leaders will hold self-transcending values. This includes universal values that apply to humankind (social justice, equality and broadmindedness) and benevolent values (e.g. honesty, responsibility and loyalty) that apply to followers and associates. In the LPC, benevolent values may be particularly important to the leader-follower relationship. Leaders, who exhibit this approach, are likely to treat followers in a way that is consistent with these values as part of their leadership promise.

Leaders using this approach would likely convey these as part of their leadership promise. In other words, followers would expect the leader to act according to these values and refrain from actions that contradict them.

The next section defines the key seven actionable and measurable variables (three antecedents, two mediator and two outcome variables) that comprise the LPC model, and can be measured via a survey.

Meeting of the Minds

This meeting of the minds refers followers' mental or cognitive response to the leader. It refers to the assessment that followers make about the congruence between the leader's promise and the leader's actual actions – *Does our leader walk the talk? Is our leader putting her/his money where her/his mouth is?* The responses to these questions constitute the health of the contract, or *delivery of the deal*. Its currency is the credibility of the leader. We measure it using three independent variables: fulfillment of expectations, trust and fairness. In turn, they will determine the consequences of the contract or leadership impact.

Fulfillment of Expectations

This variable measures the degree to which the leader delivers the promises, expectations, and/or obligations that the followers recognise as part of the contract. 'Met expectations' are often measured in psychological contract models as contract fulfillment and contract breach. Within the context of the LPC model, 'met expectations' is the first antecedent, from which trust and perceptions of fairness are based. Studies on both met expectations and PCV show that the degree to which leaders meet the expectations of their followers is associated with organisational commitment (e.g. Coyle-Shapiro and Kessler, 2000).

Trust

Trust involves a willingness to be vulnerable, an expectation that one's interests will be considered in their absence, and an assessment of the leader's intentions, character and integrity. Within the scope of the LPC model, trust is conceptualised as a cognitive variable, reflecting issues such as the reliability, integrity, and honesty (McAllister, 1995). The degree to which followers can anticipate the leader's actions and decisions, as well as the extent to which these

are aligned with expectations, are critical for workable contracts. Trust decreases when violations occur, weakening the relationship.

Fairness

Fairness directly relates to organisational justice and explains various organisational behaviour outcome variables. Perceptions of fairness influences employee citizenship behaviour. Organisational justice is a moderator in the relationship between psychological contract breach and work-related attitudes and behaviours (Kickul, Lester and Finkl, 2002).

The Mediating Role of Emotions

This mediating role of emotions refers to the depth and power that the emotions play in establishing a strong connection or bonding between leaders and their followers – ‘the meeting of the hearts’. This followers’ emotional response to their leaders comprise the emotional part of consequences of the contract or *leadership impact*. We measure it using two well-recognised constructs in the literature: affective commitment and satisfaction.

Affective commitment

Affective commitment refers to the followers’ positive emotional attachment to the leader, identification with the leader and involvement with the leader in pursuit of common goals. A follower who is strongly committed identifies with the values, principles, purpose, and goals of the leader and actively desires to be a follower. Commitment can heighten employee engagement, which in turn motivates employees to increase their discretionary effort (Shuck *et al.*, 2011). Affective commitment can be an important mediator between effective human resources practices (e.g., fair rewards and empowerment) and employee organisational citizenship behaviours.

Satisfaction

Employees tend to attribute satisfaction to the unique leadership style of their leader and the sense of achievement derived from it. It is both an outcome and motivator. More broadly, satisfaction is an emotional state reflecting a positive response to the working situation at hand. Satisfaction and affective commitment are related, with employees who are satisfied experiencing higher levels of affective commitment (Michaelis *et al.*, 2009).

Extraordinary Behavioural Outcomes

These outcomes refer to the focused, intense, relentless and creative action that is unleashed as a result of the bonding between leaders and followers – It’s about ‘moving mountains’. This constitutes the action part of the consequences of the contract or *leadership impact*. We measure it using to two well-established constructs: discretionary effort and innovation.

Discretionary effort

This describes performance (behaviours, actions or activities) in which individuals go beyond the call of duty (‘run the extra mile’) or exceed normal demands, requirements or expectations of their job. Discretionary effort is likely to add value to any team. Shuck *et al.*

(2011) examined the relationship between affective commitment and discretionary effort by surveying a sample of employees across multiple industries. They found that affective commitment was linked to discretionary effort through a mediating variable: employee engagement. A major criticism of leadership research is that it neglects “extra-role” performance as a key follower outcome (e.g., Podsakoff *et al.*, 1996). The LPC also addresses this deficiency by incorporating discretionary effort as an outcome variable.

Innovation

In this context, innovation refers to innovative behaviour. This relates to followers’ orientation towards innovation and change and is associated with the likelihood of team members generating and/or adopting new ideas and/or practices. Further, innovation relates to perseverance with the implementation of new and promising ideas and higher levels of thinking. Recent research (Ng *et al.*, 2010) suggests that psychological contract breach is associated with decreases in innovative behaviours as employees’ lose commitment towards the organisation.

LPC as a strategic leadership tool

In concluding, we would like to reiterate that managing leadership psychological contracts (LPCs) are the key to successful strategy execution and achieving organisational performance beyond business as usual. Therefore, LPCs become part of any organisation’s strategic leadership agenda, which is aimed at progressively enhancing firm performance, sustaining competitive advantage and capturing growth opportunities, while maintaining solid profitability.

The LPC model aims to enhance the value of effective and ethical leadership approaches. Models such as authentic leadership, ethical leadership, moral leadership, servant and spiritual leadership emphasise positive leader-follower relations. The LPC model complements previous models of leadership and addresses various criticisms and recommendations made in the literature. Incorporating the LPC model in the exercise of strategic leadership will bring about a refreshed approach and a new generation of respected ethical leaders capable of creating sustainable organisations.

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