The ethical downside of hiring based on internal referrals

Increasingly, organizations are turning to referral-based methods to hire new employees (i.e. "recommend a friend/acquaintance"). In fact, these practices are estimated to account for up to 50 per cent of new hires and some organizations pay up to $20,000 to people referring someone they know for a job. The practice itself is relatively simple – it consists of a hiring manager making selection decisions after receiving a recommendation concerning a particular candidate from a referrer (usually a fellow employee).

Research has shown that referral practices are cost-effective and often result in more positive consequences for both the new recruit and the hiring organisation. Employees recruited through referrals have longer organisational tenure, better performance at work, and higher levels of job satisfaction. It occurred to us, though, that referral practices have rarely been examined using an ethical lens, even though anecdotal evidence suggests that it is a practice that potentially represents morally murky territory in which special interests and the exchange of favours can dominate, above and beyond the merit of a candidate.

We identified a major and non-obvious factor to explain organisational members' reactions to referral-based hiring decisions: the relative power of the referrer to the hiring manager who accepts the referral. Though lay wisdom would suggest that referrals from high-power individuals carry more weight than those from low-power individuals, and this approach makes sense from the job candidate's perspective, accepting a referral from a high-power employee potentially opens up the hiring managers to being perceived as engaging in immoral activities.

For example, a 2015 investigation by the U.S. Securities and Exchange Commission into the investment bank J. P. Morgan revealed that powerful employees at the bank, such as senior executives, were referring the sons and daughters of Chinese businessmen and businesswomen for coveted jobs. This established ongoing system led the bank's current employees to feel resentful – especially during the 2008 financial crises, when banks were laying off employees but continuing to retain some of those who received high-power referrals. It is possible that if the referrals had come from less powerful employees at J. P. Morgan, they would not have elicited the same reaction.

We theorised that when hiring managers act on a referral from within the organisation, a situation is set up where they are potentially doing a favour for the employee who made the referral, who becomes obligated and indebted to them. When they accept a referral from a powerful employee, an observer is more likely to believe that they are attempting to increase how indebted that employee is to them, ultimately opening the door for future benefits (such as better job assignments, higher performance evaluations, higher raises). This will result in a harsher moral judgment of the hiring managers and less support for their hiring decisions. By definition, hiring managers have less to gain, personally, when a low-power employee is indebted (relative to a high-power employee), making attributions of power-related ulterior motives less likely.

We conducted three studies:

In one of them, we recruited full-time employees and told them that they would be helping us pilot-test a virtual hiring committee process. Employees were told that they would be working with a four-person hiring committee but that their collective decision would affect a real hiring decision. In reality, participants were connected virtually through a chat platform to a research assistant who played the role of other committee members using different screens.

We asked participants to review the resumes of four applicants and to select their top candidate. After making their decision, they were presented with information that the hiring manager in the committee had decided to hire a candidate they did not select, following the referral from either a low or high power person on the committee. Previously, during the chat, the referrer, played by the research assistant, had pretended to incidentally know one of the candidates, who told them they were applying for that specific job. We manipulated power by telling participants that one of the referrers was simply a "note taker" (low power), while another referrer had the ability to determine additional rewards for everyone on the committee once the study was concluded (high power).

For another study, we targeted employees who had witnessed referral-based hiring decisions within their organisations. We asked them to recount this experience and rate how much power the referrer had compared to the hiring manager. Following this, we assessed how self-interested they viewed the hiring manager, immoral judgments of the decision, and how much they supported the decision.

In **a third study,** we asked people to provide the actual names of their company's hiring manager and of two other employees, one who had less power and one who had more power than the hiring manager. Two weeks later, we followed up with these people and had them read a story, using the same names that they previously provided, about the hiring manager accepting a referral from either the low power or the high power employee. Across all studies we found support for our theory that when the hiring manager accepts a referral from a high power referrer, participants/employees are more likely to view the hiring manager as acting out of self-interest, they more harshly morally judge him/her and they have less support for the hiring decision.

Given the documented benefits of referral-based hiring, we obviously are not advocating that organisations or managers do away with these practices. However, given these findings, we do believe that it is important for those involved in hiring to be aware of these dynamics and carefully manage the referral process.

One possible solution for organisations to consider would be to set up systems with temporary anonymity of referrers, while simultaneously providing enhanced transparency regarding the reasons for the referral, thereby shifting the focus from characteristic of the referrer to the referral himself/herself and how information about them provides a valid cue with regard to their fit and potential performance in the organisation. A second implication is that high power referrers should be cognisant that their referrals might receive relatively more scrutiny and they should therefore use this practice cautiously and sporadically.

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Notes:

- *This blog post is based on the author's paper Compromised Ethics in Hiring Processes? How Referrers' Power*

Affects Employees' Reactions to Referral Practices, Academy of Management, 2018.
- *This post gives the views of its authors, not the position of LSE Business Review or the London School of Economics.*
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