About i4cp

The Institute for Corporate Productivity (i4cp) focuses on the people practices that make high-performance organizations unique. Years of research make it clear that top companies approach their workforces differently. At i4cp, we work with our network of organizations to:

- Reveal what high-performance organizations are doing differently.
- Identify best and next practices for all levels of management.
- Provide the resources to show how workforce improvements have bottom-line impact.

Through our exclusive, vendor-free network – in which peers collaborate to drive strategic research and share tools and insights – i4cp provides a unique, practical view of how human capital practices drive high-performance.

Visit i4cp.com to learn more.

Find us on

i4cp's People-Profit Chain™

The topic of performance management falls within the i4cp's Talent domain. According to the People-Profit Chain™ model, to improve market performance, PM should be aligned by leadership to create a performance culture that supports the organizations strategy by better serving the market.

About the Study

For the purposes of this study, performance management refers to the management of individual employee performance rather than overall organizational performance. Performance management includes the performance appraisal as well as the development of job descriptions, goal development, coaching, feedback, and development opportunities.


The Market Performance Index (MPI)

i4cp's Market Performance Index, or MPI, is based on self-reported ratings of organizational performance in four key areas—market share, revenue growth, profitability and customer satisfaction—as compared to the levels achieved five years previously. The average of the four ratings determines MPI score.
EXECUTIVE SUMMARY

Performance Management 2013: Still Waiting for Real Change

Performance management has been described as everything from "bull***t" (Culbert, 2010) to the most important thing managers do (Sudarsan, 2009). It is also one of the most contentious and emotional topics in human resources management, as few people have not had at least one negative experience during their careers related to performance management.

The logic of performance management seems to make perfect sense—not everyone has the same work output, so an approach to differentiate levels of performance is needed to maximize the output of each employee. In theory it appears simple, but in practice it more often than not can devolve into a messy, logistical nightmare that leaves employees feeling alienated and misunderstood.

In the past five years, research, organizational case studies and anecdotes suggest a growing movement toward radical change in performance management approaches and outright abandonment of traditional elements such as performance appraisals. But data from i4cp’s latest research refutes this anecdotal evidence and reveals some uncomfortable truths about the performance management process. It shows that while there is agreement that performance management needs radical improvement, few organizations dare execute changes beyond minor tweaks around the margins.

Use of performance ratings remains pervasive despite their shortcomings.

i4cp has been studying performance management since 1980, and our studies do not show a trend toward companies abandoning performance ratings en masse. Despite reported dissatisfaction with their performance management (PM) structure, very few companies are making drastic changes to their systems, such as starting or stopping forced rankings. In our most recent study, only 6% of the respondents surveyed indicated that their companies had discontinued their performance management or rating system in the past year.

Few companies are planning major changes.

Moreover, few companies plan to change their performance management systems in a meaningful way (a scant 3% of respondents reported that their companies plan to remove their PM system or performance appraisal system in the coming 12 months).
Performance management is widely viewed as a flawed approach, but with no better alternative. The reality is that most companies agree the system needs serious fixing, but are not sure how to go about it. The logistics of performance management are unwieldy, and changing the system can be costly and complex—the possibility of minor returns on such an effort is viewed as not worth the overwhelming upfront cost.

There are no easy answers when it comes to improving performance management. What works well at one company might not work at another. However, one thing is certain: when performance management works, it is not the what but the how—any system can be made to work if it is executed strategically.

Yet for a few organizations, doing nothing is not an option. This report profiles two companies that have found novel ways around the daunting issues obstructing successful and meaningful change to performance management:

• Adobe, which abandoned its performance ratings system for a “performance check-in” - Pg. 5

• REI, which replaced its traditional PM system with one that provides real returns for employees and the company - Pg. 19

Rewarding for performance
Pg. 12

Lockheed Martin, shares its efforts to identify the relationships of financial and non-financial rewards on performance for different segments of its employee population.
Everyone is doing it ...

Performance management processes are pervasive. Overall, 86% of respondents surveyed by i4cp reported that their companies have a formal PM process in some part of the business. While more high-performing organizations (HPOs) than low-performing organizations (LPOs) have a formal process, neither shows a strong correlation to MPI. This indicates that other factors—such as the quality of the process rather than its mere presence—matter to performance.

**Does your company have a formal employee PM process?**

<table>
<thead>
<tr>
<th></th>
<th>HPOs</th>
<th>LPOs</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>83%</td>
<td>64%</td>
</tr>
<tr>
<td>No, but are planning to</td>
<td>5%</td>
<td>17%</td>
</tr>
</tbody>
</table>

1.3x

But few are doing it well ...

**Our PM process has a positive business impact on our organization**

<table>
<thead>
<tr>
<th></th>
<th>HPOs</th>
<th>LPOs</th>
</tr>
</thead>
<tbody>
<tr>
<td>High or very high extent</td>
<td>55%</td>
<td>36%</td>
</tr>
</tbody>
</table>

1.5x

**To what extent do you believe your organization is effective at performance management?**

<table>
<thead>
<tr>
<th></th>
<th>High or very high extent</th>
<th>Small or not at all</th>
</tr>
</thead>
<tbody>
<tr>
<td>HPOs</td>
<td>28%</td>
<td>45%</td>
</tr>
<tr>
<td>LPOs</td>
<td>6%</td>
<td>45%</td>
</tr>
</tbody>
</table>

4.7x

These two sets of responses—that about 45% of respondents from HPOs say that PM does not have a positive business impact and nearly three-fourths say their PM system is moderately effective at best—are alarming when taken in conjunction with the previous result showing that over 80% of companies have a formal PM system in place. This is a serious indication that many companies have a PM system in place that their employees believe is not managed well and does not have a positive effect on their performance.

These poor performance statistics are even more startling considering these are high-performance organizations, but among low-performers the situation is worse. If the leadership of today’s top companies
believe that a ubiquitous system is broken, alarm bells should be ringing; yet in many organizations they are not. This report examines the reasons why

Employees are increasingly dissatisfied with PM

Do employees find your PM process fair?

<table>
<thead>
<tr>
<th>Year</th>
<th>Fair</th>
<th>Valuable</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>71%</td>
<td>27%</td>
<td>100%</td>
</tr>
<tr>
<td>2010</td>
<td>38%</td>
<td>27%</td>
<td>100%</td>
</tr>
<tr>
<td>2013</td>
<td>29%</td>
<td>19%</td>
<td>100%</td>
</tr>
</tbody>
</table>

Taken alone, reporting that employees are dissatisfied with the fairness of their performance management system is not surprising. Most people who have been in the workforce for any significant length of time are familiar with complaints about the PM process. What is surprising is that it seems to be getting worse—fewer than a third of those surveyed said that their employees found their PM process fair. In 2006, it was double that.

Some of the dissatisfaction can be attributed to the lingering consequences of the 2009 recession, which led to expectations on fewer employees to do a greater amount of work. According to the Bureau of Labor Statistics, productivity per employee was steadily increasing during the Great Recession as companies laid off employees while trying to maintain the same output. And the pace of current hiring has yet to reach pre-recession levels.

In addition, cuts to direct and indirect benefits meant that these same employees who were working longer, harder hours, were also doing so for a reduced reward. The fact that the workforce is dissatisfied is not surprising—what is surprising is that they aren’t in outright revolt.

Fairness, of course, is not an objective measure. If the perception of an organization’s PM system is that it is unfair, this may be related to lack of engagement, quality of conversations or quality of management. Another consequence of the “making do with less” philosophy has been that managers are required to manage many more people, rendering them unable to provide individual employees with the feedback they need or want.
Performance Management at Adobe: Outside-in Change

Sometimes getting started is the easy part. On March 27, 2012, thanks to an article in The Economic Times of India, Adobe employees, along with the rest of the world, learned that Adobe would be abolishing its old system of performance appraisals. Perhaps the circumstances of that announcement weren't the exact catalyst Adobe’s leaders planned to galvanize employees behind this change, but that didn't deter Ellie Gates, Director of Global Management Effectiveness, who led the company’s strategy and implementation team for this change, along with the SVP of People Resources, Donna Morris. The team leveraged the agile mindset prevalent in Adobe's engineering organizations to tackle such a large challenge and crowdsource feedback and solutions from the employee population.

Donna Morris requested employee feedback through an internal blog as the news item went public. The blog post became one of the most read in all of Adobe's history, and in many ways the outside-in impetus to change only served to accelerate the work of rethinking reviews they had begun months earlier.

“Donna and the team firmly believed that nothing we could do could be worse than the system that failed to deliver on exceptional feedback or to inspire our employees. Any change at all is better than nothing.” Ellie advises others who wish to emulate Adobe's success with performance management (PM) that it starts with the willingness to do it. “The key is in having an agile mindset. Just put out your ideas, get feedback, evolve it and make it work. Don't try to get it 100% perfect or you'll never implement it and wind up with yet another year of pain.”

For Adobe, the important issue was finding a solution that actually inspired employees and provided them with ongoing feedback so they could be more innovative and successful. Like many performance management systems, Adobe’s approach had long been a point of contention among the workforce. The company’s engagement survey showed evidence of high dissatisfaction for a few years. Ellie explains, “Employees didn’t really believe we were going to actually do this, it was just another passing flavor of the month from HR. But I think our communications with them, first through awareness, then equipping, then reinforcement finally convinced them.”
Communicate, communicate, communicate

The team spent time increasing awareness with information sessions conducted globally. Ellie describes the reasoning, “To be effective in driving change, you have to connect people with the desire to change, and help them understand the ‘why’ behind it. If you can't communicate the why behind what you are trying to do, you don't have buy in, without buy in, you have a useless process. We also communicated a significant power shift in this process.” The message to the employees was that rather than make minor tweaks, again, to the system in the name of ‘doing something,’ Adobe really did do something—they abolished their PM system wholesale and more than that, they shifted the power to the employee as they expected them to drive these conversations with their manager. Employees are now in the driver’s seat and their managers’ role has shifted to leading the pit-crew to support them. Ellie recommend the book *Start with Why, by Simon Sinek* as a great guide on how to do that effectively.

An imperfect system

Ellie explains that the real issue isn't finding a system that is perfect—it's finding a system that works. Considering the amount of hours spent at many companies (a recent i4cp study indicates that it is at least one day per employee per year), any move to a less time-intensive system is an improvement. The change at Adobe redirected 80,000 hours managers spent on a process that failed to yield results. Less time is spent now, but it's focused on ensuring that managers are clear with employees on what is expected in their roles and providing them both feedback and growth opportunities in their present role.

Separate performance and rewards frameworks

**PERFORMANCE CHECK-IN**
- Clear and up-to-date expectations revisited through the year
- Ongoing feedback focused on performance
- Timing and methods flexible
- No ranking or forced distributions to determine rewards
- No written formal review

**REWARDS CHECK-IN**
- Annual compensation planning
- Managers are responsible to differentiate pay based on performance and market conditions
- No fixed guidelines
As with other rating-less performance management systems, Adobe's required that compensation and PM be separated. To do this, they created two distinct frameworks: one for ongoing Performance Check-Ins and an annual Rewards Check-In.

**Global communication doesn’t always equal global understanding**

One of the interesting results of this process was recognizing that some countries have very different employment laws, which require understanding and customization in Adobe's new approach to PM. The “Check-In” framework is accepted by employees, however the company ended up keeping a written annual review in China, but changing ratings to simply “Performing or Not Performing.” Given the need for managers' opinions of performance to have additional validation in China, if an employee is trending towards non-performance, the business leader needs to work with the manager to review the employee's expectations, performance feedback given, and work with the manager to ensure they've been given appropriate direction and time to perform in their role.

The other key learning surfaced when Ellie went to China to roll out the new process. Translating the documents into Chinese was not a “nice to have” but clearly a key to ensuring employees in China really understood the expectations of them driving this process with their managers. “It's a great lesson, a humbling one for sure, to stand up and say ‘We've been talking about this for a few months' and to realize as you are standing there, that the majority of the room didn't understand the approach. All the global training you think you just did didn't have impact here. My key learning: identify the language and unique country needs to ensure they are fully equipped to execute against it.”

**The results show the risk was worth it**

A year into using the new system, Adobe has seen an increase in the reports of satisfaction with the PM system, no drop-off in overall performance, and a 30% reduction in attrition year-over-year. There have been edges to smooth out along the way, but feedback mechanisms such as the engagement survey, focus groups, and a dedicated alias to answer questions ensures the implementation team stays on top of any issues and best practices to make it even better.

Asking for honest feedback can, and did, result in some negative feedback. However, there was also some encouraging feedback and a group of engineers even took the initiative to create a video describing their ideal version of the new process. In order to satisfy customers, both internal and external, the first step will always be to listen to them.

Ellie sums up the process, “Just put your solutions out there, get feedback, learn from it, improve it and don't be hampered by your own fear. Fear is just false evidence appearing real anyway. It's good for HR to be a bit more radical, we can be so risk adverse, but the results are so worth it.”
Lessons Learned:

• Engage your employees in the process, it will help generate ideas and assist with the acceptance of those ideas when they are adopted.

• For multi-national corporations, personal attention must be paid to employees who will have different cultural expectations about performance management.

• Performance and compensation can be successfully separated, but the processes for both must be clearly delineated and explained.
Despite widespread dissatisfaction, changes to performance management approaches have been small scale

Does your organization plan to fundamentally change the way it evaluates the performance of its employees in the next three years?

- Yes: 16%
- No: 38%
- Don’t know: 46%

i4cp's 2012 Pay for Performance Pulse Survey

Has the process changed in any of the following ways in the last three years?

- Changed point scale (e.g. moved from 3 to 5 point scale): 12%
- Began forced ranking for performance ratings: 7%
- Stopped forced ranking for performance ratings: 3%
- Removed performance management system: 3%
- Removed formal performance appraisals: 3%
- Other: 17%
- None of the above: 70%

i4cp's 2013 Keys to Performance Management

Given the dissatisfaction expressed by both employers and employees, some fundamental changes to the PM system should be expected.

Against those expectations, though, is evidence that very few companies are making any significant changes to their PM systems. Although some
companies are showing activity, few are making the types of changes needed to address some of the underlying issues.

In 2012, 38% of respondents indicated that their companies planned to fundamentally change the way they evaluated employee performance. One year later, when asked if their PM system had changed over the last year, 30% said that it had. Although there is no way to tell if these are the same respondents from the same companies that had previously indicated they anticipated change, the same population was surveyed both times.

As a follow-up, respondents were asked if their companies planned any changes for the next year; 32% reported that they were. Considering that 86% of the respondents’ companies have a PM process, and 90% have a formal appraisal process, it’s difficult to ignore the evidence that most of the activity done in PM is starting and stopping forced rankings, and changing the point system from 3 to 5 and back again.

On the other hand, some companies’ activity shows up in more than one category. Consider the case of FedEx Express—the company discontinued its performance appraisal system for some employees and implemented a more robust performance appraisal system for others. These types of changes are not always reflected in the survey data, but still provide insight into the specific ways companies are addressing deficiencies in their existing PM systems—in this case, chucking them out altogether where they don’t add value and emphasizing them more where they do add value.

Is your organization planning to make any of the following changes to its PM process in the next year?

<table>
<thead>
<tr>
<th>Change Description</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Changed point scale (e.g. moved from 3 to 5 point scale)</td>
<td>9%</td>
</tr>
<tr>
<td>Begin forced ranking for performance ratings</td>
<td>3%</td>
</tr>
<tr>
<td>Stop forced ranking for performance ratings</td>
<td>2%</td>
</tr>
<tr>
<td>Remove performance management system</td>
<td>2%</td>
</tr>
<tr>
<td>Remove formal performance appraisals</td>
<td>1%</td>
</tr>
<tr>
<td>Other</td>
<td>19%</td>
</tr>
<tr>
<td>None of the above</td>
<td>68%</td>
</tr>
</tbody>
</table>

I4cp’s 2013 Keys to Performance Management
The rationale behind PM has not changed (and maybe that's one cause of the problem)

The most prevalent use of performance management has consistently been as a method for determining pay raises. As will be seen later, the underpinning assumption that pay drives performance is a commonly held belief, despite evidence to the contrary (shown by Lockheed Martin and discussed later in this report). Despite some evidence that companies are beginning to separate compensation from performance management, the majority of responses to the i4cp survey suggest that without compensation decisions to make with PM data, it would instead be used for career development and recognition.

The 2010 data is very likely a result of the Great Recession, which left many companies unable to award any sort of compensation increases to standout performers.

Moreover, many employees want help to improve their performance but many performance management processes fail to deliver it. A “check the box” mentality, absence of follow-up, lack of coaching and productive conversations, and missing links to learning and development undermine the prospects for improving individual performance.

i4cp's latest survey shows that generally, HPOs are more likely than LPOs to use performance management data for multiple purposes. The biggest gaps between HPOs and LPOs are in the most strategic uses, such as to tighten strategic alignment between skills and business goals (HPOs do this over three times more) and to support organization-wide focus on high performance (HPOs do this over 1.5 times more). The former use is strongly correlated (.176**) to market performance. This suggests that high-performance organizations use their performance management processes strategically, not just tactically.
There is a school of thought that holds that many workers are more interested in autonomy, recognition and creativity than in personal financial gain. Both Daniel Pink’s Drive and Dr. Teresa Amabile and Steven Kramer’s Progress Principle have cited numerous examples that show how workers can be motivated by rewards other than money. However, there always exists the caveat that this is only true for some types of workers (e.g. creatives, high-performers, new employees).

Many people in HR management might assume or suspect that although there is some evidence that shows non-financial rewards can be just as, if not more, powerful than monetary rewards, the culture at their particular companies would not support that claim. Dr. Jon Turner, Senior Organizational Development Analyst at i4cp-member company Lockheed Martin (LM), decided to do something about this: he analyzed his workforce and determined exactly what types of rewards worked best, and for which employees.

Turner started by dividing his workforce into segments, based on job tenure, level and job code. Once he had a baseline, the next step was to introduce different levels of financial rewards for each group (the levels in the chart below refer to bonuses as a percentages of salary with the smallest percentage at level one). By analyzing the commensurate change in employee experience (a LM designation that signifies their survey results that combine engagement, ethics, diversity and satisfaction) he could track the changes according to reward level.

### Impact of individual rewards by tenure

<table>
<thead>
<tr>
<th>Engagement</th>
<th>0-5 years tenure</th>
<th>No reward</th>
<th>Recognition event</th>
<th>Level 1 reward</th>
<th>Level 2 reward</th>
<th>Level 3 reward</th>
<th>Level 4 reward</th>
<th>Level 5 reward</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Medium</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>High</td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

How satisfied are you with the recognition you receive for doing a good job?

Please indicate to what extent the recognition outcomes you have received

- ... have seemed justified given your performance?
- ... reflected what you have contributed to the company?
- ... have been applied fairly?
As seen in the above chart, the amount that was received had a positive correlation to the employee experience, but that small amounts (less than $500) were actually harmful, Turner elaborated.

“An interpretation of why that might be that passes the ‘common sense’ test is that very low amounts actually send a message that the company sees very little value in your contributions. As evidenced by the statistics, at those amounts, a company would be better off giving nothing at all.”

Another look at the data (below) shows a specific example of how parts of the employee experience were correlated with specific dollar amounts.

However, the real revelation came when Turner looked at non-financial rewards, in this case, Lockheed Martin's "Evening of Excellence," an after-work event that showcased certain selected high-performers.

### Impact of individual rewards overall

<table>
<thead>
<tr>
<th>Engagement</th>
<th>Low</th>
<th>Medium</th>
<th>High</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>0-5 years tenure</th>
<th>No reward</th>
<th>Level 1 reward</th>
<th>Level 2 reward</th>
<th>Level 3 reward</th>
<th>Level 4 reward</th>
<th>Level 5 reward</th>
</tr>
</thead>
<tbody>
<tr>
<td>How satisfied are you with the recognition you receive for doing a good job?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Please indicate to what extent the recognition outcomes you have received</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>... have seemed justified given your performance?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>... reflected what you have contributed to the company?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>... have been applied fairly?</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Minimal amounts have minimal impact

Only higher rewards move the needle.
Event” columns highlight those employees who received that reward and show greater increase in productivity than in all levels of the financial rewards alone. Considering the cost of an evening event such as this in comparison to rewards spread throughout all eligible employees, the return on investment made this a positive reward for both employee and organization.

### Reward and promotion or recognition

<table>
<thead>
<tr>
<th>Item/Question</th>
<th>Promotion</th>
<th>No Promotion</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>How satisfied are you with the recognition you receive for doing a good job?</strong></td>
<td><img src="#" alt="No reward" /> <img src="#" alt="Level 1-3 reward" /> <img src="#" alt="Level 4-5 reward" /></td>
<td><img src="#" alt="Level 3 reward" /> <img src="#" alt="Level 4 reward" /> <img src="#" alt="Level 5 reward" /></td>
</tr>
<tr>
<td><strong>Please indicate to what extent the recognition outcomes you have received</strong></td>
<td><img src="#" alt="No reward" /> <img src="#" alt="Level 1-3 reward" /> <img src="#" alt="Level 4-5 reward" /></td>
<td><img src="#" alt="Level 3 reward" /> <img src="#" alt="Level 4 reward" /> <img src="#" alt="Level 5 reward" /></td>
</tr>
<tr>
<td>... have seemed justified given your performance?</td>
<td><img src="#" alt="No reward" /> <img src="#" alt="Level 1-3 reward" /> <img src="#" alt="Level 4-5 reward" /></td>
<td><img src="#" alt="Level 3 reward" /> <img src="#" alt="Level 4 reward" /> <img src="#" alt="Level 5 reward" /></td>
</tr>
<tr>
<td>... reflected what you have contributed to the company?</td>
<td><img src="#" alt="No reward" /> <img src="#" alt="Level 1-3 reward" /> <img src="#" alt="Level 4-5 reward" /></td>
<td><img src="#" alt="Level 3 reward" /> <img src="#" alt="Level 4 reward" /> <img src="#" alt="Level 5 reward" /></td>
</tr>
<tr>
<td>... have been applied fairly?</td>
<td><img src="#" alt="No reward" /> <img src="#" alt="Level 1-3 reward" /> <img src="#" alt="Level 4-5 reward" /></td>
<td><img src="#" alt="Level 3 reward" /> <img src="#" alt="Level 4 reward" /> <img src="#" alt="Level 5 reward" /></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Item/Question</th>
<th>Recognition Event</th>
<th>No Recognition Event</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>How satisfied are you with the recognition you receive for doing a good job?</strong></td>
<td><img src="#" alt="No reward" /> <img src="#" alt="Level 1-3 reward" /> <img src="#" alt="Level 4-5 reward" /></td>
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</tbody>
</table>

There are many examples of companies that offer non-financial rewards to their employees, everything from employee-of-the-month recognition to lunch with the CEO. However, there have been very few analyses of the impact of these types of rewards versus financial ones. What Turner and Lockheed Martin have done is demonstrate that not only is it possible to reward employees in a non-compensation method, which is useful for any company looking to separate compensation and performance management, but that it is possible to measure the effect of those rewards. Jon Turner and Lockheed Martin should now be the ones to receive the recognition for their efforts.
Lessons Learned:

- Measure the impact of financial and non-financial rewards. Non-financial rewards can have greater effect on performance. Small financial rewards can be counter-productive to engagement and/or performance. If the budget for financial rewards that will be meaningful to the employee isn't available, non-financial rewards (e.g. recognition) should be used in their place.

- When examining data for an employee population, segment the employees based on reasonable differentiators (e.g. tenure, department, level). This will help reduce contamination from external influences.

- Different forms of data visualization can help bring out the story from the numbers, and simple is almost always better.
The frequency of PM has not changed

<table>
<thead>
<tr>
<th></th>
<th>2006</th>
<th>2010</th>
<th>2013</th>
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<tbody>
<tr>
<td>Annually</td>
<td>60%</td>
<td>54%</td>
<td>57%</td>
</tr>
<tr>
<td>Every 6 months</td>
<td>23%</td>
<td>35%</td>
<td>30%</td>
</tr>
<tr>
<td>Every 3 months</td>
<td>7%</td>
<td>5%</td>
<td>6%</td>
</tr>
<tr>
<td>More frequently than every 3 months</td>
<td>3%</td>
<td>1%</td>
<td>1%</td>
</tr>
<tr>
<td>Inconsistently</td>
<td>7%</td>
<td>2%</td>
<td>6%</td>
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</table>

The frequency of formal performance appraisals remains consistent at typically once a year for a majority of organizations, or less commonly every six months or less (30%-40% of organizations). Although having more frequent reviews would be preferable from a data collection standpoint, the logistics of performing formal performance appraisals at large (10,000+ employees) organizations more than twice a year is a huge deterrent to higher frequency. At some point, diminishing returns on even the most finely tuned performance appraisal systems means that there is little to be gained relative to the enormous cost in terms of productivity hours lost. On average, respondents reported that their companies spend 7.4 hours per employee, per year, on performance management—the equivalent of losing nearly an entire day of productivity.

Regardless, HPOs are far more likely to conduct performance reviews semi-annually or more frequently, as 45% do this compared to 29% of LPOs. This suggests that the benefits these HPOs are realizing from more frequent reviews outweigh the costs.

One shortcoming of many performance appraisal approaches is that they focus on results but not the behaviors exhibited to achieve those results. This ignores the importance of teamwork and organization values in driving high performance at the enterprise level. The significance of focusing equally on results and behaviors is appreciated more by HPOs, as nearly two times more of them than LPOs measure results and behavior equally.
Are performance appraisals on their way out?

Over three-fourths of respondents indicated that they believe in principle that you can pay for performance, so the concept is not dead (and considering among HPOs, that number was 77%, there is some evidence that paying for performance really does work). But this data taken together seems to point to an inconvenient set of circumstances:

1. Pay-for-performance is believed to be a viable model.
2. Most companies have a system in which individuals or teams are rewarded for performance.
3. Few respondents believe their companies’ pay-for-performance system is very effective.
4. Fewer than half of companies plan to do anything about this.
5. Those that have done something about this are making superficial changes to their system.
6. Those that are planning on doing something plan on making superficial changes to their system.

In summation, many think the system is broke, no one knows how to fix it, and many organizations might be using activity as a substitute for real change. Performance management is one of those areas in which academicians and real-world practitioners are at odds. The solutions that have been offered are usually over-simplified (have better conversations, change your corporate culture, etc.), and are not feasible for most practitioners.

Dr. Christopher Lee, author of *Performance Conversations, an Alternative to Appraisals*, understands the divide between what should be done and what can be done, and has offered some reasonable solutions. He focuses on the types of interpersonal relationships that are the fundamental components of performance management, and wisely cautions that not everything can be on a performance appraisal form. He notes the corporate culture's over-reliance on forms, and worries that it can lead to employees...
performing to and managing to a performance scorecard/form.

Dr. Lee’s vision of the "old school" (formal annual review conversations, detailed documentation forms) vs. "new school" (frequent, informal conversations, simple documentation) methods of performance management is in line with the research on this subject. There is a growing amount of case studies, surveys and even neuropsychological evidence (Amabile, 2011; Pink, 2011; Rock, 2009) that points to a better way of motivating people.

As Dr. Lee asserts, organizations have long recognized that everyone needs a performance improvement plan, not just under-performers, and there has been a system for it—it’s called executive coaching.
Recreational Equipment Inc. (REI) is one of the largest cooperatives in the $1.8B in outdoor recreation gear through their 128 stores. In the last five years, they have moved away from traditional performance reviews for their over 8000 employees. Today, despite not having a traditional performance appraisal system, they still meet all their sales and customer service goals and were named to Fortune's "100 Best Companies to Work For." Michelle Clements, SVP HR, discusses the specifics of what led to that decision and how it was implemented.

The essential point to i4cp-member company REI was that PM wasn’t the right fit for their employee-centric culture, was costly and, most importantly, was not returning measurable results. Once REI had identified the issue, they began by discussing options with their employees and gathering support from the people the changes would affect. Once it was time to make the drastic change of removing formal performance appraisals, they made sure there was a system in place to replace it that involved continuous conversations and person-specific goals.

The end result was a workforce that reported greater satisfaction with the process and no significant problems during the changeover (as measured by network calls and other statistics used during the change). The important lesson from this case was the careful communication used by REI during each step of the process, including the planning phase. Without that transparency, employees may have seen the change as threatening, and adoption might not have been as universal.
Conclusion

The only thing that will have a truly positive effect on people performance is improving the quality of the interactions between managers and employees.

The state of the performance management process has been relatively stagnant for years. Little has changed in terms of strategies and approaches used, with the exception of technologies. We can leverage those technologies to gather data that allows us to make better decisions, and we can use the communication that technology has enabled us with to respond quicker. Whether it is a three or five-point scale, a forced distribution or not, or even if there is not a formal system in place at all, the only thing that will have a truly positive effect on people performance is improving the quality of the interactions between managers and employees. This can be accomplished only thorough strong leadership, diligence and understanding that the answer isn't to be found in a specific performance management structure. However, it is acknowledged that for a majority of people working with an existing performance management system, the changes needed to create that culture may be beyond their abilities.

There is still plenty that can be done on the tactical level with the proliferation of integrated technologies, different performance measures backed by data, and changes to form or functions.

i4cp's 2010 study, *Nine Keys to Performance Management*, includes a detailed roadmap on the techniques associated with effective performance management for companies looking to make changes, but on the strategic level, the overall approach to performance management has not altered for decades, and shows no signs of changing.

The importance of integrating the strategic (enterprise goals and performance) and tactical (individual goals and performance) sides of PM is underscored in i4cp's *Purpose Driven Performance Management* study (2012):

*HPOs provide direction by fusing strategic and tactical approaches to PM. HPOs balance their PM strategies. On the strategic level, they support an enterprise-wide focus on high performance that permeates the organization. Additionally, they tighten the strategic alignment between skills and business goals by ensuring that the company has the right mix of skills needed to execute its strategy. On the tactical side, HPOs ensure that ongoing goal review and*
managerial feedback occurs and they discuss accomplishments and development plans with employees.

The focus remains on the quality of the conversations, and using performance management for increasing productivity rather than simply collecting information to support pay decisions or meeting perceived legal requirements. For many companies though, the impetus to make sweeping changes does not exist and although some may be slowly doing away with formal PM systems, the change is more akin to erosion than landslide.

There are three basic options: One, do nothing and focus efforts on an area with a more demonstrable return on investment. Two, make minor changes to the system in a way to move slowly toward a specific goal. Three, make a massive change to the system, such as doing away with performance management or appraisals altogether and replacing them with an entirely different approach. None of these are, taken out of context, better than the others. However, the major change option has some very specific obstacles.

Why won’t anybody do anything?
Major obstacles to change are of course, buy-in, time and money. Any time spent on a major internal project is time not being spent fulfilling the businesses core. The enormous amount of time invested in performance appraisals means that spending more time getting rid of them is throwing good money after bad.

An even greater obstacle is lack of support from leadership. Although many in the HR community do agree on the fundamentally flawed nature of the performance review process, they either lack the support (this is usually an enterprise-wide initiative) or the incentive to carry out drastic changes.

Regrettably, there is no simple solution for this. While there may be a number of organizations in which the performance review process is clearly broken, the financial and organizational costs of fixing it may be too steep. For other organizations, the best course for making major changes is to introduce them in increments, by department, over a period of time (five years or more). A selection of case studies of organizations that have refined existing changes and made those changes from the bottom-up are examined by i4cp in Performance Management Playbook: Tools and Techniques for Managing Performance.

For those companies that have the support of leadership, and have decided to make a sweeping change, there are a few case studies that create a set of do’s and don’ts. i4cp recommends a presentation created by Michelle Clements of REI, “Throwing Out Traditional Annual Performance Reviews: The REI Story”, and i4cp’s “Strategy in Action: Greater Rochester YMCA on Opting Out of Performance Appraisals” as examples of companies taking a radical and modern approach to performance management.
Recommendations and actions

Organizations that have gone against the grain and made sweeping changes to their PM systems have generally made those changes in two distinct ways. Either they have had the support of senior leadership, and have mandated a change to the organization—a top-down approach—or they have implemented small changes over time to different units, which have slowly changed the culture and ultimately the entire PM system.

Both of these approaches have proven effective; the type of change that has been made has largely been determined by the amount of support for change at the executive level.

Top-down "Big Change"

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Action</th>
<th>Benefit</th>
</tr>
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<tbody>
<tr>
<td>Align the PM system with strategic goals—use the PM system for skills and career development, not for compensation decisions or justification of possible terminations.</td>
<td>Focus PM process on goals that are aligned to the overall goals of the organization.</td>
<td>Builds workforce skills, increases employee engagement.</td>
</tr>
<tr>
<td>Plan for resistance at multiple levels—from employees and leaders. Explicitly communicate not just what should be done, but why.</td>
<td>Engage affected stakeholders directly to explain change rationale and address concerns.</td>
<td>Employees will have a clearer concept of the end result, which will speed up any changes made.</td>
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<tr>
<td>Shift the focus to goal achievement—focus on explicit goals and measurable performance metrics.</td>
<td>Give recognition and rewards for achieving specific business-related goals.</td>
<td>Regardless of the system, if the focus is on PM-specific goals (completion rate, time to complete), those are the goals that will be achieved, not the more important productivity-related ones.</td>
</tr>
<tr>
<td>Separate compensation from performance management—before any large-scale changes to PM, compensation should be separated from performance management.</td>
<td>Create non-financial rewards to augment/replace pre-existing financial incentives.</td>
<td>Employees can still be rewarded for completing tasks, but will no longer be rewarded based on arbitrary distinctions, creating greater organizational trust.</td>
</tr>
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## Bottom-up "Incremental Change"

<table>
<thead>
<tr>
<th>Recommendation</th>
<th>Action</th>
<th>Benefit</th>
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<tbody>
<tr>
<td>Use PM for tactical goals—align the PM system with departmental and team goals.</td>
<td>All goals should tie into the goals at the higher level (e.g. call response times should be aligned to tie into higher customer satisfaction scores).</td>
<td>By aligning PM to goals that can be easily traced to overall company achievements, employees will see the need for PM.</td>
</tr>
<tr>
<td>Test new approaches on a small scale first—carefully choose targets for experimentation and add time for adjustments.</td>
<td>Pilot solutions in areas of the organization seeking to improve their performance and that are open to change. Validate results first, then make changes to the PM system in a slow roll-out over the course of 12 months or more.</td>
<td>Giving more time for PM changes will better allow for dealing with collateral adjustments.</td>
</tr>
<tr>
<td>Manage the informal systems as you would the formal—managers will still rate and rank employees if that is what they are used to—anticipate and mitigate this.</td>
<td>Require documentation of conversations and other PM-related decisions.</td>
<td>Proper documentation will allow checking that behaviors are being changed, not just results.</td>
</tr>
<tr>
<td>Create a system of continuous conversations—PM is about future performance, and keeping employees moving forward requires re-alignment more often than once-a-year.</td>
<td>Create a system for employees and their supervisors to document their spontaneous (but consistent) conversations.</td>
<td>Employees will receive the direction or affirmation needed, supervisors will have more leeway in their management approaches.</td>
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</table>
Author and contributors

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Tony DiRomualdo, VP of research, oversaw development of the findings discussed in this report.

For more information or to contact the author, please go to i4cp.com/contact

i4cp’s Performance Management Exchange

This survey is a product of i4cp's Performance Management Exchange group. This group is comprised of representatives from the following organizations:

- AIG
- Amway
- Catholic Health Initiatives
- Corning
- Lockheed Martin
- Pierce Transit
- Premera
- Robert Half International
- Sysco
- Virginia Mason Medical Center
- The World Bank

Our gratitude and appreciation go out to the exchange group contributors, whose dedication to the study of performance management made this research project possible. Their time and expertise were essential in the production of the initial survey instrument, in the final analysis of the data and in the source material for the case studies. We would also like to thank our interviewees: Ellie Gates and Donna Morris from Adobe, Dr. John Turner from Lockheed Martin, and Michelle Clements from REI.

About the survey

For its 2013 study of the current trends in performance management, i4cp fielded a survey that garnered responses from 244 businesspeople representing a variety of industries (35+), global locations (47% global or multinational organizations), and organizational structures and sizes (1-10,000+ employees).
References


i4cp focuses on the people practices that drive market performance.

Learn more at www.i4cp.com