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Reinventing Performance Management

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ABSTRACT

Performance appraisals have traditionally been conducted annually or semi-annually. Recently, many companies are transitioning to ongoing feedback and coaching, either in addition to periodic appraisals, or lieu of them. There have also been calls for completely reinventing performance management systems, as the result of an abundance of research that indicates performance processes are over-engineered and time-consuming, and they tend to demotivate employees while hindering candid and honest conversations. This paper examines the common problems with attribution error and rater bias in traditional performance appraisal systems. Five mini-case studies are then presented by exploring how five large companies (Netflix, Adobe, Deloitte, IBM, GE), have reinvented the way in which performance management is implemented. The paper examines why these companies moved away from traditional performance appraisal and what processes replaced it. The paper also identifies emerging trends that will impact the future of performance management and offers suggestions for the road ahead.

Keywords: Performance, management, appraisal, feedback, rating.

INTRODUCTION

Performance appraisals have traditionally been conducted annually or semi-annually. Recently, many companies are transitioning to ongoing feedback and coaching, either in addition to periodic appraisals, or lieu of them. According to Johnson, et al, this is because employees need regular feedback on their performance [2]. Employees also benefit from candid assessments of their performance. Committing management time and effort to monitoring performance also decreases turnover rates [3]. Employees and their managers often see appraisal as a chore, and something they have to do because HR requires it. The process will be more effective and seen as productive and useful if the employees and managers keep their purpose in mind. The primary purpose of performance appraisal should be to help employees to continuously improve their performance [4].

In the last few years, there have been calls for reinventing performance management systems, and some companies such as Netflix, Adobe, Deloitte, IBM, and GE have abandoned them altogether [5, 6]. This paper examines the problems with traditional performance appraisal systems, and offers five mini-case studies by exploring these five large companies have responded. The paper examines why the companies moved away from traditional performance appraisal and what processes replaced it.

First, let's distinguish between performance management and appraisal. Performance management refers to the activities, policies, and interventions designed to improve the

performance of human resources. Barends and Briner report that, in a knowledge economy, performance management at the individual employee level is essential, thus the business case for implementing a system to measure and improve employee performance is strong [1].

Performance appraisal refers to a periodic process by which employees are evaluated relative to the requirements of the job, for the purpose of indicating where improvements are needed. Many organizational decisions are made based on performance appraisals, including training or development, promotion, incentive pay, disciplinary action, and termination. Performance appraisal can be thought of as one part of the performance management process. Just as one cannot assess the fuel economy of a vehicle without monitoring data (miles per gallon), employees must be assessed to determine whether they are achieving their full potential.

TRADITIONAL PERFORMANCE APPRAISAL

What many people think of regarding a performance appraisal is when a supervisor evaluates the performance of a direct report. This is the most common type of performance appraisal but there are other variations. Appraisals are sometimes conducted by supervisors, subordinates, peers, customers, and even oneself. There also is a comprehensive approach that includes input from a variety of assessors, known as a 360-degree evaluation. Each of these variations has pros and cons, and each can be useful when implemented correctly, and in the right set of circumstances.

Traditional performance appraisal methods include Management by Objectives (MBO), rating scales, critical incidents method, and informal appraisal/feedback. MBO is a results-oriented performance management method that strives to increase organizational achievement through mutual agreement of goals between employee and manager. MBO was first widely used in the 1950s, in part because of the writings of management theorist Peter Drucker. MBO is results-oriented and seeks to measure individual performance by examining the extent to which predetermined work objectives were met.

Rating scales are a performance appraisal method whereby each employee is rated according to specific characteristics. Rating scales can be numeric (e.g., 1,2,3…) or alphabetic (eg., a, b, c…) with each number or letter corresponding to a level of performance, such as “5 = excellent” or “2 = needs improvement.” Rating scales typically have from three to five options for rating each characteristic. A simple three-level rating is easier to administer, but the five-level rating provides more differentiation between performance levels. Some rating scales also have space for the rater to write comments such as examples of positive or negative work behaviors to support the rating.

One variation of the rating method is the Behaviorally Anchored Rating Scale (BARS). The BARS method is designed to bring the benefits of both qualitative and quantitative data to the appraisal process by using behavioral statements as anchors for each rating level. BARS are time-consuming to develop but may provide improved accuracy of the ratings.

The critical incidents method is a performance appraisal technique in which a manager keeps a log of positive and negative work behaviors of subordinates. A critical incident occurs when employee behavior results in an unusual success or unusual failure on the job. Managers then keep a record of these situations in which something went well, or something went wrong.

Informal appraisal systems usually involve much more frequent feedback. For example, a supervisor might provide feedback upon completion of a project, or perhaps even weekly. They might be unscheduled and impromptu, occurring whenever a manager sees an opportunity to provide feedback or suggestions, or just to inquire with an employee as to how a project is going. Another variation is that they might be regularly scheduled such as weekly or monthly. However, they are still categorized them as informal because they do not involve a formal rating process. These regular meetings are sometimes referred to as "one-on-ones" or "check-ins." Proponents of this approach claim that it engenders more of a coaching or mentoring management style, as opposed to an authoritative one.

PROBLEMS WITH TRADITIONAL PERFORMANCE APPRAISAL METHODS

There is a basic human tendency to make judgments about those who one is working with [7]. But because humans are involved, there is the potential for unfairness, misunderstandings, and lack of consistency. Employees sometimes push back against performance appraisals because they don't think they are a fair representation of their effort. There are several problems that lead to this perception, but they all have one word in common and that word is bias. Bias is the prejudice in favor of or against one thing, person, or group compared with another, usually in a manner considered to be unfair. There are two major types of bias that are common in performance appraisal processes:

1. Attribution error
2. Rater error

Attribution error is a theory of social psychology that describes the inclination to overemphasize the influence of a person's dispositional factors while ignoring the influence of situation factors of a person's behavior. Consider the situation of Zach, a garage door installer for a large overhead door company. In his most recent performance review, his supervisor Julie noted that the frequency of call-backs on his installations is 20% higher than average. A call-back occurs whenever a customer has a problem with a new installation. Each call-back is conducted free of charge to the customer, thus the company incurs only an expense for a call-back. Now consider Julie's perspective: She needs to determine what is the cause of the call-backs. In other words, what problem should the call-backs be attributed to? The problem might be a disposition problem (Zach might not be concentrating on his work, could be distracted, not motivated to perform excellent work, or not paying attention to detail). But the problem could also be situational (lack of training, being rushed by a dispatcher to move more quickly and get on to the next job, or even electrical power surges in the area in which he works). Before completing Zach's performance appraisal, Julie should determine the true cause of the call-backs.

Most performance appraisal systems involve some type of rating system. Ratings have been used since at least the third century when members of the Wei Dynasty (221-265 AD) rated the official family members. It is insightful to note that outcries of unfairness and rater bias have been around just as long. One rater employed by the Wei Dynasty said: "The Imperial rater seldom rates men according to their metrics, but always according to his likes and dislikes." Table I below gives a summary of the main developments in the use of ratings.

Table I: History of Performance Appraisal Systems

History of Performance Appraisal Systems	
Dates	Events
221-265 AD	Wei Dynasty uses raters to rate the performance of the Imperial family members.
1540-1560.	A procedure to formally rate members of the Jesuit Society was established by Ignatius Loyola.
1800-1817	Performance appraisals were initiated by Robert Owen at his cotton mills in Scotland using monitors. The monitors were cubes of wood with different colors painted on each side and displayed above the workstation of each employee. The color of the visible side of the cube was associated with a rating to indicate performance. At the end of each day, the supervisor would turn the monitors based upon his perception of the employee's work that day.
1850-1914	Industrial revolution in America; Workers were evaluated and paid primarily on the basis of quantity produced.
1870-1915	Frederick Taylor stressed the importance of scientific management, time and motion studies, and the individual worker by advocating for the payment of individually based financial incentives (piece work).
1918-1955	Widespread use of performance appraisal techniques with blue-collar employees began after World War 1. Appraisal systems for managerial and professional employees became common after 1955.
1957	Emergence of performance appraisals based on Management by Objectives.
1964-1990	Passage of EEO laws, beginning with Title VII of the Civil Rights Act of 1964 created the need for improvement in appraisal practices to help eliminate discrimination and bias.

Psychologists began studying rater error in earnest in the 1920s. Research has provided evidence of so much bias that some researchers believe that performance ratings may reveal more about the rater than the ratee [8]. This body of research traces its beginning to Thorndike's classic article *A constant Error in Psychological Ratings* [9]. He identified what later became known as the halo effect. This and other common types of rater bias established by research studies are summarized below:

- **Halo Effect**. Occurs when the evaluator forms an overall positive general impression and then extends that positive impression to all aspects of the rating.

- **Horns Effect**. This is the opposite of the halo effect and occurs when the evaluator forms an overall negative impression and then extends that negative impression to all aspects of the rating.
- **Distribution Errors**. These occur when an evaluator has the tendency to rate everyone the same way, and fall into three categories:
    - **Strictness**. Occurs when the evaluator rates everyone low, regardless of actual performance.
    - **Leniency**. Occurs when the evaluator rates everyone high, regardless of actual performance.
    - **Central Tendency**. Occurs when the evaluator rates everyone as average.
- **Recency Effect**. This happens when the evaluator puts too much emphasis on the most recent part of the time period under evaluation. For example, if a payroll analyst is being evaluated for a one-year period and had good performance overall but made a significant payroll error one week before the appraisal, then a supervisor who rated the employee low based on this one recent event has committed a recency error.
- **Contrast Error**. This occurs when an individual's performance is compared to a co-worker, rather than to a job standard. If the employee works in a department with one or more poor performers, then the appraiser may have a tendency to rate this individual higher than would be justified by comparison to the job standard. The converse is also true: If the employee works in a department with outstanding performers, then their performance might seem inferior by comparison.
- **Similar-to-Me Error**. When an evaluator rates an individual high because they have something in common, then the similar-to-me error has occurred. For example, if the evaluator and the individual being evaluated both attended the same school, then there might be a tendency to rate the individual higher than normal. Or perhaps they engage in similar after-work activities, follow the same sports teams, or live in the same neighborhood. Similar-to-me error can also occur due to similarities based on race, religion, gender, national origin, age, and other aspects of a protected class, which can lead to charges of discrimination. This type of error can also give rise to perceptions of favoritism.
- **Idiosyncratic Rater Effect**. This refers to the tendency of humans to view things differently, and subjectively through their own biases. When two or more people see the same situation, they have a tendency to describe it differently. Three different studies have confirmed this effect, as published in a 1998 article in *Personnel Psychology*, a 2000 paper in the *Journal of Applied Psychology*, and a 2010 article, again in *Personnel Psychology*. Each study found that the idiosyncrasies of the person doing the rating accounted for 71%, 58%, and 55% of variation respectively [10, 11, 12]. Thus, in each study, over half of the variation in ratings was attributed to the rater, not the person being rated, which indicates that ratings say more about the rater than the ratee.

REINVENTING PERFORMANCE MANAGEMENT

Over the past few years, there has been an abundance of research that indicates performance processes are over-engineered and time-consuming, and they tend to demotivate employees while hindering candid and honest conversations [13]. In addition, as was mentioned at the beginning of the article, they are typically deplored by employees and their managers. Amber Lloyd of HCM Strategy puts it this way: "Times have changed, and so should our notions about

employee performance. After all, an annual performance discussion is kind of like waiting a year to tell your spouse what you appreciate about him or her or waiting until the start of the next school year to offer suggestions to your teenagers on study techniques that could help them be more effective. It just doesn't work in a fast-paced environment where agility, retention, and engagement are key to a competitive advantage [14]."

There are hundreds, if not thousands of resources (books, websites, checklists, sample feedback phrases, etc.) to assist managers in doing performance reviews. But the question that is often being asked now is: Why do them at all? In the age of knowledge workers, do performance review methods that were developed during the Industrial Revolution make any sense? Fred Nickols, Senior Consultant with the Distance Learning Company says: "The blunt truth is that, if they have any objectives at all, most people set their own [15]." Many supervisors of knowledge workers just do not have the expertise of their employees and are not in a position to set work objectives, to monitor accomplishments, or to supervise their efforts.

There is a growing movement among some companies to reinvent performance management. Over 50 large firms have transformed their performance appraisal systems and moved away from traditional rating systems [16]. Bersin by Deloitte reports that around 70% of companies are reconsidering their performance management strategy. These trends are so new, that there is little research or theory to cite here. Instead, let's take a look at some of these companies, why they have changed the process of performance appraisals (and in some cases done away with them altogether), and what is taking their place.

Netflix

Netflix was one of the first companies to eliminate formal performance reviews. People tend to look seriously at how Netflix approaches talent management because they have been tremendously successful. They are dominating the streaming industry with a subscriber base of almost 150 million, and a year-over-year increase of 16.6% in 2019 [17]. By some estimates, up to a third of peak residential internet traffic in the U.S. comes from customers streaming Netflix movies [18]. Netflix founder and CEO Reed Hastings describes the five tenets of their approach to managing talent:

1. Hire, Reward, and Tolerate Only Fully Formed Adults

"Over the years we learned that if we asked people to rely on logic and common sense instead of on formal policies, most of the time we would get better results, and at a lower cost. If you're careful to hire people who will put the company's interests first, who understand and support the desire for a high-performance workplace, 97% of your employees will do the right thing."

2. Tell the Truth About Performance

"Many years ago we eliminated formal reviews. We had held them for a while but came to realize they didn't make sense – they were too ritualistic and too infrequent. So we asked managers and employees to have conversations about performance as an organic part of their work."

3. Managers Own the Job of Creating a Great Team

"I ask managers to imagine a documentary about what their team is accomplishing six months from now. What specific results do they see? How is the work different from what the team is doing today? Next, I ask them to think about the skills needed to make the images in the movie a reality."

4. Leaders Own the Job of Creating Culture

"It's a waste of time to articulate ideas about values and culture if you don't model and reward behavior that aligns with those goals."

5. Good Talent Managers Think Like Businesspeople and Innovators First, and Like HR People Last

"During 30 years in business, I've never seen an HR initiative that improved morale…Instead of cheerleading, people in my profession should think of themselves as businesspeople. What's good for the company? How do we communicate that to employees [19]?

The overall Netflix approach seems to be that of demanding performance, but creating an environment of freedom in how individuals and teams decide to achieve their performance. For example, the Netflix Jobs website describes the company culture and states that their policy for travel, entertainment, gifts, and other expenses is five words long: "Act in Netflix's best interest." They do not have compliance departments and procedures that most companies have to enforce their policies [20]. Their vacation policy is: "Take vacation." There are no rules about how many days to take or when. The website states: "You might think that such freedom would lead to chaos. But we also don't have a clothing policy, yet no one has come to work naked. The lesson is you don't need policies for everything. Most people understand the benefits of wearing clothes at work."

Adobe

Adobe moved away from traditional performance appraisals because of the number of hours and the cost involved in the process. They discovered that the annual performance appraisal process required 80,000 hours of time from its 2,000 managers, the equivalent of 40 full-time employees [21]. Their internal surveys also suggested that the workforce felt less motivated and inspired after each appraisal. In 2012, Adobe's then Senior Vice President of People Resources, Donna Morris, was feeling frustrated with annual performance reviews. The process was complex, bureaucratic, and paperwork-heavy. It also created barriers to teamwork and innovation, since the experience of being rated and stack-ranked for compensation left many employees feeling undervalued and uninspired [22].

In lieu of annual appraisals, Adobe implemented a frequent 'Check-in' process. As part of this process, managers provide coaching and advice on a regular basis, as opposed to once a year. The process facilitates an ongoing two-way dialogue between managers and employees. The objectives of the Check-in are to help employees gain clarity about what is expected of them, guide them through performance improvement, and assist in their professional growth and development. Table II below summarizes the differences between the old performance appraisal system and the new Check-In process [23].

Table II: Adobe Performance Management: Then and Now

Adobe Performance Management: Then and Now		
	Before: The annual performance review	After: Check-in
Setting priorities	Employee priorities set at the start of the year and often not revisited.	Priorities discussed and adjusted with the manager regularly.
Feedback process	Long process of submitting accomplishments, soliciting feedback, and writing reviews.	Ongoing process of feedback and dialogue with no formal written review or documentation.
Compensation decisions	Onerous process of rating and ranking each employee to determine salary increase and equity.	No formal rating or ranking; Manager determines salary and equity annual based on performance.
Cadence of meetings	Feedback sessions inconsistent and not monitored. Spike in employee productivity at the end of the year, timed with performance review discussions.	Feedback conversations expected quarterly, with ongoing feedback becoming the norm. Consistent employee productivity based on ongoing discussions and feedback throughout the year.
HR team role	HR team managed paperwork and processes to ensure all steps were completed.	HR team equips employees and managers to have constructive conversations.
Training and resources	Manager coaching and resources came from HR partners who couldn't always reach everyone.	A centralized Employee Resource Center provides help and answers whenever needed.

Deloitte

Deloitte redesigned their performance management system after realizing that the old process for evaluating people, and then training, promoting, and paying them accordingly, was out of step with their objectives, and very costly [24]. Deloitte tallied the number of hours the organization was spending on performance management and found that completing the forms, holding the meetings, and creating the ratings consumed close to 2 million hours a year. They wanted something more nimble, real-time, and more individualized, and focused on fueling performance in the future rather than assessing it in the past.

The new system that Deloitte created had no cascading objectives, no annual reviews, and no 360-degree feedback tools. The hallmarks of the new system are speed, agility, one-size-fits-one, and constant learning, and it is underpinned by a new way of collecting reliable performance data [25]. The central component of Deloitte's redesigned performance management system is the performance snapshot. This allows leaders to see performance quickly and across the organization, freeing them to spend more time engaging with people. Deloitte created the performance snapshot by focusing on:

- The Criteria. Each part of the snapshot had to contain a single, easily understood concept. They chose four questions: one each about pay, teamwork, poor performance, and promotion.
- The Rater. They were looking for someone with a vivid experience of the individual's performance and whose subjective judgment was important. They chose team leaders because they are the closest to the actual performance of the ratees.
- Testing. Validity testing was conducted by analyzing mean responses and range of responses. They knew if there was a tight cluster of responses, the snapshot would not yield the differentiation they were looking for.
- Frequency. Since Deloitte works mostly in a project structure, they chose to produce a performance snapshot at the end of each project. For longer-term projects, they chose to evaluate quarterly.

IBM

IBM recently transformed its ten-year-old annual performance review system, with the new program aimed at spreading employee goals throughout the year and including more frequent feedback [26]. Under the previous system, employees set their annual goals in January, had a mid-year review with their manager, and would receive an evaluation and a final score at the end of the year, which represented their overall performance for the year. The difficulty with the old system was that goals set early in the year often changed and the actual work assigned to employees was realigned in response.

Many HR departments would bring in a consultant or a few performance management companies to analyze the situation and suggest solutions. IBM HR did not just request proposals, analyze them, and pick one. It turned to its 380,000 employees in 170 countries to crowdsource the process. Diane Gherson, IBM's Chief Human Resource Officer posted a message on 'Connections,' IBM's internal social media platform, asking employees to share ideas for a new performance management system [27]. Her post received 75,000 views and 2,000 comments from employees. The company then organized the comments into themes. The new performance management system that resulted from the process is an app-based performance review system called Checkpoint.

Using Checkpoint, IBM employees set shorter-term goals, and managers provide feedback on their progress at least every quarter. At the end of the year, employees are judged across five criteria—business results, impact on client success, innovation, personal responsibility to others, and skills. Managers assess whether employees have exceeded or achieved expectations for their role in each of those five dimensions or if there's a need for improvement [28].

There is no single measure of an employee's performance like before. In the old system, there was one score, and Gherson said that people tended to be obsessed with that. The new system leads to richer feedback and more meaningful discussions between the employee and the manager.

GE

Even GE, whose 'rank and yank' forced ranking system became legendary has transformed its performance management system. Annual performance appraisals and forced rankings have

long been associated with GE and their former CEO, Jack Welch. The fact that the company which business people most associate with annual performance ratings has abandoned the practice may signal that the annual performance review is an endangered species.

GE has transitioned to a new performance management app, "PD@GE," an acronym for "performance development at GE." Sonia Boyle, GE Canada's Vice-president of Human Resources said that the business exists in an environment of rapid change that does not follow a prescriptive annual performance cycle [29].

GE sought input from 30,000 employees around the world, representing about 10% of its workforce. The feedback indicated a desire for a system that would focus on work that matters, and be available in real-time. One aim of the PD@GE is to foster productive conversations. Employees set priorities in the app and can ask for insights from anyone else. They can also provide feedback to others, thus the dialogue is much broader than just manager to employee.

CONCLUSION

Many other organizations, in addition to those described above, have transitioned to performance management systems that provide more frequent, and often project-based feedback. This reinvention of performance management has spread across a wide variety of industries, including retail (Gap), pharmaceuticals (Pfizer), insurance (Cigna), investing (Oppenhiemer Funds), and accounting (all Big Four firms) [30]. Many of the companies that have reinvented their performance management systems have done so in response not only to a vast base of empirical research that glaringly showed the flaws and bias in performance ratings, but also because of the feedback they received from their own employees through surveys, focus groups, and crowdsourcing.

As we consider the road forward, and what the future of performance management will look like, several trends emerge:

- People want feedback more frequently and this could be at the end of a project, or even in real-time. Faster feedback also allows for course corrections to be made as soon as a problem is identified, instead of waiting until the end of the year.
- The idea of setting annual goals has become obsolete in many work settings. Due to the rapid pace of change and customer demands, goals are constantly morphing, and the accompanying work tasks have to be realigned.
- Performance management systems should provide input on future direction, rather than being focused on past performance. Instead of giving feedback, consider giving feedforward, a term coined by Marshall Goldsmith [31]. Feedforward focuses on providing input for future development. There is a place for feedback, such as when poor performance warrants a post mortem, because people do need to learn from their mistakes. But the overall emphasis should be on the future.
- Conversations are important. Employees and managers want to engage in meaningful dialogue about how to maximize performance. Employees also want to engage their peers across the organization.
- Employees want transparency. When their performance is being discussed, employees deserve to have all of the facts and to understand how decisions are being made.

- Performance evaluation discussions should not be done behind closed doors, where the employee is not present.
- One size does not fit all. Salaried workers should be managed differently than hourly workers. Professional workers are in a better position to manage their own projects and work tasks than industrial workers.

There are two notes of caution that should be considered in regard to the emerging performance management approaches. First, we don't really know if they work or not. The approaches described above are so new that very little empirical research has been conducted into their effectiveness. It appears that these approaches are effective, or at least that employees like them better. But whether they actually improve performance – the jury is still out on that, and this indicates a need for further research. Second, companies moved away from the traditional performance rating because of the rater bias. But many of the new systems still involve some type of performance evaluation and therefore bias is inherent. In fact, it may be that bias will be harder to discover, without the ability to analyze ratings by protected class (race, gender, age, etc.).

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