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Rating Performance May Be Difficult, but It Is Also Necessary

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The company I work for is one of the leading providers of performance management technology (Jones & Wang-Audia, 2013). This technology is used by more than 3,000 organizations worldwide, including several of the companies mentioned in Adler et al. (2016). The technology is highly configurable. It is currently being used to support performance management processes with no annual manager ratings, processes with traditional annual rating evaluations, processes that only evaluate competencies, processes that only evaluate goal accomplishment, processes that mix goals and competencies, processes that require forced-ranked comparisons between employees, processes that make no direct comparisons between employees, and much more. The capabilities of this and other human resources (HR) technology systems are allowing companies to radically rethink performance management because they enable companies to do things far differently from what was possible when they were constrained to more fixed electronic or paper forms (Hunt, 2011, 2015a). The result is an explosion in the diversity of approaches being taken toward performance management design.

My company naturally believes in the value of using performance management technology, but we do not have a strong opinion on what sort of performance management process companies should use. For example, it does not matter to us whether customers do or do not choose to collect annual manager ratings. What does matter is that whatever performance management processes they use add value to their organization, as this directly affects the value they get from using our performance management technology.

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We frequently have discussions with our clients about the value and design of performance rating methods. This often includes questions about getting rid of performance ratings. Experience working with hundreds of companies around the world has taught us there is no one "best practice" when it comes to performance ratings or performance management in general (Hunt, 2015a). Methods that work in one company can fail in another. The following are some additional observations we've gained through our work that are relevant to the topic of "getting rid of performance ratings."

Not Everyone Defines Performance Rating or Performance Management the Same Way

At the broadest level a performance rating is any systematic process that places employees in categories based on their perceived value to the organization. The following organizational processes can all be thought of as form of performance rating. First, there is the traditional performance rating done by an employee's manager. This is done annually in most companies, but manager ratings can also be collected quarterly, monthly, or following major work transitions such as completion of significant projects. Many companies also collect calibration ratings assigned during talent review sessions where managers work together to reach consensus on which employees provide the most value to the company. Compensation increases can also be interpreted as a form of performance rating because they categorize people in part based on their perceived financial value to the organization. I have worked with companies where the annual compensation increase is the only form of rating employees receive about their performance. Employees in these companies use compensation as a sign of their perceived performance relative to others in the company even though many things influence compensation decisions that have nothing to do with actual employee performance (e.g., retention risk, prior compensation levels, budget constraints). Staffing decisions are also a form of rating. For example, a promotion is a form of rating if it implies the organization values the capabilities of the promoted employee over other employees who wanted but did not receive similar promotions.

Not all companies use all these rating methods, and the definition and consistency of the processes used to make different types of performance ratings varies widely across companies. This is particularly true when it comes to compensation and staffing. It is common for employees to comment on the lack of transparency around the methods their company uses to make pay and promotion decisions. Many companies rate employees using processes that are neither clearly defined nor effectively communicated to the people being rated. The reality is that as long as a company's leaders want to know who the high performers are in the organization and believe

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compensation and staffing should reflect relative contributions made by employees then that company will rate employee performance in one form or another.

Companies that claim to have "gotten rid of ratings" usually only eliminated ratings made by managers as part of an annual appraisal. These companies still rate their employees, but they do it in a different part of the talent cycle, such as during talent reviews or compensation calibration sessions. Some companies treat these sessions as restricted and highly confidential and do not share the ratings with the employees who are being rated. They may even intentionally avoid using the word "rating" when describing the sessions. But they are still classifying employees based on their value, which is what it means to rate performance. In sum, all companies rate their employees, but not all companies do it the same way. Our question as scientists should not be whether to eliminate ratings, because companies will always rate employees regardless of what we might claim. Far more useful questions to explore are things such as whether different rating processes, including those largely hidden from employees, are better or worse than traditional annual reviews or whether different rating methods such as those used to collect calibrated ratings yield more or less accurate measures of employee performance. Ultimately what we should be talking about is not whether to rate employee performance but how to help companies rate employee performance in a manner that is accurate, efficient, and effective.

The term "performance management" is also interpreted in a variety of ways. At a general level, performance management can be defined as "processes used to communicate job expectations to employees, evaluate employees against those expectations, and utilize these evaluations to guide talent management decisions related to compensation, staffing and development" (Hunt, 2014, p. 151). There are three subprocesses in this definition: communicating job expectations (this includes ongoing coaching and feedback), evaluating performance, and making talent management decisions related to staffing, compensation, and development. Companies usually emphasize different subprocesses when they define performance management. Some define performance management as a process primarily used to measure performance in order to guide compensation decisions. Other companies define performance management as a process primarily used to communicate job expectations and provide coaching and may use a different name for the process used to collect performance ratings for compensation purposes (e.g., "compensation planning cycle").

One reason companies define performance management differently is because they have different objectives for performance management, such as these (listed in no particular order):

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1. Improve the performance of individual employees over time. This involves providing employees with job information, training resources, and developmental feedback to help increase their productivity and achieve their career goals.
2. Collect data on which employees are contributing the most to the organization and which ones are hindering workplace productivity. These data help companies invest greater resources in the employees who provide the most value and ensure appropriate action is taken to address employees who are decreasing workforce performance and morale.
3. Comply with government regulations. These regulations might have little impact on employee productivity but are things the company must do to meet legal obligations. An example is verifying that employees meet skill certifications required to hold specific jobs.

Most discussions about getting rid of performance ratings focus on improving employee performance, but this is just one of several possible performance management objectives. It is also the one least dependent on ratings. In contrast, ratings are at the core of the second two objectives. A company cannot accurately identify high performers if it does not measure performance in a standardized way that enables making normative comparisons between employees. Nor can it verify whether employees have the requisite credentials required to perform their jobs without rating them based on their qualifications. The entire idea of removing performance ratings is based on a very narrow interpretation of the objectives of performance management. What would be far more valuable is research exploring how these three objectives can be most effectively supported through the use of different performance management techniques.

Companies Are Replacing Annual Manager Ratings With Alternative Rating Methods

Contrary to claims in the Adler article, many companies get considerable value from annual performance ratings made by managers (Hunt, 2015b). But other companies have found collecting manager ratings creates more problems than it solves. This is often true in companies with a history of using rating methods that were highly inaccurate, controversial, or cumbersome (for example, overemphasizing the use of forced-ranked ratings). In these instances, it may make sense to eliminate manager ratings and shift to a different rating method. The following are three ways companies have eliminated manager ratings yet retained the ability to accurately measure, identify, and reward employee performance.

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Shift Ratings From the Employee–Manager Review to Calibration Sessions

Traditional performance reviews involve having a manager and employee sit down on an annual or quarterly basis to review what the employee has accomplished, agree on an overall evaluation of the employee's performance, and discuss future plans for employee development. Many companies are eliminating the second part of this process from the review. Managers and employees only discuss what the employee has accomplished and what to focus on going forward. There is no rating of overall performance. Instead, the information on employee accomplishments is used during subsequent talent review meetings where the manager meets with other managers to rate which employees in the company are contributing the most to the organization. This approach removes the anxiety and distraction created by including an overall manager rating in the performance review conversation. It also creates an incentive for employees to accurately document their accomplishments, because this information will be used at a later date to determine their overall performance level.

Evaluate Employees Entirely Based on Goal Accomplishment

This process starts with managers and employees meeting on a regular basis to discuss, clarify, and if needed, modify goals throughout the year. These ongoing discussions focus on improving goal clarity, supporting goal accomplishment, and evaluating whether individual goals, tasks, and projects are on track. No discussion is made about overall employee performance. The only data that are tracked are about the nature and accomplishment of specific goals. When the time comes to make decisions about employee pay or overall performance, managers refer to existing data and base their decisions on the employee's goal accomplishments. As one company using this process put it, "We focus on what people have done for the company and not who they are as individuals." Companies that use this approach often include safeguards to ensure employee behaviors support company values lest people be rewarded for accomplishing the right things the wrong way. Some companies also calibrate goals based on difficulty and importance, so certain goals are more valuable than others for enabling career advancement or compensation increases.

Rate Employees Based on Future Actions Instead of Past Performance

In this approach, managers are not asked to rate employees on performance but instead rate employees based on recommended future actions that are associated with performance. Examples include rating things like, "Do you think this employee should receive more or less pay relative to their peers?" or "Do you feel this employee should be promoted to a higher level position?" These ratings are not necessarily shown to employees. The advantage

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of this approach is it skips the whole issue of measuring performance and instead focuses on what actions to take with employees. The problem is it obscures the reasons why managers decide to favor some employees over others. This might create inconsistency around how employees are treated and could make it hard for a company to justify why rewards were given to some people but not others.

Allowing Managers to Make Compensation Decisions Without Performance Ratings Is Risky

There is a difference between accurately measuring performance and making effective compensation decisions. But most companies believe that compensation decisions should be largely based on employee performance. Consequently, the primary purpose of performance management in many companies is to collect performance ratings to guide compensation decisions. The risk is performance ratings in these processes may become so tightly coupled to compensation decisions that the two are basically redundant. This often occurs when compensation increases are linked directly to performance ratings. For example, if employees are rated as "solid performers" then they automatically get a 3% increase, but if they are rated as "outstanding contributors" then they get a 4% increase. In these situations managers may not focus on measuring performance in the ratings. Instead they assign ratings that allow them to justify their preexisting compensation decisions, even if their compensation decisions are being influenced by something other than performance (e.g., retention risk). I have worked with several companies that found themselves in this situation and decided to collect performance ratings in a separate process that occurs months apart from the process used to allocate compensation increases. These companies are moving performance ratings out of the annual compensation review process, but that does not mean getting rid of ratings entirely.

For many organizations the use of performance ratings is the only viable way to measure and compare performance across large numbers of employees. There are many reasons why it is valuable to have consistent, well-defined ratings of employee performance. One of the most important is to be able to correlate pay decisions with performance levels to ensure managers are investing more in those employees who contribute more to the company. Allowing managers to make compensation decisions without having any form of performance rating data to validate these decisions can create a host of problems, including these:

- **Confusing pay variance for accuracy.** Some companies use evidence of variance in how managers allocate pay as justification that the compensation process is working because managers are not paying

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everyone the same. The risk is these companies do not know why managers are paying some people more than others. Paying people different amounts is not the same as paying people fairly based on performance.

- **Allowing poor pay decisions.** One reason people advocate getting rid of ratings is because managers struggle to accurately evaluate performance. If managers do not know how to evaluate performance, then they probably don't know how to make performance-based pay decisions either. Allowing managers to make compensation decisions without performance data to validate these decisions can lead to ineffective and unfair allocation of pay.
- **Increasing bias against women.** Research suggests that compensation decisions made without performance ratings are likely to be more biased than processes that link compensation increases to performance metrics. A recent study looking at gender bias in pay and performance decisions found that "the sex difference in rewards (including salary, bonuses and promotions) were 14 times larger than sex difference in performance evaluations" (Joshi, Son, & Roh, 2015, p. 1516). One way to reduce biases in pay decisions is to ensure they reflect clearly defined performance criteria. This is very hard to do across large populations of employees without using some form of performance ratings.
- **Pressuring managers to make compensation decisions based on gender.** Companies often monitor whether pay decisions favor one gender over another. But gender-based pay differences do not necessarily imply biased pay decisions. By chance alone one will occasionally encounter teams where women perform at lower levels than men or where men perform at lower levels than women. If the managers of such teams are expected to ensure compensation decisions are equal, they may change pay solely to decrease perceptions of gender bias even if the differences are justifiable based on performance differences. This implicit pressure to make pay decisions based in part on employee gender is likely to generate even greater issues related to gender equality.
- **Enabling weak managers.** One thing managers think about when making pay decisions is how employees will react to the increase. Difficult conversations can result when employees discover they are not getting what they feel they are entitled to receive. Strong managers accept these conversations as a necessary part of being a good leader. Weak managers try to avoid these conversations. If weak managers don't have to explain their pay decisions, then they are prone to decisions that make their lives easier in the short-term but lead to bad long-term outcomes. Consider the following scenario. A manager has two employees, Bill and Sue. Sue is a high performer who often

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exceeds expectations. She also keeps her calm when things don't go her way. Bill is a solid employee with valuable skills, but in recent years he has grown complacent. His work is okay but far from great. He's also difficult to get along with when things don't go his way. The manager knows Sue deserves a higher raise than Bill. The manager also knows Bill is going complain loudly if he doesn't get the big raise he believes he should receive. In contrast, the manager knows Sue won't complain if she doesn't get all for which she hoped. Will this manager make the right long-term decision and give Sue more than Bill, even though it means dealing with Bill's negative attitude? Or does the manager decide to pay Bill and Sue the same amount just to keep things calm? If managers know they won't have to justify their pay decisions then underpaying Sue and overpaying Bill is going to be the easiest way to go—until Sue eventually quits out of frustration over not being recognized for her contributions and having to tolerate Bill's poor behavior.

- **Frustrating high performers while pleasing low performers.** Most high performers want to be rewarded for their contributions. Eliminating a formal connection between performance and compensation is likely to demotivate these people. High performers will also be frustrated if they discover their lower performing colleagues are getting pay raises equal to or higher than the ones they receive. In contrast, low performing employees may prefer a compensation process that does not link pay to performance. The result is a process that decreases engagement and retention of high performers while increasing engagement and retention of lower performers.

Linking pay to employee contributions is a fundamental part of a high performance work environment (Peterson & Luthan, 2006). It may make sense to downplay the role of performance ratings in the compensation process. But it does not make sense to have managers make pay decisions on their own discretion with no method to test whether these decisions reflect actual employee performance. For many jobs the only way to do this effectively is to collect some form of performance rating.

It's Time for Change, but Make Sure It's the Right Change

Most companies' existing performance rating processes could be significantly improved, many are terrible, and some should be completely replaced. But it is critical to think through the implications of radically changing performance rating methods lest companies find themselves in the following situation:

> We did away with ratings a few years ago, but it didn't really work. The performance management system kind of collapsed as a result of taking away the operating mechanism. And now

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> we are looking to revert back to the more traditional system. (Personal communication from a senior HR executive at a *Fortune* 1000 company)

The challenge of performance rating is that it requires dealing with the reality that all employees are valuable, but some employees are more valuable than others. Companies need methods that accurately assess employee performance without damaging employee–manager relationships or making employees feel like they've been divided up into winners and losers. Removing annual manager ratings may be part of this answer for some companies. But these ratings should be replaced by another clearly defined process to measure performance. Otherwise, companies are likely to replace a flawed but systematic and consistent performance rating process with one that is poorly defined, inconsistently applied, and largely hidden from employees.

The ability to measure employee performance is central to improving decisions related to staffing, compensation, and career development. Performance ratings will remain a core part of performance measurement as long as employee performance is determined in part by how leaders and managers view employee contributions. It is folly to think that leaders are not going to evaluate employees just because we tell them their evaluations aren't accurate. What we need are ideas and research that will improve rating methods, not recommendations to just give up because it is hard to do well. Creating effective performance rating processes can be challenging, but it is also necessary.

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