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Performance reviews: do they really matter?

In an age of disruption, no other managerial process is experiencing change more than the traditional performance review. It is estimated that 10% of organizations globally have ditched the annual performance review process for something more productive, agile, simple and two-way. In this article we examine the trends and the implications for People and Culture professionals globally.

The annual performance review is arguably one of the most dreaded rituals for most employees. Self-assessments of past performance, goal settings for a future that is often unclear and subject to disruption, add into the mix the occasional awkward requirement to rate one's peers – no matter the industry, the process throws up more questions than it answers.

And yet, the annual process is tolerated because there seems to be no other option to allow organizations to manage underperforming workers or reward the achievers. Once embedded in an organization with its myriad traditional HR systems and policies, it's hard to move on.

However, since 2011, a number of organizations globally have started to question whether the performance review process established by the US Army during World War I is relevant to today's modern world.

Introducing the merit rating system

Used to identify and dismiss poor performers in World War I, the US army's merit rating system soon spread to corporate America, and from there to most of the Western world. By the 1940s, it was estimated that 60% of US companies used this system. Two decades later, this figure had rocketed to 90%. The simplicity of the system which assigned a numeric score to an employee was attractive in its perceived transparency. It provided an easy tool for organizations to base decisions on wage increases and organizational advancement.

While this system worked well in an economy full of factory lines and corporate offices, the shortcomings became apparent with a shortage of managerial talent. By the 1960s, the performance review was used to make decisions on which employees should be developed and nurtured into more senior roles. And yet, there were inherent weaknesses in this use.

The merit system looked at past performance and focused on accountability; development of managerial talent required an assessment of a person's leadership potential. Furthermore, a proper assessment of an employee's development needs required two-way in-depth conversations between an employee and the supervisor in which past projects were assessed, future goals set, and development gaps identified and addressed – done properly, this would take several days for each employee and went beyond a simple number.

While the inherent weaknesses of the system have been identified by users and researchers, the legal and economic environment ensured that traditional performance reviews remained in place for decades, with only minor changes adopted. Over time, the system had become so embedded in organizational processes that it became too difficult to dislodge.

Fast-track to the 2000's and the world has changed. Digital platforms, multiple projects, globalized workforces, constant disruptions - as tasks became more complex and agility became prized, it was increasingly difficult to set goals a year in advance. Some organizations sought to address this by introducing half yearly reviews, but this created additional problems for time poor employees and their supervisors – it was seen as doubling the time commitment needed for a system that was already flawed.

In addition, survey after survey showed both managers and employees questioned the worth of the process. Employees resented being compared with their colleagues particularly if the tasks were different, and managers felt that spending weeks each year on a flawed process was a waste of time. Researchers also found that where managers were asked to assess their direct reports, bias colored the results – managers would rate more highly people whom they liked or who were like them, reinforcing the lack of transparency and fairness in the process. In a 2000 study by Michael Mount, Steven Scullen and Maynard Goff, it was revealed that 62% of the variance in ratings reflected the rater's own perceptions, with only 21% attributable to actual performance.

In the past decade, we've witnessed some organizations attempt to change their performance review processes in the face of this increasingly complex world.

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Disrupting the process

In 2011, Kelly Services was the first major professional services firm to abandon the traditional review process. This was quickly followed by other firms such as Deloitte, Microsoft, Adobe Systems and Accenture.

Why? Because it was good for business.

As the war for talent intensified in this global and technologically driven world, organizations recognized that developing their people was one of the best ways to retain their staff. An appraisal process that allowed organizations to meaningfully delve into staff development needs was necessary for them to maintain their competitive advantage. As projects became more complex, ongoing support that enabled staff to successfully complete projects was preferred to an annual system that only allowed you to look back on past performance.

The increasing complexity of work requiring team members with different skillsets also placed increasing value on teamwork. Under traditional performance processes, the focus was on individual achievement, and those who were skilled at self-promotion ultimately fared best.

To adapt to the new environment, organizations needed a system that allowed for ongoing check-ins, rather than a once-a-year conversation. It required an organizational mindset that accepted short-term goals over annual targets. It demanded an acceptance of ambiguity to allow for innovation and agility. Sounds simple? Well, implementation has thrown up some challenges as modern organizations seek to overthrow an established process that has been in place for almost a century.

Mapping the way forward

The first challenge is to create a feedback mechanism that reflect the organization's and individual's perspectives. It can be hard to find a mechanism that aligns individual's goals with organizational objectives.

Deloitte started with a basic question; what was the objective in its performance management system? The answer was threefold – it would allow the organization to recognize performance; it would provide a more complete view of the employee's performance throughout the year through aggregating data at various times; and it would help fuel performance.

In other words, rather than use the system just to measure and reward existing performance, the new system would enable Deloitte to help employees improve their performance.

With those objectives in mind, Deloitte introduced a simple system in which team leaders are asked to respond to four future-facing questions at the conclusion of each project or every three months for long-term projects.

The questions relate to pay, teamwork, poor performance and promotion:

1. Given what I know of this person's performance, and if it were my money, I would award this person the highest possible compensation increase and bonus (measures overall performance and unique value to the organization on a 5-point scale);
2. Given what I know of this person's performance, I would always want him/her on my team (measures teamwork on a 5-point scale);
3. This person is at risk for low performance (identifies problems on a yes-no basis);
4. This person is ready for promotion today (measures potential on a yes-no basis).

At the other end of the scale is the Real Time 360 Review. Rather than just soliciting views of the team leader, the 360 takes feedback from a range of people who have worked with the individual on an ongoing basis. Technology allows for this to happen seamlessly and Goldman Sachs is one organization that has adopted this.

The 360 Review involves an initial rating exercise in which every employee rates all other employees to establish a baseline. That baseline is then augmented each time a review is received which can happen daily. The drawback to the 360 is that the initial feedback from the baseline can be very confronting and having skilled people to review the feedback is critical.

There is also debate as to whether the feedback should be anonymous – will it encourage trolling or will it foster more honest reviews? Supporters of anonymity say that it encourages honest feedback on the organization's leadership, something that very few leaders receive.

The second challenge is organizational culture – with reviews firmly embedded as an annual event, how difficult is it to change?

Deloitte based their decision on evidence. In exploring whether change in their performance review system was warranted, it came down to a simple fact – in an organization of 65,000 employees, the process took up 2 million hours each year – hours were spent in filling forms, meetings between employee and supervisor, followed by more closed-door meetings about the outcomes. “We wondered if we could shift our investment of time from talking to ourselves about ratings to talking to our people about their performance and careers,” reflected Ashley Goodall, director of leader development at Deloitte Services.

The third challenge is implementation – it’s not enough to have the right questions and a workforce that has a desire to upend existing systems. The final hurdle is how the change is rolled out and this comes down to leadership.

Any change program of this scale requires championing from the top, investment in training, and investments in the appropriate systems. In many cases, this involves emerging technology which makes real-time and continuous feedback possible.

The scoresheet

Even so, it hasn’t been smooth sailing. While Adobe reports that this system of regular check-ins has led to better discussions, high employee satisfaction and fewer dismissals because employees are coached more closely, firms are weighing up the pros and cons of moving in the same direction, despite the fact that most workforces reject the traditional appraisals. This is partly due to uncertainty over how a revamped system will look and work, and the costs involved in set-up. At Amazon, which thrives on a culture of competition and sales figures, rankings provide an incentive for performance.

Deloitte, having initially withheld numeric ratings, has now reintroduced it. The rationale for withholding the rating was that experience showed there was a tendency to sugar-coat the ratings when the rater knew it would be shared. By keeping the responses private, they believed that the assessments would be more accurate. However, the unintended consequence was a perception of lack of transparency. Some employees also wanted to know where they stood, particularly if they were making decisions concerning their long-term future at the firm. So now, employees receive snapshots of their performance on a quarterly basis through ratings on each of the four categories.

Like Deloitte, other organizations have sought a middle ground. While one insurance company initially eliminated formal ratings, pay-increases were being discussed internally and became known as “shadow ratings” which affected other management decisions. As a result, that organization went back to formal appraisals but with quarterly catch-ups where the emphasis is on development.

A changing workforce

This questioning of performance appraisals is part of a shifting zeitgeist. A movement towards shared dialogue, development over accountability, and teamwork over individualism is part of the growing demand for inclusive leadership.

Leadership expert Rasmus Hougaard and his co-researcher Jacqueline Carter interviewed 250 “C-suite” executives from Microsoft, Google, Lego and others, and assessed 35,000 leaders from around the world based on more than 1,000 studies. They found that the next generation of workers are demanding a different style of leadership – one that is more direct, more personable, more approachable.

“What we’re seeing these days is a whole new population is joining the workforce, especially Generation Y, who are asking for more than just a pay check and an annual grade,” Hougaard says.

The upshot? Younger workers are changing the workforce and management must adapt accordingly. They are also not attracted by the prospect of long-term employment in one place and organizations need to consider how they can get their most from their employees who may only stay for a few years. In that context, development, personal growth, meaning, purpose, a sense of belonging and genuine happiness outweighs anything that can be conveyed with just a ranking.

Hougaard argues that organizations that put people at the center of their strategy are those that will achieve the best results. This starts with how performance is reviewed.

The journey commenced by Colorcon, Deloitte, Adobe and others this decade is one part of a long continuum that had its beginning in the military but is now reaching into every sector of society. As we seek meaning in our work and deeper connections with each other, as we look towards an uncertain future filled with disruption but also brimming with opportunities that flow from that uncertainty, the performance review process has to change to reflect the shifting priorities of the people who are asked to participate. For those organizations willing to take the leap and to bring their people with them, they stand to gain from an engaged workforce that feels they are more than just a number.

Conclusion

Shaking up the performance review process has been an effective method of shifting culture for a number or organizations. The move towards a two way dialogue, shared accountability and inclusive leadership has had demonstrated positive impacts on their organization culture and employee engagement. The competition for talent in the market is not going to decrease, so it is worth considering making changes to the performance review process for the benefit of organization culture, improved employee engagement and ultimately, the bottom line.

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