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Improving Organisation Performance

A systems approach

DISCUSSION PAPER, NOVEMBER 2015

Andrew Lambert

"Managing the knowledge worker for productivity... requires a clear mission, careful placement and continuous learning and teaching, management by objectives and self-control, high demands but corresponding responsibility and accountability for performance and results."

Peter Drucker.

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About PARC

PARC was founded in 2004 to provide a centre of excellence for the development and management of high-performing organisations.

Through the provision of informative and challenging research and briefings, PARC enables HR and Reward Directors to engage with leading thinkers, expert practitioners and each other on the key issues affecting today's organisational performance, reward and governance agenda.

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Introduction

Improving the performance of organisations is a perennial debate. The VUCA acronym (volatile, uncertain, complex and ambiguous) to describe the context for organisations today is probably over-used – but does help to explain why performance management needs to be thought about in a rigorous and holistic way.

Performance means different things to different commentators – some focus on financial measures, others on innovation for example. Even when the focus is on the contribution that people make to the collective context, the words 'performance management' are all too often narrowly interpreted as a particular kind of personnel control system. Many are unhappy with the effect, and there is an increasing clamour to discard some of the core mechanisms typically involved.

This discussion paper seeks to take a fresh look at the people components of improving organisation performance – from direction setting to reward – but frame it in the wider context of how organisations as a whole are run and developed.

It builds on previous work by the author and colleagues at both PARC and the Corporate Research Forum. It also involved fresh discussions with executives from a range of companies, mostly large and global in scope, together with input from expert commentators and researchers, and a review of relevant literature.

There is an almost overwhelming quantity of material available, but the purpose of this paper is to be succinct, and to stimulate thinking and reflection on organisational practices. We offer a model for this, together with some suggestions for improvement, and a conviction that progress can only be made when a holistic, systems-based approach is taken – the antithesis of the 'cluster of 1'(isolated initiatives) so often seen.

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SETTING THE SCENE

When looking at improving organisation performance, all too often this gets short-circuited to 'performance management' or 'performance management systems' and therefore widely viewed as something that HR functions design and manage via a narrow focus on employee performance appraisal and rating systems. But why?

The ownership of managing performance logically starts with the leadership of the organisation – accountable to key stakeholders such as owners, investors, business partners and employees.

- Leaders in turn should be seeking to ensure that every manager and employee also takes ownership of performance in respect of their area of responsibility; and leaders have a responsibility to create the conditions for employees to be effective.
- Every function – finance, IT, marketing, logistics etc, not just HR – has an important contribution to how performance is achieved and improved.

From our research we have seen that there is a rising dissatisfaction with 'traditional' ways of assessing and measuring individual employee performance, leading to a small but growing number of prominent organisations abandoning annual appraisals and performance ratings. Is the real problem that these mechanisms have been designed and implemented poorly, failing to adapt to changing work realities? Or is there something fundamentally wrong with them in principle?

There are also increasing questions about the effectiveness of the link between performance and reward. Should and do performance assessments lead to appropriate reward decisions, and do reward mechanisms in turn have any real bearing on how performance is achieved and enhanced?

Last, but not least, is the respective contributions of HR and line managers, and in particular the capability of both to address performance better. Undoubtedly there has been a history of managers ducking or being poor at managing their people issues, and HR has been sucked into filling that gap. For many years HR has been under pressure to stop this 'hand-holding'. The advent of self-help software for managers and employees, minimising the need for personnel administration, raises an even sharper question mark about how HR managers add value to the way the organisation performs.

Who manages people?

In smaller organisations with little or no HR function, it tends to be clear by default that managers manage performance. In larger organisations, the picture has been more muddled.

The notion that performance management is an HR process derived from an era when industrial relations battles placed personnel functions at the heart of employers' control mechanisms. Managers were allowed to pass off their people issues to 'HR' and concentrate on being technical specialists and task controllers. They saw 'performance management system' as an HR-led process of review and pay decisions with which they had to comply.

We are now in a very different era – where organisations must burnish their employer brand, engage employees, attract and retain talent; manage fluid, globalised and virtual structures in an increasingly unpredictable environment; replace silos with collaborative practices to drive innovation; use the 70/20/10 approach to drive learning; and develop leaders who inspire rather than command and control.

Hence organisations need to recruit, develop and promote managers who are effective at understanding, coaching and developing their people, and not just focusing on tasks. But after years of toying, are they any better at doing this? The evidence is not convincing.

DEFINITIONS AND A FRAMEWORK FOR PERFORMANCE MANAGEMENT

Performance requirements

These are the main dimensions for managing individuals' performance

- role specific outcomes and behaviour
- broader positional requirements – e.g. leadership, management, talent pool and other competency frameworks
- task specific outcomes and behaviour (including projects)
- non-job specific – e.g. general behavioural and ethical standards, personal skills and characteristics, safety behaviour.

Other aspects to consider

- effort, commitment and engagement
- education and development – personal learning, coaching, mentoring, thought leadership and sharing.

Aubrey Daniels' definition

Performance management originated as a broad term coined by Dr. Aubrey Daniels in the late 1970s to describe a 'technology' (i.e. science imbedded in applications methods) for managing both behaviour and results, two critical elements of performance. Daniels' definition of performance management is 'a scientifically based, data oriented management system that comprises three main elements – measurement, feedback and positive reinforcement'. This still misses the starting point of direction and shaping.

In the third century AD, the Chinese were not only using performance appraisal systems but were critiquing each others' biases in their evaluations of their employees.

Performance

There are many different understandings of what is meant by performance, therefore organisations need to be clear about the language they use and the meaning this conveys. It should be clear at every level what 'good' and 'poor' performance looks like – and this should be accepted as fair and valid by organisational stakeholders. For example, those at the 'front-line', particularly knowledge workers, frequently know more about what is truly effective than more remote leaders – inclusion of this wisdom can lead to more robust targets and standards.

'Performance' as a word refers to behaviour rather than outcomes (John P Campbell), but for individuals in a business context it needs to encompass both the 'what' and the 'how' – and on two broad dimensions, the collective and the personal. Performance requirements should be set for both – they should align, but will not be the same.

Performance management

The literature on the subject provides many explanations of this simple phrase that are surprisingly shallow. Many reflect the narrow view of life of traditional personnel practitioners – focusing mostly on individual performance and the relationship between managers and managed. By contrast, Boston Consulting Group in "The Art of Performance Management" expound on IT and accounting processes, with Chief Financial Officers positioned as 'chief performance officers'. HR hardly figures.

We argue that managing performance is about initiating, enabling, assessing and then re-setting performance activity – a continuous cycle, a whole system for managing people and other resources.

This whole organisational perspective involves

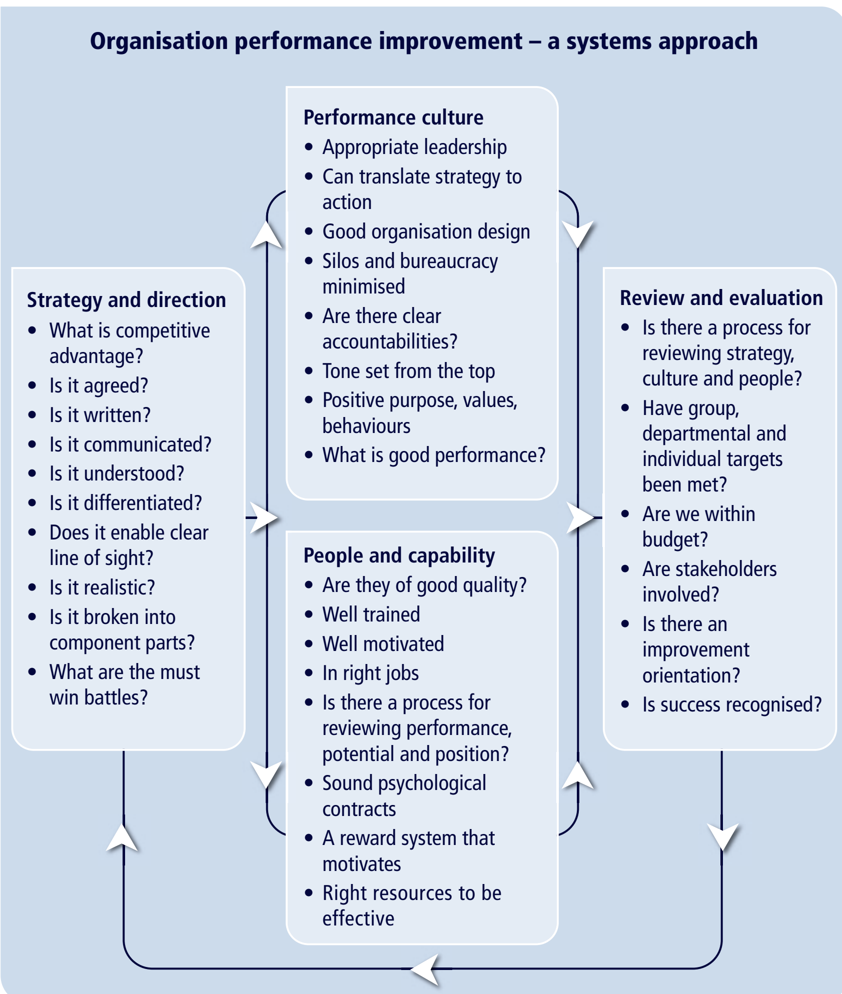
- alignment of resources – human and other assets and capabilities – to meet strategic and operational objectives, whether financial or non-financial
- integrating the ways an organisation does its business
- turning strategic goals into operational outcomes
- measurement systems that provide insights and stimulus for better results.

Important expectations of this system are that it enables performance improvement, develops capability and provides robust rationales for reward and promotion decisions. And that the organisation is sustainable into the future.

Performance management – a holistic framework

Our PARC diagram provides an overview of the components of a systemic approach to improving organisation performance with particular focus on the people related issues. It is by no means exhaustive, but it is a good frame to further explore the research. You may have your own model – but it is surprising how many do not. A couple of points

- the model looks at inputs as well as outputs – the shaping of performance and the factors that affect it are as key as evaluating what has happened afterwards
- much of the model could be summed up as just 'good management' – and that would be true. However, to what extent does this happen in practice?



When it comes to the detail of how such a model is applied, there is no 'one size fits all', as there are factors that are specific to an organisation's circumstances and context. There is no substitute for experience and judgement in getting that right.

Complementarity with other models

This performance framework has similarities to the 'star model' created by Jay Galbraith to guide organisational design – inevitably, since design of organisations and work is a core issue in managing performance. As with the star model, appreciating the interactions between the nodal points is also important.

All the inputs are key to managing performance, but the way results and behaviour are assessed also forms part of the 'management' process, and feeds back into the other dimensions of the model.

There are also complementarities with other useful models, such as those concerned with excellence – European excellence model, Deming and Baldrige awards, Investors in People, Six-Sigma, 'Lean' and more besides.

THE MODEL STAGE BY STAGE – RESEARCH FINDINGS AND INSIGHTS

Governance and performance

By 'governance' we refer to the system of principles and disciplines whereby an organisation is managed. It is fundamental both to what glues an organisation together and what ensures that it delivers on its promises. Effective governance is about both clear processes and good behaviour.

While much of the focus is naturally on how boards and top management conduct themselves, good corporate governance is as much about the culture and teamwork that leaders embed (or not) at every level.

Especially since 2000 there has been a wave of regulation and guidance placing varying requirements upon organisational governance across the globe. Why? Because of poor performance and behaviour, particularly in certain sectors – e.g. financial services, energy companies, pharma, and more recently car manufacturers.

While there are complaints from some organisational leaders about spending more time and energy on compliance than performance, the best companies rise above this and get on the front foot.

STRATEGY AND DIRECTION

Essentials and trends

The performance story of an organisation logically starts where the key decisions are made about its strategy and direction – at the 'top of the house'. This is also where the risk appetite and behavioural standards should be articulated, and governance set in place.

Commercial organisations primarily seek to please their investors – but they can vary vastly in their performance expectations and methods of oversight, from the purely short-term and financial through to longer-term, actively involved. Pressures from this and improved reporting standards are also changing the expectations of good performance.

- 'Integrated reporting' requires organisations both to pay attention to wider stakeholders' performance expectations and to improve explanation of how lasting value is created.
- This demands greater focus on non-financial performance – for example use of human, social and intellectual capital; environmental impact; technological competence – and how all that interrelates with financial results.
- In turn organisations need to be better at how they collect, analyse and present data – including about people and behaviour.
- Better governance also means focusing on values and behaviours, not just results. This is reflected in changes we found many companies are making to what they target and reward, whether voluntarily or under regulatory pressure.
- Board directors are being forced to raise their game in order to achieve effective oversight – that means devoting more time to both internal and external analysis.
- However, many organisations still struggle to generate reliable information.

Inevitably there are shifting expectations about leadership too – with a growing mistrust of the swashbuckling style, and a desire for characteristics that build lasting companies, together with the resilience and transparency to survive in an open, social media age.

Dr. Stephen Bungay's (Ashridge) '*Trilogy*'– the notion of the differences between 'Managing, Directing and Leading' – is noteworthy. Each is pivotal to effective performance but require different skills and attributes rather than being 'lumped together' – and it is rare to find someone good at all of these.

There is a fundamental requirement for leaders to provide directional clarity through the way they articulate and communicate purpose, strategy and the plans that operationalise these. Plainly, some are better than others at doing this.

A study by the Institute for Corporate Productivity for the American Management Association (AMA) identified that the largest gap between low and high performers was due to simple but fundamental factors, such as whether organisations' strategic plans were clear and well thought out, whether their goals focused squarely on satisfying their customers and publics, and whether they continuously review and improve what they do, as part of ensuring strategies keep up with events.

Dr. Rebecca Homkes (London Business School, Ashridge) highlights common failings in so-called strategies – at the flimsy end, comprising just a financial projection or target, imprecise and cheerleading soundbites such as 'being the best', and a combination of buzzwords; or alternatively being a weighty tome that no one can remember, and are hence unlikely to adhere to.

In today's complex world, leaders have to work ever harder to devise strategies that create sustainability, and need to manage tensions between often opposing pressures.

- Leaders are being pushed to achieve over the long-term when even the short-term is becoming hard to predict.
- Uncertainty saps both employee and investor confidence, and undermines performance.
- Just as different sectors move at different speeds, so do parts of large and often varied organisations. While for some activities, traditional annual cycles are increasingly too infrequent, other activities still need a more measured and longer time-scale.
- Thus most organisations need to be more flexible and variegated, while at the same time recognising where consistency and alignment ARE important.

Over 15 years ago Jack Welch and Steve Kerr at GE identified the need for an approach to strategy and organisation that was capable of adapting to any challenge. Most organisations are still struggling to get close to that state. And some 20 years ago Kaplan & Norton's research first identified that poor execution and articulation of strategy was widespread, with 10% of employees actually understanding what the strategy meant. So we still have a long way to go.

Strategy-making effectiveness

Organisations need to build their capacity for devising and executing strategies, by

- creating a lasting organisational purpose that enthuses all stakeholders
- constant environmental scanning, sensing and analysis – open to ideas but understanding their context
- 'strategising' closer to markets and fast-moving operating realities – balancing bottom-up and top-down perspectives and needs – in an iterative process
- focusing on a few critical goals, avoiding fads and 'initiativitis'
- communicating strategy effectively
- vertical line of sight from strategy to team and individual objectives – and horizontal alignment where relevant
- researching what works and what doesn't, to support decision making
- fostering innovation and improvement at all levels, with the re-setting of objectives this demands
- never relaxing in their hunt for competitive advantage
- building brand value that provides and communicates real differentiation
- head office strategy teams and central functions being facilitators – not controllers.

Top down and bottom up

In today's fast-moving environments, much knowledge about what is needed resides at the sharp-end of organisations. To ensure decision-making is agile and relevant, these perspectives should be blended with the helicopter view from head offices – not so much about overall direction or strategic choices as about priorities and ideas. But what did our investigations reveal is happening now?

- Deloitte is notable for its consultation process amongst employees about strategy, but few other organisations are as systematic in obtaining bottom-up contributions.
- Mostly, 'bottom-up' just refers to a negotiation process between business unit teams and head office about what results are deliverable. Some business unit leaders are good at consulting widely, others not.
- While employee engagement principles stress the importance of the employee 'voice', engagement surveys are of limited utility as consultation tools.
- The only other consultative mechanisms cited in interviews were innovation and improvement ideas schemes.
- Status and power-distance still pre-dominate in many business cultures.

Greater performance will likely demand greater involvement, but many organisational leaders still have a major logical and emotional shift to make. The wider context is one of increasing democratisation pressures, with millennials expecting more voice and responsibility.

Insights from interviews

We spoke to Standard Life Investments, a prominent active investor in public companies, and Bain Capital, a very hands-on private equity investor. The question of confidence in the governance and leadership of organisations is critical in their estimation of performance. But they shared one cardinal point – there is no 'one-size-fits-all' performance metric set. Organisations are compared and judged on a case-by-case basis – whether using financial or other measures.

As for the latter, there is little yet in the way of standardised metrics except for relatively tangible areas such as health and safety. Institutional investors vary in their attention to 'hygiene factors,' and in their ability to find insightful performance indicators where hard metrics are elusive.

Guy Jubb of Standard Life Investments refers to building expertise in analysing a mix of factors – employee risk and engagement data, understanding any management churn, benchstrength, skill shortages, technology track-record. "We need to be steadily more creative in how we assess both results and future capability. We use 'quadrangulation' – i.e. many touchpoints to build an accurate picture."

It is essential to get a feel for 'tone at the top', and there is no substitute for seeing how boards and executives behave in person. It can be particularly illuminating observing interaction with their employees – how formal or relaxed is this? "We start as sceptics – slick presentation won't fog us. And humility is more impressive than arrogance, particularly when there are slip-ups."

Stephen Dando – himself a former Group HR Director – explains how Bain Capital prioritise getting leadership teams in shape, and then ensuring that they create positive performance cultures, engaged workforces and deep talent pipelines in order to deliver over time. "We're in the business of building great companies, so we have developed a deep understanding of factors that create sustained performance."

Other specifics include clear accountabilities, well-cascaded objectives, open-feedback environments and avoiding bureaucracy.

However, the way cascading objectives from the top is done varies considerably.

- Clarity about direction is the first essential. A priority at Vodafone, for example, has been 'simplification' in order to generate greater collective focus.
- Some CEOs stand out in the way that they take discussion of strategy to employees at large – through roadshows, video broadcasts – bringing strategy to life and then providing regular updates on progress and shifting priorities, thereby helping business teams and individuals to refine their objectives as the environment shifts.
- High performance requires creating a sense of 'ownership'. People who feel like pawns don't perform – especially if doing 'knowledge work'. However, involving employees in decision-making is still the exception.
- Software tools that systematise objective-setting and performance tracking are spreading. This increases the sense of discipline, but can also create a mechanistic flavour.

Some more innovative organisations are learning to trust people close to markets and operations to assume greater responsibility for setting direction, in a fluid and dynamic process, within parameters set by leaders. However, traditional cultures – still wedded to hierarchies, power distance and top-down control – remain the norm, with significant differences between national cultures. The expectation is growing that such cultures will fail due to underperformance – time will tell.

AB Food Group

AB Food Group sees the way it manages strategy and performance as a significant differentiator.

- Its 64 business units generate focused strategies to meet their varied challenges, and define what good looks like in their markets.
- The relative autonomy of running your own business is a key attraction for ABF executives.
- Its slim Group office engages constantly in a challenge process – not telling people what to do but checking for any misalignment between strategy, planning and capability to deliver. HR plays a leading role in this discussion.
- It also keeps a careful watch on the shifting performance demands of external stakeholders.
- Group takes its governance and funding responsibilities very seriously, but believes that "too much process kills entrepreneurialism".

"Our levers include lots of contact and our ownership of executive careers" commented Group HRD Des Pullen. "It's about building mutual trust, and we do this continuously over time."

Meanwhile, AB Sugar HRD Quintin Heath does the same with his six business units – working with the CEO to ensure that strategies are fit-for-purpose at a time of considerable change. "Our operating reality is that some individuals have significant impact, but getting the organisation to swim in the same direction has more. I'm more concerned about the robustness of business and functional plans than how well appraisal works."

Culture and performance in banking

Some years ago all the major UK bank groups declared their intention to undergo fundamental culture change – re-orienting their performance priorities – in the face of public outrage, political pressure and the weight of regulatory punishment. Concern is universal, given the criticality of the finance sector to how both businesses and individuals operate.

They have mostly shed investment banking operations that they seemed neither sufficiently to understand nor manage, and which made their brands toxic. In retail they have all stated they have replaced a hard sales targets approach with devotion to service.

Yet progress has been patchy. A recent study by Which magazine identified that, while there has been a shift towards service, old habits die hard, with significant numbers of branch staff reporting they are still under pressure to sell regardless of whether it is appropriate. Meanwhile, many business customers have been outraged by their treatment by banks, and have sought alternative financing.

And with frequent systems breakdowns putting their technological competence under question, there are few admirers of bank performance in today's society, in contrast to the past.

So, what should their CEOs and the HR functions that support them be doing differently and better?

PERFORMANCE CULTURE

Essentials and trends

Organisational culture is the set of embedded behaviours that the citizens of an organisation display. In coining the pithy phrase "culture eats strategy for breakfast", Peter Drucker highlighted that merely setting a course does nothing to guarantee arrival. It is the way people conduct themselves that determines how well plans are executed, targets reached and value generated. How governance and leadership is exercised significantly influences these behaviours.

Aubrey Daniels' previously cited work on performance management starts with the simple point that positively reinforcing good behaviour drives desired outcomes and creativity; positively reinforcing poor behaviour does the opposite. Values and behaviours are thus critical in determining performance – personal and organisational.

These are some significant trends.

- Balancing results and behaviour, addressing both the 'what' and the 'how' – scarcely a new idea but given recent impetus by regulatory action against poor governance and bribery.
- Increasing focus on collaboration – internally and externally. This demands a constructive way of being competitive – avoiding negative rivalries and self-interest, permitting multiple winners.
- Better organisations are taking employee engagement seriously. While being more engaged does not guarantee higher performance, it clearly increases its probability, just as greater disengagement heightens the risk of performance deterioration.
- Increased attention being paid to wellbeing – research shows how performance benefits from addressing physical and mental health, and reducing negative stress. The more an organisation shows it cares for employees, the more likely the latter will care for the organisation.
- Moving towards more 'social' organisations and empowering self-management, aided by technology tools, in order to enhance agility and speed – this requires building trust rather than controlling through hierarchies.
- Learning to be more diverse – nationality, gender and thinking styles – as the pressures to innovate and globalise intensify.
- More humble and 'human' leadership – open to question by stakeholders and to engaging with the fresh thinking of their rising millennial talent.

Insights from interviews

Interviewees identified three essential building blocks in fostering a high performance culture.

- Use clear language about what kind of people you want and what you expect them to do.
- Back that up with consistent actions and processes in how you manage and reward people.
- Measure effectiveness and outcomes in ways that convey a passion for continuous improvement.

Here are three examples of approaches taken.

- Liberty Global talk about "we just do it better, every time". In raising the bar continuously and committing to constant innovation, people are challenged to find new ways of doing things. As well as growing rapidly, there is also strong emphasis on lowering costs – innovation is about economising not just adding new things.
- AB Sugar makes it clear it wants 'can-do' people with ambition, drive and tenacity, who can deliver creatively but practically. However, it is the way company processes stimulate entrepreneurship that ensures these are not just platitudes.
- Stimulated by board-level pressure, GSK has focused strongly on 'changing how we change', involving several years' work to embed better understanding and skills among managers to drive performance improvement.

Cross-referencing business results with engagement survey scores is the most typically-used temperature gauge for performance culture. HRDs agreed that if you know your organisation, it's not difficult to tell where things work well or not – but taking follow-up action is what counts.

Organisations that have had reputational challenges unsurprisingly place particular attention on behaviour. However, they still have to be firm about achieving business results if they are to avoid losing performance momentum.

Everyone we spoke to is focusing harder on collaboration and learning. Organisations also acknowledge they need to work on systematically consulting employees on what would enable them to work better – minimising the 'hassle factor'. Such consultative channels as exist tend to be focused on extracting answers to pre-determined questions or are no more engaging than a suggestion box. What works better are approaches that actively and continuously involve employees as improvement think-tanks.

Ask for more

Setting 'stretch' targets, conceiving 'big, hairy, ambitious goals', going the extra mile – these are phrases commonly used by organisations aspiring to higher performance. But there are right and wrong ways of going about it.

The key is to 'ask' rather than 'demand'. When people are pushed, the natural instinct is to resist, not to commit, to argue that all that can be done is being done already. Threats and bribes can produce short-term compliance, but not lasting effort.

The secret lies in

- involvement – invite and excite people into the idea of re-imaging what's possible
- shared interest – it's not about pleasing a leader or manager, it's about a greater good (the organisation, customers, the team); and sharing the rewards of success, both recognition and tangible rewards
- keeping it simple – what's being aimed at and what's involved
- effective support and enough resources.

Care should also be taken to avoid people being 'over-wound', so that they risk burn-out. If mistrust has created scar tissue, that needs to be dealt with before people will be ready to respond.

Good examples of how to go about this include GSK's 'change how we change' initiative and the 'work-out' process used by GE – and others subsequently – to achieve step-changes in performance.

Focus on an issue works, be that costs, sales, innovation or time to market. Relentless focus on outcomes produces improvement and is well chronicled.

What poor people management costs

The Impact of Investing in People study (TBR, 2015) was based on research into 8,750 businesses and Office for National Statistics data.

It found that six factors were statistically significant in explaining improvements in efficiency and performance – strong and inspiring leaders, having a set of strong values, recognising and rewarding performance, structuring work, delivering continuous improvement, and the adoption of sustainable practices.

The sector that would benefit the most financially, unsurprisingly, was the professional and financial services industries, which could gain an additional £29.9 billion in output. As for the public sector, health and social care could benefit by a potential £2.4 billion in productivity gains.

While no one study can be relied upon and the rigour of methodology needs checking, there have been previous studies with similar results.

The question for organisational leaders, boards and their stakeholders – including investors – is: what is the room for improvement that applies to their particular organisations? And what are they going to do about it?

PEOPLE AND CAPABILITY

Essentials and trends

High performing organisations self-evidently require good people, but also need to resource them well and maintain a cultural environment that allows them to flourish. Otherwise they won't join or stay. These are the key trends.

- Increasing automation is putting pressure on administrative as well as low-skill jobs. Smart use of technology helps small organisations challenge larger ones, whose people are often still encumbered by legacy systems and practices.
- Winners will be those that best balance adopting new technology (adapting to mobile, cloud and data-rich environments) and thereby achieving leaner but more productive workforces, whilst also sustaining an attractive employment offer that appeals to talent.
- Employers need to be sharper in every aspect of workforce planning and management to avoid the critical skill shortages – particularly in rapidly evolving markets – that recent surveys highlight.
- The increasingly globalised talent market requires more flexible thinking by employers.
- Employer reputation is particularly significant in an era dominated by social media. What is said on Glassdoor and similar websites is trusted far more than what employers say.
- Millennial talent gravitates towards employer brands that enhance employability – those that fail to live up to their promise are now found out fast. Less glamorous employers have to work harder to attract and retain mobile talent.
- Money still matters in terms of initial attraction. However, the real issue is the totality of the employee experience – a combination of many factors, not just the mercenary price tag. Is this an organisation that really understands and supports me?

Commentators agree on one overarching issue – the overall standard of people management has not improved in the last 15 to 20 years. This insidiously costs money – a recent estimate quotes an annual loss to UK companies of £84 billion. This again begs the question about how to improve both managers and HR.

Insights from interviews

Every organisation we spoke to indicated it was on a 'journey' in improving leadership capabilities among its manager population. Despite decades of spend in this area, it still seems that many feel they have some way to go.

On the one hand, talent and leadership development is a 'Forth Bridge' challenge – it never ends. Yet the talk in HR circles about more focus on engagement and coaching skills is scarcely new. It just seems that whatever has been done in the last ten years or so has been insufficient.

Where notable progress has been made, this seems generally down to strong leadership – for example Paul Polman at Unilever, Mervyn Davies at Standard Chartered, Andrew Whitty at GSK, John Malone at Liberty. Nothing new there either, excepting perhaps that CEOs now do need to be great role models as people managers. Good people will join and stick with an admired leader – which means succession remains a perennial challenge.

The best CEOs ensure they have a strong, OD-oriented HR leader in support, to help build sustainable capabilities. One of the most important roles for an HRD is working with the CEO to create the right team at the top – ensuring that those who are not right for that stage of the strategy are exited, as well as bringing the right people on board. Building the capability from the top-down.

As regards ensuring a healthier supply of 'seedcorn' talent, the concept of re-engineering recruitment processes to ensure great 'fit' is taking greater hold. This requires a combination of

- analysing an organisation's best performers and building those insights into every aspect of the selection process, from better targeting to faster on-boarding and then onward development
- ensuring a warm and welcoming 'customer-oriented' process – on-line, by phone and in person – so that even rejected applicants think well of the company.

HR – performance experts?

The bottom line is whether HR are themselves performance experts. And that divides into two areas of impact – systemically on the health of the people processes, and personally on teams and individuals.

- Processes – the design and management of all people processes should start with this question – how much does this help people to perform at their best? Anything that does not meet this simple test should be jettisoned (except when simply meeting a legal requirement).
- Personal impact – for managers who need to raise their game, HR must succeed in an educational, developmental and coaching role.

HR clearly needs to do more and better in improving the standard of people managers. Otherwise it stands accused of trying to keep itself in a job at the organisation's expense.

"The world isn't really on an annual cycle anymore for anything." **Susan Peters, Senior VP HR, GE**

TSR – a good measure of organisation performance?

Total Shareholder Return (TSR) is a measure of the performance of a company's shares over time, combining share price appreciation and dividends. However, TSR needs to be treated with caution – returns made at the expense of investment in infrastructure, people and product leads to short-termism, and there are unfortunate examples of investors reaping good rewards – followed by the collapse of the company! TSR is also subject to the vagaries of economic cycles. Relative TSR compares the performance of companies in equivalent sectors, and can be more useful.

However, whatever measures companies use, they still need to consider the imperatives that support their sustainability – and this links back to their strategic capability. Their energies need to be channelled to improving e.g. product, innovation, quality, customer service, sales and the contribution of people.

Given that organisations have limited resources, the question remains one of focus and priority; and the challenge for the HR Director is in identifying these, and translating them into the performance management cycle.

REVIEW AND EVALUATION

The necessity to apply rigorous measurement and evaluation to review processes is a key part of the PARC model, and is the part of improving organisations that HR often struggles with. We have therefore maybe given disproportionate space to this aspect of the model, and will look at three major areas that contribute here.

- Organisational performance and development.
- Individual performance and development.
- Reward and recognition.

ORGANISATIONAL PERFORMANCE AND DEVELOPMENT

Essentials and trends

Performance should be reviewed at multiple levels – whole organisation, business units and functions, team and individuals – in an interlinked way.

- Too often the perception persists that individuals' reviews are an HR process disconnected from any business performance reviews. We did find organisations trying to correct this, typically by getting the CEO and key executives at each level to take the lead, not the HR function.

Business reviews should robustly assess not only the progress towards strategic aims but also how well the structure and capabilities support performance.

- Increasingly CEOs and HR leaders jointly conduct reviews of business units and functions, in terms of performance, culture and talent. The results feed into the next iteration of strategy and plans. The quality – not just the quantity – of individual/team performance and development reviews should be just one indicator among many.

Performance review needs to be continuous.

- The increasing pace of events, opportunities and threats means that performance needs to be re-visited more regularly than just once a year. Strategy should be adaptive, adopting a continuous learning and improvement philosophy. This avoids frequent knee-jerk change, and performance degradation.

Enhancing digital and analytics competence needs to be an area of continuing focus.

- Many organisations are struggling to keep up with technology shifts, and to create clear line-of-sight and robust data infrastructures. Human capital and other non-financial data have been poor relations. The quality of both internal business reviews and external performance reporting is at stake; and the ability to pre-empt and recover from both cyber-attacks and systems malfunction has become a major performance issue. (See recent reports by PARC on HR technology and by Creelman Lambert on corporate reporting for in-depth analysis).

"These are large-scale, complex systems for making people unhappy." **Kevin J Murphy, Professor of Finance, USC Marshall School of Business**

INDIVIDUAL PERFORMANCE AND DEVELOPMENT

Essentials and trends

A Corporate Executive Board study (2012) reported 95% of managers as dissatisfied with their PM systems; 90% of HR heads believed they did not yield accurate information; 59% of employees felt their reviews were a waste of time and 56% said they did not get good feedback on what to improve. The trend-line is not healthy – only 23% of HR respondents were satisfied with their organisation's approach compared to over 50% a decade before.

How much does this reflection poor design, or poor practice? The answer is it can be either or both. These are common criticisms.

- ***Design flaws*** – undoubtedly many systems have been too complex, cumbersome and inflexible.
- ***Time-consuming*** – everyone involved ends up spending large amounts of time completing required, standardised processes.
- ***Tyranny of the forms*** – expending more effort on filling forms than on healthy discussion of performance and development.
- ***Ill-fitting*** – one-size-fits-all systems do not address variegated needs and circumstances.
- ***Misleading*** – data generated inaccurately reflects needs, is 'falsely precise', and provides a poor basis for business and personal decisions. The search for 'perfect numbers' is illusory.
- ***Unwieldy systems*** – 'forms' and software are a drag on, rather than an aid to, the process, being badly-designed or bug-ridden or both. Long-standing lack of HR competence in technology and data management has not helped.
- ***Feedback*** – can do as much harm as good if poorly designed and executed.

The use of annual review cycles is particularly questioned.

- Waiting for up to 12 months to review performance or re-set objectives is illogical and potentially harmful, given how much changes in a year.
- Psychology shows that feedback needs to be close to the event to be both useful and accurate.
- Millennials especially tend to operate in a way that demands rapid guidance, feedback and recognition, in every aspect of their lives.

Feedback is tricky!

Effective feedback is vital in managing performance yet deceptively difficult to get systemically right.

- Managers generally have a lot to learn about how to provide feedback – for many it is not a natural skill, and badly done creates more harm than good.
- Much emphasis is rightly placed on training managers to give 'tough messages' sensitively; what tends to be underplayed is helping managers, particularly at the top, to receive tough feedback and respond positively – partly because this is harder.
- Just running 'training courses', particularly voluntary ones, does not create organisation-wide competence. Other reinforcing factors are required.
- Early-career selection and development practices are necessary – trying to shift behaviour once task obsession and dictatorial tendencies have set in is largely futile. Senior role models have a critical influence, for good or bad.

The use of multi-rater (or 360°) feedback continues to grow apace, with the expectation that this is richer and more accurate. Again, this technique is only as good as the user. Badly done it can be 'gamed' and mislead. It is safer to restrict its use to aiding development, as it is less likely to be misused than if judging performance and, in particular, influencing reward.

"Too much process kills enterprise." **Des Pullen, Group HRD, AB Group**

Changing the rating game

- Continuous, anytime discussion of performance/development with diarised occasions for more structured discussion.
- Forming a judgement on performance and needs based on discussion more than scoring.
- Focusing on what people are good at rather than on what they are poor at.
- Dropping relative performance ratings for more junior employees.
- Focusing on absolute performance for more senior employees.
- Engaging more in discussing talent issues, looking forward, than past performance.
- Removing performance scoring as a core determinant of pay and bonus awards.

Some organisations are experimenting with on-line peer-to-peer feedback, encouraging transparent comments on each other's' achievements and 'learning points' e.g. at conclusion of projects. Creating a non-competitive mutually supportive culture is critical to making this work.

In removing scoring, precautions should be taken to continue to identify poorer and higher performers, so that the former can be actively managed and the latter recognised.

There are several other criticisms and issues with individual performance management – far too many to include in the main body of this paper. For a more in-depth critique including rating scales, skew factors, and the 'blame game', see Appendix 1.

So, are there really radical new approaches to overcoming the shortfalls, or is it all just about putting good practice in place?

The HR and business press have increasingly featured stories about a supposed wave of companies who are 'abandoning' performance management.

The truth is less dramatic. Some 5-6% of Fortune 500 companies are so far estimated to have made the kind of significant changes implied. These do include some well-known names, mainly in technology or professional services – Microsoft, Adobe, Facebook, Juniper, Motorola, Expedia, Accenture, Deloitte and KPMG – but also Cargill, National Australia Bank, New York Life and GE.

Some of these changes are things that many large companies say they are working on, such as

- more frequent reviewing periods
- focus on healthy performance discussions, minimising form-filling
- greater emphasis on strengths rather than measurement against competency frameworks
- better technology to support performance and development reviewing, in terms of both providing more insightful performance data and making record systems more painless.

The eye-catching change is dropping the use of performance ratings, particularly GE – famous for the 'rank and yank' or 'stacking' practice widely adopted elsewhere. While relatively few organisations have yet done so, a larger number are considering it.

Microsoft and others have highlighted the desire to boost collaboration and teamwork; the individual rating system is seen to work against this.

There has been a surveyed increase in employee engagement, attraction and retention where ratings have been dropped but direct cause and effect with business outcomes are harder to measure.

Overall we are in a period of experimentation. Time and objective analysis will reveal what practices genuinely work better in a lasting way.

"Our aim is to keep simplifying review process requirements for managers. Our performance support systems should just work in the background so that managers can concentrate on the quality of conversations." **Sharon Doherty, Global Organisation & People Development Director, Vodafone**

Insights from interviews

Our sample of interviewees, with the exception of KPMG, still deploy relatively traditional approaches to managing performance. They all judge their management population to be 'work-in-progress' as regards becoming skilled people and performance leaders. Much effort has been invested in rating and calibration systems – there is reluctance to rush into a new unknown.

Further, while these are mostly sizeable and reputable organisations, with business performance results and growth rates that range from solid to spectacular, the internal reality is that there is considerable variety of capabilities and orientation across the organisation in managing performance. Consequently all are working on improving their approach. These are their main areas for attention.

- ***Management development*** – improving skills in leadership, developing and coaching, and the art of effective performance conversations; getting people to practise.
- ***Management ownership*** – shifting the perception of performance management to one that is leader-led.
- ***Frequency*** – adopting a pattern of more frequent and less formal discussion. We found many variations, from half yearly to monthly, and in one case implanting the notion that every conversation was potentially part of a process of continuous assessment.
- ***Better articulation of objectives and desired standards*** – efforts to provide clearer descriptions of 'good' and 'poor', through both text and video guidance material and workshops.
- ***Recording*** – simplifying requirements, and adopting smarter on-line tools.
- ***Measurement*** – using employee surveys and other information to identify better where managers need help, and who provides the best role models for others to learn from.
- ***Values and results*** – generally increased attention paid here.

In a couple of instances, HR leaders had agreed that parts of their business could opt for team-based reviews and reward, reflecting the nature of work done. This was cited as evidence of a pragmatic approach, necessary in making progress in large, complex, multi-cultural organisations – and belying the caricature of HR being obsessed with conformity.

Rating scales and 9-box grid

Every company we spoke to had differences in rating scales – three point, four point, five point and in one case an eleven point scale (0-5 with half points).

Forced distributions in the bottom category varied between 10 and 20%, and 10-30% in the top category.

The 9 box grid was widely used but in different ways.

- Some regard it as an aid to discussion rather than an authoritative scoring technique.
- More often specifically to aid development discussions rather than measure performance.
- In one case it had been adapted to measure performance with results on one axis and values on another, replacing 'potential'.
- In another, it is used in risk analysis of talent, e.g. impact levels, flight risk.

GSK's performance feedback tool

GSK has sharpened the focus on managers' track record in being performance facilitators.

In addition to using staff survey results and personal 360° reviews, a specific measurement tool has been introduced that measures managers' ability to give effective feedback. Input derives from direct reports and peers, every two years. This feeds into their personal performance and development review.

"Money is an outcome of high performance. Satisfaction and respect are incentives to it."
Andrew M Lebby, Performance and reward consultant

Does the organisation care about me?

- Reward levels and decisions are one, important, way that employees estimate how they are valued. That lies at the heart of their relationship with the organisation.
- Any decrease or freeze of a pay award may be intended as objective, but is liable to trigger a subjective, emotional reaction – often negative.
- If relative pay declines, people incline to look elsewhere.
- Pay increases and bonuses can positively affect motivation, but generally short-lived. Any direct impact on performance levels is harder to ascertain. Once given, the sense typically is of entitlement, rather than gratitude – a new norm is established.
- There are many quasi-financial benefits and entitlements as an alternative to cash; some of these have a more lasting effect on commitment, where they communicate more convincingly about how the employee is valued.
- Non-financial recognition such as awards – from leaders or peers – tend to have the most lasting effect, sometimes life-long, on the health of an employee's relationship with the employer.
- Mercenary workforces are inherently unreliable.

REWARD AND RECOGNITION

Essentials and trends

Reward is a vast subject, but the reason for including it here is that it is used as a lever for both organisational and individual performance. The primary role of reward structures is to create focus.

- Focus on how we define and measure performance – it provides clarity about what is wanted, and what not.
- Focus on what behaviours we are seeking – a common example is increasing the proportion of reward attributable to observing company values and behaviours.

Reward plans can be a powerful force for change – but the organisation needs to be crystal clear about what it is seeking to change, and be very clear about the potentially unintended consequences of new approaches. As Steve Kerr (retired CLO, GE) commented "the reward hasn't been invented that can stimulate desirable future behaviour without a concomitant risk of dysfunctional behaviour."

But do pay and incentive schemes genuinely improve performance? Research that convincingly links variable incentives to higher, as opposed to different, performance is hard to find.

Pay can be an important attractant, but it is less effective as a retention tool. It needs to be seen as fair, and decisions do affect individuals' ongoing relationship with the organisation. But there are a host of intrinsic motivators at work too – belief in the organisation, job interest, opportunities to grow and develop etc. that are just as powerful.

Incentive schemes can provide a stimulus – but the effects are generally short-lived, with diminishing effectiveness over time. As Michael Beer, Professor, Harvard Business School said "The half-life of an incentive system is at best five years. When it stops paying off, employees turn against it." For more on incentive schemes see Appendix 2.

"When financial rewards are disbursed equitably and efficiently, the firm purchases employee motivation and energy to pursue organizational objectives. The trouble is that money is often distributed in ways that are neither equitable nor efficient." **Steve Kerr, retired CLO, GE**

Insights from interviews

- There was little support for the concept that variable pay intrinsically helped to raise performance.
- Ratings were widely felt be a blunt tool in determining pay awards. In some companies the emphasis is now to say that ratings are just one factor in determining pay.
- As indicated earlier, rewarding people for observing values and not just results is increasingly widespread.
- Attitudes to rewards vary across cultures – functional, national, generational. Organisations pragmatically have to nuance their approaches.
- Several organisations admitted they could do more to enhance non-financial recognition.

There was evidence of cycles – a particular stratagem works for a while and then circumstances and behaviour require a change. For example

- some companies were increasing the proportion of the collective component in bonuses in order to encourage more collaboration, and de-tune internal competition
- others were increasing the proportion of individual performance-related pay because it was felt too many had been 'coasting'
- just as Microsoft publicised its abandonment of 'rank and yank' as being harmful to teamwork, Yahoo adopted it, precisely in order to winnow out poorer performers.

Those increasing their focus on collaboration tended to be down-playing relative ratings for more 'junior' echelons. Individual performance pay was retained for more senior executives – although ironically it is the example leaders set that affects how much internal competition there is.

Higher proportions of variable pay can be effective in entrepreneurial companies like Liberty Global, because there is a shared sense of everyone benefitting. "There is a consciousness that everyone here is working to get richer", commented Liberty's head of reward.

In their own words

"Realistically, 3-5% of our people are genuinely high potential. Managers' ratings said it was 26%. We've a long way to go before they can make realistic assessments without challenge and guidance." **Group HR director, FTSE 100 company**

"Should we stop ratings and calibration? Our performance culture isn't strong enough yet. Maybe we'll feel differently in 3-5 years. Millennials don't like being rated, but they have to learn about being in a big company and demonstrating that we can get value for money. Some line managers hate rating too. We've challenged ourselves to find another way of differentiating performance, but we can't see another way. And actually our employee surveys show that people do want differentiation." **Group head of reward, FTSE 100 company**

"The higher the stakes and accountability, the less likely people are to be collegiate. Squaring that circle is one of our biggest cultural challenges." **Group HR director, growth company**

"We reduced individual as against collective rewards to encourage teamwork, but in my view we ended up losing focus." **Former HR director, FTSE 100 company**

"My CEO is greedy, quite simply. What can I do? The board won't challenge him, so how can I?!" **Group HRD, FTSE 250 company**

SO WHAT DOES HR NEED TO DO DIFFERENTLY?

The challenge for HR is to demonstrate that its contribution provides the catalyst for enhanced performance – from organisational to individual level. This is not how HR is sometimes viewed. To shift its reputation, HR needs to become expert on the topic of performance and performance management.

Many effective HR leaders and functions do guide their organisations towards practices that get the best out of people and resources, and remove obstacles that get in the way, including any dysfunctional personnel processes.

Here are some specific areas and questions to concentrate on.

1 Understanding 'performance management'

Does HR articulate and embed a systemic approach that gets the best 'fit' between the work, people, technology and information – set in a very clear external focus on the changing requirements of customers and the operating environment? (Note the continuing relevance of work done on 'high performance work systems' from the 1980s onwards.) Improvement is likely to be delivered through a holistic and systemic approach where several initiatives are tackled simultaneously. 'Clusters of 1' are often ineffective.

2 Addressing senior leadership

Is HR influential at the top of organisations, rather than just working on the mechanics of processes? How does it ensure the executive leadership team is fit for purpose, and inspiring as role-models? People management is a core dimension of good leadership, and is critically affected by the attitudes, understanding and behaviour of executive teams and the boards that oversee them. Does HR have the courage and respect to be able to hold up the mirror when leadership orientation needs to change – i.e. not as happened at Enron, Tyco, Vivendi, VW and elsewhere?

3 Adding value to strategy

As well as working to select and develop leadership teams that can devise great strategy, does HR facilitate strategy formulation by asking tough questions and contributing genuine insights – deriving from expertise and experience in organisational psychology and development – about structure, culture, motivation and capability? HR must also demonstrate deep understanding of global operating conditions and the multi-stakeholder and competitive environment.

4 Embedding strategy and aligning objectives

Are strategy and standards clearly communicated throughout the organisation? Do people have an opportunity to contribute bottom-up as well as top-down? How aligned are objectives at all levels? Are strategy and planning skills being grown at all levels? Do leaders and managers set goals and targets that motivate, and stretch without breaking (above and beyond SMART)? Do you concentrate on a few overarching objectives, and not waste energy on multiple targets and KPIs?

5 Teamwork and collaboration

HR should champion the elimination of silo behaviour and the enhancement of teamwork and collaboration. This includes ensuring key central functions align with the strategy and work as a team to ensure its delivery. It also requires robust mechanisms to improve processes, ensure alignment and line of sight, and to eliminate blockages.

6 Performance culture

Do you have a high performance climate where success is demanded, inadequacy is eradicated, and excellence is championed? Is there a real sense of both accountability and empowerment at all levels? Are learning and improvement embedded in the way performance is managed? Do leaders understand the drivers of positive and negative cultures – and display this in how they speak and behave? Does HR itself act as a role model?

7 Strategic talent management

Have you identified critical roles (20? 30?), and placed high performers in each? These may be at the top of the organisation, or specialist roles elsewhere. Do you recognise great current and potential performers? Do you identify and remove poor performers promptly and sensitively? Does your reward system genuinely motivate lasting performance and a sense of collective endeavour? Do you strike the right balance in rewarding the 'what' and the 'how' (results and values)?

8 Attraction and capability

Does the organisation have a desirable reputation for attracting and developing talent, embedded in the way leaders and managers operate? Does it successfully transform potential into better operating outcomes? How effective has HR been in developing people and performance development capabilities throughout the management cadre, from top team to the front-line?

9 Performance review

Do you rigorously review organisation results, people and climate; admit and learn from mistakes; and provide honest feedback – from organisational to team/individual level? Do you have robust and insightful data management and analytics, and make smart use of technology? Do these work in an integrated way across the organisation, rather than in functional, business or geographical silos – and thereby enable a clear performance story to be articulated to stakeholders? Has HR enabled managers to achieve the maturity to move beyond performance and pay 'control' mechanisms such as forced ranking?

10 HR's purpose and capability

Has HR addressed its own capability challenges, such that it becomes recognised for its excellence in performance facilitation, future-focused organisation and work design, business acumen, ability to align human and technology systems, workforce analytics, organisation and capability development, and the management of change? Once HR becomes recognised as real performance experts, it may be able to shift bad habits in reward and performance management – having first tackled its own bad habits.

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APPENDIX 1

INDIVIDUAL PERFORMANCE MANAGEMENT – A MORE DETAILED CRITIQUE

There is a wealth of criticism of individual performance management – we give a taster of the main themes here.

Rating systems come in for especial criticism, with some challenging the entire concept. How judgements are formed and recorded is a major influence on satisfaction or otherwise with performance management.

- Neuroscience identifies that numerical ratings and ranking generates a 'fight or flight' response that impairs good judgment.
- Critics accuse companies of using evaluation criteria that are ill-fitting by being variously subjective, standardised and simplistic – where true this creates further anxiety and grievance. If people accept being judged, they will only do this if it is fair and relevant.
- Forced distribution of rankings are especially controversial – despite the intention to induce consistency, they are perceived as arbitrary and unfair.
- There has been a tendency to get in a muddle about rating for performance and potential. Some managers struggle to differentiate between these, and to make effective judgements about potential in particular.
- The focus on ratings is seen to distract from discussion of development. Performance reviews tend to be too backward-looking, and foster a 'fixed mind-set' that in effect keeps people labelled and hinders the potential to grow. (For more information see the article *"Kill your performance ratings"*).

Additionally, the tendencies of managers towards either 'safe' centre-marking or over-rating their particular team members has long been a major concern for both leaders and HR, especially when this inflates the pay bill.

HR's response has historically been to mistrust managers' willingness and ability to differentiate accurately, and consequently pulled harder on bureaucratic and disciplinary levers – including forced distribution. This increases resentment among the reluctant. The end result too often is not more motivating experiences for employees; rather the reverse – a lose-lose vicious circle, which gives an extra excuse for poor people managers to be rejectionist.

'Skew' factors that undermine accurate assessments of people include

- 'recency' – being swayed by people or performance experienced recently rather than 11 months ago (another reason to conduct more frequent reviews)
- 'idiosyncratic rater effect' – research findings that up to 50% of a rating reflects the personal rating tendency of the rater, undermining objectivity and inviting game-playing
- narcissistic, self-promoting and upward-managing people selling themselves better – i.e. the 'wrong' people emerge well, even in multi-rater appraisal systems.

Much work is performed as teams not just as individuals. Systems of review and reward that do not reflect this – and many don't – are inherently misdirected, especially given the strong trend across organisations to improve teamwork and collaborative behaviour.

There's a natural tendency for different actors to blame each other for the performance management 'problem'.

- It's HR's fault.

HR is serially blamed for over-engineering processes, not really understanding the realities of performance, using the PMS as a lever to exercise power (negatively), etc.

- It's the managers' fault.

It's not the system but poor people managers who are intrinsically bad at developing and appraising their people. If they were better, there wouldn't be a need to create standardised requirements, impose ratings and forced distribution, and more besides.

- It's the leadership's fault.

Criticisms include being poor role models, overloading everyone with too many objectives, not really understanding what good development looks like, preventing HR from adopting more progressive performance management techniques and so on.

Few disagree that ***some*** kind of review process is essential.

- Decisions about employees' pay and future without discussion are even more unsatisfactory!
- The challenge has always been to have a fair and consistent process that people really want to use, and look forward to.
- That has always been as much about effective managers as about process design.
- And that, quite simply, has been a question of developing the necessary orientation and abilities over a period of years – just tinkering with procedures without addressing fundamental skills misses the point and makes matters worse.

The responsibility for developing effective managers surely falls upon both the leadership and HR.

- Leaders set the tone, frame the performance and behaviour requirements, and should serve as role models.
- HR should provide real expertise in the art of motivating high performance and developing capability, and have the design and facilitation skills that help leaders achieve their aims.
- Both leaders and HR need to work together over the long term to ensure the critical mass of managers are effective people developers and performance inspirers.

Leaders need to own performance management and, without good leaders, HR and everyone else is hamstrung. What HR ***can*** seek to do, if it has the courage and tenacity, is to ensure for the organisation's sake that good leaders are developed and appointed.

APPENDIX 2

MORE ON INCENTIVE SCHEMES

Whatever the logic and psychological 'truth', the reality is of course that incentive payments are established features of organisational practice, despite some very evident downsides.

- Examples of employees receiving a high proportion of their reward as variable pay are sales forces, financial traders and investment deal-makers – no surprise that mercenary behaviour is often highly evident, and that mis-selling scandals and risk blow-outs occur periodically.
- Typically, incentives in commercial companies increase proportionately towards the top, with the CEO getting paid up to several hundred times more than front-line employees. No amount of public anger and regulatory requirements has caused any significant shift in this pattern.
- Institutional 'checks and balances' have little visibility. There have been some high profile investor objections to complex incentive schemes, but actual rejection is rare. The recent PARC report on RemCos argued for an increasingly vigilant stance but also questioned RemCo effectiveness to date, particularly in relating pay to performance.
- 'You pay for what you get' is something any shopper should know and also applies to rewards. People in Aldi or Goldman Sachs are expected to work hard for their above-average pay and bonuses. What annoys people is 'soft' deals – whether an overpaid executive or an under-performer in your team.

The current trend is to demand longer terms for top executive incentive payments, allowing claw-back if the desired outcomes evaporate in years ahead. The reasons are understandable, in giving some degree of compensation to investors if things go wrong. However psychology shows that far-distant rewards tend to have little impact on immediate behaviour – just as much delayed performance reviews are too late to have a beneficial impact.

If it's such a bad idea, why do it?

Given there are aspects of incentivisation practices that seem illogical, perverse and ineffective, why do they persist?

- First, because humans generally adjust to powerful norms and imposed belief systems. Some learn how to profit from the system, the majority are socialised into acceptance, and the most disadvantaged have to be in real difficulty before they organise to protest or create change, overcoming fears about harming themselves irreparably – for example by going on strike.
- Second, because pay is just not that important in influencing performance. As stated earlier, once reasonably satisfied with pay, people get on with their job, and many other factors shape their behaviour and contribution. Nurture is more powerful than cash.
- Third, because HR functions spend much time and energy working within prevailing reward systems to get the best results they can, in terms of attracting, retaining and motivating good people. Sometimes it may feel like fire-fighting, but generally it works.

After all, as with shoppers and discounts, who turns down a bonus?

APPENDIX 3

KPMG RE-DRAWS PERFORMANCE MANAGEMENT

KPMG in the UK decided to drop performance ratings because they had proved to be a disengaging force which undermined trust and collaboration. Other KPMG member firms worldwide are considering following suit.

The re-shaped Performance Management System (PMS), dubbed 'Honest Conversations', involved extensive initial analysis and co-creation, with 1500 staff involved in road-testing. It was launched as part of the 'Our Deal' change programme to a gathering of 13,000 staff at London's O2 arena in September 2014.

The guiding philosophy is to be more 'human' and enhance the 'colleague experience'. Senior Partner Simon Collins talks of "bringing the whole self to work".

Previously the cycle was a conventional annual appraisal with mid-term review. Now the pattern is

- a formal bi-annual review of objectives and performance, with regular one to one discussions encouraged and a focus on having honest conversations about performance, development and progression
- the removal of performance ratings.

"We have decided to remove the discomfort that ratings generated and instead focus on the quality of the conversations. It's more about the business and less about bureaucracy," says Colm Coffey, UK HR Director. The quality of performance discussion is now tested in three ways.

- An annual engagement survey.
- Half yearly surveys specifically on quality of performance/development discussion.
- A confidential hotline which indicates to HR if there are poor instances; they then discuss this with appropriate leadership to address the issue.

Performance discussions address the 'what' and 'how' – both results and values are important.

360 degree feedback will be launched in 2016 to leadership with a focus on values and behaviours. Additionally, KPMG has initiated a rapid feedback tool, in order to encourage a culture of continuous feedback. For example, after projects, people can share feedback with colleagues directly via the tool, providing timely feedback that is securely stored and easily accessed for future Honest Conversations.

The pay cycle is still annual, even if performance discussions are more regular. Previously the rating system was found to skew discussion and encourage central marking. People were not being honest with each other given that money was at stake. Now it appears people are talking more openly.

Coffey continues: "Managers still decide on pay and have to justify their decisions – using data about our various performance objectives, KPIs and a range of inputs. But we found that ratings were too dominant and too blunt an instrument. The thousands of hours that we were spending on rating and the moderation process are now being re-invested in talent reviews."

Dependent upon KPMG's financial performance, everyone who is meeting expectations receives a one firm profit share. There is a bonus for Senior Managers, and Directors which is partly profit share and partly based on in-year performance. Beyond that KPMG is convinced that application of variable pay has to be carefully managed and constantly reviewed to ensure it is creating alignment in the organisation. Coffey concludes: "Our new philosophy is all about ensuring the colleague experience reflects our ambition. Performance Management, or Performance Development as we refer to it, is at the heart of any colleague experience. We need to ensure the quality of development conversations is not affected by pay discussions."

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