

CEO Working Paper Series

Cutting Edge Performance Management: What About Rewards?

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No society can provide its members with a high quality of life unless it has effective organizations.

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Performance management has long been central to the reward system of most organizations. Individuals receive appraisals based on their performance and the result is used to determine pay increases, bonuses, stock grants, and rewards such as recognition and training opportunities. In most organizations, performance management has become a once a year activity that generates a quantitative score or grade that is supposed to represent how well someone has performed during the year. The score often directly determines reward levels and actions.

After years of increasingly strident criticism of performance management from inside and outside the organization, some companies are making major, disruptive changes in their practices. Adobe Systems, Microsoft, Deloitte, and GE, among others, have adopted innovations that have changed the way performance management is being conducted. With support from WorldatWork, the Center for Effective Organizations has conducted a survey study of 244 organizations that have adopted one or more of three cutting edge practices: ongoing performance feedback, ratingless reviews of performance, and crowd-sourced feedback. Ongoing feedback involves performance and development discussions multiple times per year, typically monthly or quarterly. Ratingless reviews avoid assigning a numerical or letter grade to the level of performance. Crowd-sourced performance feedback uses social media for employees to provide real-time feedback to others.

This article focuses on issues that are specific to rewards. Two other WorldatWork publications provide additional findings. These publications are a [WorldatWork Journal](#) article (Ledford, Benson, and Lawler, 2016a) and a monograph that provides detailed findings (Ledford, Benson, and Lawler, 2016b).

Reasons for Adopting Cutting Edge Practices

The survey included a number of items about the reasons that companies are adopting cutting edge practices. Factor analysis revealed three primary reasons: creating better strategic alignment, improving the performance management process, and meeting rewards objectives. Meeting rewards objectives was slightly less important than the other two factors. As Figure 1

indicates, the most important rewards objectives included motivating employee performance, developing employee skills and abilities, and rewarding top talent. These findings indicate that those who advocate “blowing up performance management” and pay for performance with it have not changed company practice.

Effectiveness of Cutting Edge Practices

We examined the effectiveness of cutting edge practices, using the same survey items that we used to assess adoption. Most companies adopted these practices within the previous two years, so company assessments of effectiveness are preliminary. Companies reported moderately positive levels of effectiveness, and the degree of effectiveness corresponded roughly to the reasons for adoption. Strategic alignment and improving the performance management process outcomes were more positive than rewards objectives both as reasons for adoption and for level of effectiveness. Among reward system objectives (see Figure 1), the highest reported effectiveness was for motivating performance, developing skills and abilities, rewarding top talent, and rewarding employees more effectively. Attracting new employees received lower marks, perhaps because the new systems are unfamiliar and difficult to explain to potential recruits.

The Impact of Cutting Edge Practices on Rewards Administration

We asked a series of questions to determine the impact of cutting edge practices on rewards administration. First, we explored the impact of the new practices on total rewards costs, a vital concern for rewards professionals. About half (47%) of the sample reported that they had no basis to judge the answer to this question, probably because so many implementations were new. For those who provided a rating, fully 89% indicated that costs remained “about the same” versus the market; only 10% reported an increase in costs (including 1% who saw “greatly increased” cost), while 3% stated that costs had decreased.

Table 1 presents the results for seven reward administration outcomes. The results are very encouraging. To a moderate degree or greater, most respondents reported that the level of

employee development increased, top performers received more rewards than before, changes in pay were more differentiated based on performance, managers have greater discretion in delivering pay, and pay decisions are more transparent to employees. These outcomes were consistent with the reasons for adopting cutting edge practices. Only 21% said that employees were less clear about how they were performing. Overall, the data clearly suggest that the practices are supportive of effective pay decision making and have a positive impact on reward outcomes.

A question that rewards professionals often ask about ratingless reviews is, “How does the company make pay decisions in a ratingless system?” Their concern is that companies adopting ratingless reviews may abandon pay for performance. We asked those who used ratingless appraisal (52% of the sample) how they made pay decisions in parts of the organization using this practice. Table 2 indicates that companies do not abandon pay for performance when they adopt ratingless reviews. The most common approach (used by 80% of companies that use ratingless reviews) is to give managers discretion to make decisions within budget constraints. Next most common (42%) is to determine rewards in calibration sessions involving a large pool of employees. One-quarter or fewer companies use a specific distribution for allocating rewards, use “shadow” ratings for decision making that are not communicated to employees, or use stacked ranking. The percentages indicate that many companies use multiple approaches.

Role Of The Rewards Function in Adoption and Design

Tables 3 and 4 indicate that Rewards leaders are playing a secondary role in the adoption and design of cutting edge practices. Top HR executives are playing the lead roles in adoption and design. They are involved in adoption to a “great extent” or “very great extent” in 73% of companies, and are involved in design “to a great degree” in 74% of companies. Performance management appears to be one area in which HR executives are heeding calls to take a leadership role in implementing HR practices that matter to the business. Non-HR top executives of the

organization are heavily involved in adoption in almost half the cases. Non-managers play a minor role, meaning that the changes are made with relatively little employee involvement.

Rewards leaders are heavily involved in design in 39% of the cases, but mean responses suggest that they are not playing a larger role overall than either top executives in the organization or top managers in units adopting the changes. We expected that reward leaders would be more heavily involved in the design of specific practices because of their relevant expertise and because of the implications of the changes for reward plans. Only non-managers play a sharply lower role.

Rewards and The Future Role Of Cutting Edge Practices

Overall, the results suggest that cutting edge practices have a favorable impact on performance and rewards. The companies in the study report that these practices lead to compensation that is more motivating and more transparent, while increasing the levels of employee development and performance.

A key reason for the reported improvement in reward system effectiveness may be that ongoing feedback, a practice that almost all companies in our sample use, can guide behavior and aid performance. It also may help create a clear connection for employees between their behavior and their rewards. The elimination of the scoring feature of performance reviews also may remove an irritating distraction that often makes it difficult for employees to hear performance feedback and rewards messages. Crowd-sourced feedback may generate a type of feedback that employees are especially receptive to hearing.

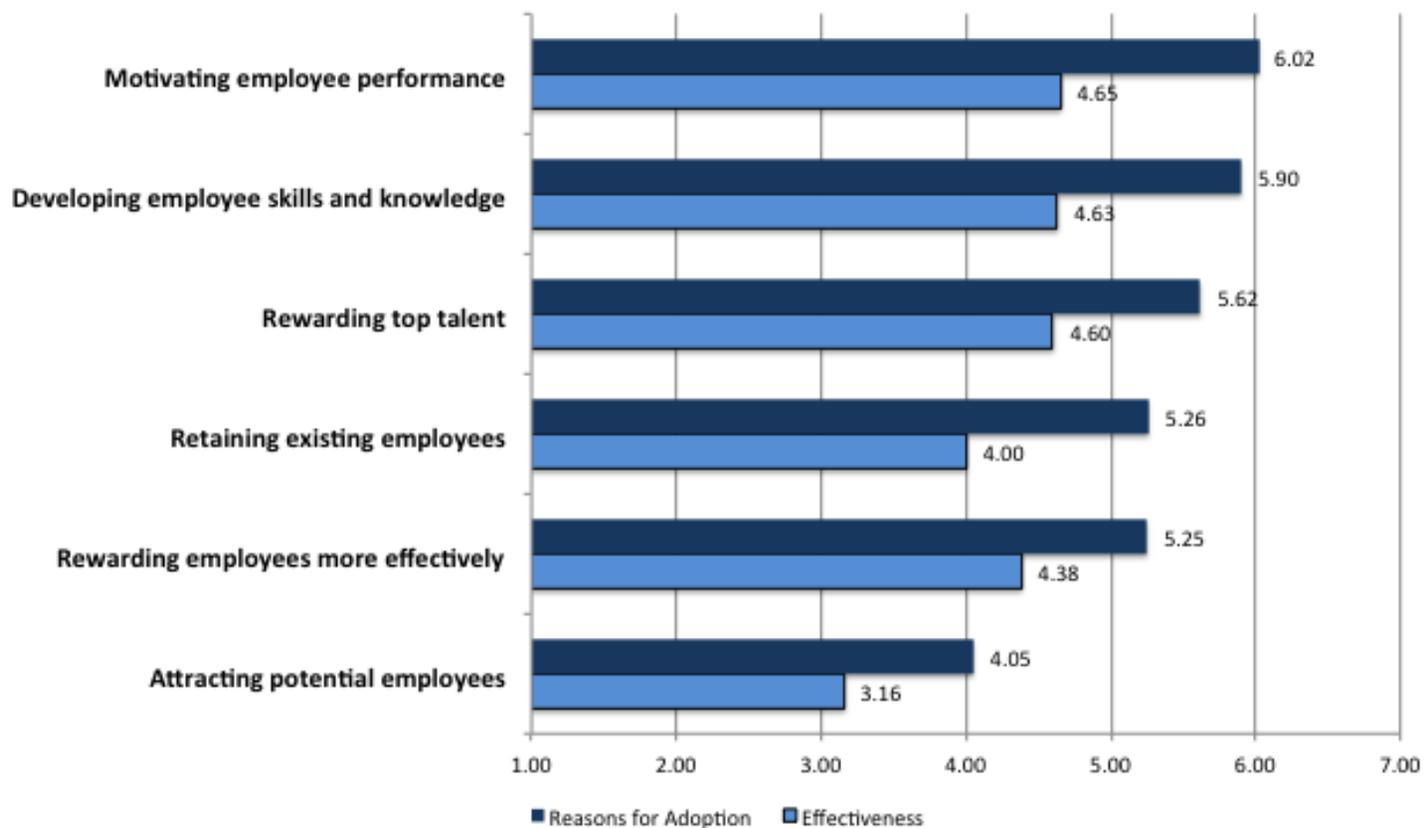
The results suggest that those who manage rewards should welcome the cutting edge changes in the performance management system. A note of caution is in order here, however. The data are opinion data, not performance data. Furthermore, the programs reported are relatively new. Ongoing monitoring of these practices is needed to understand their impact on rewards and organizational effectiveness.

On a final note, rewards professionals may be underutilized when they become just another stakeholder in the adoption and design of performance management changes. We believe that rewards leaders can play a larger role in these change efforts. For example, companies using cutting edge practices tend to rely heavily on empowering supervisors to make pay decisions, but rewards professionals know that pay programs can become ineffective due to an overreliance on front-line supervisors. (Broad banding and certain recognition programs are cases in point.) We urge rewards leaders to take advantage of opportunities to play a major role in the adoption and design of changes in performance management in their organizations.

References

- Ledford, G., Benson, G., & Lawler, E. (2016a, in press). A Study of Cutting Edge Performance Management Practices: Ongoing Feedback, Ratingless Reviews, and Crowd-Sourced Feedback. WorldatWork Journal, 25(2).
- Ledford, G., Benson, G., & Lawler, E. (2016b, in press). Cutting Edge Performance Management: 244 Organizations Report on Ongoing Feedback, Ratingless Reviews, and Crowd-Sourced Feedback. Scottsdale, AZ: WorldatWork.

Figure 1
Rewards System Objectives:
Reasons for Adoption and Effectiveness of Cutting Edge Practices



Scale – Reasons for Adoption: 1 = Not at all important; 4 = Moderately important; 7 = Extremely important

Scale – Effectiveness: 1 = Not effective at all; 7 = Very Effective

N = 244

Table 1
Impact of Cutting Edge Practices on Rewards Administration

Type of Impact	Means	“Moderately” Or Greater
The level of employee development has increased	3.67	80%
Top performers receive more rewards than before	3.12	70%
Changes in pay are more differentiated based on performance	3.15	65%
Managers have more discretion in delivering pay increases and/or bonuses	3.09	63%
Pay decisions are more transparent to employees	3.00	62%
Changes in pay are less differentiated across the organization	2.46	44%
Employees are less clear about how well they are performing	2.18	21%

Scale: 1 = Not at all; 3 = Moderately; 5 = To a great degree

Ns range from 172 to 194

“Don’t know” responses were excluded from calculations (18% - 27% of responses depending on the item)

Table 2
Reward Allocation Decisions

Type of Decision	Percent ‘Yes’
Managers make decisions on their own within budget constraints about how to allocate rewards	80%
Reward allocation is determined in calibration sessions involving a large pool of employees	42%
Rewards are allocated according to a specific distribution	24%
Managers use “shadow” performance ratings for allocating rewards that are not communicated to employees	22%
Management ranks employees from first to last (stacked ranking), whether or not this ranking is communicated to employees	20%

N = 144

Table 3
Adoption of Cutting Edge Practices

To what extent are the following descriptive of the change process for adopting (cutting edge practices) in your organization?	Mean	Percent “Great extent” or “Very Great Extent”
Led by top executives for the organization	3.74	45%
Led by Human Resource executives	3.88	73%
Led by the Rewards function (Compensation, Compensation and benefits, Total Rewards, etc.)	2.63	33%
Led by managers in local business units	2.72	32%
Based on a bottom-up implementation approach	1.91	10%

Scale: 1 = Little or no extent; 2 = Some extent; 3 = Moderate extent; 4 = Great extent; 5 = Very great extent
N = 244

Table 4
Design of Cutting Edge Practices

How involved was each stakeholder group in designing (cutting edge practices) in your organization?	Mean	Percent “To a Great Degree”
Top executives of the entire organization	2.85	29%
HR leaders	3.61	74%
Top managers in the specific units that adopted the changes	2.72	26%
Rewards leaders (Compensation, Total Rewards, etc.)	2.86	39%
Managers	2.40	13%
Non-management employees	1.76	5%

Scale: 1 = Not at all; 2 = To a slight degree; 3 = Somewhat; 4 = To a great degree
N = 244