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PERFORMANCE MANAGEMENT AND "RUNNING THE BUSINESS"

CEO PUBLICATION
G 95-4 (280)

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March, 1995

To appear in a special issue of Compensation and Benefits Review, 1995

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Abstract

In this paper, we define performance management as a set of processes needed to guide performance. Performance management includes the processes needed to define and plan performance, to develop the capabilities to perform as planned, to review performance, and to reward performance. These processes need to be applied to all levels of performer: individual, team, and business. Prevailing formal practice has tended to focus on individual performance management by using a set of administrative people management systems that are perceived by many to be separate from and distract attention from the actual managing of performance needed to run the business. Today's competitive environment has made the shortcomings of these prevailing practices salient. This paper enumerates the characteristics of the new approaches to performance management that are arising in response to these problems and that tie directly to running the business.

Performance Management and "Running the Business"

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Performance management is a broad term that has come to stand for the set of practices through which work is defined and reviewed, capabilities are developed, rewards are distributed, and other performance-based decisions are made in an organization. In any particular organization that uses the term it can include goal-setting practices, selection and placement, performance appraisal practices, compensation systems, training and development systems, career management systems, or any subset thereof. Some organizations use the term to refer to what used to be called the performance appraisal system, in acknowledgment of the fact that most appraisal systems these days include more than simply appraisal, such as goal setting and development planning.

This is an arena rife with strong opinions, wishful thinking, and avoidance. In the past decades, organizations, sometimes assisted by industrial and organizational psychologists, have searched for perfect practices that are: fully equitable, not subject to rater error, developmental, and highly motivating. Managements have searched for compensation systems that reward the best performers, and that will motivate the right behaviors to contribute to business success. The ideal training and development systems will provide employees with those skills they need for their job and prepare them for the next series of jobs that they will have in their organizational career. Organizations often work hard at establishing practices that maximize the fit of the potential the individual has and the career he or she wants with the needs the organization has and opportunities it can provide. All of this searching for better performance management systems has resulted in some rather interesting, inventive, and complex practices.

Meanwhile, managers feel that they don't have time for all this "people management"--they're too busy "running the business." And despite the great amount of attention given to the development of the performance management methodologies and their unending iterations, employees generally report that they get very little helpful, substantive feedback, receive pay unrelated to their performance, and experience almost no real developmental direction. The generally negative affect that surrounds these people management activities is illustrated in the observations of a third year chemist in a research laboratory:

> Does the performance management system here help me perform better? No. And it's a terrible ordeal. The week when all the managers get together to do whatever they do in those long meetings is the worst week of the year. Everyone is in a terrible mood. People snap at each other. The managers seem like they're determining prison sentences, not performing a process that has some benefit to someone. And the next week we have to sit down and hear some meaningless pablum about ourselves and why we got the raise we got, which isn't much different, really, than the raise everyone else got. And since five of us work together in a team, it seems a bit silly for our managers, who have very little knowledge of who's doing what, to try to determine who deserves what. Would I like meaningful feedback? Sure I would. If someone could figure out a system that really works, it would be great.

Difficult business environments of the past decade have exacerbated these problems: Greatly downsized managements feel more stretched and less able to spend time managing people. The amount of money to be distributed is even smaller and, in the eyes of many, perhaps not worth the hassle managers and employees go through to distribute it. Attention to development is less likely to happen when a company is not sure it will even need its employees next year and isn't sure of what kind of career paths to prepare people for. The increased emphasis on lateral organization, with teams and mini-business units performing in increasingly fluid and dynamic patterns, threatens the viability of managing individuals with approaches that assume they occupy clearly defined jobs.

This gloomy scenario belies a strong current of activities in organizations that are reconceptualizing performance management to fit the new business realities and make them an integral part of the running of the business. This article provides an overview of the major strands of this reconceptualization. First, it describes the limitations of prevailing performance management approaches.

Problems With Prevailing Performance Management Practices

Prevailing human resource management approaches grew up to fit the hierarchical line and box bureaucratic form. Pay relates primarily to the "box" or job that an individual person occupies, how people doing similar jobs are paid in the marketplace and how high it is in the hierarchy, as well as to how the incumbent compares to others in similar job-boxes. Work is defined in terms of job descriptions that enumerate the tasks that box incumbents are responsible for. Performance is evaluated based on the quality of the performance of the tasks of the job, often compared to others performing similar jobs. Development occurs largely as people move through boxes and are required to perform new tasks that require new competencies. It may be facilitated by attendance at generic courses and programs, often geared to one's level and job.

Focus on the "Box"

The focus of prevailing practices on the individual performer in the box, often to the exclusion of collective performing units, is a limitation of prevailing practice. This focus reflects not only the reality that individuals are performers, but also the emphasis on clearly delineating individual jobs. At higher levels, managers often receive bonuses based on their unit's performance, but interestingly, business unit performance is generally perceived to be a manifestation and an indicator of the individual's performance at the head of the unit.

The prevailing model has an insidious impact on the split in managers' minds between people management and running the business. This split is manifest in many different but equally dysfunctional syndromes. Business goal-setting and planning have often been separate from defining work for individuals, despite the application of frameworks such as Management by Objectives. For example "doing an excellent job of one's ongoing tasks" is often not seen as a goal; an individual's goals are considered something above and beyond--special projects and perhaps development activities. Thus, in these organizations, individual goals have tended to emphasize special activities, and not the here and now business requirements for responsiveness, quality, and productivity--the areas that have consumed recent management attention. Other organizations have overemphasized in the other direction: assignments to design and task teams to generate organizational improvements to support long-term organizational performance are often not taken into account in a performance management system that stresses current performance of core tasks.

Another way the box approach separates individual performance management from organizational performance is that individuals often get excellent performance ratings despite being embedded in projects that are failing or units that are not meeting customer needs. This leads to the ironic consequence that there is often no correlation between the performance ratings of people in projects or workteams and how well or poorly the project or team is performing (Mohrman, Mohrman and Lawler, 1992). People dissociate their views of their performance from whether their collective business unit is doing well: "I'm doing an excellent job even though we're failing collectively." In such a situation, the rational response is to concentrate on one's own goals, and not take responsibility for coordination or group-wide tasks.

Focus on the "Line"

Another problematic consequence of devising performance management practices to fit the line and box organization is that they embody the notion of the boss as the performance manager. This leads to a closed system: one where the rational behavior of an employee who cares about rating and merit is to please the boss, not necessarily to do the tasks required for organizational or team effectiveness. Such an orientation flies in the face of organizational approaches that emphasize empowerment and lateral decision-making. Indeed, in many of today's organizations, managers have huge spans of control that preclude good visibility of the performance of any subordinate to the manager. Employees operate in a complex network of co-workers and customers each of whom place expectations on their performance and have direct knowledge of their contribution.

In such an organizational setting, a closed boss-subordinate performance management system makes little sense. It is an obstacle to learning and development and leads to performance out of sync with performance demands.

Focus on Separate, Administrative Practices

The component performance management practices have often been broken apart from each other organizationally and in practice. Different "branches" of the human resource function have generated different practices. Compensation, appraisal, job evaluation and descriptions, and development systems often issue from different groups and have only loosely related rationales. These practices, certainly the most formal and often the most visible manifestations of "people management", are separated in managers' minds from "managing the business". At best it is understood that doing these carefully is important because evaluation, pay, career and job development, and job definitions are central to people's relationship to the organization. At worst, these activities are seen as bothersome wastes of time.

This state of affairs is problematic for a number of reasons. First, the segmentation of these practices from one another means that any desired connection among these activities is continually interrupted. Evaluation of performance deficits or anticipated new skills do not always trigger developmental activities. The link between assessment and compensation is portrayed as tight (merit pay) but in fact is a tenuous connection clouded by "position in range," comparative rankings, and all the human frailties that prevent raters from accurately rating and/or entering the unsettled waters of honest feedback and discussion. Job descriptions often don't accurately or completely capture the essence of expected performance or particular business priorities. Often they were formulated primarily to elicit a higher evaluation that would enable a larger base salary, rather than being an accurate description of the performances required from the incumbent. Thus, each H. R. "system" becomes a separate set of practices and achieves a life of its own as it continues to metamorphize, undeterred by the potential of being part of a larger, integrated performance management system. The fact that these practices are usually designed and administered by human resource departments exacerbates the perception that these are practices that are the concern of staff and have no direct connection with the line's interest in running the business.

Focus on Past

The evaluation and rewards practices of performance management have been the predominant focus of most participants. These are essentially backwards looking activities that truly distract managers from concentration on here and now and especially future business performance. This issue is exacerbated when performance management events take place months after the conclusion of the performance period. The rapidly changing environments faced by most organizations today make this issue more salient. Goals and priorities change even before the ink is dry on the yearly goal-setting document. Environmental requirements for continuous improvement carry with them an ever escalating performance standard. In such environments, the notion of a yearly cycle for people management makes very little sense, and such systems are doomed to be experienced as administrative requirements largely unrelated to the requirements of managing a business.

The New Performance Management

As organizations have stepped up to the challenges of their changing environments and their greatly increased performance requirements, the separation of people management from managing the business is no longer tolerable. Performance management systems must add value to the organization's ability to deliver high quality, profitable services and products to the customer. New organizational forms are emerging as organizations are required to be responsive to customer needs in a global environment and meet challenging new time-to-market requirements. Hierarchical levels are being eliminated and spans of control are radically increasing. Work is increasingly being organized and performed laterally, in a dynamic constellation of teams and alliances. The line and box organization is being blurred, and its predominant vertical logic replaced in part by a lateral logic. Hierarchy is no longer adequate to manage the complex dimensions of business performance required for competitiveness (Galbraith, 1994); nor, we argue, is a hierarchically oriented performance management system suitable. New approaches to performance management are emerging, geared to fit new ways of doing business, and better integrated with the management of business performance.

Organizations in the midst of fundamental change in their business model such as is implied by process management, .re-engineering, team-based designs, globalization, and increased lateral linkages need to quickly align the performance of employees with the new business model. The new organizational forms often depend on new capabilities and a different distribution of these capabilities across the organization. For example, engineers may find themselves carrying out complex negotiations with people in other companies when they are involved in joint development. These negotiations have both technical and business ramifications. The engineers' horizons need to be expanded beyond their technical expertise. Clearly, the development part of performance management has become critical to the ability of the organization to perform successfully. Goals must include development and development of competencies must be reviewed and rewarded. Because individuals generally align their behavior to the goals that are set and to what is reviewed and rewarded, these performance management practices can be a tool for change or a barrier to change. In short, it is of critical importance to companies to align all of these practices with changing business requirements and with one another.

Performance management must fit with the new business model. Table 1 illustrates the changing aspects of performance management, each of which is described below.

Integrate Systemic Levels of Performers

Individual roles in organizations are being conceptualized less as occupying a job-box on a chart, and increasingly within the context of an interdependent collective unit such as a team, project, program, or process that has collective responsibilities and outputs. The individual's performance requirements are not predetermined by a job description nor specified by a boss. Rather, they emerge from the team's needs. In turn, the responsibilities of the team are often determined by a management team at a more inclusive business level that determines charters for teams and makes sure that they collectively constitute the needed business unit performance. Conceiving of the organization as a set of nested performing units (Mohrman, Cohen and Mohrman, 1995), makes clear the necessity to manage the performance of each performing unit within the framework provided at the more inclusive levels of the organization. It also points out the need to align the goals of each level, so that each performing unit is contributing to the performance of the larger unit.

Two major changes of mindset are required for this to become a reality. First, entities such as teams, programs, and mini-businesses have to be understood as collective performing units, with all members collectively accountable for their success. This contrasts markedly with past practice of holding just the manager responsible for the performance of reporting units. The second mindset change is to see performance management processes as applicable and necessary at all levels. Teams not only receive goals and charters that define their work, but they have to be developed (through collective skills development, team building, resource allocation, and the importing or developing of needed individual expertises), reviewed as teams, and rewarded as teams. The same is true for the larger business unit, where development occurs largely through organizational development and organizational design activities.

Some of the elements of multi-level performance management are becoming more common in organizations. Gainsharing, profit-sharing and team bonuses are examples of rewards at a higher systemic level than the individual. Business unit-wide development have become common in the implementation of total quality management (TQM) and other systemic change initiatives. Team reviews are becoming increasingly common. Research findings support the premise that performance management when done at the team level is related to team effectiveness, and when done at the business unit level is related to business-unit effectiveness (Mohrman, Cohen and Mohrman, 1995).

It is becoming increasingly common for all elements of performance management to be tied to business objectives. System functioning and outcomes are emphasized over the isolated contribution of a function or an individual. This trend stems in part from the TQM emphasis on systemic metrics and from the process management emphasis on measuring the value delivered to customer and examining each sub-process in terms of value added. Thus, it is now common to see goals phrased in terms of cycle time, quality metrics, or customer satisfaction. Each performing unit is then goaled and reviewed in the explicit context of these business goals. Structurally, this has been enabled by the trend toward mini-business units that are expected to perform on the same dimensions as the overall business (eg., profit, market share, etc.) and by the emergence of process structures in which different functions of the organization are combined into units that perform an integrated process that delivers measurable value to the customer. Business performance management and the performance management of the performing unit are easily integrated under such circumstances. It requires that reviews focus not only on results, but also on the strengths and weakness of the performing unit that generated the results, and on developmental steps to enhance performance.

Open Performance Management Laterally

The increased lateral orientation of organizations requires that coordination that used to be achieved through hierarchical mechanisms occurs laterally within and across performing units. Manufacturing plants may provide product to multiple customer-oriented units serving different geographies or different large customers. Three different development teams may be developing different components of an overall system that has to fit together. Historically the goals, reviews and rewards of each of these units may have been separately mediated by a different boss. Integration among performance management activities of the units, if any, would not take place until a common reporting level was reached. Increasingly, goals are generated in forums that enable mutual influence, to ensure that each unit's goals are compatible with those of the interdependent units

(Galbraith, 1994). Units need to have input into each other's reviews, since they are stakeholders in one anothers' performance. Multidirectional performance management is exemplified in cross-functional approaches to planning that ensure that plans and goals are aligned both vertically and laterally.

Manager-centered performance management is becoming obsolete. Increased lateral orientation means that performing individuals, teams and business units are as likely to receive direction from co-workers, co-performing teams, and customers as from their managers. Decisions about how work is done and who will do what are as likely to occur laterally as vertically. Individuals increasingly perform in forums such as cross-functional task teams where their performance is chartered and judged by managers and management teams other than their own. In fact, individuals may be part of teams that have no one manager: rather, the team reports to a higher level team. Teams may be essentially self-managing. A variety of roles--coaches, team leaders, facilitators, and sponsors--are complementing and sometimes replacing functions traditionally performed by the supervising managers.

In such rich, multi-directional environments, a constrained manager-subordinate performance management process fails to register the rich interconnections that have bearing on performance definition, review and improvement. It limits the learning required for performance improvement. An open system of input and feedback needs to be created to enable multi-directional influence. On the other hand, maintaining multiple input and feedback channels requires orchestration, a function that may best be carried out by managers as a central part of managing the business.

Concrete manifestations of open system approaches to performance management are springing up in many companies. Peer reviews, upward appraisals, and three-hundred sixty degree feedback processes are becoming increasingly frequent. These most often are aimed at individuals and are used to trigger goal-setting and development and improvement activities, but in some cases are also being linked to rewards. Systematic customer feedback, for example, is included in a number of bonus systems.

Use Systematic Performance Management Processes to Run the Business

The formal administrative practices that constitute performance management have their basis in everyday processes that must be accomplished for any person or organizational unit to perform. Any performer--whether an individual, a team, or an entire organization--needs to know what the performance needs to be, needs to develop its capabilities to accomplish the performance, needs to know how well it is performing, and needs to feel like it is getting something it values out of the performance. Even without formal performance management practices, processes occur that make sure that these things minimally happen. From this perspective administrative performance management practices can be seen as formal organizational attempts to establish systems that drive and support these basic everyday processes of managing performance.

We earlier made the point that the formal performance management practices are often managed separately by different human resource management specialties and are therefore may not be well integrated. The tendency therefore has been to develop formal linkages among the various practices so that the necessary integration occurs. Unfortunately, acting on this tendency may result in even more complex and time consuming administrative systems, with the result that the perceived disconnect between formal performance management and running the business will increase. The secret to successful integration is not to compound the problem in this way but to reverse the approach. Performance management practices will become better integrated when they are all practiced in ways that are perceived to directly contribute to running the business. The common goal of running the business becomes the integrating factor among the many practices that constitute performance management.

The elements of the new performance management discussed below make it apparent that performance management <u>is</u> the managing of the business. It is the way that work is integrated, goals are aligned, performing units are developed to do the task, accomplishments are reviewed and corrective action is taken, and outcomes are tied to how well the business has performed. On the other hand, these activities could still be seen by managers to detract from their ability to manage the business if they see the events and administrative processes of performance management as disconnected and extra.

Rather than using a special event, such as goal setting, held for formal administrative purposes there are plenty of "natural" opportunities in which performance definition occurs that should be perceived as essential to running the business and can be used to double up for such things as administrative documentation needs. For instance, processes and documents used to "scope" projects with customers and project planning meetings used to plan and document steps and responsibilities of project teams and project members can be used to double as formal performance definition processes. Documents and practices that are used for "running the business" and that are seen as fitting the business needs can be used rather than creating a parallel system for enumerating and recording performance definitions.

Appraisal and review practices can also be aligned with managing the business and its performing units so that they are treated as a natural part of conducting work. Soliciting customer feedback after each engagement is an example. To the extent that this alignment can occur, performance management ceases to be seen as a "special event", and becomes part and parcel of the way work is done.

Many organizational activities don't fall neatly into the yearly, administratively convenient performance management cycle. People may be involved in a series of projects during a year, for example. A team's project may continue over several calendar years, although milestones may occur at odd times throughout the year. In these situations, engaging in artificially created time-consuming goal-setting sessions, formal reviews, developmental initiatives and reward decisions to coincide with the company's calendar driven administrative cycles instead of a natural performance cycle may dilute their value and get in the way of doing the work needed at the time. A greater convergence between business-management activities and performance management activities implies that these activities will coincide with the natural cycle of the work. When a team achieves a milestone, for example, it can trigger not only a technical review of the work, but also a review of the team's structure and process, planning for future activity, and appropriate development and reward activity.

The ultimate way of combining the process of rewarding performance with the actual performance is to make the performance in and of itself rewarding to the performer. This is the notion behind "work design" (Hackman and Oldham, 1980); to design the work people do in such a way--with variety, meaningfulness, and feedback, for example--that the work itself is rewarding. Another way to link rewards directly with performance is to create a reward mechanism that allows performers--individuals, teams, business units--to *share* directly in the value of their performance. Commissions, gainsharing, and profit sharing are examples of such mechanisms. Reward practices that are conceived, designed and administered as *exchange* (as opposed to sharing) mechanisms separate the performance from the reward so that some administrative connection must be made. In order to deliver performance rewards, for example, merit pay systems have to create a mechanism for measuring performance, convert that measure into a percentage of a compensation budget, determine the budget available, and calculate the particular reward. Each such step is not only administrative in nature but it further separates the actual performance from the reward that it generates so that in the end most, if not all, connection is lost.

The paradox pointed out in this section is that attempts to create formal people management systems to drive performance management ironically result in administrative bureaucratic practices that are perceived (and used) as something separate and detracting from the performance management processes that people use to run the business. This does not mean that we should not try to create systematic performance management processes. There is plenty of evidence to show that systematic processes are one of the most important determinants of high performance (Mohrman, Cohen, and Mohrman, 1995). This is one of the important reasons why TQM processes can be so powerful when used properly. The problem is: how can we create value-adding systematic performance management processes without them becoming value-detracting administrative systems!

Part of the reason the paradox occurs is because of the tension in any organizational setting between local needs for managing performance and people and organizational or corporate needs. Corporate needs reflect total system needs for both performance and consistency in people management. Local needs reflect subsystem idiosyncracies unique to their business situation and people. When corporate needs are imposed through administrative systems that detract from local needs they become separated from the managing of the local business. When local needs are allowed full reign in the form of locally invented practices they can detract from total corporate performance and install inconsistencies in people management that are problematic. The solution to the paradox is therefore to recognize that performance management systems should be designed and maintained by both local and corporate representatives.

Performance management systems--often consisting of a “tool-box” of approaches that can be adapted by local units--are increasingly being designed and reviewed by multi-level line task teams, using human resource professionals as consultants. This enhances the probability that these processes will fit the logic of the work, and also puts the ownership squarely where it belongs: in the lap of line management.

Focus on Performance Improvement

While the prevailing approaches to performance management have accentuated past performance by focusing on performance review and rewards for past performance, dynamic and competitive environments demand a focus on improving performance in the future. The performance management processes that directly serve this improvement orientation are: a) defining and planning performance and b) developing the capabilities to deliver it. Reviewing and rewarding performance must be done in service to defining and developing. This is precisely the stance of much of total quality management and especially of Deming (1986) for whom performance reviews are a necessary prelude to planning better performance and developing better ways of performing. Using reviews and rewards as a way of evaluating past performance are anathema to his philosophy that reviews are meant to reveal how to improve, not to evaluate results. One of the most consistent and strongest findings in social science is that goal-setting is one of, if not the, major determinants of subsequent performance (Locke and Latham, 1990). This appears to apply for both individual and collective performers.

Reward systems serve future performance and performance improvement if they lay out the mechanisms by which future and especially improved performance will be converted into rewards. Such practices as commissions, gainsharing, some bonus programs and sometimes profit sharing do this explicitly. Merit pay systems often cannot make a tight connection, and spot awards are completely focused on the past.

As work responsibilities increasingly spring from dynamic business priorities and are defined in the context of a dynamic collection of performing units, roles are increasingly defined by competencies rather than fixed job descriptions, and performance management systems must ensure the development of needed competencies. Skill and competency-based pay systems are concrete manifestations (see Ledford, this issue). Some companies have applied this concept to team pay as well, giving increases or bonuses to teams that demonstrate self-management capabilities. An important part of the management of teams and business units is ensuring that they are composed of needed competencies, and the development piece of performance management may consist of identifying needed skills that have to be developed in members or added to the unit. This focus on competencies required by the business to staff a dynamic constellation of performing units brings a future-oriented developmental focus to performance management.

Implications and Challenges

We have argued that new organizational forms demand performance management systems that align managing the business and managing performing units at all levels. The systems must fit the way work is done rather than the line and box structure that may still constitute the formal reporting structure of the organization.

One implication of this discussion is that performance management practices will derive from and be tailored to fit each business's changing requirements. The search for the perfect system and widespread adoption of accepted professional practice will give way to the tailored system. This will lead to a wide diversity of practices designed to fit the business.

A second implication is that making sure that performance management practices are occuring will be even more central to the responsibilities of managers. However, rather than being the sole agent of these practices, they will be orchestrators of multi-directional, open processes. Managers will manage performance management. Performance management practices will increasingly be seen as tools to manage the complex dynamics of new organizational forms operating in increasingly complex environments.

The challenges are immense. They include the necessity to overcome manager's belief that managing performance is primarily managing individual excellence, and individuals' culturally held value placed on recognition and reward of their individual contribution. Another challenge lies in convincing stretched and stressed managers that the activities required to manage performing units effectively constitute an integral path to business performance. Tremendous system design and skill development efforts are implied in this transition. Another challenge is to prevent the pedulum from swinging too far. We have already seen cases where managers so totally accept performance management as a business management tool, that they no longer see it as a people tool. Compensation systems can be designed totally from a business perspective without regard to the way they affect people. This, of course, will be detrimental in the long run. Business management **is** people management.

Yet, most of the elements of the new performance management have begun to emerge in many organizations. They are emerging out of necessity, because practices that worked in the vertical line and box organization don't fit with the flat, dynamic, laterally-oriented process and team-based organizations.

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Table I

The Evolution of Performance Management

From Administrative People Management	To Running the Business
Focus on individual as performer (box).	Focus on integrating multiple systemic levels of performers (individuals, teams, processes, business units). Manage performance in context of business performance.
Focus on boss as performance manager (line).	Focus on performance management as open system, involve all stakeholders in the performance. Manage performance laterally and mutually.
Focus on separate performance management practices.	Integrate all performance management processes by focussing on running the business.
Focus on administrative systems and practices.	Use systematic processes that serve both administrative needs and running the business.
Focus on past performance by emphasizing reviews and rewards, minimizing improvement.	Focus on performance improvement by emphasizing planning and development.