Modern Performance Management
Why companies are rethinking the annual performance review

Rethinking Employee Performance Management in the Digital Workplace

Performance management processes are not "going away," but they are transforming in the digital workplace to support more frequent, contextual and transparent feedback. HR leaders should explore these new approaches and consider their impacts on related processes and talent management applications.

Impacts

HR leaders should evaluate the following:

- Increased collaboration and transparency in the digital workplace requires re-evaluating traditional performance management systems for more continuous, engaging approaches.
- Changes in performance management practices, such as removing the annual appraisal score, force a rethink of compensation policies, programs and tools.
- Increased performance feedback frequency and gamification will lead to increased usage of individual employee performance metrics.

Recommendations

- Embrace new approaches in employee performance management that support frequent performance conversations, personalized development and visibility of accomplishments.
- Adjust compensation practices to make new performance management alternatives more effective.
- Determine what operational business performance metrics affect individual and team performance, and actively manage how those are measured and communicated to employees.

Strategic Planning Assumption

By 2020, 20% of large global enterprises will have abandoned the performance review rating score.

Analysis

Performance reviews are not "going away" anytime soon, as has been frequently predicted in press and industry journals. Organizations fundamentally need a way to evaluate and communicate who is performing well and who needs to be let go, to identify where development opportunities exist, and to determine how to pay employees for their contributions with a somewhat equitable or at least defensible approach.

However, the effectiveness of traditional performance management processes is questionable, and satisfaction levels are low.

- Almost 60% of surveyed HR leaders are unhappy with their current performance review and rating processes (rating them a grade C or less).[1]
- Fifty-eight percent of executives believe that their current performance management approach drives neither employee engagement nor high performance.[2]
- Managers and employees alike view performance reviews as a waste of time that results in demotivated employees,[3] despite the millions of dollars (in time and software) spent.

Here are some of the commonly cited problems or complaints with performance management processes.

- Goals cover too long a period and so are not flexible with changing business needs, or are set too late in the review cycle to drive appropriate focus throughout the year.
- Delayed feedback is counterproductive, delays the impact of corrective actions and breaks the linkage in pay for performance.
- Feedback coupled with a performance "score" puts more focus on the score than the feedback.
- There is typically insufficient focus on meaningful coaching and employee development.
- Stack ranking forces competition, not collaboration, within teams; it also drives "average" performance effort when employees understand they will usually receive "midrange" scores.
- Rankings and ratings can make people feel like a label ("average performer" or "high potential").
- The appraisal process itself is often needlessly complicated and time-consuming.
- Performance management processes often result in demotivated culture and performance.

Despite these and other challenges, performance reviews remain firmly entrenched in organizations.

- More than 90% of organizations indicate the use of some type of performance review.[4]

- Forty-five percent of organizations implement performance management ahead of other talent management suite applications, including recruiting, learning, compensation and succession management (see "Magic Quadrant for Talent Management Suites").

- Gartner continues to see steady demand for performance management solutions, usually as the first step in a broader, integrated talent management initiative (see "Hype Cycle for Human Capital Management, 2015").

In recent years, Gartner has seen growing but shifting interest in performance management processes and technologies, driven both by dissatisfaction with current systems as well the increasing demands of the digital workplace, where a more consumerized work environment promotes employee agility, effectiveness and engagement.

Some organizations are looking to abolish the performance review rating for its divisive nature. Other organizations are looking to augment or even replace the annual review meeting with more frequent conversations – face to face or virtual, formal or informal – between employees and managers. Still others are hoping to leverage more consumerlike tools such as social networking to drive engagement and collaboration around goals and objectives, to improve individual and team performance as well as organizational culture.

Regardless of underlying drivers, in the digital workplace the performance management process is being re-evaluated at each of its component parts, as organizations seek new ways to improve employee alignment, performance and engagement. HR leaders can use this research to anticipate and leverage the impacts of these new performance management practices across the enterprise (see Figure 1).

Figure 1. Impacts and Top Recommendations for Rethinking Performance Management in the Digital Workplace

Impacts	Top Recommendations
Increased collaboration and transparency in the digital workplace requires re-evaluating traditional performance management systems for more continuous, engaging approaches.	• Embrace new approaches in employee performance management that support frequent performance conversations, personalized development and visibility of accomplishments. • Hire managers with strong coaching and communication skills, and hire for and develop digital dexterity across the workforce.
Changes in performance management practices, such as removing the annual appraisal score, force a rethink of compensation policies, programs and tools.	• Adjust compensation practices to make new performance management alternatives more effective. • Examine the roadmaps of talent management suite or specialist compensation management providers to see how the solutions will adapt to changing performance management practices.
Increased performance feedback frequency and gamification will lead to increased usage of individual employee performance metrics.	• Determine what operational business performance metrics affect individual and team performance, and actively manage how those are measured and communicated to employees. • Re-evaluate practices and policies around data sharing with individuals and teams, balancing the risks of oversharing and undersharing while supporting the need for greater transparency.

Source: Gartner (August 2015)

Impacts and Recommendations

Increased collaboration and transparency in the digital workplace requires re-evaluating traditional performance management systems for more continuous, engaging approaches

The concept of abolishing the annual performance review has been discussed, adopted, reversed, reinstated and modified many times across thousands of organizations over the past 50 or more years. The underlying concern is that the performance review is a process that requires considerable time (and money) for little – or even negative – return.

However, despite its flaws and often reviled status, the traditional performance review isn't going away, because it provides a system for identifying and tracking performance, documenting this, and potentially providing guidelines for associated rewards. Regulatory and labor contract compliance requirements are also common reasons why performance reviews remain in place. What is emerging, however, is a series of tools that supplement these documentation and compliance requirements with the ability to focus on the continual process of performance improvement, fostering regular feedback and guidance to employees in the context of daily work activities. In the forward-looking 2013 research note "Maverick* Research: Living and Leading in the Brain-Aware Enterprise," Gartner described a "typical day in the brain-aware enterprise" in 2020: Annual performance reviews have been replaced by frequent feedback and coaching, leaders are held accountable for employees' career progression and the corporate hierarchy has been broken down to foster greater innovation and collaboration. This futuristic scenario is not only wholly plausible today, it is in fact emerging across early adopters of new agile performance management practices.

The advent of social networking and the hyperconnected workplace has increased the demand for faster and more contextual communication, not just in our daily personal lives but also within the corporate work environment. Rather than focusing on long-term look-back periods, more frequent and contextual feedback is becoming the workplace norm in early adopter organizations, as managers guide and coach employees regularly and in context with the patterns of work. Organizations are increasingly focused on:

- The processes that support regular performance feedback and development

- Alignment of work with the shifting goals and objectives of the organization

- Improved employee/manager communications as well as expanded peer-to-peer collaboration

- Increased organizational transparency

- Improved, sustainable workforce engagement

Additionally, across the globe and driven by the demands of the digital workplace, the roadmaps of human capital management (HCM) technology vendors reveal heavy investments in new performance management approaches. These are aimed at transforming performance to a regular cadence of feedback and coaching while improving workforce engagement and collaboration across the enterprise.

The latest approaches in performance management include the following:

- **Frequent check-ins and coaching** – In an era where consumer feedback through "likes" and retweets is almost instantaneous, new approaches to employee performance reviews have emerged that address this desire for immediate feedback within the enterprise. The concept of regular "check-ins" and updates between employee and manager to foster conversations, identify accomplishments and roadblocks, and provide coaching for future success is manifesting in a series of new apps, delivered from not only startup providers but also large ERP suite vendors. Common features include – but are not limited to – the following:

    - Employee summary of projects, actions and roadblocks

    - Manager review and commentary

    - Coaching tips

    - Pulse surveys and other assessments

    - Team dashboard for managers

    - Personal dashboard for employees

    - Other analytics and reporting

    With these solutions, companies are shifting their focus away from infrequent conversations centered on the shortcomings of individuals to frequent and more positive conversations centered on goals and objectives, accomplishments and development opportunities. Professional services organizations such as Accenture have recently moved to such a model,5 but others such as Cargill6 and Adobe7 and even government agencies such as JPL NASA8 have made similar moves in the past. What these and other companies recognize is that employees increasingly want more timely and direct feedback on their performance, without "surprises"; waiting until the end of the year to provide feedback – especially negative feedback – is counterproductive. Regular coaching and feedback fosters better relationships, enables real-time course-corrections, supports clarity in career development opportunities and more. With this approach, any formalized year-end performance appraisal becomes simply a summary of the documented conversations, actions, accomplishments and observations made throughout the year.

    Additionally, regular interaction and feedback also supports a more agile organization. The brain perceives change as a threat – change that may come through coaching or feedback, or from new or modified goals. Organizations can reduce the brain's threat response by introducing regular dialogues and check-ins that build reputation, recognize excellent performance, create opportunities to develop or demonstrate mastery, and more (see "Accelerate Digital Workplace Momentum by Understanding How the Brain Works").

    Related caution:Your culture will change when you move from a look-back, measurement-focused mindset to a continuous development and coaching mindset; ensure the organization is effectively trained to embrace this. Specifically, managers will need to be properly trained in providing effective feedback and coaching in order to effectively meet employee expectations. Without the proper guidance, frequent conversations can drive even greater employee dissatisfaction (for example, they may be perceived as micromanagement disguised as performance check-ins).

- **Social employee recognition** – Another form of frequent employee feedback that is seeing increased adoption is the peer-to-peer feedback enabled by social employee recognition software (see "Social Employee Recognition Systems Reward the Business With Results"). These social tools make it easy for colleagues (and managers) to provide recognition and thanks for performance or support any time, and make that recognition visible across the enterprise through social activity streams. The increasing element of gamification in these systems encourages regular participation and combines the benefits of intrinsic motivators (achievement, purpose, mastery, for example) reinforced by extrinsic motivators (cash, points and other rewards).
  Related caution: Recognition systems are not an alternative to equitable and effective compensation practices. They should complement, but not replace, bonuses and merit awards. Also, cultural acceptance varies across the globe: don't assume the social recognition model you deploy in the U.S. will work in other geographies.

- **Ditching the performance review score** – While most organizations will maintain some level of documentation of performance management conversations (either through traditional review processes or documentation of regular check-ins and coaching), some have decided very specifically to eliminate the employee ranking and performance scoring process. Texas Roadhouse9 is an example of a restaurant chain that did just that, maintaining (but improving) the performance appraisal process but dropping the performance review score in order to focus the performance conversation on growth, support and future development initiatives, while basing future compensation changes on COLA and discretionary bonuses.
  Related caution: Ensure you have a clearly defined and well-communicated methodology for future compensation and bonus adjustments; without a performance review score employees may not be able to focus on the performance feedback, as they try to discern how said feedback will translate to future monetary rewards.

- **Agile (and social) objectives and key results (OKRs)** – Goals and objectives have long been components of the performance management process, but they come with a series of challenges. They're typically set up annually (but may be as frequent as quarterly) with limited ability to significantly modify their

details or even identify related projects/tasks at a detailed level. Most goal management software is driven through a top-down cascading process, intended to provide direct line of sight from the company's top strategic objectives to an individual employees' goals. Unfortunately, direct line of sight is sometimes obstructed, and employees often feel disconnected from or challenged to fully support their goals and objectives.

New tools change this dynamic through the development of bottom-up goal setting, giving employees greater flexibility in how their goals are accomplished as long as they clearly understand the higher-level goals and objectives of the organization. Additionally, goals and objectives are becoming increasingly social, allowing employees to assign shared responsibility for their delivery and/or to broadcast their progress or completion to the enterprise social network. Key results or accomplishments, communicated frequently and broadly, help connect employees to the work and development of their peers, enable frequent recognition and reputation development, help identify individual performance measured in the context of the team performance, and contribute to a more engaged workforce.

Related caution: While goal management is typically an integrated component of a broader performance management offering, there are stand-alone OKR offerings that provide greater support for project and task management, social sharing, employee recognition and more. Weigh your needs for goal/task management transformation against the costs of user interface and process integration.

Recommendations:

- Embrace new approaches in employee performance management that support frequent performance conversations, personalized development and visibility of accomplishments.

- Hire managers with strong coaching and communication skills, and hire for and develop digital dexterity across the workforce to effectively leverage emerging performance management technologies (see "Defining Digital Dexterity – The Core Workforce Resource for the Digital Business").

- Evaluate the analytics capabilities of these new tools for their ability to provide meaningful insights and performance support for employees and managers alike. Optimize new performance and goal management solutions for tablets and smartphones, as these are increasingly the devices of choice for logging regular interactions as well as capturing visuals through photos and videos.

Changes in performance management practices, such as removing the annual appraisal score, force a rethink of compensation policies, programs and tools

Many organizations have decades-old pay-for-performance practices whose general purpose is motivating employees and instituting a meritocracy. These practices have been generalized across most types of organizations except some public sector and highly unionized organizations, where pay increases and grade changes are still based largely on tenure. Through inquiry with a number of such organizations, Gartner has observed that the nondifferentiation of performance ratings or compensation practices often leads to employee demotivation and a sense that extra effort will not in itself reap any rewards. It was to mitigate such workforce risks that pay-for-performance practices were first instituted. These include:

- **Annual or quarterly bonus/incentive programs for all staff** – Sales executives are given quarterly targets for revenue generation, and are incentivized against those targets with financial rewards. Other functions within the business define their own set of objectives, how to measure their accomplishment and what weighting to apply to each one. Frequently, these include highly qualitative objectives with very little or no quantitative input. Annual goals in many organizations are part of the annual appraisal cycle, where ratings on goals determine both the performance rating and the percentage of the target bonus to be paid out.

- **Merit matrix for annual salary review** – During annual salary increase cycles, many organizations apply a merit matrix or set of guidelines for minimum and maximum salary increase percentages. This is based on a combination of performance rating, market compensation levels (generally as compa-ratio or position-in-range) and the allotted salary increase budget per country, which takes into account varying inflation rates.

- **Equity and long-term incentives (LTIs)** – Practices related to these compensation elements have varied over time as tax regulations and accounting rules have changed, especially relating to stock options and deferred compensation schemes. Although most frequently reserved for senior executives, some organizations have also rewarded LTIs to employees with a combination of high performance and high potential ratings.

As organizations shift to performance management practices that rely on frequent feedback rather than annual reviews, they will equally need to consider what to do about compensation practices. To date, little has been published about new compensation practices resulting from changing performance management practices as the focus is currently on the removal of the annual appraisal.10 The same can be said for Gartner inquiries. This will not be sustainable, however, as pay-for-performance practices rely on a heavy linkage between performance ratings and financial rewards, and both managers and employees need a way to understand the mathematics behind how the profits (or merit budgets) of the company are distributed in a somewhat "equitable" fashion across the enterprise. Make this compensation process too opaque and the decreased levels of employee dissatisfaction stemming from improved performance will be wiped away with dissatisfaction around the pay practices.

Changes in performance management practices will require rethinking the organization's compensation programs as well, with several examples including:

- **The shift from annual to periodic bonus/incentive programs** – The increased frequency of feedback and check-ins within new performance management practices could, for some industries, lead to the dismantling of annual bonus programs, replaced by more short-term, one-off bonuses related to the successful completion of a major project, or milestone accomplishments against a bigger goal. These smaller but more frequent bonus payouts may also take the form of point accumulation or other gamification techniques that reflect a more personalized approach to bonus programs beyond pure monetary payouts.

  Related technology challenge: As compensation practices shift in light of more frequent feedback and related rewards for accomplishments, organizations will require much more robust compensation technology that can maintain short-term incentive programs, manage bonus payout calculations, interface seamlessly with payroll and manage global tax regulations. The benefits of more-frequent rewards will need to be balanced against the increased administrative burden.

- **Removal of annual appraisal ratings** – The measurement of employee contributions to company performance – and the accompanying financial rewards for that performance – is an expectation of employees and managers alike. Remove the annual performance rating and suddenly annual salary reviews are unable to leverage those appraisal ratings to determine "equitable distribution" of increase budgets. Organizations may experiment with practices such as applying a single, across-the-board increase for all employees per the budget, aligned to local inflation rates and economic conditions, or a separate increase budget for one-off "true-up" increases for employees significantly below market compensation rates. Alternatively, predictive analytics may be used

to suggest a specific increase amount to be used to retain specific employees considered to be at high risk of leaving (see "Use Data Science to Address Employee Flight Risk"). In these and other cases, the organization will need to develop alternative approaches to compensation that have historically relied upon performance-based merit matrices.

Related technology challenge: This will demand significantly more flexibility in compensation tools to manage varying annual salary review processes and approaches. Also, increased usage of analytics to ensure appropriate market comparisons and calculate employee flight risk will help ensure that budgets are being used for employee retention.

- **OKRs and bonus/incentive payouts** – Though OKRs are nothing new, their approach and practices firmly draw the line between objectives driven by financial incentive and those driven by professional accomplishment. Some organizations, especially those in environments where variable pay programs must be negotiated with workers' councils, may separate objectives that have a bonus amount attached to them from those that do not, but may still be challenged with the ability to differentiate bonus payouts. The practice of paying for smaller but more frequent accomplishments, however, will increase as greater utilization of freelancers and temporary staff inures organizations to the concept of incremental rewards. Well-defined OKRs, broken down where appropriate into smaller accomplishments or milestones with their own payout targets, may be the basis for new approaches to salary progression or at least shorter-term incentive programs.

  Related technology challenge: Practices will likely evolve slowly and compensation tools for variable pay programs will need to increase significantly in flexibility in order to meet varying demands around bonus programs linked to more detailed, periodic employee objectives.

- **Crowdsourced bonuses** – With the rise in adoption of social employee recognition programs, organizations may turn to their use in a more formalized approach to bonus allocation and distribution. Social employee recognition programs typically involve the peer-to-peer allocation of points or tokens throughout the year in recognition of performance, innovative ideas or other valued actions (see "Technology Overview for Employee Recognition and Rewards Software"). Some companies such as IGN11 and Shopify have based bonus allocations on percentages of tokens earned, gamifying the bonus program by incentivizing employees to earn more recognition tokens that in turn garner greater bonus payouts.

  Related technology challenge: Social recognition programs often garner high levels of sustained adoption because employees value their peer-to-peer nature. Such programs are usually kept separate from performance management systems. Tying them to bonus payouts can dramatically alter the nature of activity within the platform. Organizations should look to recognition platforms that allow program separation of regular peer-to-peer feedback from bonus-based point allocations, to avoid diluting the underlying program drivers and employee participation motivations.

Recommendations:

- Adjust compensation practices to make new performance management alternatives more effective. In an effort to make performance processes less onerous and more engaging, organizations run the risk of making the compensation process less transparent and more contentious when increases and other rewards are not tied to quantitative review scores.

- Examine the roadmaps of talent management suite or specialist compensation management providers to see how the solutions will adapt to changing performance management practices.

- Ensure effective program governance in light of the new challenges of social and gamified approaches. Peer-to-peer social engagement within the enterprise is on the rise, but utilization can morph when social goals and social recognition become tied to increasingly significant portions of an employee's total rewards package.

Increased performance feedback frequency and gamification will lead to increased usage of individual employee performance metrics

Ratings and personal metrics pervade our lives: fitness scores and other wellness metrics, number of "likes," ratings on a five-star scale, number of followers, level of activity on social networks, position on a game's leaderboard and so on. In their personal lives, employees have grown accustomed to seeing – and sharing – their performance scores. This is not so much the case in their professional environments, except perhaps for sales functions where quota attainment and leaderboard practices are frequently used to promote sales growth and revenue target achievement.

In order to meet the demand for more-frequent feedback, organizations will need to rethink what employee performance metrics are delivered and how they're communicated. Most organizations today look at corporate performance in three very different ways:

- **Program success for corporate strategic initiatives** – Focused on a set of high-level strategic KPIs that are reported on and reviewed in strategy review meetings with senior executives.

- **Success against financial plans and budgets** – Focused on planning metrics that are reviewed through regular financial budget and forecast processes, leveraging corporate performance management suites.

- **Cascaded goals and employee performance ratings** – Generally supported by performance management modules in talent management suites.

The three approaches are typically only loosely aligned through verbiage showing assumed connections between particular goals or financial targets and corporate strategy. Employees generally have access to their own goals in their performance forms, not those of the rest of their immediate team, and those goals rarely include data feeds from other systems to incorporate results from other business performance metrics.

For example: An IT support professional within an IT shared services center needs to meet certain targets around ticket volumes, timeliness of response, accuracy of response, how frequently the case is completely resolved with no follow-up ticket or complaint, and customer satisfaction. In addition, the IT support professional has the following goals:

- *Improve team efficiency by actively participating in knowledge sharing and documentation exercises (measured by activity in the social technology in the IT service delivery tool)*

- *Improve IT services by participating in a project designing and piloting a new service (measured by project participation and deliverables)*

In a traditional performance management approach, the employee would enter these goals at the beginning of the year and then update the results periodically or at the end of the year. The manager would take this into consideration, enter a performance rating and follow a calibration process to ensure the performance rating meets a required rating distribution. Organizations looking to replace this annual cycle with an ongoing feedback process as well as a more frequent and transparent goal management process need to also consider how employees get regular feedback about their performance. This should include not only basic feedback discussions, but also employee self-service dashboards that allow employees to track in real time how their specific actions, decisions and behaviors are enabling them to reach their goals.

Trends in gamification and the consumerization of enterprise applications will drive demand to include employee performance metrics in performance management tools, and enable employees to share individual or team results with management, other team members or as a public achievement that they would like to make visible to others in the organization. For many organizations, this would represent a significant change in terms of performance culture, exposing accomplishments, actions and other aspects of performance beyond the silo of the employee-manager relationship. It would also be a significant change in terms of enabling employee self-service analytics within business applications, and enabling the results of those analytics to be sent to other applications to facilitate performance management discussions. Currently, some organizations have created employee dashboards on their enterprise BI platforms for certain employee segments and data types, but this activity is typically far removed and disconnected from performance management modules in talent management suites. In addition, organizations will need to revisit their current policies around the data that is exposed to employees on personal performance dashboards or scorecards. They must balance the risks of oversharing, which can be demotivating, and undersharing, which can lead to an insular opinion of one's work disconnected from how others are performing.

Recommendations:

- Determine what operational business performance metrics affect individual and team performance, and actively manage how those are measured and communicated to employees.
- Re-evaluate practices and policies around data sharing with individuals and teams, balancing the risks of oversharing and undersharing while supporting the need for greater transparency in individual, team and corporate performance measures and metrics.
- Evaluate performance management technology in HCM or talent management suites for its ability to enable the easy and quick inclusion of snapshots, data elements or metric result feeds from third-party systems.

Acronym Key and Glossary Terms

COLA	Cost-of-living adjustment
Digital workplace	The digital workplace is a business strategy for promoting employee effectiveness and engagement through a more consumerlike computing environment. (see "Digital Workplace Key Initiative Overview")

Evidence

1 "2010 Study on the State of Performance Management," WorldatWork/Sibson, 2010. In the study, 58% of senior HR professionals (n = 750) rated their performance review process with a grade C or lower.

2 "Performance Management Is Broken: Replace 'Rank and Yank' With Coaching and Development," Deloitte University Press, 4 March 2014.

3 S. S. Culbertson, J. B. Henning, S. C. Payne, "Performance Appraisal Satisfaction: The Role of Feedback and Goal Orientation," K-State Research Exchange, 2013.

4 "HR Professionals' Perceptions About Performance Management Effectiveness," SHRM, 2014. The study found that over 91% of organizations have periodic formal performance reviews.

5 L. Cunningham, "In Big Move, Accenture Will Get Rid of Annual Performance Reviews and Rankings," The Washington Post, 21 July 2015.

6 "Why Cargill Is So Good at Performance Management," CEB, 6 May 2014.

7 "Just Checking In," Adobe Life.

8 "Universe," Jet Propulsion Laboratory, December 2013.

9 C. Arringdale, "Oh My God! They Killed the Performance Appraisal!" SHRM Connect, 8 July 2014.

10 Deloitte briefly mentions the needing to review its compensation policies in its Global Human Capital Trends 2015 report. Adobe publicizes new performance practices, but not those of compensation.

11 E. B. Boyd, "At IGN, Employees Use a 'Viral Pay' System to Determine Each Other's Bonuses," Fast Company, 16 December 2011.

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