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Before Saying Goodbye to Performance Ratings, Consider This

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If there's one theme that sticks out in my mind following last week's Radford IMPACT 14 conference, it's the notion that performance ratings might be on their way out. For example, all four companies represented on our human resources leadership panel (Juniper Networks, Pandora Media, Regeneron Pharmaceuticals and Workday) said their companies do not use performance ratings or rankings, and have not done so for some time — if ever.

While it might be easy to dismiss this fact as a strange coincidence – due to a small sample size or as an artifact of polling a select group of companies with cutting edge HR practices – it is far harder to ignore Radford's preliminary Q2 Hot Topics Survey results that show 22% of companies have moved away from performance ratings. What's more, a full quarter of attendees polled during our *Pay-for-Performance for Everyone Else* sessions at Radford IMPACT 14 said they are considering a move away from ratings. Clearly, this issue is top of mind and a potential trend is brewing.

With that said, the decision to move away from performance ratings is incredibly complex, especially if your company "pays for performance." Without specific performance ratings to serve as benchmarks, assessing employee performance levels across an organization can become a highly ambiguous task. It is already challenging enough when ratings exist, so losing the security blanket of performance ratings can seem downright scary. Additionally, getting rid of performance ratings is probably not right for everyone. Indeed, several of our human resources leadership panelists agreed that bringing back forced rankings at Yahoo! was probably "the right decision for Yahoo! right now." So, how does one go about making this all-important call?

To help facilitate a dialogue, we've come up with a list of five things human resources teams should consider if their company is considering a move away from performance ratings or rankings:

1. Consider Your Culture

Most companies that abandon performance ratings do so because they believe the practice serves as a barrier to their desired culture or business needs. In collaborative or mission-driven environments where a "we're all in this together" ethos is required, performance ratings or rankings can have the adverse effect of pitting individuals against each other in a race to out-rank one another. Companies that live on the bleeding edge of innovation require teams of brilliant people who have incentives to share ideas rather than protect their turf. If your company seeks to create an innovation-first environment, dropping performance ratings could make sense. Conversely, if your company faces a tough turnaround situation where difficult staffing decisions lie around the corner, performance ratings could be a critically important tool.

2. Manager Discretion Requires Manager Training

According to Radford's preliminary Q2 Hot Topics Survey results, 56% of companies without performance ratings rely on managers to use discretion when determining merit increases. This makes sense for experienced leaders who have the right coaching in performance management and understand how to allocate compensation pools strategically. However, the same may not be true for new managers or young companies with managers in stretch roles. In these cases, removing the guardrails of performance ratings without proper training could be disastrous. If your company is poised to remove performance ratings, make sure your company is also ready to invest in training on how to handle performance conversations and compensation decisions.

3. Defining Pay for Performance Still Matters

Almost every company represented at Radford IMPACT 14, whether they use performance ratings or not, would say they have a pay-for-performance philosophy. This means that a lack of performance ratings does not suddenly make the evaluation of employee performance irrelevant. On the contrary, it's still a major issue and critical to success. Eventually, every team needs to determine the relative contributions of its members and make compensation trade-offs to stay within budget. As such, before pulling the plug on performance ratings, team leaders need to sit down and redefine how base salary increases, bonuses and long-term incentives will be awarded going forward. Without initial clarity, managers might avoid making trade-offs altogether (a "peanut-butter approach") or might make irrational decisions (i.e., favoritism).

4. Employees Will Hear What They Want to Hear

One real risk of dropping performance ratings is that under-performing employees will leave performance conversations without picking up on the tough messages they need to hear. Without a well-coached manager or carefully scripted conversation, weak performers could easily think they meet expectations. What's more, they will be surprised, confused or angered by compensation decisions. In line with several of our previous points, providing managers with proper training and guidelines will go a long way toward minimizing mixed signals in a performance rating free zone.

5. Goals Will Count More Than Ever

A good number of companies that abolish performance ratings also reconfigure their performance conversations to tackle forward-looking goals. They do so in favor of looking backwards at past successes and failures, which is a commonplace tactic in most performance review discussions. In growth-oriented companies, most employees want to know what they are aiming for, and good goal-setting is critical for their ongoing motivation. Measuring performance against these goals, rather than a zero-sum game of performance ratings, becomes the benchmark for determining bonus payouts, long-term incentive awards and promotion opportunities. In the absence of performance ratings, creating and tracking employee goals becomes more important than ever.

Making the Right Call

When it comes to adding or removing performance ratings, there is no right answer. And certainly, this is not the time or the place to follow the herd. Listening to the market to keep abreast of new trends and to learn best practices is important, but the decision to drop performance ratings needs to come from inside your organization. Making the right call requires understanding your corporate culture, assessing your growth trajectory and a willingness to make investments in other performance management areas required to support an environment without performance ratings or rankings.

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