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EXECUTIVE SUMMARY

Research Question

What organizational changes have companies experienced upon eliminating ratings within their performance management system? Additionally, how have eliminating ratings positively or negatively impacted companies?

Increasing Transition to Performance Management 2.0

Over the past decade, organizations have begun to move away from traditional performance management processes (annual reviews, assigned performance ratings, a link to compensation) to remove "performance ratings" based on the perception that traditional PM is not working.

- As of 2015, more than 55 companies have removed performance ratings. Among those are some high-profile companies such as GE, Microsoft, Accenture, etc. (see Appendix A).
- According to a study of 244 companies in 2016, almost all companies in the study use ongoing feedback, 52% of companies have adopted ratingless reviews, and 34% of companies use ratingless reviews and ongoing feedback.
- 80% of participating organizations say that managers make decisions how to allocate rewards without ratings while staying within budget constraints.

The perceived impact of these new performance practices is high: 90% of companies that have redesigned performance management see direct improvements in engagement, 96% say processes are more simple, and 83% say they see the quality of conversations between employees and managers increasing. **It is noteworthy that the positive impact may not all be attributed to the removal of performance ratings**.

Going Back to Performance Management 1.0

While an increasing number of organizations are transitioning to PM 2.0, some companies have reversed course and reinstituted their conventional PM processes due to different reasons. The following are a few examples:

Ideology at the top matters - Intel and Sun Communities had eliminated ratings, and the supervisors reported that they had no difficulty differentiating performance without ratings. However, company executives insisted on returning to ratings since they believe ratings could create healthy competition and clear accountability.
Some companies seek "third way" - Deloitte has backpedaled from eliminating ratings to having project leaders assign four different categorical ratings by quarter. Employees in PwC receive ratings on five competencies rather than a single rating.
"Shadow ratings" are harmful - One insurance company went back to formal appraisal because employees interpreted merit-pay increases into performance scores. However, this company keeps other changes it had made to its performance management system, such as quarterly conversations.

The Real Impact of Eliminating Ratings

Recent research suggests that eliminating ratings can adversely affect performance management goals. CEB's research analyzed the effect of ratings across 10,000 employees globally and a variety of industries and found the following outcomes.

Decreased Satisfaction, Especially in High Performers - Satisfaction declines after the first performance review process without ratings (see Appendix B). One HR VP highlights, "Without the visible symbol of a rating, employees didn't understand the processes or philosophies behind them." This was especially true of high performers, who experience a 16% greater decrease in manager conversation quality than low performers.[6]

Decreased Employee Engagement - Companies that eliminate ratings experienced a 6% decrease in the average employee engagement score.[6] Research indicates this is due to the decreased time managers spent in informal conversations, decreased manager conversation quality, and decreased perceptions of pay differentiation.

Decreased Time Spent on Informal Conversations - While managers in companies that eliminated ratings saw a decrease in the time spent on performance management activities, the bulk of this decrease was time spent in informal coaching conversations (see Appendix C). Without ratings, managers did not have a clear process to follow up with employees and diverted attention to other activities.[6]

Decreased Manager Conversation Quality - Companies who eliminated ratings experienced a 14% decrease in the perception of manager conversation quality surrounding performance. One employee compared their performance review without ratings to "reading my horoscope. I could interpret it any way I wanted to."[6]

Decreased Employee Perceptions of Pay Differentiation - Companies who eliminated ratings experienced an 8% decrease in the perception of pay differentiation, due to employees feeling that compensation decisions were less transparent without ratings.[6]

Alternatives to Eliminating Ratings

As seen in the above outcomes, performance management boils down to managers having quality conversations with employees. It is not the ratings themselves that matter most, rather, it is leaders ability to communicate these judgments expressed as ratings.[7] The preeminence of manager conversation quality can even be seen when companies eliminate ratings. In a personal interview with the Cigna CHRO John Murabito, he argues that the point of eliminating ratings is "all about getting leaders talking to their employees."[8] The issue, however, is that data shows eliminating ratings does not always accomplish this. An alternative to improving coaching conversations is investing in manager quality and best practices.[9]

One real-life example of this is GE, which incentivizes managers to be "people leaders" as opposed to "people appraisers," focusing on leading and inspiring their teams.[4] This has given GE positive results in employee engagement, time to market, and innovation.

Conclusion and Recommendations

There are three scenarios when companies should consider eliminating ratings: when organizations have hyper-competitive cultures, forced rankings, or place an unnecessary weight on numbers.[6] Considering the potential negative impacts of eliminating ratings and that there are alternative means of accomplishing the same goal, removing ratings could be a risky and costly endeavor for some companies to pursue.

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7) Adler, S., Campion, M., Colquitt, A., Grubb, A., Murphy, K., Ollander-Krane, R., & Pulakos, E. D. (2016). Getting Rid of Performance Ratings: Genius or Folly? A Debate. Industrial and Organizational Psychology, 9(02), 219-252. Retrieved September 16, 2017, from https://search-proquest-com.proxy.library.cornell.edu/docview/1801399916?pq-origsite=summon.

8) Murabito, J. (2016, September 26). Personal Interview.

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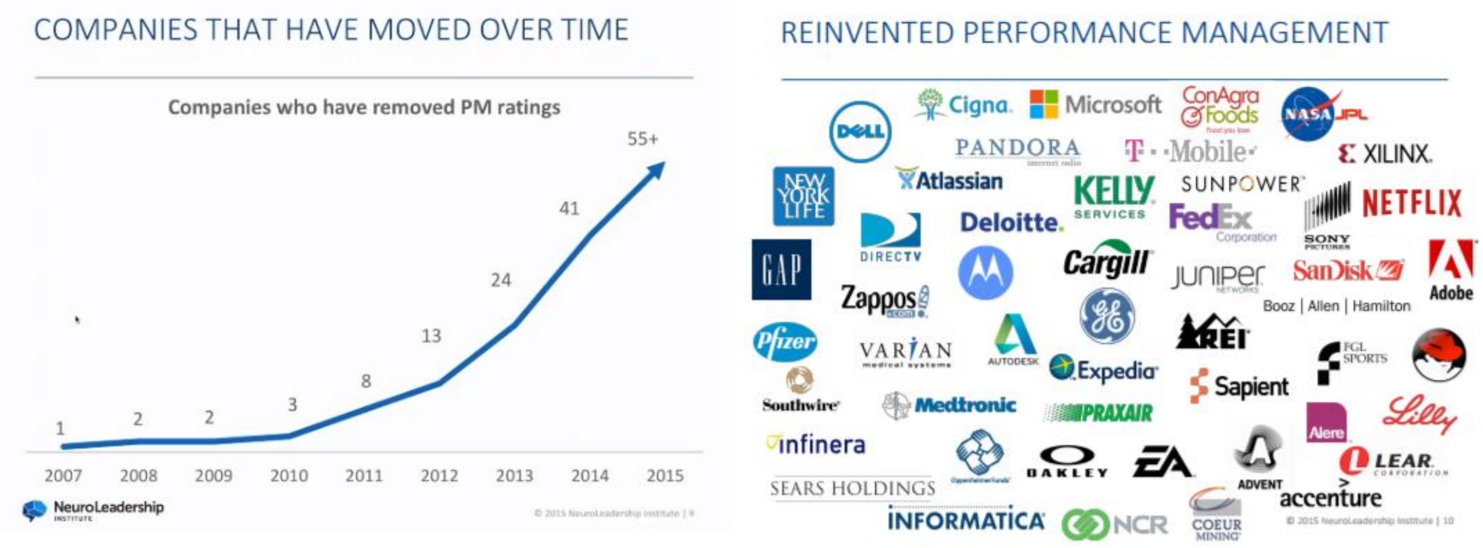
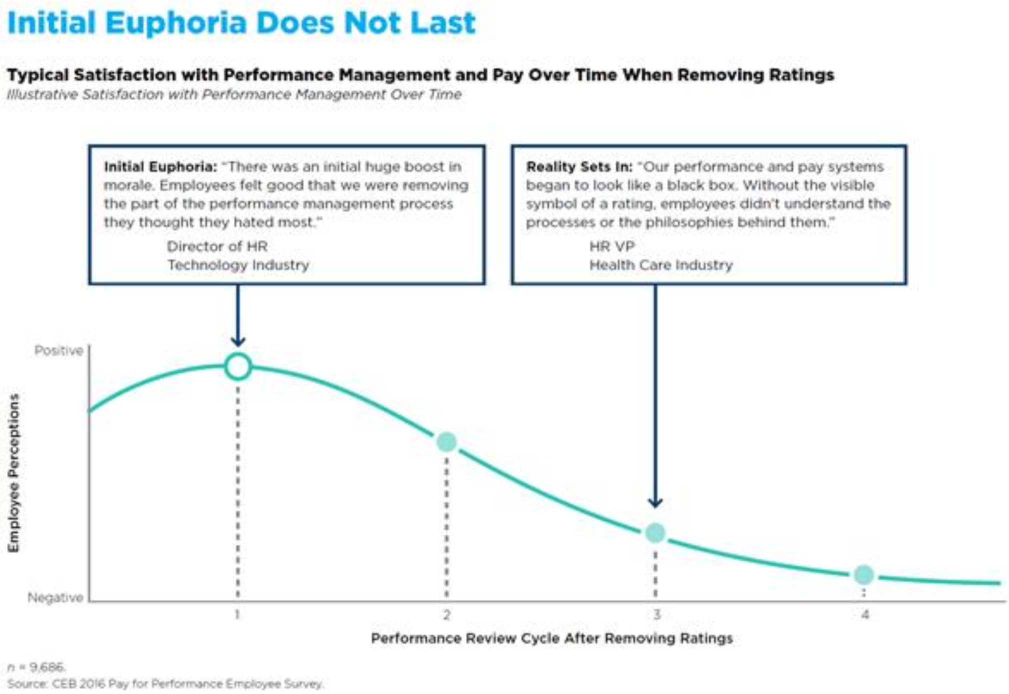
Appendix A - Companies that have Eliminating Ratings in 2015



Appendix B - Decline of Performance Management Satisfaction after Eliminating Ratings

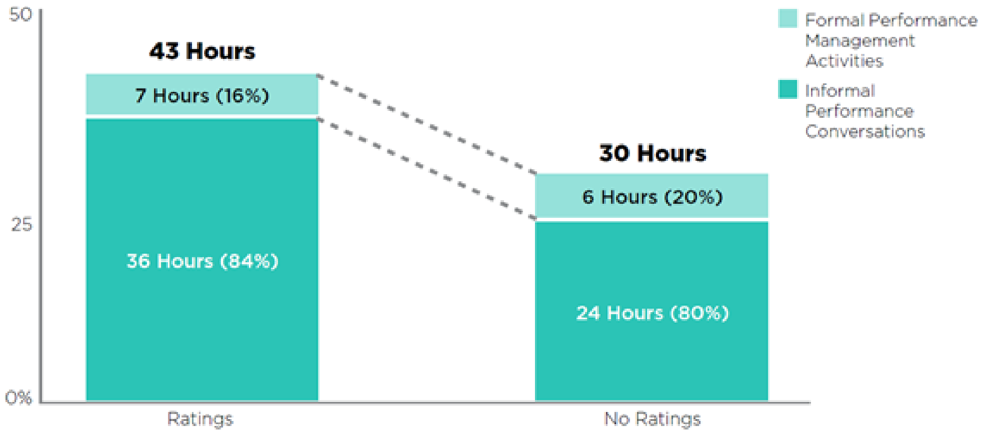


Appendix C - Decrease in Time Spent on Informal Conversations after Eliminating Ratings

Reality: Managers Spend Less Time on Informal Conversations Without Ratings

Manager Time Spent on Performance Management Activities[a]

Average Hours (and Proportional Time Spent) on Performance Management per Year, per Direct Report



n = 9,686.

Source: CEB 2016 Pay for Performance Employee Survey.

[a] Formal performance management activities include goal setting, performance evaluation and calibration, documenting employee performance, and preparing for performance conversations. To calculate time spent on informal conversations per year, manager conversation sessions were estimated to last one hour.

Note: The reduction in time spent on performance management activities is statistically significant $p < 0.001$.

The Bottom Line

In the absence of ratings, managers spend less time on performance management activities. But they do not shift that extra time toward ongoing, informal performance conversations.