Should managers be allowed to make pay decisions?
How one company transformed performance management by redefining the role of managers

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A common objective in redesigning performance management methods is to improve the quality of performance coaching dialogue between managers and employees. This objective is a reaction to traditional performance appraisal processes that focused heavily on evaluation with relatively little attention given to ongoing continuous performance management conversations. In fact, traditional review processes often made performance management something of a competition between employees and managers. Employees had one chance a year to convince managers they were exceeding expectations and deserved greater investment in the form of pay, promotions or development opportunities. On the other side, managers had to persuade employees to accept investment decision that often failed to meet their expectations.

The traditional once a-year annual process frequently creates tension by pitting managers and employees against each other. This tension makes it hard to foster collaborative performance coaching discussions. Employees do not feel managers are truly "on their side" so they are reluctant to engage in open dialogue about performance improvement. Managers shy away from proactively offering constructive feedback to employees for fear they interpret it as an attack on their value rather than a gift of support to help them succeed. It also does not help that many managers do not know how to give effective feedback.

Some companies have sought to reduce manager-employee tension by changing how managers evaluate employee performance. The performance of employees continues to be rated by managers, but manager ratings are collected in calibration sessions that occur outside of the employee performance review process. Removing ratings from employee performance reviews reduces tension associated with performance discussions. Although these methods may foster better employee-manager performance coaching conversations, they still do not fully address a fundamental source of tension that affects virtually all performance management redesigns: how to handle compensation and staffing decisions that require directly or indirectly rating employee performance.

Compensation and staffing decisions pose one of the main challenges to efforts to "remove ratings" from performance management. First, compensation and promotion decisions are a form of performance rating since they involve placing employees into categories based on their perceived value to the organization. If you pay some employees more than others then you are rating them. Having managers make compensation and staffing decisions about employees creates the same issues between managers and employees caused by other forms of performance ratings. Second, there are many reasons why it is bad to make compensation decisions without some link to well-defined performance ratings. Companies cannot make accurate and fair decisions about pay and promotions without some standardized way to assess performance contributions. Because compensation and staffing decisions are inextricably linked to performance ratings, it is not possible to have managers make these decisions without risking tension that can undermine effective employee-manager coaching discussions.

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The best example I have seen of a company directly addressing this dilemma occurred during a session entitled "Creating the conditions for continuous performance management" at the recent SuccessConnect conference. A company in the session discussed having a policy where managers do not make compensation and staffing decisions. Managers and employees at this company talk throughout the year about performance and career development. Once a year managers and employees collaborate to create a qualitative description of the employee's major accomplishments, capabilities and development goals. This description goes to a workforce management team consisting of senior operational leaders and HR business partners. This team integrates data about individual employees with broader data about the existing organization, external market trends, and future business strategies to decide how to invest compensation, staffing, and development resources. Managers provide extensive information to help this team make compensation and promotion decisions. Managers also explain how these decisions are made to their employees. However, managers do not make actual compensation or staffing decisions for their direct reports.

Two interesting things happen when managers are not responsible for making compensation and staffing decisions and instead cross-functional leadership teams make the decisions. First, the decisions reflect a more holistic view of the company. Managers inherently view compensation and staffing from a limited perspective heavily influenced and often constrained to the teams they manage and the business problems they are facing in their departments. Any decision made by a manager in isolation is necessarily going to be biased based on their point of view. Second, managers do not have to defend compensation and staffing decisions to their employees. They do have to explain the decisions so employees understand how the company allocates scarce resources like pay. However, they are able to remain on the same side as the employee in this conversation. In this sense, it is similar to the conversations managers and employees might have about obtaining budgets and funding for work projects. The manager and employee both want to get the resources they believe they need and deserve, and they work together to provide information to the company to justify their request. But neither the manager nor employee ultimately makes the decision. As a result, discussions about compensation and staffing decisions are less likely to devolve into tense arguments between employees and managers about allocation of company resources.

The company sharing this story talked about managers being "advocates" for their employees. Managers are expected to be coaches who encourage employee performance success and agents who argue in support of their employees' career goals. Managers can fully embrace this role because they do not have to make compensation and staffing decisions that require favoring one employee over another. Rather than asking managers to categorize employees based on their contributions, managers work with employees to present them in the best possible light to the company's executive teams. These teams are then responsible for categorizing and investing in employees based on their performance contributions.

The company stressed that this approach to management would not work for every organization. They noted that managers are surprised and in some cases frustrated when they join the company and discover they do not have ownership over compensation and staffing decisions. They also stressed that a strong level of leadership commitment and role modeling is required for this approach to work. Nevertheless, this strategy is an important factor underlying their success in creating a feedback rich, ongoing coaching environment among managers and employees. It is also a very innovative way of rethinking what the role of a manager is in most companies compared to what it perhaps should be.

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