

The 'Whys' and 'Hows' of Performance Appraisals

One expert recommends tying pay to company performance, avoiding automatic merit increases and "rating inflation."

By Wil Naylor, the Elite Group

It has been proven that the key to achieving maximum employee productivity and satisfaction is to provide employees with factual, candid, and objective feedback. One of the most effective methods for accomplishing this goal is through formalized performance appraisal processes. According to research by Watson Wyatt, effective performance management programs can increase a company's "shareholder" value by nearly 50 percent.

The benefits of a legally compliant—and effectively executed—employee appraisal process include:

- Enhanced employee motivation
- Identification and reward of top performers—so a firm can truly "pay for performance"
- Reduction in unwanted turnover
- The ability to better identify and document performance problems, thus supporting discipline and potential termination or reduction in force actions
- A possible defense against lawsuits
- Enhanced compensation and salary planning; and
- Increased ability to identify training needs and competency gaps, establish behavioral change goals, and to provide an opportunity to discuss with employees potential career options and establish agreed-upon milestones.

Still, for varied reasons, many companies have not established a formal appraisal process. The absence of such a program raises issues of employee dissatisfaction and leaves a company vulnerable to litigation and at a disadvantage in terms of defending their program in the event of an official complaint.

In fact, in the event the employer fails to show that its performance appraisal program was designed and administered on the basis of the Uniform Selection Guidelines established under the authority of the Title VII of the Civil Rights Act of 1964 as amended, the court may render the employer liable for back pay, court costs, specific management training programs for and/or promotion of the protected group employees as part of the case settlement.

In addition, there are both state and federal legislation regarding privacy issues that mandate that an effective privacy protection policy must provide employees access to records relating to their qualifications for promotion, pay raises, or to records relating to discipline and potential termination. The bottom line is that, regardless of size or industry, companies are well-served to establish and maintain an appraisal process.

Elements of Effective Performance Management

There are many elements that must be included in a legally-compliant and effective performance management and feedback program. These include, but are not limited to:

- Periodic interview with employees regarding their career progress;
- Recording of systematic measure of an employees' overall value to the organization;
- Documentation of information regarding of information concerning the strengths and weaknesses of all employees as they relate to career development; and
- Well-defined expectations that allow employees to establish goals that align with corporate goals.

And perhaps the most important benefit of a formalized process is the recognition that the appraisal process is a part of the corporate culture, supported and encouraged by management, communicated to all employees, and accepted by the company as a whole. When this happens, managers understand that their primary responsibility is to help develop the skills and talents of those who work for them and employees feel confident in the support of their managers.

Merit pay increases are the reward for reaching common goals and reward employees for performance through increases to base pay. Too often, however, salary increases are perceived by employees as an entitlement. Employees assume that if the company annually reviews their salary, and is in the financial position to award salary increases, they will receive an increase. This perception is, of course, entirely counter to the intent of a merit increase and an effective appraisal process.

It is important to note too that, as difficult as it may be to avoid, "rating inflation" can undermine an employee appraisal process. If a pay-for-performance system is truly working effectively, not every employee can receive an "exceptional" or "excellent" rating. This is not easy – especially for kind-hearted managers. But it's necessary and important.

Formal appraisal processes are not easy to implement or maintain. The benefits, however, in terms of employee performance are significant. And, when the appraisal processes are based on corporate goals and objectives, the benefits can be dramatic in terms of both individual and corporate performance.

Wil Naylor is co-owner and Executive Vice President of the Elite Group. Based in Exton, Pennsylvania, the Elite Group provides a coordinated approach to addressing the challenges of managing employee benefits, benefits administration, human resources, risk management and payroll services. For more information, call 610-423-4129 or visit www.elitegrp.com.