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Performance Appraisal and the Balanced Scorecard

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Elements of Performance Management

In 1982, organizations reported that 62% of their resources were in tangible assets. By 2002, those same organizations reported that 80% of their assets were intangible (Kaplan & Norton, 2001). This dramatic change is largely due to a new emphasis and understanding of human capital – the knowledge, experience, and skills employees bring to their employers. In his book The ROI of Human Capital, Jac Fitz-enz (2000) asserts, "it is the information that the person possesses and his or her ability and willingness to share it that establish value potential" (p.6). As leading firms have begun to discover and acknowledge this shift in their assets, managing their largest resource has meant switching from a focus on optimizing operational processes and financial activities to focusing on a human resources issue - maximizing returns through performance management.

The goal of performance management is to direct employee behavior toward the organization's strategic goals and to develop employee talent toward the achievement of future goals. Performance management, by definition, is an organized method for monitoring employee behaviors and the outcomes of those behaviors, collecting information about whether or not goals were reached, and using that collected information to make decisions about the behaviors' value in terms of organizational objectives (Kirchhoff, 2006). The contribution performance management makes to the achievement of organizational objectives makes it a strategic tool in organizational success (Weatherly, 2004). The

enormity of the human capital asset demands that organizations seeking to outperform their competitors ensure the organization's largest asset (its workforce) is aimed precisely in the direction the firm wishes to go. More precisely: competitive superiority is driven by performance management superiority. According to Fitz-enz (2000), "The key to sustaining a profitable company or a healthy economy is the productivity of the workforce, our human capital" (p.1).

Traditionally, performance management has brought to mind ideas of lengthy performance appraisal forms and annual employee reviews. In the typical scenario, an employee is given his job description at the beginning of employment and told he will be evaluated after a certain period of time, maybe after the first three months and then again at the end of the year. Then the manager and employee each put the job description away in the bottom of a drawer somewhere and push the conversation to the back of their minds until it is time for the annual employee performance review one year later. In some cases, even a yearly appraisal does not happen. According to the *2005 Compensation and Benefits Report*, 1/3 of the workforce surveyed rarely, if ever, received a formal employee performance evaluation. Another 1/3 was unsure about their organization's performance standards (Petrimoulx, 2007). In this situation, goals are rarely remembered, much less accomplished, and an entire year is spent before goals are reviewed and progress is documented.

Another problem with traditional performance appraisal systems lies in the goal-establishment process itself. Goals or "performance standards" are often subjective and vague, almost ensuring that the score given will demonstrate a manager's perceptions of or feelings toward the employee rather than be an actual measure of performance. It is not clear what specific behaviors or activities are expected to ensure goals are reached, and it is up to the employee alone to remember the goals and set an action plan for accomplishing them. Yet another problem arises when employees are asked to write a self-evaluation for managers to use as a guide during appraisal. Clearly, different writing abilities and even personalities skew this tool, as some star employees may downplay their performance in the name of humility while low performers with egos or strong writing skills can paint a false picture of outstanding performance (Petrimoulx, 2007). The score at the end of the year, therefore, reflects the employee's talent for selling himself as a great performer, instead of actual performance. Perhaps the greatest weakness of traditional performance appraisals, however, lies in the all too common practice of making the performance appraisal an annual event, with no regularly conducted performance checks or conversations across the year.

With a system structured around goals set at the beginning of the year, and appraisal only occurring at the end, a disconnect inevitably occurs between the behaviors an employee has engaged in and the review the employee is given. First, research has time and time again shown that in this situation "recency

bias" reigns, so that only the few months or even weeks preceding the formal review are reflected in the manager's appraisal. Second, if the employee does not achieve the established goals, it is often unclear what behaviors should have been avoided or alternatively engaged in to reach a different outcome. After all, it is very difficult for anyone to recall every task performed or process employed in a year's time. The most striking problem with traditional performance appraisal, however, is that instead of projecting forward to the future or even focusing on the present, traditional appraisals are anchored in the past. By the time the manager and employee realize goals have not been met, the entire year is over (Petrimoulx, 2007). It is then time to set new goals and start the entire process over again. If the employee is told at the end of the year that his performance has been unsatisfactory, it stands to reason that the employee has been performing unsatisfactorily for an entire year. True action plans cannot be created since no one can be sure what went wrong at this point. No strategic employee development can occur since specific needs cannot be identified. The year has been wasted.

In summary, traditional performance appraisal, particularly when poorly administered by management, often results in the setting of unclear goals with subjective rating scales which in no way support the organization's strategy, and does not identify problems in performance until the review period is over and time has been wasted.

In order to fulfill its role as a strategic tool in an organization, performance management must take on a more aggressive face. The process must begin with clearly-defined goals and objectives, identification of behaviors which will support those objectives, and the design of a system for monitoring the achievement of each. In her essay "Performance Management: Getting It Right From The Start," Leslie Weatherly (2004), SPHR lists the following critical success factors of an effective performance management system:

- "Mirror your corporate culture and values" (p.4) – the objectives defined and the process used should align with the organization's beliefs, not only about what it is trying to achieve, but also about what it values in its processes and its employees' behaviors.
- "Focus on the right company performance measures" (p.4) – ensure that the things measured are the things that matter. Weatherly suggests sticking to a "vital few" metrics that, when combined, show a picture of the organization's most important objectives.
- "Link job descriptions to the performance management system" (p.4) – Employees must be able to see how their individual behavior, the skills they possess, and the job they are expected to do will contribute to the organizational objectives they will be responsible for.
- "Set clear expectations for employee development" (p.4) – define what future goals are likely to be and clearly establish what talent

development employees will need to engage in to be prepared to meet those objectives.

- "Track effectiveness of the performance management system" (p.4) – at any point, Weatherly suggests, an organization should be able to clearly identify the alignment between employee and organizational goals and also calculate the likelihood that performance objectives will be reached.

Following these criteria will help ensure the organization's performance management system effectively drives employee performance toward the achievement of organizational objectives. The first step, however, is to ensure that the behaviors necessary to achieve those objectives are clearly identified. The technique of defining goals for each employee and then monitoring performance toward achievement of those goals is nothing new in the management realm.

Management by objectives (MBO) is not a new management technique but, when seen in the light of a comprehensive performance management system, it certainly takes on new relevance. According to Weatherly's 2006 article "Management by Objectives," the technique is defined as, "the joint setting of performance objectives between a manager and his or her employees" (p.1). As part of the MBO process, managers and employees determine the methods through which these objectives will be achieved and also set timelines for achieving those objectives.

MBO operates on the basis of four key assumptions. The first is that employee buy-in, and then performance, will be greater if the employee is involved in the goal-setting process and is consulted about how goals should be achieved. Second, MBO assumes that if employees have a clear understanding of what goals they are expected to achieve, performance will improve. Third, the goals and objectives chosen should be "measurable and should define specific results, performance outcomes, or deliverables" (p.2). Finally, subjective language should be avoided (Weatherly, 2006a). The way outcomes are measured should be as objective as the metrics that are chosen.

Operating under these four assumptions, MBO first strives to ensure that employees make the goals their own. This escalation of commitment will result in improved performance, since the accomplishment of the goals is something employees see themselves as having promised to do in partnership with their manager, instead of as a demand handed down by their employer. Making the goals explicit allows the employee to fully understand exactly what is expected, and prevents the frustrating situation in which an employee has worked hard to achieve a goal other than the one management had in mind.

Though MBO has been a management practice for some time, most organizations initially approached it from a direction that undermined its core purposes. The traditional MBO process used a top-down approach, meaning that only executives and top managers were included in the process. The popular reasoning was that these were the only employees truly responsible for

organizational success and were also the only ones with enough control to substantially affect it. When this technique failed to improve organizational performance, management theory switched to a bottom-up approach, allowing front-line employees to set goals and using different performance management programs for executives and top-managers. The result of this practice was that the two sets of goals were often established in a vacuum. The top sought no input from the bottom and the bottom received no guidance from the top. Without input from the rank and file employees, executives failed to take into account information about the day-to-day operations which affected organizational strategy. This failure resulted in key decision-making about the organization occurring without critical input from the people who saw the problems up close. The bottom-up approach meant that no executive and top-manager input was provided, so individual employee goals were not aligned with the organization's goals and there was no overall vision. Employees would accomplish their goals, just as MBO theory predicted, but that success was not necessarily linked to the success of the organization. The firm's largest asset was performing work that was not contributing to the firm's strategy (Weatherly, 2006a). To change this outcome, organizations need to create an approach that marries the best of the two systems.

When traditional MBO techniques are paired with a set of performance management best practices, an effective performance management system that links employee performance to organizational success emerges. By altering goal-

setting to include management and employees, linking objectives to organizational strategy, employing the use of continuous feedback, and linking performance to rewards, organizations can turn traditional management theory into a powerhouse for organizational success.

The first of these three key elements, goal setting, involves effectively merging individual and organizational needs. “Human behavior is fundamentally goal directed. Goals direct attention, increase persistence, and motivate development of strategies or plans to attain those goals” (Findley & Amsler, 2003) (p.2). Common sense dictates that before an individual sets out to accomplish something, he must first decide what it is he will try to accomplish. Well defined goals establish what it is a person or organization is striving to do, and provide measurement of whether or not it has been accomplished when the effort is over. In order to significantly contribute to the accomplishment of an organization’s strategic objectives, however, employee performance goals must be designed one step further. The goals must be clearly tied to the organization’s strategy. The first step to accomplishing this alignment is to share the strategy with employees. Communicating to employees that their individual behavior should be directed toward organizational goals allows them to be part of the vision. Giving people a vision, a “higher goal,” has been shown to dramatically increase performance (Fitz-enz, 2000). The idea that a firm’s vision only belongs to its executives and top managers undermines a belief in leveraging the power of human capital. If a firm believes its employees possess valuable knowledge,

skills, and experiences but fails to leverage that capital toward organizational objectives, the firm is scattering its largest resource – brain power – in every direction but the one it wishes to go. In order to accomplish an objective, individuals must first know what it is. The workforce is no different. In order to have employees who contribute to the organization's strategic objectives, the firm must first make them strategic partners by sharing the vision and the plan for making it happen.

An important element to take into account is that while employee goals should align with organizational objectives, the expected outcomes should remain within the employee's span of influence and control. The employee goals should support both the organization and the development of the employee. If the firm's strategic goals are, as they should be, its core objectives, every employee should in some way be able to contribute to that goal. For example, holding a department manager responsible for the overall financial success of the company will only lead to frustration. There is no way for the manager to control this outcome with his own behavior. In fact, he could lead his department to great financial success and still be punished for the financial downfall caused by other managers in other departments. It is reasonable, however, to hold the manager responsible for financial success in his own department. If each manager is held to that standard, the overall organizational goal of financial success will be supported and each manager will be judged on something he has direct control over. In some instances, identifying a metric to

measure an individual employee's contribution to a specific organizational objective can be difficult, but it can be done if the firm has truly identified its core objectives and believes that every position in the organization contributes to them, or should, in some way. Goal-setting should also be coupled with action plans or the identification of specific activities that will support the employee's achievement of his goals. While traditional performance reviews seek only to assess performance and identify areas for improvement, true performance management systems give employees a "how" and a "why" for the "what." Allowing employees to partner in creating their individual goals will increase employee buy-in and commitment to the goal, which will affect not only the effort the employee puts forth but also the perceived validity of the performance appraisal (Weatherly 2006a).

The use of continuous feedback, the second key element of success, to support the achievement of goals ensures the performance management system will focus on the present and the future instead of the past, and will also prevent poor performance going unaddressed for a year or longer. James Laumeyer (1997), SPHR, MBA suggests formal performance discussions occur two to four times a year. This, he claims, relieves the formal appraisal from having to discuss the past, since past performance was praised or redirected at the time it occurred. The performance appraisal can then focus on the patterns of performance that developed over the course of the year and opportunities for employee development can be clearly identified. Furthermore, Laumeyer

suggests that the overall tone of the performance appraisal focus on the future and the present instead of what happened during the year. Questions like "what have you done this year?" should be replaced with "what can be done better next year?" Employees can be asked to identify gaps in their skill set or room for development by looking at the notes from the multiple performance discussions that took place over the course of the year.

Another benefit of a continuous feedback system is that goals or strategies, which should be living things within an organization, can be modified as soon as necessary and employee behavior can quickly be redirected toward the new goal. If an organization decides to emphasize a new part of the business, managers can feed that new information to employees and have action plans designed within the course of a few months instead of only annually. This technique decreases time wasted focusing on the wrong objectives or striving toward the wrong goals (Laumeyer, 1997).

The first two success factors feed the third, linking performance to reward. If the performance management process is fair and objective, goals are clearly communicated and performance is appropriately monitored throughout the year, implementing a pay-for-performance plan can be the icing on the cake to motivating employees to achieve their goals. While this is true, it should be noted that several problems plague traditional pay-for-performance plans. In her article "The Problems with Pay-for-Performance Plans (and What to Do

About Them)" Suzanne Petrimoulx (2007), PHR, examines the elements that are often problematic.

One major flaw with many pay-for performance plans is the use of a forced distribution method to determine employee pay increases. The idea is to plot employee performance on a bell-shaped curve with only a certain percentage (say 10% each) falling at the low and high ends and the rest (80%) falling in the center as "average" performers. The problem is that a manager with 20 employees, all of whom are outstanding performers, must come up with some way to call two of them "below average." Outstanding performers can end up punished and frustrated, which will eventually cause a drop-off in motivation, commitment, and effort. The opposite scenario can also occur. Departments with no outstanding performers will be forced to call some of them outstanding anyway, so unsatisfactory performance is rewarded and therefore reinforced simply to satisfy the bell curve. This technique is often employed in the name of cost containment, but its effect can drive the organization to loss. By rewarding poor performance and ignoring great performance, organizations blur the link between performance and reward. This confusion will destroy motivation and undermine the objective to link employee performance to strategic goals. Furthermore, the technique pits employees against each other. Instead of seeking to fulfill their performance goals and drive organizational success, employees can become more concerned with outperforming each other.

The end result can be a lack of employee buy-in and the destruction of teamwork (Weatherly, 2006b).

Another common flaw with pay-for-performance programs is that organizations fail to significantly distinguish rewards for unsatisfactory, satisfactory, and outstanding performance. Often the difference between any two levels of performance is a mere .5% merit increase, not enough to really reward outstanding performers and make their extra effort worthwhile. Furthermore, the budget for merit increases is usually small, with a maximum increase of between 3 percent and 4 percent. Dividing the pie, then, can become more like cutting slivers. "Faced with a 4% merit trend, the ability to motivate through the system becomes a futile effort. The pie has become a tartlet…" ("Linking," 1994) (p.1). Employees are unlikely to change their behavior in the hopes of gaining an extra percent of increase, so the money is wasted and employee performance is unaffected (Petrimoulx, 2007).

It is the purpose of this paper to present a performance matrix model that remedies many of the problems associated with prevailing performance management systems. The following chapters will demonstrate that a properly constructed and managed performance matrix can achieve realistic goals tied to both individual and organizational goal attainment, encourage and support ongoing monitoring of progress through exact measurement, and produce true pay-for-performance compensation.

The Balanced Scorecard:
Tying Performance to the Strategy

In the early 1990's Drs. Robert Kaplan and David Norton developed a comprehensive management system that combines financial measurements with other metrics to produce a performance measurement system that provides a snapshot of the business (Kaplan and Norton, 1993). While the structure and process of the Balanced Scorecard matrix is simple, the tool is a sophisticated method that successfully links employee performance to organizational strategy and serves as a highly effective performance management system, doing exactly what performance management should do: direct employee behavior toward organizational objectives.

The idea to align individual goals and organizational objectives is not a new one. In his seminal work titled, The Human Side of Enterprise, Douglas McGregor (1960) outlined the details of his so-called "Theory Y," which encourages the creation of situations where employees can best achieve their own goals by achieving the goals of their employing organization. According to McGregor, there are four appropriate steps to implementing this strategy. The first is to clarify the requirements of the job. Second, goals or targets must be established and defined for a specific time frame. Next, organizations must engage in management processes during the specified time period. Finally, results of the initiative must be evaluated. McGregor's Theory Y recognizes

individual and organization needs and seeks to align them so that each is accomplished by way of the other. Human nature dictates that a person will first be concerned about accomplishing his own goals before focusing on another's goals, therefore the best way to ensure employees are motivated toward organizational objectives is to make those objectives important to the employee personally (McGregor, 1960). The Balanced Scorecard uses a goal-cascading technique to accomplish this objective. By tying each individual's scorecard to his manager's scorecard, and then each manager's scorecard to a division-head's scorecard and so on, organization goals are filtered down through all levels of the organization. Organizational goals then become supported by individual activities and employee motivation and buy-in are dramatically increased (Kaplan and Norton, 1992). Another differentiating factor between the Balanced Scorecard and traditional performance matrices is the collection of metrics it utilizes.

The Balanced Scorecard differs from early performance matrices in that it does not rely exclusively on financial metrics for its makeup. Kaplan and Norton define financial measures as "lag indicators," meaning that they only report the outcomes of past activities and therefore cannot be relied on to predict future success. The authors assert that exclusive reliance on financial performance measures is short-sighted and will not prepare the organization to meet the challenges of the future. Furthermore, Kaplan and Norton recognize that intangible assets like knowledge, experience, creativity, and technology do not

always have a direct impact on the financial outcomes of the organization, especially where revenue and profit are concerned. For example, customer service and overall quality can be improved through increased investment in employee training programs. This higher service quality will lead to increased customer satisfaction and loyalty, which in turn generates increased revenues. Measuring revenue, however, will not reveal that the cause of success was the employee training. The Balanced Scorecard clarifies the link through the combined use of indicators that measure success from different angles. While financial measures are employed by the Balanced Scorecard, they are combined with "lead indicators" which drive performance and can predict future success. Specifically, the tool is built around four perspectives: Financial, Customer, Internal Business Processes, and Learning and Growth. When these perspectives are combined using relevant and strategy-linked metrics, both a picture of individual performance and a predictor of future business success emerges (Kaplan and Norton, 1992).

The Financial Perspective is important to every organization. Whether striving to increase shareholder wealth or, in the case of a non-profit organization, supporting future development goals, every company needs money to survive. Monitoring financial indicators allows an organization to ensure it remains on track with its financial targets. The Customer Perspective measures the organization's contribution toward its strategy to differentiate and create value for the customer. This perspective is the customer's own. The

metrics associated with this pillar are not based on activities, but rather on outcomes – things the customers themselves have experienced. The third perspective, Internal Business Processes, speaks to the organization's progress toward the achievement of its specific operational objectives. The metrics associated with this perspective focus on the inner workings of the business in terms of quality, efficiency, excellence, or some other organizational initiative. Finally, the Learning and Growth perspective seeks to ensure that the organization is facilitating change and growth that will allow it to remain innovative and prepared for future challenges. Though each of the four perspectives is focused on measuring something specific and unique, there is an overarching theme found among them. Each of the perspectives, through the metrics it employs, is directly tied to the organization's strategy. It is this characteristic that makes the Balanced Scorecard such a powerful and effective performance management system (Kaplan and Norton, 2001).

A 1998 study by Ernst and Young reported that "the ability to execute strategy was more important than the quality of the strategy itself" (Kaplan and Norton, 2001). This stands in stark contrast to what most business students spend a great deal of their time doing – studying how to create great strategies. Similarly, many organizations focus on developing business plans that will lead to success, finding the best ways to compete, and conducting market research to determine the best plan of attack. While these things are certainly important, the heart of the matter is that any strategy no matter how great must be

implemented in order to produce results (Chapman, 2005). What is also striking is that the makeup of the strategies being developed is changing. In the past, the focus has been on the management of tangible assets – supply chains, inventory systems, and tightly monitored budgets. Increasingly, companies are focusing on the intangible – customer relations, innovation and creativity, and employee skill. While the strategies have changed, the methods employed to measure the strategies have not evolved. Companies, though now focusing on the intangible, are still measuring the tangible, and only the tangible. Strategies are designed and, in successful cases, implemented, but something entirely different is measured. The Balanced Scorecard, through the use of the four different perspectives, seeks to realign the measurement process with the strategy so that the resulting tool presents both a picture of the level of employee performance and the organization's movement toward the achievement of its strategic goals (Kaplan and Norton, 2001).

The Balanced Scorecard is designed to be a measure of both the quality of the organization's strategy and the implementation of the strategy. Without implementation of the strategy, there would be nothing to measure. By measuring the strategy and the outcomes of the associated activities, an organization can see how well the strategy is working. For this reason, all of the metrics included on the Balanced Scorecard should be objective measures of the strategy itself. If what you measure is what you get, as popular management opinion often states, then what a Balanced Scorecard company gets is exactly

what it wants – the activities and outcomes that drive its strategy. Kaplan and Norton assert that a focus on organizational strategy is the key to success and growth (Kaplan and Norton, 2001). In their book The Strategy Focused Organization, the authors outline key principles of such a strategy-focused firm.

The first principle of a strategy-focused organization is to "translate the strategy to operational terms" (p.9). Organizations seeking to align their activities with their strategies must first decide which activities, processes, and goals will drive the strategy. Once the drivers of the strategy have been defined, they can be filled into the matrix and measured, ensuring the company stays on track and continues performing in the direction necessary to accomplish strategic objectives. The authors liken the process to the development of a recipe – simply decide which ingredients are necessary to get the final product you want, then measure each to ensure perfection. There is no one correct framework for measuring a strategy. The frameworks used by various companies will differ as much as the strategies themselves (Kaplan and Norton, 2001).

The second principle of a strategy-focused organization is to "align the organization to the strategy" (p.11). This is perhaps the most critical and most complex part of designing an effective Balanced Scorecard. Each department or unit cannot be exclusively concerned with its own strategy or well-being, but each section must support all others in achieving joint goals. "For organizational performance to become more than the sum of its parts, individual strategies must be linked and integrated" (Kaplan and Norton, 2001) (p.11). This characteristic is

about creating synergy, identifying how each part of the business contributes to the strategy and how they can work together, each contributing in unique ways, to achieve the overall organizational objectives. Alignment of the organization and the strategy is done through the metrics the Balanced Scorecard is built on. Once the strategy has been translated into operational terms, activities that support those goals should be identified and measured.

The Balanced Scorecard derives a great deal of its power by leveraging the third principle of a strategy-focused organization, "making strategy everyone's everyday job" (Kaplan and Norton, 2001) (p.12). In order for this to be possible, every employee in every level of an organization must first have a clear understanding of the strategy. Research cited by Kaplan and Norton (2001) estimates that only five percent of the typical workforce has a clear understanding of their organization's strategy. Some firms are nervous about this step since it dictates sharing the organization's key plan for success, and the way it plans to compete, with a large group of people. If people do not know what the goals are, however, they cannot hope to achieve them! According to Mobil's Brian Baker, the risk is worth the reward, "Knowing our strategy will do [our competitors] little good unless they can execute it. On the other hand, we have no chance of executing our strategy unless our people know it. It's a chance we'll have to take" (Kaplan and Norton, 2001) (p.12). The fourth principle, "make the strategy a continual process" takes the whole process one step further

by ensuring performance monitoring, measurement, and management become part of the business culture and day-to-day practice.

The Balanced Scorecard is not designed to be a year-end performance review. It is designed to be a continuous feedback system that can be used to monitor constant progress toward the achievement of goals, identify problems and solutions early-on, and ensure the activities employees are engaging in are driving the organization in the direction it wishes to go. Strategy-focused organizations make conversations about strategy a frequent occurrence. Progress toward objectives is reviewed quarterly or even monthly to ensure timelines are being met and goals will be reached. This characteristic is what makes the process, and performance management as a whole, a strategic tool for an organization's success. Finally, the strategy-focused organization seeks to "mobilize change through executive leadership"(Kaplan and Norton, 2001) (p.15).

"Experience has repeatedly shown that the single most important condition for success is the ownership and active involvement of the executive team" (Kaplan and Norton, 2001) (p.15). Without buy-in at the top, there is no hope of buy-in from employees. Furthermore, executives define the strategy and are responsible for communicating it down through the organization. If executives are not passionate about the implementation of the strategy and are not full believers in the drivers of breakthrough performance, the Balanced Scorecard will fail to motivate employee performance toward the achievement of

organizational objectives (Kaplan and Norton, 2001). The overarching vision and the motivation to realize it comes from top executives. Strong leaders will ensure successful implementation and therefore great performance by getting their employees on-board with the process.

Once an organization has made the decision to switch to a strategy-focused organizational model, leaders must flesh out the specifics of their tailored Balanced Scorecard. Kaplan and Norton outline several success factors for the identification of appropriate metrics and explain how to ensure the Balanced Scorecard is, as the name indicates, balanced.

First, an effective Balanced Scorecard employs both lag and lead indicators to ensure the strategy is measured from all relevant angles. The difference between lagging and leading indicators is fairly straightforward. A lagging indicator is a measure of the result of an event or organizational initiative. For example, sales is a lagging indicator since it simply measures the outcome of efforts undertaken thus far. Knowing the sales figures for this month does not in itself predict anything about the organization's success and cannot indicate what was done correctly or incorrectly or make suggestions about how to improve. Leading indicators, on the other hand, have been shown to be correlated with organizational success. Measuring and monitoring these can tell an organization what needs to be changed or what actions should be encouraged further to achieve objectives. In her article "Maximizing Human Capital: Demonstrating HR Value with Key Performance Indicators," Nancy Lockwood,

SPHR, GPHR, suggests that employee turnover can be used as a leading indicator in industries where it has been found to affect customer service scores. When causation can be established and correlation can be measured, leading indicators develop which can predict future outcomes for the business (Lockwood, 2006). Management can use these measures to quickly identify where things have gone wrong and adjust processes before the problem takes hold.

Another important point to consider when designing a Balanced Scorecard is that the measures used should be clearly defined and employees throughout the organization must understand how the measures are calculated and what the source of the data will be. If employees do not have clearly defined goals and if they do not understand where the measures come from, their behavior and decision-making processes will fail to be affected. No one can attain a goal if he does not know what it is. Furthermore, no one can determine how to achieve a goal if he does not first understand how he will know whether or not he has met it. Though this idea of clearly defined goals seems fairly obvious, many organizations fail in this regard. Goals must be clear and concise, and only those that can be objectively measured should be used (Kaplan and Norton, 2001).

Though the Balanced Scorecard strives to provide a comprehensive view of the business and the organization's progress toward its strategic goals, the tool should be kept simple. While there should be at least one metric for each of the

four distinct perspectives, Kaplan and Norton suggest that in total no more than 15 indicators should be used. The idea is to keep the tool simple and prevent it from becoming overwhelming and burdensome. In short, the simpler the matrix is, the clearer the message will be. By identifying measures of strategy, the organization communicates to its employees what it values and what is important to success. Cluttering the matrix with a myriad of indicators and metrics results in a loss of focus. Employee efforts will be scattered and the core strategy will be lost (Kaplan and Norton, 2001). Placing constraints on the number of metrics used forces top leadership to determine and communicate what is important. This in turn clearly communicates the strategy and allows employees to become strategic partners in success.

When researching the extent of the alignment between personal and organizational goals, Kaplan and Norton discovered a startling fact. Only 51 percent of senior executives in United States businesses said their personal goals were linked to the strategy. The numbers got even smaller from there, with only 21 percent alignment with middle managers and a mere 7 percent for front-line employees. Without a link between organizational goals and individual goals, an organization's efforts are scattered in all directions. Kaplan and Norton suggest that total alignment can be achieved by ensuring that each employee's individual scorecard supports the manager's or supervisor's scorecard. In this way, objectives and the accountability for the achievement of those objectives are cascaded down through the organization. The result of this technique is that

every measure in an individual's scorecard contributes in some way to the organization's strategy so that employees can clearly see how their individual behavior affects the organization's progress toward attainment of its strategic goals (Kaplan and Norton, 2001). Again, this is the core purpose of performance management – to direct employee behavior toward the organization's strategic goals and to develop employee talent toward the achievement of future goals. The first part of this objective is accomplished through alignment. The second part is accomplished through the Balanced Scorecard's fourth perspective: Learning and Growth.

The Balanced Scorecard technique requires that every supervisor's scorecard have "an objective and measure related to coaching, counseling, or employee development" (Kaplan and Norton, 2001) (p.246). Each individual, along with their manager, should create a personal development plan that will ensure they continue to be prepared to meet not only the organization's current objectives, but the challenges it will face in the future. If properly designed, the tool's leading indicators can be a source of information for this action plan, since it will show the parts of the business the organization will need to strengthen or further develop in order to produce the outcomes it desires. Since the manager's matrix contains the measure for this personal development, it becomes the manager's responsibility to ensure that employees are enabled to get the training and development they need in order to maintain the company's human capital competitive advantage (Kaplan and Norton, 2001).

The final building block in the design of an effective Balanced Scorecard is the communication built into the process. According to the 2006 Employee Engagement Report which presents research conducted by BlessingWhite, a global leadership development and performance management consulting firm, communication is the key to getting employees on-board with the process. Leaders must constantly communicate the strategy, why it is important, and how employees can contribute to it. The first step is to define the "what" – the desired behaviors. The second step is to provide the "why." Educating employees on why their efforts matter and how they contribute to the organization's success increases motivation and commitment to their organization's goals. Employees must feel they themselves have a personal stake in the achievement of the goals they are assigned.

Some questions remain. Does the Balanced Scorecard successfully overcome the faults of traditional performance management? If a firm implements the Balanced Scorecard method, what outcomes can it expect? Finally, how can an organization ensure that employees will feel the personal stake necessary to motivate them toward the desired behaviors? These questions and others will be explored as we examine the success of the Balanced Scorecard in organizations employing it in conjunction with a pay-for-performance plan.

The Balanced Scorecard: Implementation and Results

Certainly the Balanced Scorecard is a sophisticated and well-designed tool for measuring organizational strategy, but do its distinctions from traditional performance appraisals and its complexities make it worth the extra effort to create and implement it? How is it to be properly implemented? What are the secrets to success, and what results have companies experienced when using the Balanced Scorecard? In this chapter, we will examine how the Balanced Scorecard can be properly implemented to become a state-of-the-art performance management system, what specific ingredients are necessary to make it effective, and what results have been enjoyed by organizations that have already incorporated the Balanced Scorecard into their management practices.

The shortcomings of traditional performance appraisal are not a mystery. Most systems are comprised of annual reviews that utilize subjective measures and self-appraisals to paint an only somewhat accurate picture of employee performance. Furthermore, most appraisals involve very little feedback with managers and employees only talking about goals and expectations during the formal review which occurs once the year is over. Finally, the review focuses on the past and on what did or did not happen instead of what should happen in the future and ways to improve (Weatherly, 2004). The framework of the Balanced Scorecard allows it to overcome all of the problems associated with

traditional performance review and therefore become a valuable tool in organizational success.

First, the Balanced Scorecard is not designed to be and should not be used as an annual performance review. The scorecard should be tied to a dashboard that constantly measures progress toward goals. According to Valerie Pike, MBA and SHRM content expert, “best practices” dictate that employees and managers should be able to view balanced scorecard or dashboard data quarterly, if not more often. Enabling employees to view the data quickly and regularly keeps them focused and encouraged. Furthermore, allowing managers to view other managers’ scorecards can help everyone excel. Managers who are failing in a certain area can look around to see which of their colleagues are performing well, then seek advice from their peers. In this way, the Balanced Scorecard becomes not only a steady source of goal identification and monitoring for employees, but also helps to unite the human capital of a firm together (Pike, 2002).

In his article “Performance Management Systems: What Do We Want To Accomplish,” James Laumeyer (2002), MBA, SPHR suggests that the proper focus of a performance review should be the present and the future, not the past. Kaplan and Norton overcome this obstacle by designing the Balanced Scorecard to combine different types of metrics to form a comprehensive picture that looks backward but projects forward. Lagging indicators make the Balanced Scorecard aware and mindful of the past, but leading indicators make it focused on the

future. When appropriate metrics are used, the scorecard helps employees take over their own future success by telling them what needs to be improved to meet their organization's goals. By utilizing a set of best practices when designing and implementing a Balanced Scorecard, organizations can ensure success is maximized.

Another great way the Balanced Scorecard outperforms traditional performance appraisal methods is in the level of employee buy-in it creates. According to research conducted by Brown and Latham in 2000, employee commitment and performance is greater when employees participate in the goal setting and planning processes. Specifically, the research found that both job performance and job satisfaction increased significantly when employees were asked to participate in setting high goals for measurement through their annual appraisals (Brown and Latham, 2000). When designing and implementing a scorecard, organizations should ensure that employees are highly involved, not only in the design of the overall system, but also in the data collection and selection of metrics for their individual scorecards. Allowing employees some control over the metrics they will be evaluated against increases their commitment toward those goals and establishes a feeling of personal ownership (Weatherly, 2006).

In her 2002 article, "Balanced Scorecard Basics on Implementation," Pike presents a list of implementation best practices. First, Pike suggests organizations establish ahead of time what they wish to achieve. Is the project

designed for pay and promotion or is it a change project? According to Kaplan and Norton (2001) it should be both. Attaching a pay for performance plan to the Balanced Scorecard adds complication, as we will discuss, but the authors assert the tool was designed for this purpose as well as an overall organization focus-changing and response-enhancing system. In other words, the Balanced Scorecard is intended to provide a picture of employee performance as well as a tool for organizations to identify needed changes in strategy or action and implement those changes organization-wide very quickly. When beginning to design a scorecard program, senior management must establish an objective. A scorecard designed solely to document employee performance and justify pay changes is very different from a program designed to lead the organization through its strategy (Kaplan and Norton, 1996).

Organizations should also ensure that goals are in place before the scorecard is implemented. Pike suggests organizations implement a pilot scorecard first to ensure the tool functions as intended. These steps ensure that employees have a clear understanding of the process as well as the metrics they will be evaluated on, the method for collecting the data, and how final results will be calculated before the process actually begins. If employees feel thrown into the process before they are comfortable with it, the project will suffer a lack of commitment and buy-in and employees may become discouraged (Pike, 2002).

It is also essential that management actively support the Balanced Scorecard project. The leadership of the organization is responsible for

motivating employees and establishing enthusiasm. Without clear support from the top, employees will not believe in the significance of the project and it will fail to direct their behavior toward established goals. According to Kaplan and Norton (2001), "the process to initiate the Balanced Scorecard management system starts with a leader creating the sense of urgency for change"(p.333). Furthermore, Pike suggests organizations identify a top-level non-financial project sponsor to further establish that the initiative is organization-wide and not simply a financial interest tool (Pike, 2002).

Best practices also indicate what organizations should not do when implementing a Balanced Scorecard project. First, organizations should not use the scorecard project to establish top-down control. As we discussed in the first chapter, traditional management by objectives was implemented this way and failed as a result. In order to be an effective motivator and to establish the necessary level of employee commitment, the project needs to be presented and perceived as a team initiative with sponsors identified from all levels of the organization (Pike, 2002). The Balanced Scorecard is designed to facilitate top-down communication, with executives identifying the firm's strategy and the processes for accomplishing strategic goals, but is not intended to be a facilitator of top-down control (Kaplan and Norton, 2001).

Another pitfall for organizations to avoid is standardizing the project with pre-made scorecards. Because each position contributes to the organization's strategy differently, scorecards should be tailored to fit each individual (Pike,

2002). Because incorporating this level of detail into the scorecard project is time-consuming, organizations should understand that designing and implementing a Balanced Scorecard is not an overnight process. Ideally, organizations should plan to spend six to eight months in the design phase of the project (Kaplan and Norton, 2001). Furthermore, organizations must not underestimate the extra administrative workload and costs associated with designing, implementing, and then continuously monitoring a Balanced Scorecard (Pike, 2002). Data must be collected and interpreted, dashboards or other monitoring systems must be created, and taskforces must be assembled and charged with identification of proper metrics for individual scorecards. Developing a scorecard program is a large commitment and should not be undertaken without a clear understanding of the work and resources required (Kaplan and Norton, 2001).

Perhaps the most valuable component of an effective Balanced Scorecard program is the establishment of a pay for performance component that links variable pay for employees to organizational success in strategy implementation. When tied to compensation, the scorecard becomes more than an organization's initiative. It becomes an individual responsibility in which employees have a personal and vested interest.

In his SHRM White Paper titled "Variable Pay: How to Manage it Effectively," Robert J. Greene (2003), PhD, SPHR asserts, "the motivational potential of variable pay is stronger than that of other forms of compensation." Research concerning variable pay programs has time and time again confirmed

that, when properly structured, it can be an effective motivator. Furthermore, Greene asserts, there are significant business reasons for implementing a variable pay plan. First, variable pay awards do not compound over time; instead, employees must earn the money again each year. The use of a variable pay program helps an organization keeps costs under control while also allowing it to focus money where money is due, instead of handing out merit increases year after year regardless of whether or not the reward is continuously warranted (Greene, 2003). Furthermore, utilizing individual incentives can also help organizations increase productivity. In a 2000 study conducted by Rynes and Gerhart, introduction of such incentives increased productivity an average of 30%.

The use of a variable pay plan can also help foster teamwork and team development. Greene (2003) states, "to the extent that people are provided with a 'shared destiny'…there can be a strong motivation to support each other and to work cooperatively…" (p.2). By tying each employee's financial success to the organization's overall success, the Balanced Scorecard can ensure employees are joined in helping their organization, by way of themselves and each other, succeed. Unlike forced ranking or fixed merit distributions where a fixed amount of money must be divided among employees, a variable pay plan enables each employee to be a winner. The Balanced Scorecard measures employees against a set of objectives instead of against each other and thus avoids creating a dysfunctional competitive atmosphere.

For companies that have long been evaluating employees against a set of objectives, implementing a pay for performance plan can provide the extra motivation employees need to commit to the goals fully. As one plant manager at a Balanced Scorecard company said after the organization linked a reward system to the program, “We have always had the measures. And we have always communicated them. Now our people are interested in them” (Kaplan and Norton, 2001) (p. 253).

Different Balanced Scorecard companies have taken different approaches when linking a compensation and reward program to the scorecard. As Kaplan and Norton (2001) state, “The only generalizable finding from all of the company experiences in linking compensation and reward to Balanced Scorecards is that they do it” (p.265). Linking a reward system to the scorecard is essential because it sends a clear message about the value the organization places on the scorecard program and communicates how much support the project has from senior management. Without this linkage, the Balanced Scorecard metrics become little more than suggestions about what the organization would ideally like employees to accomplish. Though establishing a connection between the reward system and the scorecard is essential, organizations should be cautious about implementation of such a system (Kaplan and Norton, 2001).

First, it is suggested that organizations delay linking compensation to the scorecard for six to twelve months. One reason for this is that, at first, organizations may not be sure they have chosen the right measures. Companies

should give themselves time to become comfortable with the idea that the metrics they have chosen truly reflect the strategy the organization is pursuing and ensure employees understand those metrics and the system as a whole. A second reason for the delay is that organizations need time to ensure the data sources used are valid and that any problems with data collection have been identified and corrected. Often, companies need time to design and implement new programs and processes that will generate data needed for a complete list of metrics. Few organizations are currently measuring the four Balanced Scorecard perspectives. This change cannot occur overnight. Until an organization is completely confident in the chosen metrics and the methods for collecting data for those metrics and employees fully understand the Balanced Scorecard program, a link to compensation should be delayed (Kaplan and Norton, 2001).

There are several decisions an organization must make when designing a pay for performance plan. One of great significance is whether individual or team-based rewards will be used. Again, there is no one right answer to this question, though most Balanced Scorecard companies use a mix of organizational and individual rewards. Team-based rewards go further to encourage teamwork and collaboration while individual rewards acknowledge the individual efforts of each employee and help organizations avoid rewarding all members of a team when only one or a few may be responsible for the success. It is also important to consider that team-based reward systems are not appropriate when the work being done is not truly interdependent. Whatever

the decision made, tying the Balanced Scorecard to a reward system is the final step in ensuring results (Kaplan and Norton, 2001).

The Balanced Scorecard has been successfully implemented in private-sector firms as well as government and healthcare organizations. Some of the more well-known Balanced Scorecard companies in these different sectors currently enjoying tremendous success include Mobil North America Marketing and Refining (NAM&R), The City of Charlotte, and Duke Children's Hospital (Kaplan and Norton, 2001).

Without question, one of the Balanced Scorecard's flagship companies is Mobil North America Marketing and Refining. A steadfast commitment from senior leadership and a no-nonsense approach to designing a quality scorecard make Mobil NAM&R's experience worthy of study and imitation. In order to help define its strategy, the organization first developed a set of themes for each of the four perspectives, then set out to define metrics that supported each theme for each employee. Senior leadership determined that the Learning and Growth perspective provided the foundation for the organization's strategy, monitoring the development of skills and the role of information technology. Metrics to support this perspective, however, were the most difficult to identify and, like many Balanced Scorecard companies, Mobil NAM&R realized new processes needed to be designed and implemented. Before the scorecard was officially launched, Mobil NAM&R conducted an employee survey to determine how well employees understood the process and metrics involved as well as the

sophisticated three-tiered reward system. Within five years of implementing the Balanced Scorecard program, Mobil NAM&R experienced a 20 percent reduction in refining, marketing, and delivery costs per gallon of gasoline. Furthermore, annual yield losses fell 70 percent, safety incidents were reduced 80 percent, and environmental incidents by 63 percent. Furthermore, monitoring leading indicators on the Balanced Scorecard enabled Mobil NAM&R to successfully implement its new *productivity and growth* strategies (Kaplan and Norton, 2001).

The City of Charlotte decided to design its scorecard to highlight the city's five strategic themes: community safety, transportation, preserving and improving older urban neighborhoods ("city within a city"), restructuring government, and economic development. Cabinets initially comprised of department heads were designed for each theme. These cabinets eventually grew to include a number key operating people who shared a common interest in the theme. The teams realized that the Balanced Scorecard perspectives could be applied for each of the themes and thus decided to design and implement a scorecard for each. The financial perspective was used to ensure the city was able to deliver services at a good price, secure funding and external partners for services, and maintain the city's tax base and credit ranking. The internal and learning and growth perspectives were used to support the city's customer service initiatives, including improving services offered and boosting efficiency. Additional scorecards for other city service divisions were not allowed to be designed until that division could demonstrate and communicate how it

supported one or more of the strategic themes. Using the Balanced Scorecard method, the City of Charlotte was able to implement several city initiatives including community problem-oriented policing, inner-city developments, and a new transit-land use plan, all of which lead to dramatic increases in financial efficiency and resident satisfaction scores. (Kaplan and Norton, 2001).

Duke Children's Hospital, an academic children's hospital in Durham, North Carolina, faced a multitude of difficulties when first experimenting with the Balanced Scorecard method. First, the organization was uncertain about which of its services were most important, which resulted in an initial confusion about the strategy and therefore what to measure. The fact that the organization had never stated a strategy was of concern to its leadership which saw the Balanced Scorecard as a way to define the direction the organization intended to go and provide a map for how to get there. The hospital also faced a breakdown in communication with referring physicians and difficulty balancing quality care and patient satisfaction with education and research and its financial objectives. Senior leadership decided to utilize a Balanced Scorecard process to help align goals among administration, staff, and physicians while also articulating strategy and outlining the organization's expectations. The hospital's Balanced Scorecard initiative required the implementation of a whole collection of new processes, all of which were benchmarked and continuously monitored. As a result of the effort, Duke Children's Hospital experienced a $30 million reduction in costs and a $50 million increase in net margin as a result of a balanced scorecard system.

Clinical outcomes and employee satisfaction were also improved through the use of the scorecard in aligning academic and clinical staffs to the hospital's strategy. Cost per case and length of stay were reduced 25 percent and both patient and physician satisfaction were improved, all within the first two to three years (Kaplan and Norton, 2001).

The United States Department of Energy's Department of Procurement and Assistance Management also utilized the scorecard and enjoyed positive results. When beginning the Balanced Scorecard process, the department first established a strategy for the scorecard process itself. That strategy, "To change the present system's culture, management systems, and line processes consistent with the principles of Quality Management, in order to establish and maintain: a customer focus, a sense of urgency, continuous and breakthrough process improvements, and an emphasis on results," became the guide for selecting metrics and establishing programs to support those metrics. As a result of the department's Balanced Scorecard initiative, customer satisfaction scores were improved, performance based service contracts rose 22% and cost to spend ratio targets were met or exceeded for three consecutive years ("Federal Procurement", 2005).

Finally, the University of Virginia Library used a Balanced Scorecard to accomplish its strategic objectives of providing excellent service, educating its users, building, maintaining, and preserving high quality collections, and providing convenient and timely access to users. Clearly, the main focus of the

Library's scorecard was service to its users, and all four perspectives of the program were focused accordingly. Unlike the other companies mentioned, the University of Virginia Library took a two-tiered approach to goal-setting, utilizing a "target 1" and "target 2" goal for each of its metrics. Target 1 represents the Library's most aggressive or stretch target while target 2 represents a challenging but less aggressive goal. At the end of 2005, 40% of target 1 goals were reached and 80% of total goals (target 1 or target 2) were reached. As a result of the Balanced Scorecard effort, each of the Library's overall ratings its major user groups (undergraduate students, graduate students, humanities faculty, social science faculty, and science faculty) rose to an all-time high that exceeded the Library's target 1 stretch goal of 4.00 on a 5 point scale ("Balanced Scorecard at UVa", 2007).

When organizations follow best practices for the design and implementation of a Balanced Scorecard project and appropriately tie the system to a pay for performance plan, employee motivation and engagement, as well as the organization's bottom line, can be dramatically improved. Furthermore, these organizations will experience increased success in the pursuit of their strategic objectives and can rapidly and effectively implement and monitor changing strategies.

Conclusion

Certainly there is great success to be gained through the proper design and implementation of a Balanced Scorecard. Not only does the Balanced

Scorecard accomplish the core mission of performance management, but it also serves as an organizational change tool that helps firms identify and communicate their strategies and focus the power of their human capital on the achievement of organizational objectives. In order for these successes to be gained, however, organizations must be willing to make the necessary changes in both culture and processes. The Balanced Scorecard is itself a culture, a way of thinking and operating, and a large and continuous commitment to excellence. Not only must technology be developed and implemented to support the data generation and collection, but people at every level of the organization must be committed to the execution of the scorecard, and must believe in the results it can deliver. Just like a commitment to the pursuit of the Malcom-Baldridge Quality Award or to a Six-Sigma goal, the decision to launch the design and implementation of a Balanced Scorecard-based performance appraisal system is one that requires the highest level of commitment and it is not a decision that should be entered without careful planning and consideration. Senior management should be aware of the costs and sacrifices involved. First, success requires a clear understanding of the basic elements of performance management and effective performance appraisal, including commonly made mistakes and how these can be avoided. Next, an organization must understand the purpose of the Balanced Scorecard – to communicate and measure organizational strategy while at the same time tying individual performance to organizational success – and how the design supports this objective. When the Balanced Scorecard is

seen as just the latest management fad, the most important part of its framework, consideration of the strategy, is omitted and the scorecard becomes simply another complicated set of metrics. Finally, metrics must be chosen and must fit the design of the scorecard as outlined in the previous chapter. Only when all of these pieces are present can the Balanced Scorecard fulfill its purpose as both a strategy and a performance management tool. In the following case study, we will examine how the Balanced Scorecard was poorly implemented in a healthcare setting, hoping to gain insight into real-world difficulties organizations face and how they can be avoided.

Balanced Scorecard in Healthcare:
A Case Study

Hospital X is the largest hospital in a state-wide health care system, with over 760 beds serving over 25, 000 patients per year. The hospital employs over 4,000 people, ranging from physicians and nurses to administrative assistants and cooks.

The hospital employs the use of a modified Balanced Scorecard method, called the Accountability Matrix, in the performance reviews for its management team. Participants include all directors, divisional directors, and vice presidents hospital-wide.

The matrices are split into five pillars: Financial Success, Team Member Engagement, Operational Excellence, Customer Service, and Leadership. Each pillar accounts for 20% of the participant's total score. Each matrix is both tailor-made for the individual participants and linked to all other participants through the use of a bi-level metric system. Two metrics under each pillar measure organization-wide performance, while other metrics under each pillar measure departmental or some form of individual performance. The weights assigned to these metrics are varied by position in the organization so that senior-level managers assume more responsibility for overall organization performance than do directors, who assume more responsibility for the performance of their departments. Divisional directors' responsibility is split evenly between the two.

Therefore, for a vice president, the 20% weight assigned to each pillar is split with 15% assigned to the two organizational metrics, and just 5% assigned to individual or departmental metrics. For a director, the weights are the opposite, with only 5% assigned to the organizational metrics and 15% accounted for by departmental metrics. Divisional directors use an even split, with organizational and departmental metrics each accounting for 10%. The two organizational metrics under each pillar are not weighted evenly – for a vice president, for example, one may be worth 9% and the other 6% (see Table 1). The same is true for individual or departmental metrics – the individual weights vary, though the total weight of each section (organizational metrics and individual metrics) is the same for each level of management (director, divisional director, vice president). For each indicator or metric, a scale is used to determine performance and assign points earned. The levels of performance are labeled as follows: Great (100 points), Good (75 points), Acceptable (50 points), Needs Improvement (25 points), and Unacceptable (0 points). For each level, a specific outcome is listed. For example, under Financial Success: Operating Margin, "great" is defined as "4.4% or greater." The point value of the level achieved is multiplied by the weight of the indicator to reach a final score. Therefore, if the organization achieved a 4.4% operating margin, a vice president for whom the indicator was valued at 15% would receive 15 points (100 points X 15% = 15). A divisional director would only receive 10 points (100 points X 10% = 10), etc. It is also necessary to note that in rare instances no "Needs Improvement" score was

available, and the scale simply went from "acceptable" at 50 points to "unacceptable" at 0 points. This only occurred in the event that "total expense for responsibility" was chosen as the individual metric under Financial Success.

Table 1: Metrics and Weightings by Management Level

Metric	% by Org. Level	Financial Success	Team Member Engagement	Operational Excellence	Customer Service	Leadership
Org. Wide Metric #1	**9%** **6%** **3%**	Metric: operating margin	Metric: Retention	Metric: Core Measures (JCAHO)	Metric: Inpatient Mean Score	Metric: Overall Job Fulfillment
Org Wide Metric #2	**6%** **4%** **2%**		Metric: Team Member Development	Metric: Patient Throughput	Metric: Likelihood to recommend	Metric: Physician Satisfaction
Department or individual performance measures	**5%** **10%** **15%**	Metric: Total expense for responsibility	Metric: measures defined by departments – common are department turnover and retention rates and employee satisfaction data	Metric: measures defined by departments – designed to allow for unique measures associated with department leader effectiveness	Metric: measures defined by departments – most common are departmental Internal Customer Service Scores and Patient Satisfaction Survey	Metric: Most common measure is leadership ratings assigned by the participant's direct supervisor

Vice President
Divisional Director
Director

Levels of Performance:
Great = 100 points
Good = 75 points
Acceptable = 50 points
Needs Improvement = 25 points
Unacceptable = 0 points

Financial Success

Initially, two organizational metrics, operating margin and surgical case volume, were included under this pillar. A local natural disaster during the fiscal year rendered the surgical case volume data unreliable. The organization's Chief Operating Officer made the decision to remove the surgical case volume metric from the matrices and add the weight of that metric into the weight of the operating margin metric.

Most participants chose to use only one departmental metric for each pillar, though there were cases in which two or more indicators were used. "Total expense for responsibility" was most commonly used for the Financial Success departmental indicator. The data for this metric came directly from the hospital's Financial Operations department. The scale most commonly used for this indicator listed "great" as 3% or more under budget, "good" as up to 2.99% under budget, "acceptable" as at budget, and "unacceptable" as over budget. No "needs improvement" score was available for this metric. Some participants who were responsible for several different departments chose to include a separate financial indicator for each, splitting the weight evenly between them. Furthermore, some participants separated out salary and supply budgets into two separate indicators.

Team Member Engagement

Two organizational metrics were included in the Team Member Engagement pillar. The first, retention rate, was calculated by subtracting the turnover rate from 100. Turnover data is collected by the Human Resources Information Systems department. The second indicator is termed development, and was calculated as the percentage of full-time team members who completed their annual training requirement. Retention rate is weighted more heavily than the development indicator and accounts for 9% of the score for vice presidents, 6% for divisional directors, and 3% for directors. Development is weighted at 6%, 4%, and 2% respectively.

The indicators chosen to represent department success are varied, though department results from the organization's Employee Satisfaction Survey are popular metrics. Also commonly used are department retention and turnover rate.

Operational Excellence

The two organizational metrics chosen for this pillar are "core measures" (this is calculated as a percentage of metrics that scored above the average listed by the Joint Commission for the Accreditation of Healthcare Organizations) and "patient throughput," a score that comes from the organization's Patient Satisfaction Survey. Both the Core Measures and Patient Satisfaction Survey data

are collected by the Quality Management department. Core measures is weighted at 9%, 6%, and 3% for vice presidents, divisional directors, and directors, respectively, while patient throughput is weighted at 6%, 4%, and 2%.

The departmental indicators for this pillar are the most widely varied, with nearly every participant having something distinctly their own. Such a high level of uniqueness is to be expected in this pillar because operational excellence is defined by the effectiveness to which each member of the management team runs his or her department, each of which is unique in some way. When several managers have responsibility for different aspects of the same division, however, the indicators are usually the same. The four directors of the information systems division, Clinical Information Systems, Physician Clinical Information Systems, Application Information Systems, Technical Information Systems, and Management Information Systems, for example, all use both "system availability" and a peer review metric under this pillar. Likewise, all nurse managers use two indicators from the Patient Satisfaction Survey, though each of the managers uses the data for their individual nursing unit.

Customer Service

The two indicators for the Customer Service pillar, Inpatient Mean Score and Likelihood to Recommend, are from the Patient Satisfaction Survey. Inpatient Mean Score carries the higher weight for this pillar, accounting for 9%,

6%, and 4% for vice presidents, divisional directors, and directors, respectively, while Likelihood to Recommend is weighted at 6%, 4%, and 2%.

Many participants used their department's score from the organization's Internal Customer Service Survey as one of the departmental indicators for this pillar. Nurse managers use a customer service measure from the Patient Satisfaction survey, which is weighted as the full 15% (nurse managers are considered directors). In the event that a participant is responsible for more than one department, two indicators are often used to separate each department's individual success.

Leadership

Overall Job Fulfillment (from the Employee Satisfaction Survey) and Physician Satisfaction (from the Physician Satisfaction Survey) are the two organizational metrics used for this pillar. Overall Job Fulfillment is weighted more heavily, accounting for 9%, 6%, and 4% for vice presidents, divisional directors, and directors, respectively, while Physician Satisfaction is weighted at 6%, 4%, and 2%.

The individual indicators used for this pillar are perhaps the most subjective, as most are simply leadership ratings assigned by the participant's direct supervisor. In some cases, metrics for the achievement of departmental goals are used.

Analysis

The Accountability Matrix is riddled with problems stemming from both poor design and poor execution. Perhaps the most obvious flaw in the system is the set of metrics it utilizes.

First, the metrics chosen were inconsistent both in terms of measurements used for the same purpose and rating scales applied to the same metrics. For example, though turnover was an indicator on nearly every individual matrix, some matrices utilized a number based on a calendar year while others utilized fiscal year data. Furthermore, levels of performance (great, good, acceptable, needs improvement, unacceptable) were defined differently for different participants, and some used a percent change from the previous year instead of the present year's data. These inconsistencies made it impossible to compare one individual's results to those of his peers. In other instances, the same outcome was measured by two different metrics. For example, an overall patient satisfaction score was used by some nursing units while scores from specific questions on the patient satisfaction survey were used for other units. This difference allowed nurse managers to highlight areas they usually excel in while avoiding those they know may not result in as high a score. Participants used their knowledge of their areas to create a matrix that would paint the most flattering picture possible. Again, this inconsistency made it impossible to

compare individual scores or identify either high achievers or areas that needed improvement.

Another major problem with the metrics used was that they were often based on invalid data or valid data analyzed inappropriately. For example, nearly every manager's matrix utilized an internal customer satisfaction survey score. This survey, administered through the hospital's Quality Management department, was supposed to be conducted each quarter so that each department in the hospital was able to score each other department four times per year. Unfortunately, however, the survey was only administered twice for fiscal year 2006 and some departments were actually only surveyed once in the twelve month time span. Furthermore, some surveys received only a handful of responses. It was clear in several cases that there were too few responses to draw a valid conclusion. The data were used however, and these suspect scores were applied and rated. Matrix participants were well aware of the situation and were very displeased, but the survey scores remained a part of the matrix as planned. Also, some data was simply mishandled. The bulk of this problem occurred for the employee satisfaction metric which was present on nearly every matrix. The Press Ganey Employee Perspectives Report benchmarks scores against corresponding scores in the same department of every other hospital of comparable size in the Press Ganey database. From this comparison, a percentile score is assigned. This percentile score was utilized for the matrices and was appropriate for managers or directors responsible for only one area, department,

or unit. Divisional directors and vice presidents, however, are responsible for multiple areas that are surveyed separately and receive different scores and thus different percentile rankings. When this occurred, the percentile scores from each of a divisional director's or vice president's areas were put into a weighted average according to the number of participants for each survey. The resulting number was clearly irrelevant and meaningless and was in no way a measurement of actual employee satisfaction. Nevertheless, the number was used and rated against a scale, though again the scale used was not consistent across participants. In this case as well, some matrices used a percent improvement scale instead, or ignored the percentile score altogether and utilized a mean score.

A third problem with the metrics used on the Accountability Matrix was a lack of connectivity between activities and outcomes. In many instances, it was unclear how an individual participant could control or even affect the metrics on their matrices. For example, every matrix included the indicator "surgical case volume." This clinical indicator measures the number of surgical cases the hospital handles each fiscal year. While clinical units could usually articulate how they could contribute or somehow at least support this number, there was a clear lack of connectivity for the Divisional Director of Human Resources or the Director of Plant Services. This same problem occurred several times throughout the matrix, usually in clinical organizational metrics that were not tied to individual non-clinical performance. While it may be possible, with much

research and thought, to articulate how every department in the organization contributes to this outcome, the fact is that the connections were never defined or communicated, which lead to the perception that there was no connection at all.

The final problem with the hospital's Accountability Matrix is that it went largely unmonitored and un-enforced. The Matrix performance review was scheduled to take place in October. The data collection process, however, began in late September. That month was the first time in a year participants had seen their matrices. The data was a complete surprise to nearly everyone, since it had not been monitored at all during the year. Furthermore, some participants had not even had a matrix created the previous year, so the matrices were designed on the spot, then filled in with the necessary data. One participant likened this process to taking the test after you have seen the answer key! To make matters worse, participants were often allowed to change the metrics on their matrices at the last minute, literally minutes before final scores had to be delivered to senior management. There was rarely an explanation or justification for these changes. Finally, scores were adjusted at the end by way of 10 extra "attitude, teamwork, and accuracy" points that were available on a purely subjective basis and were awarded by each participant's direct supervisor. A true pay for performance plan was not utilized but instead scores were "taken into consideration" when annual merit increases were assigned.

The results of these serious shortcomings were disastrous. The lack of support and enforcement by senior management caused the Accountability

Matrix to suffer a complete lack of employee buy-in and the process was seen as a management headache and absurdity. Employee buy-in was further lessened because of the invalidity and lack of connectivity of the metrics used. Because the indicators were not monitored throughout the year, action plans could not be developed and behaviors could not be modified, therefore the Accountability Matrix failed to drive performance in any way. The end result was a meaningless measurement tool that neither communicated a strategy, measured a strategy, or motivated employees toward organizational goals.

In order to avoid similar pitfalls, organizations must fully understand the design of a Balanced Scorecard and must be willing to commit to the changes and implementation necessary to make it valid and effective as a means of performance appraisal. Once these steps are taken, management must then be willing to tie the scorecard to a pay for performance plan in order to demonstrate the organization's commitment to the tool and to generate the level of employee commitment necessary for success.

Following a thorough review of Accountability Matrix 2006, major changes to the system were proposed. Senior management's resistance to change and lack of commitment to a metrics-based performance system continues to be an obstacle to the successful design of a Balanced Scorecard system. To date, very few meaningful changes have been implemented and the Accountability Matrix continues to be a frustrating and useless tool.

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