Should We Abandon Performance Measures?

by David Parmenter

I have worked with performance measures for over 20 years, and in that time I have witnessed minimal progress in the right direction. Deriving measures is often viewed as an afterthought. Measures are regarded as something we fill into a box to say we have achieved a goal.

I firmly believe that performance measures exist for a higher purpose — helping align the staff's daily actions to the organization's critical success factors (CSFs). Yet all too often the measures in an organization amount to a random collection prepared with little expertise signifying nothing. To make matters worse, these measures cost the organization dearly:

- Measures are gamed to the detriment of the organization so that executives can increase their pay.
- Teams are encouraged to perform tasks that are contrary to the organization's strategic direction.
- Costly "measurement and reporting" regimes lock up valuable staff and management time.
- Measures are often derived from six-figure consultancy assignments that yield little more for the organization than another "doorstop" report.

A RADICAL TREATMENT FOR AN ACUTE PROBLEM

Why would an author who has preached about implementing winning KPIs now have a change of heart? Because I have witnessed the failure of too many performance measurement initiatives. I am now convinced that, in many cases, a more radical approach is necessary.

For centuries the medical profession has realized that acute cases demand extreme action. Some treatments for critically ill patients involve the eradication of the immune system and then slowly, step by step, reintroducing it. An abandonment of all performance measures, albeit on a short-term basis, may well be the radical treatment required before we can cure the patient (the organization). We need to cut the rot out; otherwise it will eventually destroy all new performance measurement initiatives. Starting anew will enable the organization to rebuild the way performance measures are used from the ground up.

PERFORMANCE MEASUREMENT SYSTEMS ARE BROKEN

Performance measurement systems are broken, and the reason for this is very simple. Organizations, in both the private and public sectors, are being run by managers who have not yet received any formal education in performance measurement. Unlike accounting and information systems, where rigorous processes have been formulated, discussed, and taught, performance measurement has been left as an orphan of business theory and practice.

Whilst writers such as Edwards Deming,[1] Margaret Wheatley and Myron Kellner-Rogers,[2] Gary Hamel,[3] Michael Hammer,[4] and Dean Spitzer[5] have for some time illustrated the dysfunctional nature of performance measurement, their valuable arguments have not yet been reflected in business practice. There is a long journey ahead in order to get performance measurement functioning properly. We will be well on our way to this goal when students are attending lectures on measurement and professionals are being examined on their understanding of performance measurement in order to obtain their desired professional qualifications.

In order to get performance measures to work, we need to challenge the myths they have been built on. To illustrate my point, I would like to draw your attention to six of the performance measurement myths[6] that need to be challenged:

1. Most measures lead to better performance.
2. All measures can work successfully in any organization, at any time.
3. All performance measures are KPIs.
4. By tying KPIs to pay, you will increase performance.
5. There is a need to set annual targets.
6. You need performance measures in order to drive performance.

MYTH #1: MOST MEASURES LEAD TO BETTER PERFORMANCE

Measurement initiatives are often cobbled together without the knowledge of the organization's CSFs and without an understanding of a measure's behavioral consequences. It is a myth of performance measurement that most measures lead to better performance. Every performance measure can have a dark side, a negative consequence, an unintended action that leads to inferior performance.

In order to make a performance measure work, one needs to anticipate likely human behavior and minimize the potential dark side of the measure. The key is to find the dark side and then tweak how the measure is used so that the behaviors it will promote are appropriate.

I suspect well over half the measures in an organization may be encouraging unintended negative behavior. Dean Spitzer's book *Transforming Performance Measurement* provides a vast array of examples of dysfunctional performance due to poor measurement. Below are some examples of dysfunctional activities promoted by the inappropriate use of performance measures:[7]

Public-Sector Examples

- Experienced caseworkers in a government agency will work on the easiest cases and leave the difficult ones to the inexperienced staff because they are measured on the number of cases closed.
- An Australian city rail service penalized train drivers for late trains, resulting in drivers skipping stations in order to achieve on-time schedules.
- A UK accident and emergency department was measuring timely treatment of patients. The nurses then delayed the ambulances from offloading patients until the doctors could see them, thus achieving a zero time difference. Within hours of this measure being implemented, ambulances were circling the hospital, as the ambulance bay was full. The follow-on result was obvious: ambulances arriving late at emergency calls.

Private-Sector Examples

- A fast-food restaurant manager was striving to achieve an award for zero wastage of chicken. The manager won the chicken efficiency award by waiting until the chicken was ordered before cooking it. The long wait times that resulted meant a huge loss of customers in the following weeks.
- A company that was measuring product that left the factory on time had a 100% record, yet 50% of customers complained about late delivery. The reason was that nobody cared about what happened next after the product left the factory.
- Sales staff met their targets at the expense of the company, offering discounts and extended payment terms and selling to customers who would never pay. You name it, they did it to get the bonus!
- Purchasing departments awarded for receiving large discounts started to buy in too large a quantity, creating an inventory overload.
- A stores department maintained a low inventory to get a bonus, which resulted in a production shutdown because of stock outs.

Spitzer's statement that "people will do what management inspects, not necessarily what management expects" is very apt. The greatest danger of performance management is dysfunctional behavior. As Spitzer notes, "the ultimate goal is not the customer — it's often the scorecard." He has heard executives, when being candid, say, "We don't worry about strategy; we just move our numbers and get rewarded."[8] The checklist in Table 1 will help you assess the potential damage in your organization.

MYTH #2: ALL MEASURES CAN WORK SUCCESSFULLY IN ANY ORGANIZATION, AT ANY TIME

Contrary to common belief, all measures will not work successfully in any organization, at any time. The reality is that there needs to be, as Spitzer argues, a positive "context of measurement"[9] for measures to deliver their potential.

In order to have an environment where measurement will thrive, the following seven foundation stones need to be in place:[10]

1. Partner with the staff, unions, and third parties.
2. Transfer power to the front line.
3. Measure and report only what matters.
4. Source KPIs from the CSFs.
5. Abandon processes that do not deliver.
6. Understand human behavior.
7. Ensure organization-wide understanding of winning KPIs.

Table 1 — Dysfunctional Performance Measures Checklist

1. Is the reward structure tied to the key performance indicators?	Yes/No
2. Are measures constructed by teams or individuals who have not received training or guidance on what makes measures work or fail?	Yes/No
3. Are annual targets set that will trigger bonuses if met?	Yes/No
4. Does management believe that performance can only be achieved if there is a financial reward attached to that performance?	Yes/No
5. Are measures typically adopted without testing and assessing their potential negative behavioral impact?	Yes/No
6. Is it common for staff to be asked to "force" compliance to a measure just to achieve a target, even though the action may damage the organization's reputation?	Yes/No
7. Does your organization have some measures that are leading to dysfunctional behavior?	Yes/No
8. Has your organization had to remove measures due to the damage they have created?	Yes/No
9. Does your organization have measures that are solely used to make departments look good rather than focusing on actions that will benefit the overall organization?	Yes/No
11. Does your organization have a history of "gaming" performance measures?	Yes/No
12. Do you have over 100 measures in your organization?	Yes/No
13. Are measures introduced without any estimation of the likely cost/benefit?	Yes/No
14. Is there a high degree of cynicism about the effectiveness of performance measures in your organization?	Yes/No

Your score: Every "yes" indicates a problem. If you have over five affirmative responses, it may be best to put a stop to all new performance measures and start rebuilding your measures from scratch.

These seven foundation stones are explained at length in my recent book *Key Performance Indicators for Government and Non Profit Agencies*.[11]

MYTH #3: ALL PERFORMANCE MEASURES ARE KPIs

Throughout the world, from Iran to the US and back to Asia, organizations have been using the term "KPIs" to mean all performance measures. No one seems to worry that the KPIs have not been defined by anyone. Thus, measures that are truly key to the enterprise are being mixed with measures that are completely flawed.

Let's break the term down. "Key" means key to the organization, while "performance," naturally, means that the measure will assist in improving performance. I have come to the conclusion that there are four types of performance measures.[12] They have different functions and frequency of measurement (see Table 2).

The common characteristic of key result indicators (KRIs), which are often mistaken for KPIs, is that they are the result of many actions. They give a clear picture of whether you are traveling in the right direction and of the progress made toward achieving desired outcomes and strategies. They are ideal for governance reporting, as KRIs show overall performance and help the Board focus on strategic rather than management issues.

KRIs do not tell management and staff what they need to do to achieve desired outcomes. Only performance indicators (PIs) and KPIs can do this. Examples of KRIs include:

- Customer satisfaction
- Employee satisfaction
- Return on capital employed

Separating out KRIs from other measures has a profound impact on the way performance is reported.

Table 2 — The Four Types of Performance Measures

Type of Performance Measure	Number of Measures in Use	Frequency of Measurement
1. **Key result indicators (KRIs)** give an overview of the organization's past performance and are ideal for the Board (e.g., return on capital employed).	Up to 10	Monthly, quarterly
2. **Result indicators (RIs)** summarize activities of a number of teams and thus have a shared responsibility (e.g., yesterday's sales).	80 or so (If it gets over 150, you will begin to have serious problems.)	24/7, daily, weekly, fortnightly, monthly, quarterly
3. **Performance indicators (PIs)** are measures that can be tied back to a team but are not "key" to the business (e.g., number of sales visits organized with key customers next week/fortnight).		
4. **Key performance indicators (KPIs)** are measures focusing on those aspects of organizational performance that are the most critical for the current and future success of the organization (e.g., planes that are currently over two hours late).	Up to 10 (You may have considerably fewer.)	24/7, daily, weekly

There is now a separation of performance measures into those impacting governance (up to 10 KRIs in a Board dashboard) and those result indicators (RIs), PIs, and KPIs that impact management.

Probably the most controversial statement in my work has been that every KPI on this planet is nonfinancial. I argue that when you have a dollar amount, you have simply quantified an activity. Whilst financial measures are useful, they are RIs, not KPIs. The seven characteristics of a KPI are:[13]

1. It is a nonfinancial measure (not expressed in dollars, yen, pounds, Euros, etc.).
2. It is measured frequently (e.g., 24/7, daily, or weekly).
3. It is acted upon by the CEO and senior management team.
4. All staff understand the measure and what corrective action is required.
5. Responsibility for the measure can be tied down to a team.
6. It has a significant impact (e.g., it impacts on more than one of the CSFs and more than one balanced scorecard perspective).
7. It encourages appropriate action (i.e., it has been tested to ensure it has a positive impact on performance, whereas ill-thought-through measures can lead to dysfunctional behavior).

Examples of KPIs include:

- **Planes late by more than x hours or x minutes.** This would be measured 24/7 and would focus staff on the important issue of getting a plane back on time even if it was not a problem of their own making.
- **Late deliveries to key customers.** By focusing only on timeliness of deliveries to key customers, we are telling staff to focus on these shipments first. If you measure *all* deliveries, staff will pick the easiest and smallest deliveries in order to achieve a high score, thereby sacrificing the large, complex orders to key customers, which is where companies typically make most of their profit.
- **Number of CEO recognitions of staff achievements planned for next week, next fortnight.** Recognition is a major motivator, and great CEOs are good at giving it frequently. As Jack Welch says, "Work is too much a part of life not to recognize moments of achievement."[14] This KPI could be reported each Friday morning so that the CEO has the opportunity to say, "There must be more teams we can celebrate next week. Please find them and organize it." In nonperforming organizations, everybody is invariably too busy chasing their tails to stop and celebrate success. Not so in high-performing ones. That is why this measure deserves to be called a KPI.

The winning KPIs methodology clearly indicates that KPIs are a rare beast. KPIs are reported immediately and thus will never find their way into a balanced scorecard that is reported to the senior management team two or three weeks after month end.

MYTH #4: BY TYING KPIs TO PAY, YOU WILL INCREASE PERFORMANCE

It is a common belief that the primary driver for staff is money, and thus one needs incentives in order to get great performance. Although this is the case with employees who are sitting on the first two rungs of Maslow's hierarchy of needs,[15] it does not apply to

Table 3 — A Performance-Related Pay System That Will Never Work

Category	Perspective Weighting	Measure	Measure Weighting
Financial	60%	Economic value added	25%
		Unit's profitability	20%
		Market growth	15%
Customer	20%	Customer satisfaction survey	10%
		Dealer satisfaction survey	10%
Internal	10%	Above-average rank in industry-based quality survey	5%
		Decrease in dealer delivery cycle time	5%
Innovation and learning	10%	Employee suggestions raised vs. implemented	5%
		Satisfaction from employee survey (re: coaching, empowerment, etc.)	5%

many managers or staff. Recognition, respect, and self-actualization are more important drivers. This factor has a big impact on how we treat KPIs.

In all types of organizations, there is a tendency to believe the way to make KPIs work is to tie them to an individual's pay. I believe KPIs are so important to an organization that performance in this area should be treated as a given, or as Jack Welch says, "a ticket to the game."[16] When KPIs are linked to pay, they create key *political* indicators, which will be manipulated to enhance the probability of a larger bonus.

Because KPIs are special performance tools, it is imperative that they not be included in any performance-related pay discussions. KPIs are too important to be manipulated by individuals and teams to maximize bonuses. Although KPIs will show — 24/7, daily, or weekly — how teams are performing, it is essential to leave the KPIs uncorrupted by performance-related pay.

Performance bonus schemes, using a balanced scorecard, are often flawed on a number of counts:

- The balanced scorecard is often based on only four perspectives, ignoring the important environment, community, and staff-satisfaction perspectives.
- The measures chosen are open to debate and manipulation.
- There is seldom a linkage to progress within the organization's CSFs.
- Weighting of measures leads to crazy performance agreements such as the one in Table 3, in which the message is "Find a way to manipulate these numbers, and you will get your bonus." The damage done to the business by such schemes is only discovered in subsequent years.

MYTH #5: THERE IS A NEED TO SET ANNUAL TARGETS

We'd like to think that we know what good performance will look like before the year starts and, thus, can set relevant year-end targets. In reality, as Jack Welch observes, it leads to constraining initiative, stifling creative thought processes, and promoting mediocrity rather than giant leaps in performance.[17]

All forms of annual targets are doomed to failure. Far too often management spends months arguing about what is a realistic target, when the only sure thing is that it will be wrong. It will be either too soft or too hard. I am a follower of Jeremy Hope's work. He and his coauthor Robin Fraser were the first writers to clearly articulate that a fixed annual performance contract was doomed to fail.[18]

Far too often, organizations end up paying incentives to management when in fact you have lost market share. In other words, your rising sales did not keep up with the growth rate in the marketplace.

As Hope and Fraser point out, not setting an annual target beforehand is not a problem as long as staff members are given regular updates about how they are progressing against their peers and the rest of the market. They argue that if you do not know how hard you have to work to get a maximum bonus, you will work as hard as you can.

MYTH #6: YOU NEED PERFORMANCE MEASURES IN ORDER TO DRIVE PERFORMANCE

If the organization has recruited the right staff, there is a clear understanding of what the organization's CSFs are, and if staff work in a supportive environment with great managers and leaders, the organization will succeed. Performance measures don't drive performance — they support and enforce the positive environment that already exists.

I am now convinced that an organization with dysfunctional performance measures would function much better without them, for the following reasons:

Staff Management

Managers would spend time discussing goals with staff. Having one-to-one meetings on a regular basis would ensure that progress against goals was monitored, feedback was given, and celebrations were held.

Performance-Related Pay

Bonuses would no longer be based on very dubious formulae matrices. Instead, the organization would reward staff based on a retrospective look at their performance, including a comparison against the performance of peers and that achieved by third parties. Taking this approach would dispel one of the greatest myths of performance measurement, which is that linking pay to performance measures increases performance.[19]

Balanced Scorecard Initiatives

All those balanced scorecards that are not delivering would be frozen, giving the organization a chance to evaluate how it is using this important methodology.

Measurement of Team Progress

The organization would monitor progress against milestones achieved and output from the team. Comparisons could be drawn from prior periods of outstanding performance, and agreements could be reached relatively painlessly between the manager and staff concerned.

Ascertaining the Organization's CSFs

With no measures, the CEO could take a step sideways and realize that the organization does not in fact know what its CSFs are. This is a vital realization. Whilst most organizations know their success factors, few organizations have:

- Worded their success factors appropriately
- Segregated out success factors from their strategic objectives
- Sifted through their success factors to find their *critical* ones
- Communicated the CSFs to staff

Monitoring the Organization's Performance

The CEO would be analyzing actual performance and would be notified of exceptions that warranted his or her attention. There would be daily and weekly reporting, as well as some instantaneous exception reports beamed to his or her smartphone in cases where a phone call was needed to chase something up. The CEO would be encouraged to "go out and see" — a Toyota principle — rather than hide behind a bank of data.

The CEO would now need to promote leadership and innovation within the organization and adopt more of the management practices preached by great paradigm shifters such as Jim Collins, Gary Hamel, Jack Welch, and Peter Drucker.

Consultancies Rethinking Their Product Range

The abandonment of performance measures would have a profound impact on the bottom line of consultancy firms. Large assignments performed on balanced scorecard implementations would cease, for the time being, and clients' staff would no doubt breathe a sigh of relief.

Gaming of the Performance Management System

The manipulation of performance reporting for the sole benefit of one's pay packet would no longer be a worthwhile activity. Senior management would now spend more time improving the bottom line. The annual target-setting travesty would be replaced by the setting of "big hairy audacious goals" that motivate and energize staff.

SUGGESTED ACTION STEPS

To address the issues discussed above, I propose the following action steps:

- **Do some background reading** on the topic. The sources listed in the endnotes to this article would be a good place to start. Everybody, no matter how busy they are, can find the time to read a chapter or two, three times a week.
- If you think you are working with dysfunctional measures, **negotiate a three-month moratorium on**

using performance measures within your organization. In this window of opportunity, perform the tasks set out below.

- Complete a thorough exercise to **ascertain your organizations' CSFs** and then ensure that all measures used by the organization relate back to the CSFs.[20] It is the CSFs, and the performance measures within them, that link daily activities to the organization's strategy. This, I believe, is the El Dorado of management.
- **Commence the grooming of an inhouse expert in performance measurement.** Dean Spitzer suggests using the title "Chief Measurement Officer" (see below).

A Three-Month Moratorium on Using Performance Measures

After three months with no performance measures being monitored or reported, management would have a good idea of the measures it has missed and the ones that should be permanently abandoned. The CEO would be invigorated from the closer contact with the operation and be in a better position to lead an initiative to revitalize performance, more effectively linking staff to the CSFs of the enterprise. As part of the gradual reintroduction of measures, I would recommend:

- **Establishing a measurement project team** with four to five representatives from the finance, HR, IT, and operations teams. Their role would be to explore how to embed wining KPIs in their organization, approve all measures, and start a process of education within the organization. This project team would be disbanded once the organization established the Chief Measurement Officer position and appointed someone to fill it.
- **Consulting with staff** so that you have some idea of the possible unintended consequences of a measure. Ask, "If we measure x, what action will you take?"
- **Piloting each performance measure** you intend to use. This simple step will enhance the measure's chance of success. Implementing measures without doing this testing is at best naive and at worst incompetent.

Appointment of a Chief Measurement Officer

Performance measurement is worthy of more intellectual rigor in every organization that is on the journey from average to good and finally to great. The chief measurement officer would be part psychologist, part teacher, part salesperson, and part project manager. He or she would be responsible for:

- Testing each new measure to ensure the dark side is minimal
- Vetting and approving all measures in the organization
- Leading all balanced scorecard initiatives
- Promoting the abandonment of measures that do not work
- Developing and improving the use of performance measures in the organization
- Learning about the latest thinking in performance measurement
- Being the resident expert on the behavioral implications of performance measures
- Replacing annual planning with quarterly rolling planning

I envision this position having a status equivalent to the senior IT, accounting, and HR officials. The position would report directly to the CEO, as befits the knowledge and diverse blend of skills required for this position. Only when we have this level of expertise within the organization can we hope to move away from measurement confusion to measurement clarity.

IN CONCLUSION

I hope this article will trigger some actions in your organization. Perhaps it will encourage you to abandon some broken measures, reexamine the way measures are introduced, or launch a KPI project to put some intellectual rigor into your performance measurement process. If nothing else, I hope it has sparked a commitment to ensuring that performance measures exist to better align your staff to the organization's CSFs.

ENDNOTES

[1]Deming, W. Edwards. *Out of the Crisis*. MIT Press, 2000.

[2]Wheatley, Margaret, and Myron Kellner-Rogers. "What Do We Measure and Why?" *Journal for Strategic Performance Measurement*, June 1999.

[3]Hamel, Gary, with Bill Breen. *The Future of Management*. Harvard Business Press, 2007.

[4]Hammer, Michael et al. "The Seven Deadly Sins of Performance Measurement (and How to Avoid Them)." *MIT Sloan Management Review*, Vol. 7, No. 1, Spring 2007.

[5]Spitzer, Dean R. *Transforming Performance Measurement: Rethinking the Way We Measure and Drive Organizational Success*. AMACOM, 2007.

[6]Parmenter, David. "The Myths and Flaws of Performance Measurement." White paper, DavidParmenter.com, 2013.

[7]Spitzer. See 5.

[8]Spitzer. See 5.

[9]Spitzer. See 5.

[10]These seven foundation stones are explained at length in: Parmenter, David. *Key Performance Indicators for Government and Non Profit Agencies*. John Wiley & Sons, 2012.

[11]Parmenter, David. *Key Performance Indicators: Developing, Implementing, and Using Winning KPIs*. 2nd edition. John Wiley & Sons, 2010.

[12]Parmenter. See 11.

[13]Parmenter. See 11.

[14]Welch, Jack, with Suzy Welch. *Winning*. HarperBusiness, 2005.

[15]Maslow, Abraham H. *Motivation and Personality*. Harper, 1954.

[16]Welch. See 14.

[17]Welch. See 14.

[18]Hope, Jeremy, and Robin Fraser. *Beyond Budgeting: How Managers Can Break Free from the Annual Performance Trap*. Harvard Business School Press, 2003.

[19]I have written about how to fix performance-related pay in: Parmenter, David. *The Leading Edge Manager's Guide to Success*. John Wiley & Sons, 2011.

[20]This process is outlined in: Parmenter, David. "Finding Your Organization's Critical Success Factors." White paper, DavidParmenter.com, 2012.

David Parmenter is an international presenter who is known for his thought-provoking and lively keynote addresses and workshops, which have led to substantial change in many organizations. Mr. Parmenter has worked for Ernst & Young, BP Oil Ltd, Arthur Andersen, and Price Waterhouse. He is a fellow of the Institute of Chartered Accountants in England and Wales. He is the author of four books published by John Wiley & Sons Inc. and has written over 50 articles for accounting and management journals. Mr. Parmenter has won two "article of merit" awards from the International Federation of Accountants. He can be reached at parmenter@waymark.co.nz; website: www.DavidParmenter.Com.