Performance measurement, evaluation and reward: the role and impact of subjectivity

Briefing

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Performance measurement and reward systems (PMRSs) are among the most important processes in an organisation’s toolkit. Effective design and use of performance measurement and evaluation will motivate employees to strive to attain the firm’s goals while ineffective systems can lead to a wide range of problems. At its worst, a PMRS will cause employees to work against the organisation’s goals for their own interests – and may even reward them for doing so.

The financial crisis of 2008 has pointed the spotlight on the design and effectiveness of PMRSs within organisations. While regulation has been at the heart of recent changes in the financial sector, the scale of the crisis has led to renewed interest in the role and outcomes of PMRSs across all industries by investors and other stakeholders. This report focuses on two important aspects of PMRSs that have been overlooked in empirical research to date: the role and the impact of subjectivity. Subjectivity is based on opinions or perceptions that cannot be independently verified by a third party. It is prevalent in the PMRSs of many companies across a wide range of industries, and apparent in the use of measures such as ‘leadership behaviour’ or ‘teamwork’ and in the use of ratings to summarise an employee’s performance. Subjectivity occurs in many other elements of the measurement and evaluation process too, where its existence and effects may be less obvious.

The main purpose of this report is to provide evidence of how and why firms incorporate subjectivity into the performance evaluation process. Despite its prevalence and recent academic research into specific aspects of subjectivity, there currently exists little empirical evidence for the rationale and extent of its use within individual firms. Furthermore, the processes and mechanisms for overcoming the problems associated with the use of subjectivity are not well documented in prior research. We therefore also explore the impact of subjectivity on evaluators, evaluatees and the integrity of the performance measurement and reward process. We examine these issues directly by collecting evidence from participants in performance measurement and evaluation processes. We draw on interviews with evaluators and evaluatees at two hierarchical levels within four diverse companies. Each firm was drawn from a different industry: food manufacturing, professional services, asset management, and equipment manufacturing. Our study was guided by the following research questions.

1. How and why do firms incorporate subjectivity in performance measurement and reward systems?
2. How is subjectivity perceived by those involved in the process, and what are its impacts?
The firms in our study have demonstrably different approaches to PMRSs. Despite the variability in design and use, each firm’s PMRS appears to have an internal logic that suggests our findings may have implications beyond these specific firms. We find that subjectivity is a purposeful element within the PMRSs we studied, underpinned by a rationale that is implicitly shared by the managers in each firm. Subjectivity is incorporated into the design of performance measurement and reward practices in ways that influence bonus determination, merit increases, and promotion processes – but the extent of subjectivity is not always apparent, even to those who are most involved in its use.

Reasons given by managers for the use of subjectivity include a desire to avoid the recognised deficiencies of objective performance measurement as well as perceiving real advantages in its use. Fairness, for example, is a major consideration for the firms in our study. Firms also recognise the potentially negative effects of subjectivity, such as bias, and mitigate these through a range of practices. These practices include explicit criteria to guide managers in applying subjectivity, calibration processes to standardise evaluations across several managers, and distribution curves to assign performance ratings and determine subsequent rewards. Interestingly, and despite the inherently subjective nature of the processes involved, these firm-level practices generate manager-level perceptions of ‘objectivity’. That is, the pervasiveness of subjectivity is largely hidden to managers despite (or perhaps because of) its prevalence. We identify evidence of the impact of subjectivity on a range of organisational outcomes. These outcomes include the perceived integrity of performance evaluation practice, leniency bias, favouritism, and the costs of communicating poor performance. We also identify the potentially high direct cost of subjectivity in PMRSs.

Overall, our study identifies an enormous amount of complexity within PMRSs that incorporate subjectivity. In particular, the findings from our study have the potential to inform managers about the ‘hidden’ layers of subjectivity in what are often construed as objective performance measurement and reward practices. While the nature of our study does not permit us to link the use of subjectivity to performance outcomes, our findings may prove of use in large-scale survey-based studies in which researchers seek to measure the relationships between different variables. In the following sections we present an abbreviated review of the academic literature on subjectivity in PMRSs, the research design for this study, and a summary of the results across the four companies studied. We conclude with practical considerations drawn from the results.
2. Subjectivity in performance measurement processes

2.1. What are objectivity and subjectivity in performance measurement and evaluation?
PMRSs usually contain elements of both objectivity and subjectivity. Objectivity in PMRSs is reflected in quantitative performance measurement and formulaic reward systems where for example, a certain level of sales performance achieves a pre-specified bonus result. Such measures or outcomes involve no judgement and can be verified by an external source. Objective measures are regarded as transparent and easier to implement. Perceived wisdom suggests that objective measures are therefore inherently preferable and that companies use subjective measures only when they are unable to obtain accurate or reliable objective measures.

Subjectivity is evident when managers rely on their opinions, perceptions or beliefs in making an evaluation. A critical characteristic of subjectivity is that it cannot be independently verified by a third party. For example, subjective measures such as ‘teamwork’ or ‘leadership behaviours’ are not objectively measurable. Subjectivity can also enter into PMRSs through the application of judgement to the scoring of performance on objective criteria. For example, a division’s performance may be measured by profit but an evaluator may subjectively assess the adequacy of the profit achieved, given actual circumstances facing the division during the period. Managers may also subjectively weight a range of objective and subjective performance measures or subjectively alter the level of bonus paid for a given performance. Thus the distinction is not always clear. In summary, quantified measures are not always objectively determined and subjectivity can occur in many parts of the performance measurement and reward process.

2.2. Why do firms use subjectivity in performance measurement and reward?
Objectivity has a number of deficiencies. For example, objective measures can be imprecise or incomplete. They can be regarded as unfair when for example, an employee’s performance is affected by uncontrollable or unforeseen events. The use of objectivity in performance measurement and reward can lead to unintended consequences, such as when employees take actions to improve measures that do not add value to the organisation (referred to as ‘gaming’). In extreme cases, as seen during the financial crisis, the pursuit of high rewards linked to objective targets can lead to the destruction of organisational value and the collapse of firms. Enron and Lehman Brothers are commonly cited examples of firms whose reward systems were directly implicated in their subsequent failure.
The use of subjectivity in PMRSs is regarded as a way of overcoming some of the problems with objective measures and evaluation because it gives managers more discretion in their evaluation of employees’ performance. It allows managers to ‘adjust’ for uncontrollable events, to discourage and penalise gaming, to reward ‘difficult to measure’ attributes of effective employees, and to recalibrate bonus allocation to achieve greater fairness.

2.3. What effects of subjectivity are documented in academic research?
Subjectivity can lead to increased perceptions of fairness when it is used to offset the problems associated with the use of objectivity, such as as adjusting for uncontrollable events. However, it can also result in undesirable outcomes. For example, managers may provide biased evaluations of their staff because they do not want to give negative feedback, or because of favouritism, or because they want to present themselves as a competent leader of good performers. Bias can be costly when a company pays unwarranted salaries or bonuses or when valuable, but demotivated, employees leave. For example, academic research documents evidence of general leniency in performance measurement that leads to the majority of employees being rated ‘above average’. Managers who fail to differentiate adequately among their subordinates impair the quality of information that is used to decide whether to give an employee greater responsibilities. Any bias which systematically over- or under-rates employees can have a real cost to an organisation if it obscures differences in performance between employees and leads to poor decisions around promotions or the assignment of tasks.

In summary, academic research has suggested that subjectivity in PMRSs can overcome some of the known problems with objectivity but also highlights several potential deficiencies in its use. However, empirical evidence on the use and effects of subjectivity is very limited.
3. Research questions and method

As the purpose of our study is to understand more about the role and impact of subjectivity in performance measurement processes, it was important to obtain data on different types of PMRSs. Our study employs a cross-sectional field study design, which enhances our capacity to identify recurring patterns across our field study sites and unique aspects that are associated with specific contexts. We selected firms from four different industries because PMRSs can often look similar among competitors within the same industry. The selection of firms from different industries is more likely to provide a larger variety in the way subjectivity is used. In our selection of firms to participate in the study, we required some level of subjective evaluation in the determination of performance-based rewards. This excluded, for example, settings in which bonuses are based on sales or allocated solely on the basis of job title or position.

We conducted in-depth semi-structured interviews with two hierarchical levels of managers in our four case firms in order to obtain information from both evaluators and evaluatees. All of the firms in our study are successful within their respective industries and none were seeking to change their existing performance measurement and evaluation processes. This provided a sound basis for examining the key influences and implications of their different approaches. In all four firms subjectivity is used to determine performance and make decisions about merit increases, promotions, and bonuses. Bonus pools in all of the firms are initially allocated by the firm’s executive management. In total, we interviewed 44 managers, spread evenly across the four firms. The length of interviews ranged from 23 to 61 minutes.

We used a qualitative data software package to code our data according to the sections contained within our interview guide as well as to identify additional themes that were raised by the participants. We obtained ethics approval from our respective institutions and informed consent from each of the firms involved. In the subsequent sections, all identifiers have been removed in order to preserve the anonymity and confidentiality of the firms and their employees.
4. Contextual background

Before presenting the findings from our study, we provide a brief overview of each of the firms from which we collected data. Table 1 summarises and compares the key features of each firm’s PMRS.

**EquipMan** is a global leader in equipment manufacturing. Two segments within one of the company’s several business units are the focus of this case study. EquipMan is a matrixed organization with each manager having a solid-line reporting structure to a segment head and a dotted-line reporting structure to a functional head (e.g., finance, quality, engineering, etc). The segment head (evaluator) evaluates manager (evaluatee) performance with input from the functional heads.

**FoodMan** is the subsidiary of a large multinational parent company. It has three business units – one regional and two product focused, and several functional support units including R&D and HR. Functional specialists operate within a matrix structure with both functional and product-group/regional accountability. Participants in the study are drawn from all subunits and a range of functions.

**AssetCo** is an international asset management firm. The focus of this study is a subsidiary with several hundred employees. The firm’s total bonus pool is determined by executive management and allocated to all teams including the support functions. The head of each team evaluates the team members and decides the allocation of bonuses. Our study includes participants from three different areas of the business.

**ProServ** is a multinational partnership operating in the professional services industry. It has three business units of which one, containing several hundred employees, forms the focus of this study. Work activity is based on discrete projects fulfilled by teams that exist only for the duration of each project.
### Table 1
Key features of the PMRS in each of our four case firms

<table>
<thead>
<tr>
<th></th>
<th>EquipMan</th>
<th>FoodMan</th>
<th>AssetCo</th>
<th>ProServ</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Number of goals</strong></td>
<td>6–12</td>
<td>6–8</td>
<td>2–8</td>
<td>12–18 in 6 main categories</td>
</tr>
<tr>
<td><strong>Evaluation of behaviours</strong></td>
<td>Separate from goals</td>
<td>Separate from goals</td>
<td>Integrated with goals</td>
<td>Integrated with goals</td>
</tr>
<tr>
<td><strong>Use of a performance rating</strong></td>
<td>1–3</td>
<td>1–5</td>
<td>Nominally 1–5 but not used</td>
<td>1–4</td>
</tr>
<tr>
<td><strong>Bonus as a proportion of base salary</strong></td>
<td>Small</td>
<td>Moderate</td>
<td>High</td>
<td>Moderate</td>
</tr>
<tr>
<td><strong>Use of a bell curve</strong></td>
<td>✓</td>
<td>✓</td>
<td>–</td>
<td>✓</td>
</tr>
<tr>
<td><strong>Use of an advisory distribution curve</strong></td>
<td>–</td>
<td>–</td>
<td>–</td>
<td>✓</td>
</tr>
<tr>
<td><strong>Calibration committee</strong></td>
<td>✓</td>
<td>✓</td>
<td>–</td>
<td>✓</td>
</tr>
</tbody>
</table>
5. Results

In this section we present and discuss the main findings arising from our study. We organise this section according to those key themes of particular interest in relation to current knowledge in this area. Due to the richness of the data we collected, themes incorporate both of the research questions as presented in the Introduction. At the end of this section we also provide summary information in tabular form. Table 2 compares the extent of subjectivity and discretion across our four case firms while Table 3 summarises the impact of subjectivity in each firm.

5.1. The extent of use of subjectivity

All firms in our study use subjectivity in a range of ways including the use of subjective measures of performance, the negotiation of targets, and the assessment of performance on specified metrics.

‘You might give yourself a target of “I will make contact with two new clients” but you don’t go back and say “well, I only talked to one, so I get half marks”. It’s not like that.’ (ProServ)

In one firm (AssetCo) each team manager is allocated a bonus pool and has discretion over how they distribute this among their team members. In the other three firms there is considerable subjectivity in the determination of individual performance ratings, although FoodMan has the most formulaic approach of the four firms. Explicit weightings are attached to each element included in the performance evaluation.

‘So 70% of my remuneration is regional, 30% is the business unit, and that is just multiplied out. Then the individual performance multiplier is applied to that. So if the business and regional business get 100%, and an individual has an “exceeds” rating it multiplies out by 1.2–1.5.’ (FoodMan)

Key finding: subjectivity can be incorporated into many elements of a firm’s PMRS.

5.2. Justification for subjectivity

We find that subjectivity in PMRSs is a largely purposeful element, deployed for reasons beyond those associated with the deficiencies of objective approaches. Of critical importance to each of the firms in our study is a desire to balance the attainment of short-term goals with behaviours that will also support the firm’s longer-term aims. This manifests as a trade-off between the ‘what’ and the ‘how’ of goal attainment. Regardless of the nature of their business, the firms in our study eschew high levels of objectivity in the selection of measures and targets and in the evaluation of performance. There is strong recognition that objective criteria will fail to capture many important aspects of performance that deliver value to the business.
‘Those objectives are in order to stimulate the behaviours that we want as opposed to saying “he has had 19 meetings and 45 phone calls”.’

(ProServ)

A significant influence in the use of subjectivity is its flexibility as a tool for promoting fairness in the distribution of rewards while simultaneously supporting the long-term goals of the firm. For example, subjectivity enables managers to carry out three tasks.

It gives them the flexibility to adjust for uncontrollable events:

‘Things change and there are surprises, exceptions, challenges, changes in the business, those types of things.’ (FoodMan)

Subjectivity also enables them to capture the long-term potential of employees:

‘I also think about the potential of the individual, so their worth to me on a scale of one to ten [is] probably four. But actually they’re taking all their exams, they’re clearly bright, they clearly want to move, then … I may actually have to overpay them for a couple of years, [because] I want to keep them here.’ (AssetCo)

Finally, the use of subjectivity enables them to assess difficult-to-measure performance qualities:

‘How much have you cost us this year in an error? Was it something you weren’t in control of and it would have happened anyway, or how proactive were you in putting in a control?’ (AssetCo)

In comparison, objective processes were perceived as too inflexible.

‘If the manager is close to the people who work the process, the manager will be aware of subtle demonstrators that aren’t formulaic. I’ve been really able to motivate or use that as a tool to really reward or recognise somebody that’s done outstanding work.’ (EquipMan)

‘You’ve got developing people who are only on a “quarter bean” and now they deserve “three quarters of a bean”, and your pot hasn’t grown … as soon as you become quantitative you couldn’t adjust for all those sorts of things.’ (AssetCo)

‘It’s probably the best that I’ve participated in of all the organisations I’ve worked in and the main reason for that is the flexibility, but the fact that it’s not flexible enough to reward poor performance. And it’s very clear what “good” looks like … I’ve worked in other businesses whether you either hit the P&L or you don’t: if you miss it by a couple of percentage points you get nothing, if you hit it you get everything and I have seen that is a demoralising way of bonusing people.’ (FoodMan)

‘You could have someone in the regions, who has worked on a job in London alongside London colleagues, and they get the same rating, but because they’re on a regional salary, their bonus is lower … that’s not really fair.’ (ProServ)

Key finding: subjectivity offers flexibility in evaluating and rewarding employees.
5.3. Hidden discretion behind formulaic bonuses

In one of our cases (AssetCo), bonus allocation is acknowledged to be completely discretionary. In the other three companies, bonus determination is quite formulaic. Explicit weightings on corporate, business unit and individual performance multipliers are applied to elements of the formula. Managers then average a range of scores to arrive at a single numeric score which then translates directly into a bonus allocation. The extent to which subjectivity influences bonus determination is often not well understood by participants but instead emerged through discussion during the interviews. Firm-level processes increase the perceived objectivity of the PMRS in each of these companies.

‘When you talk about discretion, I’m not sure what you mean …
if you take it to its extreme, subjectivity is not at all relevant because
it all comes down to something that is empirical.’ (ProServ)

‘There is discretion, but it is within small bounds.’ (FoodMan)

While subjectivity is pervasive in the four PMRSs we studied, we find that the nature of firm-level practices generates manager-level perceptions of ‘objectivity’ in inherently subjective processes such as the assignment of performance ratings to individuals. The use of rating guidelines, bell curves and calibration panels are all important in creating an impression of objectivity. Overall, the perception of objectivity within these firms is probably overstated given the amount of subjectivity that enters into the choice of measures, the setting of targets and the subsequent rating and weighting of performance.

Key finding: the extent of subjectivity can be taken for granted by those closely involved in its use.

5.4 Perceptions of transparency

The use of subjectivity throughout the various stages of the evaluation process is not hidden from employees. However, there is considerable variation in perceived transparency in the determination of ratings and performance-based rewards.

‘There aren’t a set of neat KPIs, much to people’s annoyance, where
you can say, “if I do X, Y and Z I’ll get that rating”.’ (ProServ)

‘At our level, it’s probably 70% leadership skills and 30% actual results. That’s just my gut opinion on how those are evaluated. I think that probably varies from leader to leader, depending on how much emphasis they put on the “how” and not the “what”. I think that’s one piece that probably is inconsistent.’ (EquipMan)

Transparency influences perceptions of fairness:

‘I trust that the process is fair because it’s not overly complicated.’
(AssetCo)

Two of the firms demonstrate relatively low transparency in both the determination of performance ratings and rewards. ProServ has just a single rating for overall performance and AssetCo doesn’t require managers to use a rating at all. Participants in EquipMan and FoodMan are confident that they understand initial ratings but feel that the calibration process is more opaque.
Complete transparency is difficult to achieve with high levels of subjectivity or
discretion in performance ratings and rewards.

Key finding: perceptions of fairness are enhanced by transparency and trust.

5.5. The use of calibration committees and advisory distributions
to reduce bias

One reason for the relatively high levels of trust and perceived fairness in our firms
is the use of calibration committees. These committees play a vital role in reducing
bias among a group of evaluators in the assignment of performance ratings and
subsequent allocation of rewards:

‘… to make sure everybody’s exercising the same level of fairness and
judgement.’ (ProServ)

They achieve this by standardising subjectively derived performance ratings across
a specific group of evaluatees.

‘You’ve got a sticky label for every single person. You can imagine
drawing that bell curve on there, moving people around based on
other people’s input. It’s important to go into the review well armed
with evidence-based discussion points on performance.’ (EquipMan)

However, the capacity of calibration committees to reduce bias is influenced by
the extent to which evaluators are able to argue the case for particular employees.

‘There can be differences in who’s the partner who looks after you,
how loud does he shout in a meeting, how cross does he get, does he
attend?’ (ProServ)

Advisory distribution curves are used to classify employees into broad groups
based on their performance. The majority of discussion revolves around those
employees at the margins, which can be up to 10% of the total group. In these
situations, reversion to objective measures of performance is one way to reduce
the potential for bias.

‘What is the first measure of moving somebody in a moderation
process? It’s not the measures around good behaviour and good
corporate citizen, it’s “this person’s utilisation was 60% and this one’s
was 55”.’ (ProServ)

Calibration appears to introduce ‘objectivity by consensus’ and it assists with the
formulation of evidence-based subjective performance assessments.

‘If you’re one of those folks that, you know, everybody you got is
fantastic. You’ve got to sit in that room and tell your peers why Joe
and Jane are so much better than John and Sue. And you force the
dialogue back to things that are specific to what that employee has
done. So I have to come in and be able to say, “here’s why, do you
agree?”’ (EquipMan)

Key finding: calibration committees can reduce perceptions of bias.
5.6. The costs of subjectivity

The use of subjectivity can have a high hidden cost. This cost is evident in many elements of the process. For example, direct costs are involved in: the negotiations between evaluator and evaluatee to agree upon appropriate goals, measures, and targets; the efforts of both evaluator and evaluatee to collect evidence about the evaluatee’s performance; the use of appraisal meetings to discuss performance in relation to subjective criteria; the aggregated time spent in calibration committees; the training on appraisal and evaluation processes; and any ongoing conversations between evaluator and evaluatee during the year to manage and align expectations in relation to subjective goals or measures. The wide range of approaches among our four case firms indicates significant differences in the total cost associated with the use of subjectivity. However, the managers in our study appear largely indifferent to these costs. This indicates that they view the processes in their respective firms as supportive of its overall aims, and thus take them largely for granted. However, another interpretation is that these processes provide a vital means for managers to exchange information about the activities and performance achieved by employees. Additional information about employees can lead to reduced levels of uncertainty, more effective HR management, fewer errors in compensation and promotion, and better harnessing and retention of talent within the firm.

Key finding: firms are largely unaware of the full direct cost of incorporating subjectivity into their PMRSs.

5.7. The costs and management of communicating poor performance

Communicating poor performance is an indirect cost associated with the use of subjectivity in PMRSs. These ‘confrontation’ costs are driven by the time required to collect evidence and conduct meetings to justify the outcomes of the performance evaluation process. They manifest when evaluators or evaluatees experience adverse psychological effects associated with the communication of poor performance. The imposition of ratings and an advisory distribution curve to differentiate employees can automatically generate confrontation costs because evaluatees who receive a lower rating than anticipated are more likely to request additional evidence to understand the decision. Calibration committees can reduce this cost by enabling evaluators to communicate final decisions about rating and rewards as an ‘objective’ outcome achieved through consensus.

‘The same thing that makes it difficult for managers to give courageous and constructive feedback to individuals makes it hard for some managers to not write their direct reports as superstars. And you need a process of some kind ... let’s get around a table and we do it [calibration] in two ways, we do it within each function and then the senior management team does it across functions.’ (FoodMan)

Key finding: costs of confrontation can be reduced by the use of firm-level practices that induce ‘consensus’.
### Table 2
Extent of subjectivity and discretion in the performance measurement and reward process across each of our four case firms

<table>
<thead>
<tr>
<th></th>
<th>EquipMan</th>
<th>FoodMan</th>
<th>AssetCo</th>
<th>ProServ</th>
</tr>
</thead>
<tbody>
<tr>
<td>Discretion to choose performance measures</td>
<td>Medium (negotiated with evaluatee)</td>
<td>Medium (negotiated with evaluatee)</td>
<td>High</td>
<td>Medium (negotiated with evaluatee)</td>
</tr>
<tr>
<td>Subjective assessment of measures (both qualitative and quantitative)</td>
<td>High and implicit</td>
<td>High and explicit (ie, reported separately)</td>
<td>High and implicit</td>
<td>High and implicit</td>
</tr>
<tr>
<td>Subjective weighting of each measure</td>
<td>Implicit</td>
<td>Explicit, set at firm level</td>
<td>Implicit</td>
<td>Implicit</td>
</tr>
<tr>
<td>Subjective rating of final performance</td>
<td>Medium (verified by calibration committee)</td>
<td>Medium (verified by calibration committee)</td>
<td>High</td>
<td>Medium (verified by calibration committee)</td>
</tr>
<tr>
<td>Discretion to adjust rewards prior to payout</td>
<td>Low</td>
<td>Low</td>
<td>High</td>
<td>Medium</td>
</tr>
</tbody>
</table>

### Table 3
Impact of subjectivity in PMRSs on our four case firms

<table>
<thead>
<tr>
<th></th>
<th>EquipMan</th>
<th>FoodMan</th>
<th>AssetCo</th>
<th>ProServ</th>
</tr>
</thead>
<tbody>
<tr>
<td>Potential for bias in performance evaluation</td>
<td>Low</td>
<td>Low–medium</td>
<td>High</td>
<td>Low–medium</td>
</tr>
<tr>
<td>Potential for bias in bonus awarded</td>
<td>Low–medium</td>
<td>Low–medium</td>
<td>High</td>
<td>High (partners make adjustments)</td>
</tr>
<tr>
<td>Perceptions of gaming</td>
<td>Medium</td>
<td>Low</td>
<td>Low</td>
<td>Low-medium</td>
</tr>
<tr>
<td>Time/effort involved (inferred cost)</td>
<td>Medium</td>
<td>Medium</td>
<td>Low</td>
<td>High</td>
</tr>
<tr>
<td>Perceptions of fairness/transparency</td>
<td>High trust in the process</td>
<td>High trust in the process</td>
<td>High trust in the evaluators</td>
<td>High trust in the process</td>
</tr>
<tr>
<td>Confrontation costs (evidenced by complaints or staff turnover)</td>
<td>Low</td>
<td>Low</td>
<td>Low</td>
<td>Low</td>
</tr>
</tbody>
</table>
The findings from our study indicate that the use of subjectivity within an organisation can be both highly pervasive and implicit. The information contained in Tables 1 and 2 hints at the enormous complexity in each firm’s PMRS, and in the difficulties involved in attempts to focus on any one element without a full understanding of the interactions with other components. While new approaches and modifications to PMRSs are often the responsibility of HR departments, close involvement from the finance function is critical to ensure that performance measurement and reward processes are cost effective and congruent with the organisation’s long-term goals. In the remainder of this section we provide a list of practical considerations for firms when incorporating subjectivity in their PMRS. We begin with a set of questions for managers that encourages them to consider their understanding of the role and use of subjectivity in their firms. We finish the section with some broader organisational issues related to the design of PMRSs.

6.1. Checklist for managers

- Can you identify all points at which subjectivity enters the performance measurement and reward process?
- Can you articulate the reasons for the use of subjectivity at different points in the process?
- What are the direct costs involved in operating your PMRS?
- Do your employees have a consistent understanding of your PMRS?
- Where do potential sources of bias arise and how do you mitigate them?
- What are the potential sources and costs of communicating poor performance (confrontation costs) and how do your performance measurement and reward processes seek to mitigate these?

6.2. Action points for organisations

- Assess the reasons for incorporating various aspects of subjectivity in your PMRS and consider articulating them in training manuals and workshops.
- Achieve as much transparency as possible in the various stages of the process.
- Avoid using quantitative proxies for inherently subjective performance qualities – evaluatees understand subjectivity and accept it if it is used fairly, consistently and predictably.
- Ensure that there are clear criteria for subjective measures.
- Ensure that there are explicit criteria for applying subjectivity or discretion.
• Identify and seek to address potential sources of bias at various points in the performance measurement and reward process.

• Consider the pros and cons associated with ranking employees’ performance – such an approach is not always necessary.

• Consider carefully the potential effects of different ranking systems (eg, 1–4 or 1–5).

• Consider the pros and cons of using an advisory distribution curve – such an approach is not always necessary.

• Consider the pros and cons of using a calibration committee – such an approach is not always necessary.

• Consider the bias introduced into calibration committees by managers with greater influence or a stronger voice than others.

• Ensure that supporting evidence for subjectively assessed performance is drawn from appropriate sources.

• Consider the optimum split between centralised versus decentralised decisions eg, a formulaic approach to the determination of performance ratings or rewards versus managerial discretion.

• Consider the impact of subjectivity on perceptions of trust and fairness.

• Consider whether the same outcomes could be achieved with a simpler (ie, less costly) PMRS.

• Ensure that evaluators are aware of the various interactions between different subjective elements of the PMRS.

• Consider carefully the unintended consequences of making modifications to any aspect of the process.
A PMRS can have a significant impact on a company's performance. It is therefore essential that a firm implements a PMRS which elicits performance consistent with its goals. Objective performance measurement is not an end in itself. Subjectivity or discretionary components can play a key role in creating a congruent PMRS which rewards both short-term and long-term value-enhancing effort by employees throughout the firm. It is important that the design is purposeful in its use of both objectivity and subjectivity and that it reflects an assessment of the relative costs and benefits. Many of the costs of confrontation, consultation, calibration, communication and complexity are implicit. These costs also tend to increase with the level of subjectivity/discretion in the PMRS. Nonetheless, they need to be assessed against the costs of excessive reliance on objective PMRSs, which include a short-term focus, gaming of performance measurement and an instrumental rather than value-enhancing culture.

In summary, our findings enrich and expand on prior research by describing the use, role, costs and benefits of subjectivity from the perspective of participants in the performance measurement and reward process. The findings from our study challenge current thinking about optimal PMRS design including the presumption of inherent preferences for objectivity, the assumed relationship between subjectivity and bias, and the limited role for subjectivity within performance-based reward systems. We also identify a range of firm-level practices that mitigate the downside of subjectivity and support the use of informed discretion.

Finally, the firms in our study are successful within their respective industries. While evidence from successful firms is arguably more relevant to managers seeking to improve current practices, it inevitably limits our ability to explore whether specific elements of the PMRS are associated with variations in performance. We also acknowledge the potential for bias in the selection of participants, who were chosen by our initial contact in each firm. However, participants were not uniformly satisfied with all aspects of their PMRS and we have attempted to capture some of that in this briefing. This was an exploratory study in an area about which little empirical research exists. We also hope that the findings from this study will prove of use in survey-based studies in which researchers can measure the strength of relationships between different elements of PMRSs across a wide variety of firms.
Additional reading


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Dr Julia Mundy is a Senior Researcher at the Centre for Governance, Risk and Accountability at the University of Greenwich in the area of performance measurement and management. With publications in top academic journals and practitioner experience in investment management and financial services, she has advised firms in the fields of publishing, financial services and social housing. Julia is a member of the Research Advisory Board of ICAEW and Secretary of the Management Control Association, a network for academics and practitioners interested in performance measurement and management.
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