DEVELOPING PERFORMANCE APPRAISAL AND PAYMENT DETERMINATION PROCESSES IN SAP - CASE KELA

Information Systems Science

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Elisa Saarela

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ABSTRACT

Objectives of the study

Research problem of this study is to find answers to the question of how performance appraisal and payment determination processes can be combined as a process and as an IT-tool in SAP. This study also introduces how case company Kela have performed this combination. In addition, this study gives further information regarding whether the benchmarked companies are combining appraisal and payment determination processes, and what are their experiences regarding the combination / non-combination, as well as how their IT-tools support these processes.

Academic background and methodology

Earlier literature introduced in this study provides background information to the topic, including support and criticism regarding should payment be linked to performance. Methodology of this research is a case study. In addition, this research has also elements of Action Design Research (Sein et al.,2011). Qualitative empirical study includes benchmarking of four companies. Scope of the benchmark study is companies who are utilizing SAP in performance appraisal or who have experience in combining the performance appraisal and payment determination processes.

Findings and conclusions

There exists both support and criticism regarding should payment be linked to performance. Psychological and economic theories supporting the linkage of performance and payment imply that combining payment and performance would enhance the individual employees' performance. According to critics, payment is not the main motivator for employees, but job satisfaction can be derived from eg. responsibility, recognition or optimal amount of challenges. It seems that no single truth is available to the questions whether pay should be linked to performance. In addition, it seems that linking pay to performance in public sector is more challenging than in private sector. Within the benchmarked companies, there exists more support for keeping payment and performance as separate process, including separate discussions.

Keywords

Performance appraisal, payment system, payment discussion, payment determination, e-HRM, SAP, pay-for-performance, HR, HRM

ABSTRAKTI

Tutkimuksen tavoitteet

Tutkimuksen tavoitteena on vastata kysymykseen miten kehityskeskustelu- ja palkanmääritysprosessit voidaan yhdistää yhdeksi prosessiksi, keskusteluksi sekä yhtenäiseksi IT-työkaluksi SAP:ssa. Tässä tutkimuksessa esitellään miten Kela on toteuttanut tämän yhdistämisen. Tutkimuksen empiirisessä osassa selvitetään ovatko haastatellut yritykset yhdistäneet edellä mainitut prosessit, mitä kokemuksia niillä on prosessien yhdistämisestä tai erillään pitämisestä, sekä miten IT-työkalut tukevat näitä prosesseja.

Kirjallisuuskatsaus ja metodologia

Kirjallisuuskatsauksessa annetaan taustatietoa aiheesta, kuten esitellään prosessien yhdistämistä tukevaa materiaalia sekä yhdistämiseen kohdistuvaa kritiikkiä. Tutkimuksen metodologia on tapaustutkimus. Tutkimuksessa on myös elementtejä ns. Action Design –tutkimukseen (Sein et al., 2011). Kvalitatiivinen empiirinen tutkimus sisältää neljän yrityksen benchmark -haastattelut. Benchmark -haastattelujen kohderyhmänä ovat yritykset, jotka käyttävät SAP:ia kehityskeskusteluissa tai joilla on kokemusta kehityskeskustelu- ja palkanmääritysprosessien yhdistämisestä.

Tulokset ja päätelmät

Suoriutumisen ja palkan linkittämiseen kohdistuu sekä tukea että kritiikkiä. Yhdistämistä puoltavien psykologian ja taloustieteiden teorioiden mukaan yhdistäminen lisää yksittäisten työntekijöiden tehokkuutta ja suoriutumista. Kriitikot puolestaan väittävät, että palkka ei ole työntekijän ainoa motivaattori, vaan työtyytyväisyyttä voi lisätä myös esim. vastuunanto, tunnustus tai sopiva määrä haasteita. Vaikuttaa siltä, ettei yhtä totuutta löydy kysymykseen pitäisikö palkka määräytyä suoriutumisen mukaan vai ei. Vaikuttaa myös, että suoriutumisen ja palkan yhdistäminen on julkisella sektorilla haastavampaa kuin yksityisellä sektorilla. Tutkimuksen kohdeyrityksissä palkka ja suoriutuminen on koettu parhaaksi pitää erillisinä prosesseina sekä palkkakeskustelut omana aiheenaan kehityskeskustelun ulkopuolella.

Avainsanat

Kehityskeskustelu, palkkausjärjestelmä, palkkakeskustelu, palkanmääritys, e-HRM, SAP, HRM

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LIST OF ABBREVIATIONS

KELA = Kansaneläkelaitos (FI) Folkpensions-anstalten (SE), The Social Insurance Institution of Finland (EN)

HR = Human Resources

HRM = Human Resources Management

e-HRM = IT-based Human Resources Management

TAM = Technology Acceptance Model

ESS = Employee Self Service functionality in SAP

MSS = Manager Self Service functionality in SAP

1. INTRODUCTION

1.1. Background and motivation

Performance appraisal is formal discussion between employer and employee with the aim of evaluating the performance of the employee (Murphy and Cleveland, 1995). On the other hand in payment discussion, the work, work performance and payment are discussed in order to evaluate their equivalence, that is, does the work and performance match with the payment (Palkkakeskustelut Suomessa, 2011).

In Kela, which is the The Social Insurance Institution of Finland the appraisal and payment determination processes have historically been separated both in process and in system wise. In practice, these two discussions have been held at different occasions and by utilizing different SAP functionalities. However, the decision from HR department was to combine these processes in process wise as well as in SAP, which is the IT-tool used in these processes. Project regarding the combination started in autumn 2013 and the technical part in the beginning of 2014. The new combined process and IT-tool supporting it, both which are introduced in this thesis, have been in use since January 2015.

In Kela it is believed, that the common process and functionality supports goal orientation, the management of performance and expertise, and the work welfare. In addition, the information transfers to other needed systems (eg. payment system) automatically. (Norra, 2014)

This research gives benchmark information for Kela's HR and IT management about how the benchmarked companies are handling the appraisal and payment determination process both in process wise and as a technical solution. With this information, Kela can evaluate the possible next steps of developing their process and system in relation to the appraisal and payment determination process. In addition to the information derived from the benchmark study, this research introduces also the theoretical background regarding the topic including the debate should payment be linked to performance or not.

1.2. Objectives and scope

Research problem of this case study is: ***How performance appraisal and payment determination processes can be combined as a process and as an IT-tool in SAP?***

Aims of the benchmark study are to give further information regarding:

- Whether benchmarked companies are combining appraisal and payment determination processes
- What are their experiences regarding the combination / non-combination & how the case companies have built the technical solution in relation to this process

In addition, the literary review section provides background information regarding the topics of performance appraisal, payment determination, pay-for-performance and also the critics as well as support towards linking pay with performance.

Scope of this study is companies who are utilizing SAP in performance appraisal or who have experience of combining the performance appraisal and payment determination processes and/or IT-tools.

1.3. Research design and methodology

Methodology of this research is a case study. Qualitative empirical study includes benchmarking of four companies, which are introduced later on in chapter 4.1.

Kela has established guidelines and principles for benchmarking and these are followed in the benchmarking process. These guidelines consists of permission for benchmarking, guidelines for information exchange, communication with benchmarked company, preparations and execution, as well as what information can be shared and how. In addition to guidelines regarding benchmarking, Kela has also established a benchmarking process, which is followed in the case study. This process is introduced in chapter 4.

In addition to case study, the research has also elements of Action Design Research. Sein et al. (2011) define Action Design as a research method focused on building, intervention and evaluation of artifacts in the organizational setting. It deals with both theory and influence of users of the IT artifact.

1.4. Empirical study

Criterions for benchmark selection were that the company should use SAP in performance appraisal and/or the company should have experience of combining performance appraisal and payment discussions. Several companies were found that are utilizing SAP in performance appraisal. From those companies three companies were chosen. One company was found that had experience of combining the performance appraisal and payment determination. Luckily, that company is also a public organization. Since three out of the four benchmarked companies wished to stay anonymous, all the companies are handled as anonymous in this study.

1.5. Results

Concerning discussion of should payment issues be linked with performance, there exists both support and resistance to the topic. It seems that the success of the combination is also heavily related to the payment system and organization. According to research performance appraisals are considered to be more effective in cases where the outcome of the results were linked to payment determination (Lawner, 2003). According to other research, merit pay was more related to improved employee attitudes than improved performance (Heneman and Werner, 2005). There exist both psychological and economic theories supporting the linkage of performance and pay implying that the combination of the payment and performance would enhance the individual employees' performance and by that increase the overall performance of the organization (Maanieniemi, 2013). As well as support, also criticism is found towards linking pay-to-performance, including eg. that payment is not the main motivator for employees, but job satisfaction can be derived from eg. responsibility, recognition or optimal amount of challenges. (Maaniemi, 2013). It seems that no single truth is available to the questions whether pay should

be linked to performance. In addition it seems, that linking pay to performance in public sector seems to be more challenging than in private sector. This is because lack of clear linkage between performance and outcome, as well as lack of funding for rewarding good performance (Ingraham, 1993). In addition in public sector managers do not have enough flexibility, legitimacy and control over the budged, and employees in the public sector may be motivated better by other means than actual monetary payment(Ingraham, 1993).

Main finding of this research, based on the benchmark study is that there seems to exists more support for keeping payment and performance as separate topic and process, including separate discussions. This finding is based on the experiences of the case companies regarding separate and joint discussions. It should be however noted, that even though the performance appraisal and payment discussions were separated into two discussions in one of the case companies, there exists still strong link between performance and payment since the targets are set in the payment discussions.

This study has limitations among others what comes to generalizability of the results due to small sample size. Topic of combining performance appraisal and payment discussion definitely needs further investigation both from public as well as private sector.

1.6.Structure of the thesis

This thesis is structured as follows. Chapter 1 provided an introduction to the topic, including overview regarding background and motivation, objectives and scope, research design and methodology, empirical study, and summarized the main results. Chapter 2 builds a theoretical foundation for the study by defining more thoroughly the main concepts including performance appraisal, payment discussion and pay-for-performance. It also includes theoretical background regarding how knowledge of pay and payment system satisfaction affect to performance and introduces the psychological and economic theories supporting linking pay to performance as well as critics towards the linkage. In chapter 3, the performance appraisal and payment determination of Kela is introduced including the introduction to the new combined process and IT-tool as well as reasoning behind the combination. Chapter 4 introduces the research problem

and methodology and provides introduction to the benchmark company selection. Chapter 5 includes the empirical study, containing introduction to the performance appraisal and payment determination of the benchmarked companies. Chapter 6 summary and discussion as well as limitations and the suggestions for the future research. The benchmark questions are included in Appendix A.

2.   LITERATURE REVIEW

2.1. Performance appraisals –what and why?

Performance appraisal is a formal discussion between employer and employee with the aim of evaluating the performance of the employee (Murphy and Cleveland, 1995). According to Grote (2002) performance appraisal can also be called in other terms, such as performance assessment, performance evaluation and performance review. Performance appraisal serves a variety of different purposes including target setting and measurement, providing feedback, evaluation of training and personal development needs and goals, and evaluation of performance, possible compensation changes as well as possible promotions (Grote, 2002). In addition, performance appraisal process can include topics related to eg. work planning and succession planning (Grote, 2002).

Sources of performance appraisal information are employees' personal qualities as well as how he/she masters the job. Thus, the criterions for performance evaluation are personal capabilities as well as professional expression. Performance appraisal methods can be qualitative (non-numerical data) or quantitative (numerical data). Figure 1 sums the performance appraisal sources, criterions and methods. (Chen and Fu, 2008)
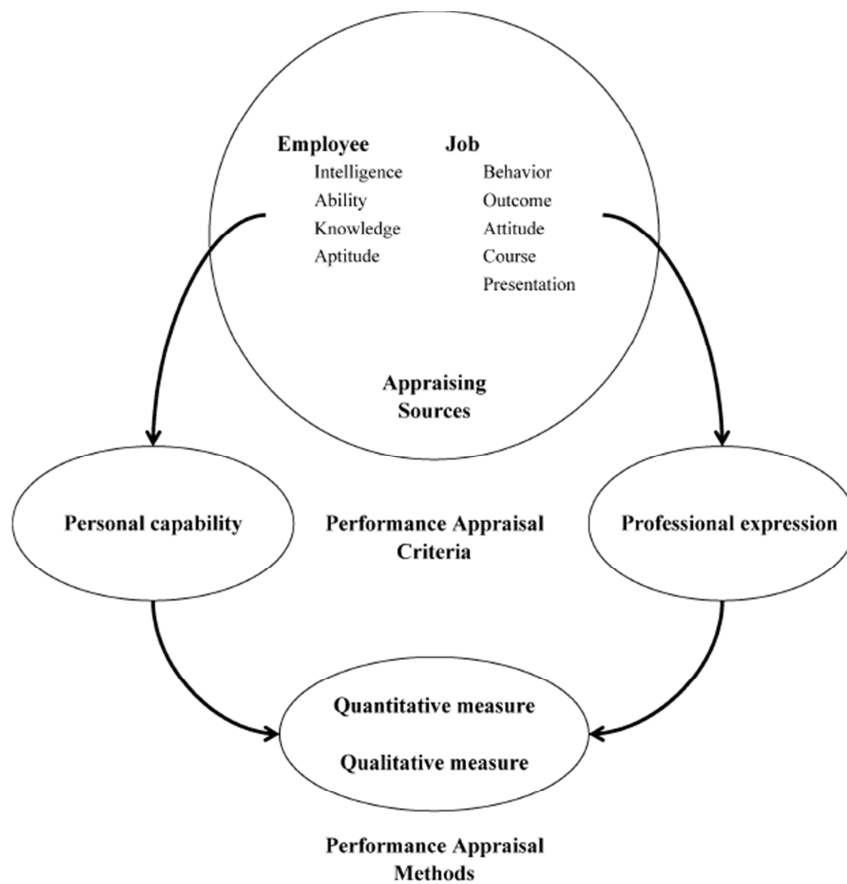
Figure 1 Performance appraisal sources, criterions and methods (Chen and Fu 2008)

According to Grote (2002) the performance appraisal process is often considered to include four steps consisting of:

1. Performance planning
2. Performance execution
3. Performance assessment
4. Performance review

Often these one-on-one meetings between employee and employer are held twice a year, consisting of performance planning for the coming period and performance assessment of the past period. It is however recommended, that at least one review is held during the assessment period. (Grote, 2002)

Despite of its benefits, performance appraisal is often considered as frustrating constraint that takes time and effort but does not bring any actual value. Reasoning behind these perceptions and the resistance both from employer and employee side can be related to poorly managed appraisal process or system for handling the appraisals. One way to enhance the appraisal system and at the same time increase the motivation among employees is to include them into the development of the appraisal system and that way increase the acceptance of the system. This increases feeling of job-related autonomy, gets the employee's voice heard, increases their acceptance to the performance ratings, enables the utilization of performance information possessed by the employees, and increases the collaboration and support from personnel towards the system. (Mulvaney et al., 2012)

2.2. Performance appraisal and payment system as part of overall business strategy

Performance management system and performance appraisals should be heavily linked to the organization's strategy, which should set the direction of the company as well as long-term goals and plans. Based on these goals and plans organization's overall objectives should be formulated and cascaded to each unit and finally to each employee optimally resulting in a situation where everyone has objectives supporting the unit strategy and by that way the overall organization strategy. (Grote, 1996)

Chen and Kuo (2004) note, that in addition to the need to ground performance appraisal to organization strategy, the organization should also understand its strengths before designing the performance appraisal system. In order to establish performance appraisal system to support organization's strategy and competitive advantage Chen and Kuo (2004) propose three steps as illustrated in Figure 2 to be taken into consideration. These include identification of competitive status, setting the strategy, and aligning performance management system based on these. Identification of the competitive status includes analysis of the strengths and weaknesses of the competitive environment. Setting strategies includes formulation of corporate strategy and HR strategy as well as identifying the needed employee behavior to support them. Finally, in the

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performance management aligning stage the performance criteria and type of performance appraisal method are chosen. (Chen and Kuo, 2004).
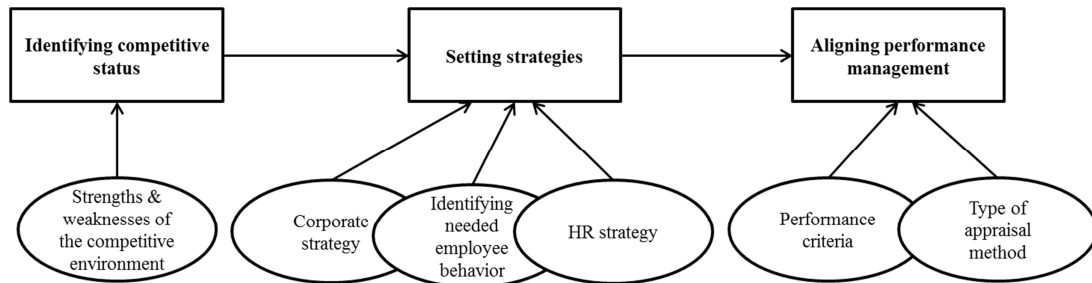
Figure 2 The Process of performance management (Chen and Kuo, 2004)

In addition to performance management system and performance appraisal, also compensation strategy, including compensation in forms of both monetary and non-monetary incentives and benefits is essential in supporting the fulfillment of organization's overall objectives. Methods of compensation can be either extrinsic (eg. salary, promotion, retirement plans, stocks) or intrinsic (eg. respect, relationship, achievement). (Chen and Fu, 2008)

Payment system as part of compensation strategy should support the overall management system of the organization and by that way support the personnel to aim and to achieve the overall targets of the organization. Without this linkage, the payment system does not possess enough meaning. (Huuhtanen et. all, 2005)

Figure 3 by Lawler (1990) illustrates the linkage of strategy, structure, rewarding, personnel and processes to the competitive advantage of a company.
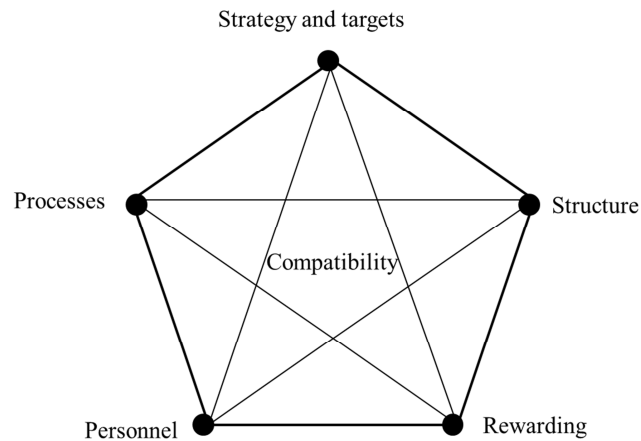
Figure 3 Linkage between strategy, structure, rewarding, personnel, processes and competitive advantage (Lawler, 1990)

2.3.Payment discussions – what and why?

Payment discussion is a discussion held with every employee and in this discussion the work, work performance and payment are discussed in order to evaluate their equivalence, that is, does the work and performance match with the payment. In Finland the payment discussion is often mixed with payment raise discussion, although the payment discussion is not merely about applying for payment raise. (Palkkakeskustelut Suomessa, 2011)

Payment discussion originates from the Nordic countries from mid-1990s. In 2008 in Finland only appr. 20% of the white collar and upper white collar employees and 10% of the blue collar employees had payment discussions with their supervisors. This is muss less than the percentage of employees included in the annual performance appraisal discussions (white collar and upper white collar appr. 90% and blue collar appr. 50%). Statistics of payment discussions in Finland are compiled in Figure 4. There has been found evidence between companies utilizing payment discussions and the increase in their productivity. This link has traditionally been explained by the incentive effect created by linking increased performance with better payment. Payment discussions also increase the payment knowledge (discussed more in chapter 2.5) and help matching payment with the actual work effort. (Palkkakeskustelut Suomessa, 2011)
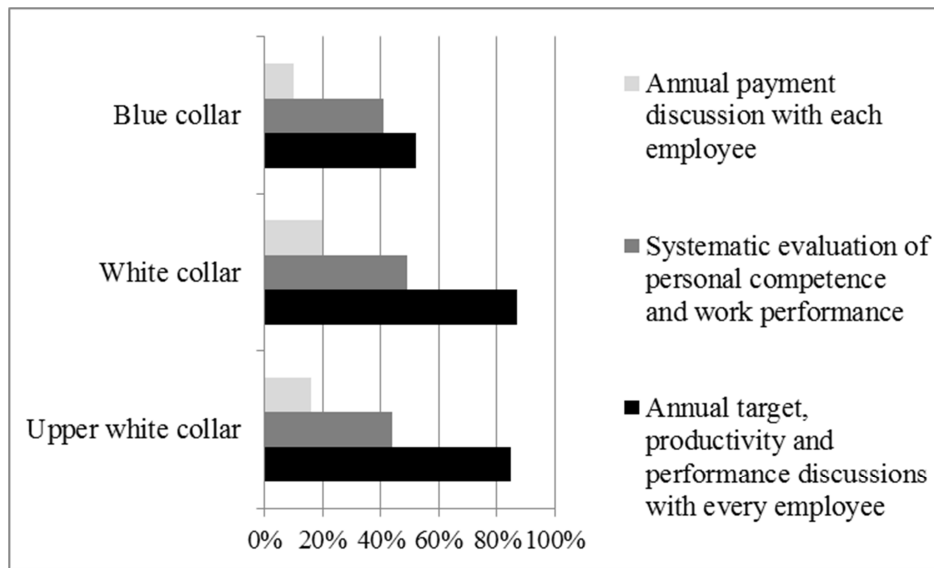
Figure 4 How employees' competence and performance was evaluated in Finland in 2008. (Palkkakeskustelut Suomessa, 2011: EK:n palkkausjärjestelmätiedustelu 2008)

Criticism and benefits of linking payment and performance discussions are more thoroughly discussed in 2.4.1, but without payment discussions several companies have lacked means and process for discussing payment topics apart from the pay discussion held when new employee is hired. Payment discussions can help this deficiency by fostering communication between employee and manager and emphasize supportive and fair payment of all employees of the company. (Palkkakeskustelut Suomessa, 2011)

There has been a lot of discussion among should payment be discussed simultaneously with performance. Fear has been that the payment as a topic will draw the employees' attention from other issues and hinder the performance discussion by some means. Pros and cons of combining the performance and payment discussions is discussed in next chapter. (Palkkakeskustelut Suomessa, 2011)

2.4.Pay-for-performance

Combining performance appraisal and payment determination processes is one example of pay-for-performance practices, which refer to linking payment determination to the actual performance to some extent (Milkovich and Newman, 2005). By doing this management often aims eg. at increasing motivation of employees (Milkovich and Newman, 2005). For a pay-for-performance plan to serve its purpose, it needs to contain job specific performance with clear measures for low and high performance, thorough and well-structured appraisal discussion process, and finally, justified rules for merit increases related to the performance. (Mulvaney et al., 2012)

Performance-based pay increases can be fixed (merit pay) or variable (bonus) and paid either on individual or collective level. In addition, measuring the performance can be based on more subjective or objective measures. Subjective measures refer to behavioral issues, for example developed skills. Objective measures on the other hand refer to more result-oriented issues like financial effectiveness or sales figures among others. (Salimäki and Heneman, 2008)

Merit pay is considered as a fixed pay type, which is resulting from actual individual performance and is based on performance appraisal and subjective measures. Often the merit pay is a result of long-term performance and not necessarily based merely on the performance of the present appraisal period. Therefore, merit pay is differing from traditional annual bonuses. (Heneman, 1992)

2.4.1.   Support and criticism regarding pay-for-performance

Concerning discussion of should payment issues be linked with performance, there exists both support and resistance to the topic. It seems that the success of the combination is also heavily related to the payment system and organization. Research by Lawner (2003) done in USA with 102 large companies revealed, that performance appraisals where considered to be more effective in cases where the outcome of the results were linked to payment determination. On the other hand, research by Heneman and Werner (2005) found out that merit pay was more related to improved employee attitudes than actual improved performance. In addition to previous

studies, there exist both psychological and economic theories supporting the linkage of performance and pay. These are introduced next and summarized in Table 1.

Economic theories supporting the linking pay to performance are for example tournament theory, utility theory, agency theory and efficiency wage theory (Maaniemi, 2013). In tournament theory, the prize, in this case payment is based on relative performance and is divided so that the best performer gets highest pay and worst performer the lowest pay (Knoeber and Thurman, 1994). Utility theory traditionally implies that price of a good or service is compared to its marginal utility (Aleskerov et al., 2007). In pay-for-performance concept it can be interpret that the utility, in this case payment, is compared with the price, in this case performance (effort) and the marginal utility needs to be at least the same or preferably greater than the utility of another job. Agency theory examines the relationship between principals and agents and the problems in case the goals and targets of these two are in conflict, and if the principal is not able to ensure what the agent is doing (Gasaway, 2000). From pay-to-performance point-of-view it could be interpret that the employee acts as agent and employer as principal. Efficiency wage theory implies that payment is set above the equilibrium payment level in order to increase the employee's productivity/performance due to more loyal employees who are willing to put effort in keeping the job and the payment level (Akerloft and Yellen, 1986).

Psychological theories supporting the pay-for-performance include reinforcement theory (Skinner 1953), expectancy theory (Vroom 1964), equity theory (Adams 1963) and goal setting theory (Locke and Latham 1990). Reinforcement theory suggest, that work performance is based on its consequences, meaning that in case there is link between performance and pay, there shall be increased performance (Skinner 1953). When applying expectancy theory, linking payment to performance would increase the employee's motivation in case employees value the payment and are confident that they can perform on a needed level in order to earn the payment (Vroom 1964). Equity theory according to Adams (1963) is based on an assumption that what individual gets is based on the amount what he/she contributes and this contribution and outcome is then compared to the contribution and outcome of others. In case there is inequity, according to equity theory, the individual shall try to balance the inequity either by changing attitudes or amount of performance. According to goal setting theory, individuals are intentionally targeting to goals, which are motivating them in case those goals are challenging, specific and accepted (Heneman

and Werner, 2005). Psychological and economic theories supporting pay-for-performance are summarized in Table 1.

Table 1 Psychological and economic theories supporting pay for performance

Psycgological theories supporting pay-for-performance	
Reinforcement theory	Link between performance and pay increases performance
Expectancy theory	Link between performance and pay increases motivation if payment is valued
Equity theory	Employee's compares his/hers payment and contribution to others and tries to balance possible inequity by changing attitudes or amount of contribution
Goal setting theory	Employee is targeting to goals, which are motivating them in case those goals are challenging, specific and accepted
Economic theories supporting pay-for-performance	
Tournament theory	Payment (prize) is based on relative performance and is divided so that the best performer gets highest pay and worst performer the lowest pay
Utility theory	Employee compares the utility (payment) with the price (work effort)
Agency theory	Relationship between principals (employer) and agents (employee) and the problems in case the goals and targets of these two are in conflict and if the principal is not able to ensure what the agent is doing
Efficiency wage theory	Payment above equilibrium increases employees' productivity sine they are more loyal and eager to keep the job and payment level

Both economic and psychological theories supporting the linkage imply that the combination of payment and performance would enhance individual employees' performance and by that way increase the overall performance of the organization (Maanieniemi, 2013). According to Gerhart et al. (2009) this linkage can increase motivation by means of incentive effect and sorting effect. Incentive effect implies, that higher amounts of pay lead to higher amounts of effort. Sorting effect on the other hand implies, that employees who are motivated by payment based on performance are eager to work in organizations with these payment systems and those who are not, will be leaving the company at some point (Gerhart et al., 2009).

Critics regarding linking pay to performance are arguing that payment is not the main motivator for employees, but job satisfaction can be derived from eg. responsibility, recognition or optimal amount of challenges. One viewpoint is that if there shall be increase in the performance, that is only temporary, and the long-term commitment is based on interest towards the job, not the payment. Criticism has also included arguments that this linkage can even decline the

employee's motivation to perform better. In addition a lot of problems are seen in the implementation of these pay systems. These problems include subjective measures instead of objective ones leading to inadequate performance measures, biased and conflict-avoiding managers, lack of open communication, and payment increases based on non-performance issues. In addition it is argued, that the payment increase should be large enough to create actual motivation increase. Unfortunately, the implementation challenges can end up creating poor acceptance of the system both within employees and managers. Table 2 summarizes the criticism and possible problems in linking pay to performance. (Maaniemi, 2013)

Table 2 Criticism and possible problems in linking pay to performance

Criticism and possible problems in linking pay to performance
• payment is not the main motivator for employees (job satisfaction from other things)
• performance increase is only temporary (long-term commitment is based on interest towards the job)
• linkage can even decline the employee's motivation to perform better
• subjective measures instead of objective ones -> inadequate performance measures
• biased and conflict-avoiding managers
• lack of open communication
• payment increases based on non-performance issues
• payment increase should be large enough to create actual motivation increase

2.4.2. Pay-for-performance in public sector

In the 1990s there was structural payment system renovation in the public sector in Finland with the first new payment systems implemented in 1994. Previously the payment had been based on organizational position, title and service years. This was considered to be too hierarchical, inflexible and not supporting the productivity, leadership and recruitment of competent personnel. In addition, the new payment system was targeted to support fairness better than the previous one. The new system takes into account three grounds for payment determination; 1) level of demand and value of the work, 2) productivity and proficiency of the employee, and 3) performance of the employee, work group or organization. Payment is on the other words based on work, productivity and performance. (Huuhtanen et. all, 2005)

In the current payment system the main part of the payment concerns the actual work and how demanding it is. Parts of the payment system and grounds for the payment are described in Figure 5. Following the payment system and grounds for payment the different organizations of the public sector have however been able to decide and built their own measurement systems to suit best the needs of their own organization. (Huuhtanen et. all, 2005)

What is the question?	Payment Grounds		Payment component	
What is the outcome of the work?	Outcome		Bonus	Performance of individual, team, group or organization
How work is done?	Personnel		Personal component	Qualities and performance of group or individual
What work is done?	Work		Job- or task-related component	Demand level of the work

Figure 5 Payment grounds and components (Huuhtanen et al., 2005)

Huuhtanen et. all (2005) have summed in their study the outcome including the difficulties of the payment system renovation in the public sector. It seems that the positive outcome is that they enhance discussion about contents of the work and by that way support the clarification of the job descriptions and targets. However, there can also be difficulties and pressure in defining the value of different work since different tasks are valued with higher points than others are. Historically in Finland, evaluation criterions like collaboration skills have been more unclear and unaccepted criterions compared to for example the actual measurable outcome of the work. In sum, the payment system renovation was seen as positive and needed change. However, there was stated work still to be needed in the actual utilization and implementation of the new system and that the actual value will be derived based on how well the management and personnel are able to utilize the payment system. (Huuhtanen et. al., 2005)

There is also other earlier literature about the fit of pay-for-performance systems in public sector, which is of interest to this thesis since Kela operates in public sector. Based on this earlier research, linking pay to performance in public sector seems not be a success story (Maaniemi, 2013). Merit pay in public sector is not argued to increase employee motivation and organizational performance. In general, it seems that implementation problems of these payment systems are even more challenging in public compared to private sector (Maaniemi, 2013). Reason for this can be the differences between these two sectors. Ingraham (1993) has listed possible reasons for successful payment system implementations in private sector and by comparing the list with public sector, this gap can be the explanation to poor pay-to-perform system success in public sector. The reasons include managers' having enough legitimacy to reward good performance – and there is enough funding for this rewarding, but and in addition they can also take needed actions in case of poor performance. In addition, there exists ability to link pay to performance and clear measures for evaluating employee and organizational successful performance (Maaniemi, 2013).

To summarize, the challenges with linking pay to performance in public sector include according to Ingraham (1993):

1. No clear linkage between performance and outcome of it, that is, no motivation triggered.
2. Not enough funding for rewarding good performance adequately.
3. Managers do not have enough flexibility, legitimacy and control over the budged due to bureaucracy and complex rules in the public sector organizations.
4. Employees in the public sector may be motivated better by other means than actual monetary payment.

2.5. Knowledge of pay, payment system satisfaction and their effects to performance

Since combined performance appraisal and payment determination processes involve the issue of payment, it also touches the employees' knowledge of pay. In practice good knowledge of pay means that the employee knows the payment process, the grounds for the payment determination

and understands how his/her performance is related to the pay. This important, however not always clear issue is heavily related to how payment serves as managing instrument and as a means of motivating personnel to perform according to the desired knowledge and performance level. Payment as a motivator can also help to clarify the goals and missions for single employees. Overall, the employees' knowledge of pay has studied to increase the motivation, job satisfaction and performance level. (Moisio et. al. 2012)

Research from 2012 by Moisio et. al. studied the level of satisfaction towards payment level and payment system in Finland. The study shows that the satisfaction can be increased with increasing the employees' knowledge of the basic payment, fostering open communication, and securing the fair application and thus perceived justice of the payment system. In addition, these elements enhance also employees' commitment and work atmosphere, however, can also advance competition among employees. The research also reveals, that in general the level of payment knowledge in Finland is in quite low level, especially concerning basic payment (more than 50% of the respondents were not aware of the payment determination principles). What comes to the satisfaction level, in general 42% of the respondents were dissatisfied with the payment level. Notable result is also the level high of dissatisfaction towards the actual payment system and the inconsistent process related to payment determination. (Moisio et. al. 2012)

In order to foster payment knowledge among employees, Moisio et. al. (2012) have also listed rules of thumb related to the communication of payment determination in order to increase the payment knowledge. These include among others:

- Setting common ground for payment determination within all managers
- Having payment grounds and payment determination process descriptions available to everybody in intranet
- Making payments within own unit visible to all managers
- Linking payment grounds tightly with actions and goals of the organization
- Designing the payment increase process so that the manager nominates, second level manager approves and HR organization gives final approval for the payment increase
- Payment related information sessions held by HR department
- Training new managers regarding payment system

- Giving needed decision rights to managers regarding payment within certain boundaries
- Making sure that after the payment determination process is over, each manager communicates the outcome to each employee

Overall, it is crucial that the payment system is highly related to well-defined performance management process with clear rules and guidelines (Moisio et. al. 2012).

2.6. e-HRM

Although performance appraisals and payment discussions can be mastered without involving any IT-systems, competence systems do offer various benefits by functionalities such as registering and storing competence data and outcome of the appraisal discussion, enabling analysis of possible competence gaps, and mapping current and targeted future performance levels (Hustad and Munkvold, 2005).

Handling development appraisal and payment determination processes with IT-system, for example in SAP as in the case of Kela is one example of e-HRM, which refers to IT-based Human Resources Management (Rüel and Bondarouk, 2004). Examples of e-HRM are e-recruiting, e-selection, e-learning and e-compensation (Lin, 2011). According to Ruël and Bondarouk (2004) IT can support all HR processes, and the stages of e-HRM can be divided in to three types as follows:

1. Operational; automation of operational HRM, eg. payroll
2. Relational; automation of basic processes and functionalities, eg. recruiting, training and performance management
3. Transformational; linking HR to business strategy by matching eg. strategic competence management and knowledge management with the overall business strategy

According to Ruël and Bondarouk (2004) reasons why organizations want to implement e-HRM are willingness to focus on strategic HRM issues, cost reduction and efficiency possibilities, and giving better customer service to employees and management in HR processes. Outcomes of e-HRM implementation are cost-effectiveness, increased commitment of staff by increased

interaction and trust, increased competence of staff in taking new tasks and roles, and finally, increased congruence of all stakeholders of the company (Ruël and Bondarouk, 2004). In addition, supporting HRM processes with IT decreases the administrative tasks in the HR department, enables decentralization of HR tasks as well as supports the standardization and harmonization of HR processes (Ruël and Bondarouk, 2004). Parry & Tyson (2011) include also improvement of organizational image in terms of showing technological sophistication into the list of e-HRM goals. Linking performance appraisal and payment system to overall business strategy was discussed in chapter 2.2. e-HRM can support in performing the corporate strategy (Lin, 2011). Goals, types and outcomes of e-HRM as per Ruël and Bondarouk (2004) with addition from Parry and Tyson (2011) are gathered in Figure 6.
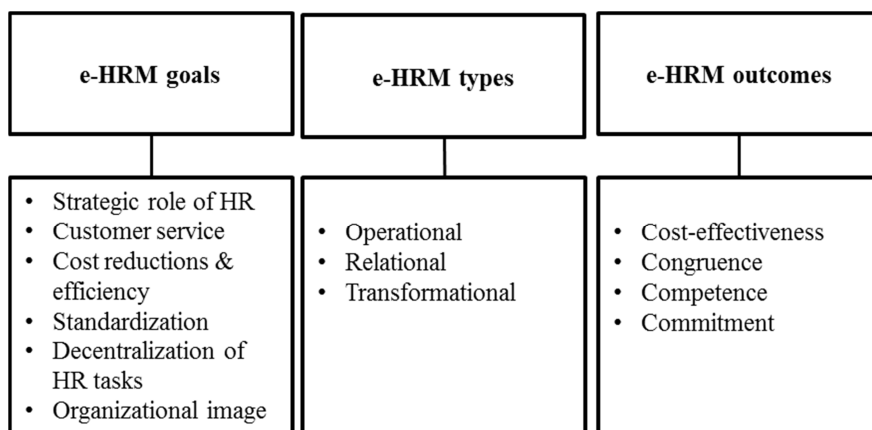
e-HRM goals	e-HRM types	e-HRM outcomes
• Strategic role of HR • Customer service • Cost reductions & efficiency • Standardization • Decentralization of HR tasks • Organizational image	• Operational • Relational • Transformational	• Cost-effectiveness • Congruence • Competence • Commitment

Figure 6 Goals, types and outcomes of e-HRM (Ruël and Bondarouk, 2004 & Parry and Tyson, 2011)

According to Technology Acceptance Model (TAM) developed by Davis et al. (1989) user acceptance towards IT system is related to how useful the system is perceived and how easy it is to use. In case the system is perceived as difficult to use, the usage will be low although the usefulness of the system would be perceived as high. Therefore, the usability of e-HRM systems should be highlighted when designing e-HRM tools. (Davis et al., 1989)

Does e-HRM then fulfill the value creation promises in practice? Study by Rüel and van der Kaap (2012) confirms link between e-HRM usage and value creation. Value in this respect is meaning a benefit provided eg. in terms of improved effectiveness, efficiency and customer

service. According to the study, the prerequisites for e-HRM to create value are to have contextual factors facilitating the usage and to synchronize the usage with the intended purpose. Contextual factors in this respect refer to quality of the data, technological competence of HR department and HRM policies and processes in line with the e-HRM tool. (Rüel and van deer Kaap, 2012)

Study by Parry & Tyson (2011) investigated e-HRM in 10 organizations and indicated that there are several factors that influence the realization of the goals set for e-HRM. These include skills of HR department to be transformed from administrative tasks to more strategically-oriented tasks, adequate e-HRM training provided for users, facilitating engagement with e-HRM system, designing the e-HRM system to match needs and taking user-friendliness into account, and finally, level of familiarity with technology within the organization. (Parry & Tyson, 2011)

Study by Ruta (2005) regarding implementation of employee portal on the other hand revealed, that in the implementation of e-HRM tools not only the Technology Acceptance Model (TAM), but also change management principles should take into consideration. In this consideration, the TAM model focuses on "what" determines usage and change management model on "how" usage can be influenced. Change management principles include taking into consideration the contextual factors both in the industry and company level (including eg. competition, customers, technological competence etc.) as well as process factors (implementation plans including change strategy, change agents and management actions ect.). (Ruta, 2005)

According to Lin (2011) e-HRM can also improve organizational innovation but it has two crucial cornerstones; IT adoption and virtual organization adoption. IT adoption refers to the level in which IT-tools are adopted in the everyday activities of the organization. Virtual organization refers to virtualized functions and teams. Virtual organizations include potential advantages by:

- Enabling focus on organization's core competencies and giving possibility to outsource other activities
- Creating connection between core and non-core activities via IT-tools
- Enabling virtual teams and flexible organization structure

These cornerstones can foster rapid information sharing, creation of new knowledge and in addition, give HR management real-time information based on which they can measure and manage personnel and make proactive decisions based on changes in the organization and competition environment. In addition, Lin (2011) stresses the importance of HR managers to understand the corporate strategy, IT adoption and the need to keep themselves updated about the latest developments and innovations in the e-HRM area. (Lin, 2011).

Effectiveness of e-HRM in public sector has been studied by Bondarouk et al. (2009). The study implies that the quality of the e-HRM system should be the key focus leaving the easiness of use to lower importance, even if the easiness increases the usage. In practice, this means that even if the users would consider the e-HRM tool as easy to use and the usage would be high, the actual effectiveness of the e-HRM tool is derived from the quality of the content and design of the IT-tool. It should however be noted, that effectiveness can mean different things for different stakeholders, like employees and managers. (Bondarouk et al., 2009)

3. PERFORMANCE APPRAISAL AND PAYMENT DETERMINATION IN KELA

Case company Kela (Kansaneläkelaitos in Finnish), which is the Social Insurance Institure of Finland is independent social security institution supervised by the Finnish Parliament. Kela handles social security benefits related to childbirth, study, sickness, unemployment and retirement. Kela's mission is to "*secure the income and promote the health of the entire nation, and to support the capacity of individual citizens to care for themselves*". Kela's values are respect for the individual, expertise, cooperation and renewal. In 2014 Kela had approximately 6 300 employees (Kela's web pages)

All the material in this section is based on Kela's internal material, including material from Kela's intranet pages, as well as material prepared and compiled by HR Coordinator Sanna Norra who was working as a project manager in the performance appraisal and payment determination combination project. In addition to the internal material, this section includes

material also from the interviews of Ariana Hellman working as is Development Manager of Kela responsible of the performance appraisal process and Tuija Jokinen working as Employment Relations Manager of Kela.

3.1. Performance appraisal and payment determination process as part of Kela's business strategy

According to Development Manager Ariana Hellman Kela has only one strategy, meaning that besides overall strategy there is no separate HR strategy. However, HR department has developed development program of personnel resources ("Henkilöstövoimavarojen kehittämisohjelma" in Finnish) which has strategic elements. Hellman sees it crucial that this development program is derived from Kela's strategy and that the linkage between Kela's strategy and personnel development program should be strengthened. She adds that Kela's strategy should be more heavily related to personnel planning and in the evaluation of what kind of resources and knowledge is needed in Kela. What comes to the project regarding combining performance appraisal and payment determination process and system, it is related to Kela's overall strategy via personnel development program. Figure 7 is Kela's internal material and illustrates how Kela's strategy is linked to performance appraisal discussions.
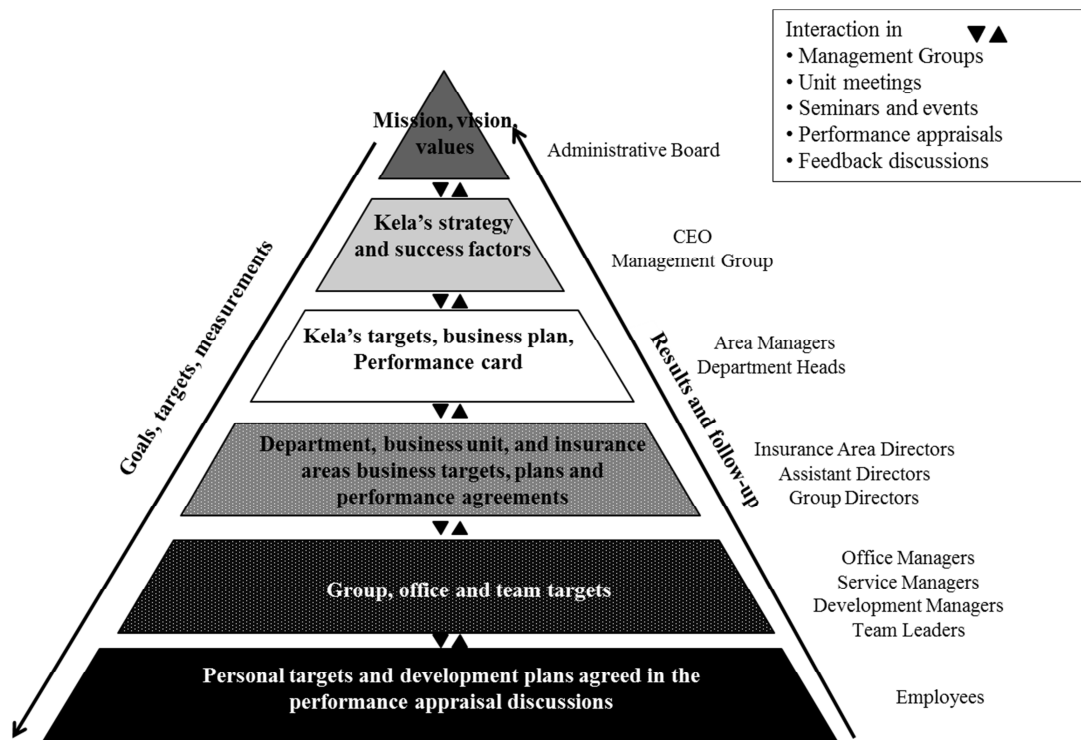
Figure 7 From strategy to performance appraisal in Kela

3.2. Previous performance appraisal process in Kela and reasoning for change

Previously in Kela the performance appraisal discussions were held between November and February and payment discussions during February and March. Both discussions were held separately, meaning in two different occasions. Proximity of the timing and overlapping contents were causing frustration and challenges with time scheduling. Two different discussions were a burden for both subordinates and supervisors, and performance evaluation was discussed in both processes.

According to Ariana Hellman, at first the aim was to develop only the appraisal functionality since the results of internal personnel barometer showed declining trend regarding satisfaction towards the appraisal. According to the internal barometer in 2012 only 63,5% of Kela's personnel considered performance appraisal discussion useful and there had been a declining trend in these results since 2010. HR department had also received direct feedback from managers about the heavy workload that two separate discussions about almost the same topics created for them. In addition, the internal inspection had given feedback about the appraisal

23

process and had recommended coordinated development of HR-related processes as a whole. The topics and concerns highlighted in the report from internal inspection (2011) concerned:

- The role and jurisdiction of managers in the performance appraisal process and how process-like leadership can affect them: how managers should implement strategy
- Target setting and follow-up of results: how to develop measurement of productivity and accomplishments
- Evaluation of competencies (what information and to be used by who) should be developed and long-term development needs should be recognized and also be forecasted
- Interaction between manager and employee in the performance appraisal discussion should be increased and employee's activeness should be supported

In addition to the barometer results, direct feedback and report from internal inspection also the pilot from 2010 concerning reassuring expertise had found several development items. These included:

- Form-orientated performance appraisal discussion: heaviness of the form, difficultness to set targets
- Too much variation in the target follow-up and also in the rewarding of good performance
- Both performance appraisal discussion and payment discussion included same topics and were done in quite the same time of the year
- Poor timing of the discussion since the turn of the year is busiest time of the year
- It was felt that the evaluation of competencies did not give additional value
- Managers need more support on their yearly discussion

It was therefore decided, that the performance appraisal process should be evaluated from performance management, expertise, and work well-being point-of-view. It was seen, that managing performance was heavily related to setting targets, following fulfillment of them and rewarding of it and therefore these elements were seen logically related. In addition, for increasing the satisfaction regarding performance appraisal, easing the workload of managers, goal for combining performance appraisal and payment determination processes were also

increasing the payment knowledge among personnel. Hellman sees it very important, that the managing of performance should be highlighted in the discussions between employee and manager.

In Kela's management system the performance element has been fundamental item and the idea has always been that the company-level strategy is reflected in the unit level targets. How the individual target setting with each employee as well as the job description is then anchored to these targets and strategy was something that Kela's management saw as issue that needed to be highlighted.

According to Ariana Hellman each company and organization should consider their own functionality and operations when considering should performance appraisal and payment determination be combined. She sees that in this point, there were strong reasoning to execute the combination in Kela, but in case the new process and system at some point in Kela's future seems inappropriate, the process and system can be separated again or otherwise developed. This is also something that is taken into account when developing the IT-system (SAP). She also believes that professional managers have already built a bridge between performance appraisal and payment determination discussions and have not given conflicting feedback in these two discussions. Therefore combining the discussions is natural in order to clarify how payment relates to performance management. However, it is a big challenge that payment system as such does not at the moment support performance management enough and it creates pressures to develop the payment system in the long run.

According to Employment Relations Manager Tuija Jokinen, there had been discussions about combining the performance appraisal and payment determination processes already before, but there was strong resistance from the employee union side. It was in the history considered by the union representatives that monetary issues should not be discussed together with development topics or the latter will not be given enough attention and employees are not able to give honest and straightforward feedback to managers in a fear of losing possible payment raise.

3.3.Payment determination process in Kela

Kela has own collective agreement. What comes to SAP functionality regarding payment determination, it is completely tailor-made to suit Kela's needs. As discussed, previously in Kela there was payment discussions held during February and March. Contents of these discussions between employee and manager was to go through the job description, consisting the role and tasks of the coming period. Based on this the "verification of job grade" –document was created and approved by the manager. In addition the discussion included evaluation of personal work performance, touching issues of expertise, collaboration, productivity and quality. This was then approved by the payment decision approver (Chief HR Manager). Details of these evaluations and payment determination is introduced next.

Payment in Kela consists of job-related component and personal component, which is maximum 32,5% of the total payment. Job-related component concerns the level of demand of the work, and personal component the employee's performance. Evaluation of personal components (performance) consists of following items:

- Managing the work; level of knowledge and experience, developing own skills
- Collaboration skills; within work community, customers and other stakeholders
- Productivity and quality; achievements, taking initiative, responsibility

Based on these criterions, employee receives personal points. Maximum number of personal points is 56. Figure 8 describes the payment determination in Kela. (Kelan palkkausjärjestelmäopas, 2014)
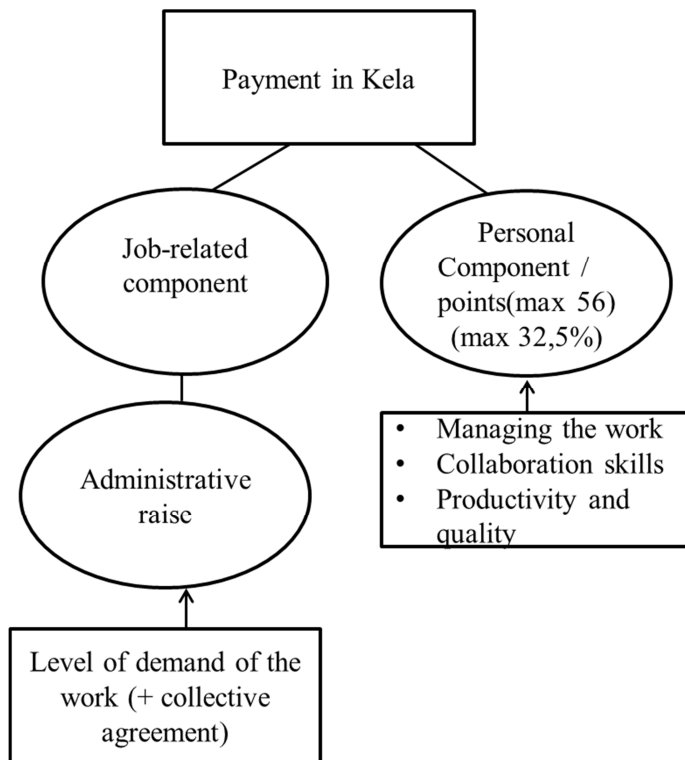
Figure 8 Payment determination in Kela

Level of demand of different tasks is evaluated based on general job descriptions, which are classified based on the level of demand of the work. Factors affecting the level of demand are:

- Education needed
- Experience needed
- Expertise and knowledge needed
- Problems solving skills needed
- New information and personal development needed
- Cooperation skills and personal relationship skills needed
- Responsibility of the work's outcome
- Independence of the work

(Kelan palkkausjärjestelmäopas, 2014)

When the demand level of the work rises, the manager evaluates the new level of demand of the work and employee gets administrative raise, which is part of the job-related payment component. Changed demand level of the work involves always that the personal component points are evaluated simultaneously. When the employee performs more demanding work and gets administrative raise, the personal component points are lowered simultaneously. (Kelan palkkausjärjestelmäopas, 2014)

As discussed previously, the payment components were determined in the payment discussion. In the new process, the payment discussion is included in the performance appraisal discussion. New process is introduced in chapter 3.5.

Kela does not apply incentive system in its payment system. However, incentive system has been tested during 2004 and 2006 but there have not been decisions so far to start official incentive system in Kela. According to Tuija Jokinen the current top management of Kela does not see incentive system (bonus) applicable for Kela at the moment. It is seen problematic that there does not exist similar measurements with which personnel in the field and in the headquarters could be evaluated.

3.4. Knowledge of payment and payment system satisfaction in Kela

As discussed in chapter 2.5, employees' knowledge of pay has studied to increase the motivation, job satisfaction and performance level (Moisio et. al. 2012). Kela has performed payment system survey in 2007 with 473 respondents (Kela's Intranet pages). Results regarding functionality of the payment system, knowledge about payment and satisfaction towards payment and payment system are introduced next in order to give indication about the current opinions of Kela's personnel.

As can be seen from Table 3 the functionality of the whole payment system as well as the different payment components, that is, job-related and personal payment component were considered to be poor. Especially the personal payment component was considered to function poorly. What comes to knowledge of payment (Table 4), in general the knowledge seems to be on a good level, although there is room for improvement especially what comes to understanding

the criterions used in performance evaluation and what the employee should do in order to get a payment increase. Concerning perceived satisfaction towards payment and payment system (Table 5), the survey results reveal that there is dissatisfaction towards both of them. However, the way in which managers handle payment discussions is considered good.

Table 3 Perceived functionality of payment system in Kela (2007)

	Poor	Good	Moderate	NA
Payment system as a whole	**51 %**	33 %	11 %	5 %
Job-related payment component	**43 %**	32 %	16 %	9 %
Personal payment component	**59 %**	22 %	11 %	9 %

Table 4 Knowledge of payment in Kela (2007)

	Disagree	Not disagee or	Agree	NA
I understand the ground for payment raise	24 %	19 %	48 %	9 %
I know what I should do to get a raise	**39 %**	14 %	33 %	14 %
I know how my raise is decided	32 %	16 %	36 %	16 %
I know how my the difficulty level of my job is determined	16 %	14 %	63 %	7 %
I understand why my job is determined to this difficulty level	25 %	14 %	53 %	8 %
I receive enough knowledge about the payment system	17 %	22 %	55 %	6 %
I understand how the personal component of my payment is determined	22 %	16 %	**54 %**	9 %
I know how my performance affects the payment	27 %	16 %	**49 %**	8 %
I understand what criterions are used to evaluate my performance	**34 %**	20 %	37 %	10 %

Table 5 Satisfaction towards payment and payment system in Kela (2007)

	Dissatisfied	Not dissatisfied or satisfied	Satisfied
Payment as a whole	**43 %**	26 %	32 %
My general payment development	**55 %**	24 %	21 %
The way that my organization handles payment issues	**52 %**	34 %	14 %
How the payment system is used	**54 %**	35 %	11 %
How my subordinate handles the payment discussion	19 %	33 %	**48 %**

It can be assumed that by combining the performance appraisal and payment determination processes in Kela the employees' knowledge of pay should be increased at least by certain amount due to more obvious and emphasized link between actual performance and payment outcome. However, that does not automatically mean that the employees' satisfaction level towards payment is increased at the same time. It is recommended that Kela performs a payment system survey again after the performance appraisal and payment determination processes have been combined and the appraisal discussion are held with the new process. In addition, the current survey results date back to 2007 and updated information would be needed.

3.5. Introduction to the combined performance appraisal and payment determination process in Kela

In Fall 2013 Kela started a project in order to combine the performance appraisal discussion and payment determination discussion process as well as modify the SAP functionality to match and support the new process. Project was led by HR Coordinator Sanna Norra from HR department and the IT execution project by Senior IT Specialist Elisa Saarela from IT department. IT execution of the project was performed during 2014 and since January 2015, the new process and IT functionality has been in use. As described earlier, previously in Kela the performance appraisal discussions were held between November and February and payment discussions during February and March. In the new process the combined performance appraisal and payment discussion is held between December and February. Reasoning for the combination was

described in chapter 3.2. Figure 9 illustrates common yearly clock for performance appraisal and payment discussion in Kela and gives overview of the related activities during the year.
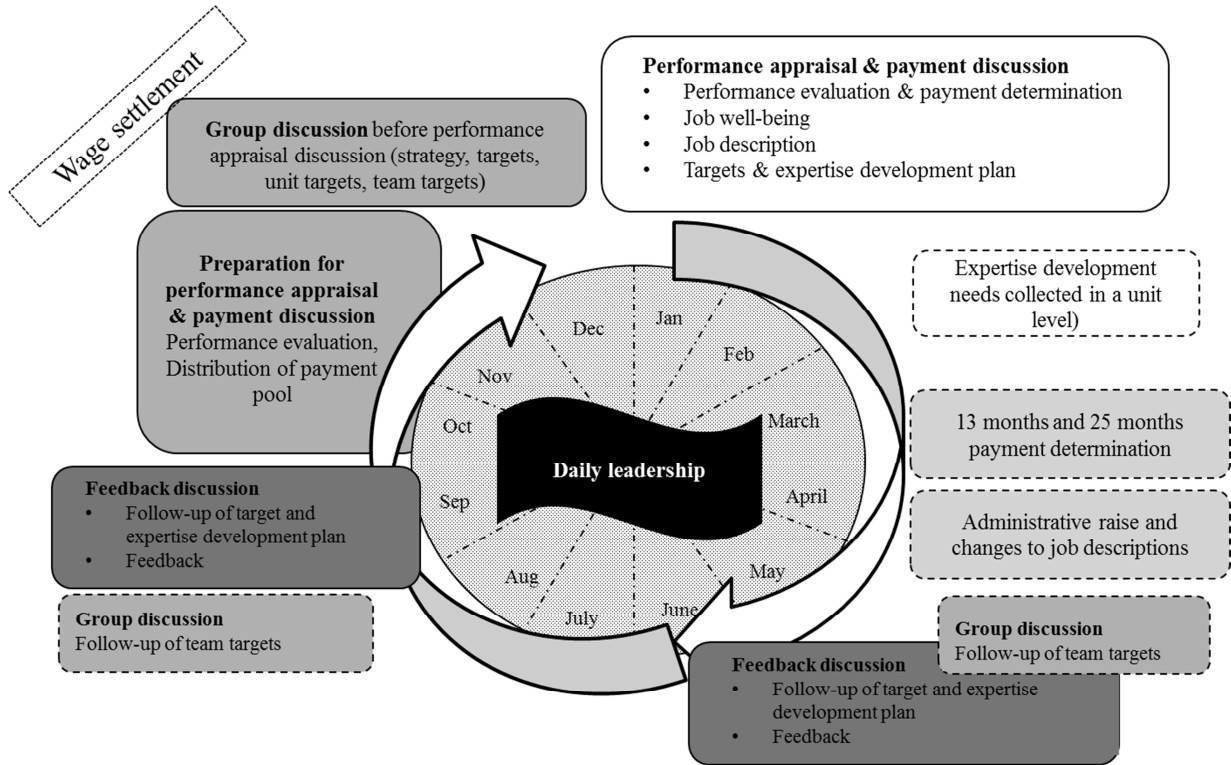
Figure 9 Common yearly clock for performance appraisal and payment discussion in Kela (Norra, 2014)

Kela's performance appraisal and payment discussion process is divided into two parts

1. Evaluation of previous period and development
2. Planning of the coming period

The process is illustrated in Figure 10 and the different parts explained later in this chapter.
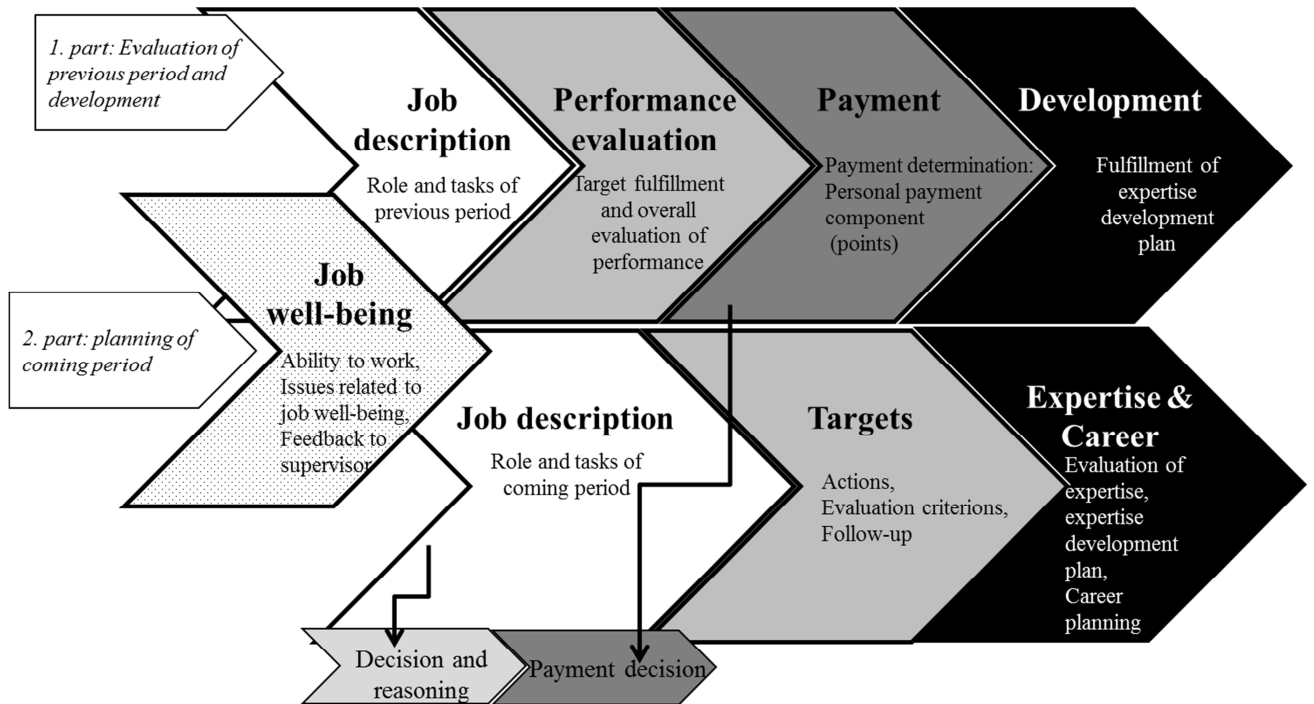
Figure 10 Kela's performance appraisal and payment discussion process (Norra, 2014)

In Kela, the performance appraisal and payment discussion is held with all white collar workers and the discussion is documented in SAP. This discussion includes four parts and SAP functionality correspondingly four tabs, which include:

1. Job well-being
2. Job description
3. Targets & performance evaluation
4. Competence evaluation & development

These tabs are explained in the illustration in Figure 11 and in print screens in the next chapter.
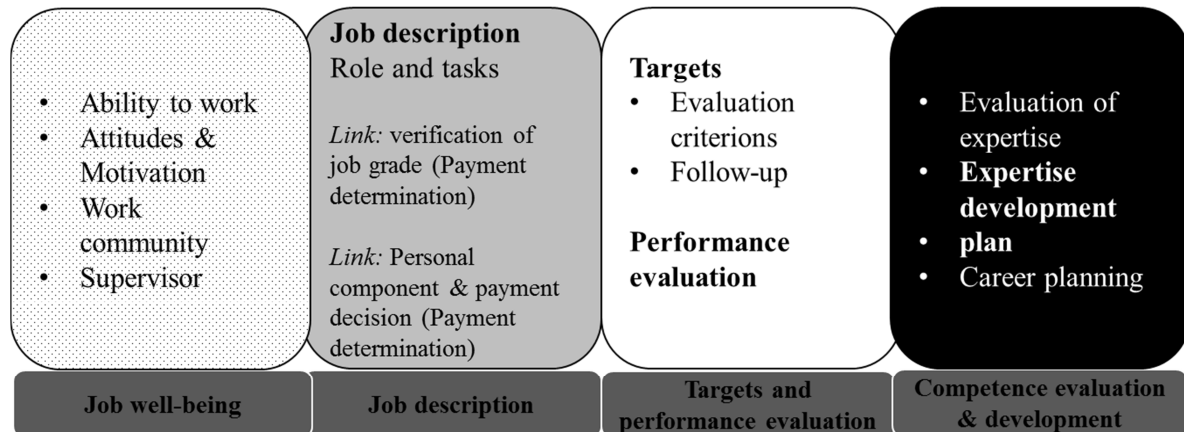
Figure 11 Tab view of performance appraisal and payment discussion (Norra, 2014)

Before the discussion, there are preparatory tasks needed both by manager and employee. Before the discussion manager should prepare by:

- Evaluating performance of previous period and prepare general evaluations
- Do performance evaluation regarding personal payment component and divide the payment points based on these evaluations
- Add unit or team targets to the performance appraisal form (what issues are emphasized in the coming period)
- Define targets based on target models that are provided to managers to help in the target setting by serving as examples

Also the employee is expected to be prepared for the discussion by taking following actions:

- Create job description in SAP (possibility to copy old form)
- Think and list possible targets for the coming period. Go through Kela's and unit's targets and common target models that can be used as example
- Evaluate own expertise in relation to expertise requirements. Think and list expertise development targets and career plans
- Think and list issues related to own job well-being, motivation, work and functioning of the work community
- Evaluate manager's success and think feedback to manager

After the preparatory tasks, the actual discussion starts by evaluating the performance of the previous period. Evaluation of previous period, target fulfillment and overall evaluation is done for all employees. Also the fulfillment of expertise development plan is discussed. After the manager has given overall performance evaluation (reached expectations/ exceeded expectations/ room for improvement) the manager explains the reasoning for the evaluation and explains how the employee can improve his/her performance. What comes to annual salary review, for those employees who are part of the yearly payment determination round the personal payment component is discussed at this point and manager informs if the employee shall receive additional personal component points. In this section also the job well-being topics are discussed. Purpose of the job well-being –tab filled in this part is to map the employee's working ability and work resources that have impact to the target setting of the coming period. In addition, in this section the discussion should handle topics related to work community, how to motivate the employee, and what kind of feedback the employee has for the manager.

Next follows the planning of coming period. In this part the job description is approved and the manager prepares "verification of job grade" –document related to evaluating the level of demand of the work. Targets for the coming period are agreed as well as their priorities and evaluation criterions. Manager and employee agree also how the target fulfillment is actively followed during the period. This part includes also evaluation of expertise, setting targets for expertise development and what actions are needed to improve the expertise. Expertise development –tab filled in this part ensures that the expertise evaluation is part of the discussion and also helps in planning the expertise development. It also produces information about the development needs and development status overall in Kela as well as in unit level. In addition it produces data about the career expectations and ensures career planning as part of performance appraisal and payment discussion.

Performance appraisal and payment discussion round ends to payment decision, meaning that the employees involved in the yearly payment determination round receive the payment decisions. The payment determination part is done only for those employees that are part of the yearly payment determination round. After the manager has approved the performance appraisal and payment discussion forms, prepared the payment determination documents and done the "verification of job grade" –document related to evaluating the level of demand of the work the

proposal report of the payment decision regarding the personal payment component is done. Payment determination process was more thoroughly described in chapter 3.3.

3.6. IT execution of the new performance appraisal and payment determination process in SAP

Figure 11 listed the tab view of the new performance appraisal and payment determination section is SAP. In this chapter, the IT set-up is introduced in print screen views. Since Kela is using Finnish language version of SAP, the print screens provided in this chapter are in Finnish. All the print screens are taken from the test system. In Kela the Manager Self-Service (MSS) and Employee Self-Service (ESS) functionalities of SAP are in use for all employees.

First tab (Figure 12) in the tool is called Job well-being & work. It includes issues regarding enthusiasm and motivation related to work, as well as meaning of the own work and general strengths of the employee.

Figure 12 Kela's IT execution: Job well-being & work

Second tab (Figure 13) is called Job description. In this section the employees' tasks are listed and percentage of how much each task takes from the working time is defined for each task. This section includes also the general job description and explanation of the main responsibilities. This tab has also two links regarding the payment determination:

1. <u>Verification of job grade</u> (Figure 14)
2. <u>Personal component & payment decision</u> (Figure 15) including topics related to managing the work, collaboration skills and productivity & quality

Details of the payment determination process were described in chapter 3.3.

Figure 13 Kela's IT execution: Job description

Figure 14 Kela's IT execution: Verification of job grade

Figure 15 Kela's IT execution: Personal component & payment decision

Fourth tab (Figure 16) includes the targets. The targets are set in four different themes, which include:

1. Customer & societal purpose
2. Reformation of personnel & work community
3. Processes
4. Finance

In this section, managers can add targets for their subordinates. Every target has also corresponding "actions & evaluation criteria" field. This section is also used in the follow-up discussions where follow-up fields are filled and updated during the year.

Figure 16 Kela's IT execution: Targets

Last tab is called Expertise & career (Figure 17). In this section the targets for the personal development are set. Also area (eg. IT or customer service) and method (eg. self-learning or

course) is chosen for each development targets. This section includes also topics related to career path and career expectations.

Figure 17 Kela's IT execution: Expertise & career

4. RESEARCH PROBLEM AND METHODOLOGY

As explained in the introduction, the research problem of this study is: ***How performance appraisal and payment determination processes can be combined as a process and as an IT-tool in SAP?***

Aims of the benchmark study are to give to Kela's IT and HR management further information regarding:

- Whether benchmarked companies are combining appraisal and payment determination processes
- What are their experiences regarding the combination / non-combination & how the case companies have built the technical solution in relation to this process

Research methodology of this study is a case study. Why this method was chosen is simply because the author of this thesis was during the writing process working for the case company Kela and acting as the IT project manager for the combining project discussed in this thesis. Qualitative empirical study includes benchmarking of four companies.

Kela has established guidelines and principles for benchmarking and these are followed in the benchmarking process. These guidelines consists of permission for benchmarking, guidelines for information exchange, communication with benchmarked company, preparations and execution, as well as what information can be shared and how.

In addition to guidelines regarding benchmarking, Kela has also established a benchmarking process, which is followed in the case study. The process is described in Figure 18.
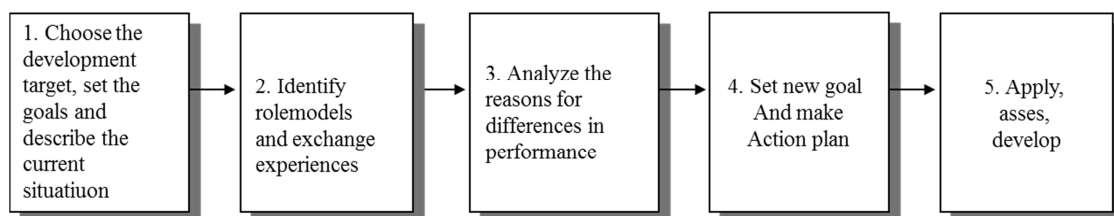
Figure 18 Kela's benchmarking process

In addition to case study, the research has also elements of Action Design Research. Sein et al. (2011) define Action Design as a research method focused on building, intervention and evaluation of artifacts in the organizational setting. It deals with both theory and influence of users of the IT artifact. Action Design Research method is illustrated in Figure 19.
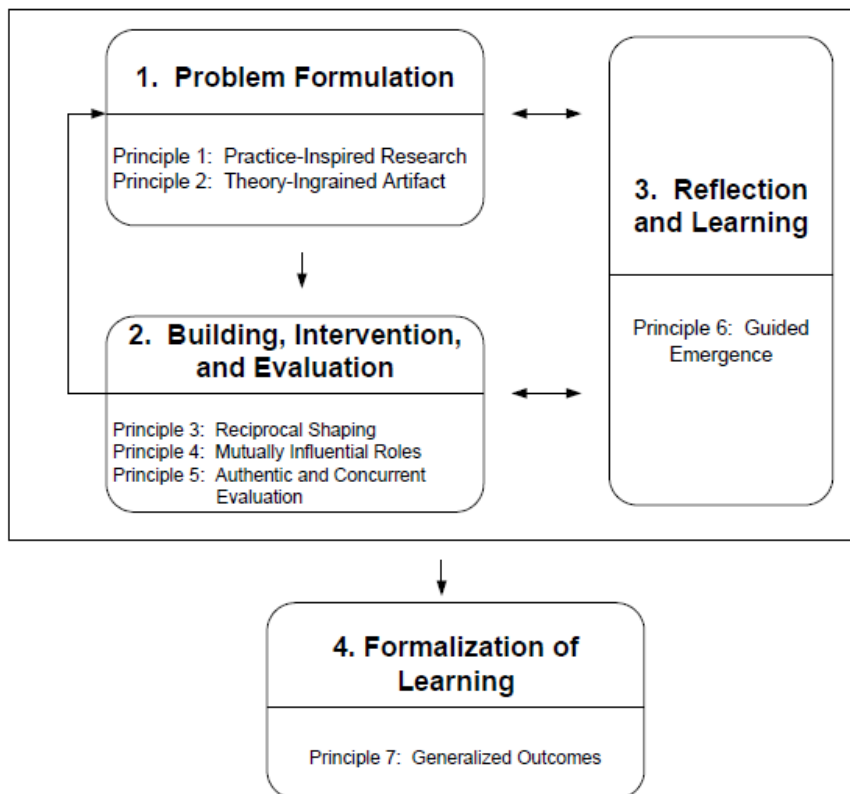
Figure 19 Action Design Research (Sein et al., 2011)

4.1. Introduction to the benchmark company selection and the benchmark process

The most optimal candidate for the benchmark would have been a company that would have fulfilled three below described criterions:

1. Has combined the performance appraisal and payment determination processes both as process and as system wise

2. Utilizes SAP in performance appraisal and payment determination process
3. Is public sector organization

Unfortunately, despite of thorough search including inquiry to SAP Finland, SAP Finnish User Group Ry (SAP FINUG), Google search, and utilizing own professional and personal network, the optimal benchmark target was not found. The remaining criterions for benchmark selection were then in the end:

A. Company should use SAP in performance appraisal OR
B. Company should have experience of combining performance appraisal and payment discussions.

Several companies were found that are utilizing SAP in performance appraisal (criterion A). From those companies three companies were chosen. One company was found that had experience of combining the performance appraisal and payment determination (criterion B). Luckily, that company is also a public sector organization. Since three out of the four benchmarked companies wished to stay anonymous, all the companies are handled anonymous and are therefore named as Company A, Company B, Company C and Company D in this study. Figure 20 maps the chosen companies based on their IT-tool (criterion 1), and performance appraisal process (criterion 2). Next, the benchmark companies are introduced very shortly and superficially in order to secure their anonymity.

IT-system

	SAP	Non-SAP
Combined performance appraisal and payment determination system	**NO OPTIMAL BENCHMARK COMPANIES FOUND!**	Company A ↓ Why?
Separate performance appraisal and payment determination systems	Company D Company C Company B	
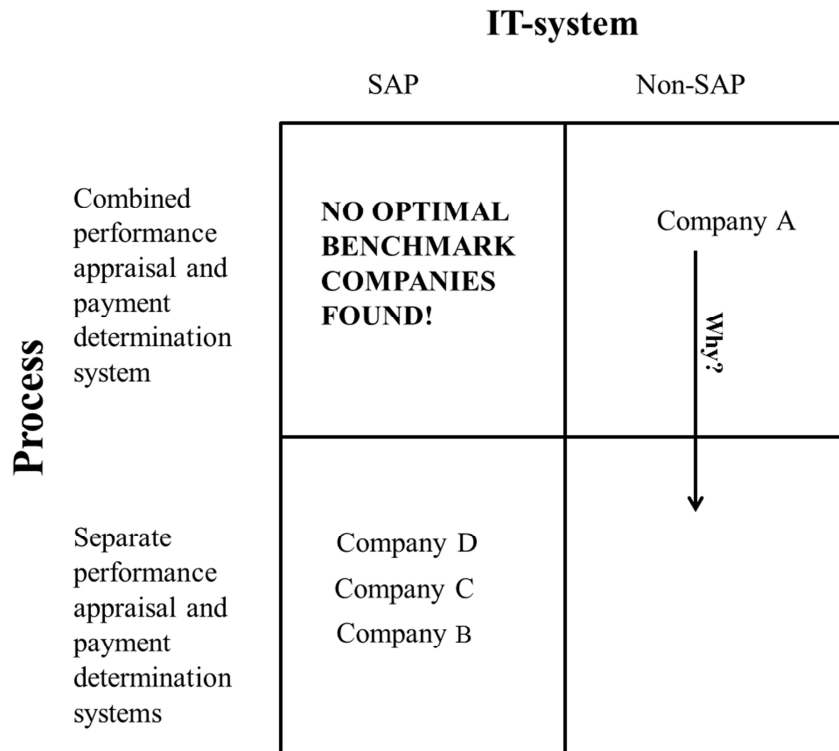
Process

Figure 20 Map of benchmarked companies based on their IT-tool and performance appraisal and payment determination process

Company A is a Finnish public sector organization. In 2012 it had approximately 5 300 employees. Company A used to have performance appraisal and payment determination combined, but has separated the processes later on. Company B is a Finnish limited liability company operating in more than 10 countries with more than 25 000 employees. Company C is a Finnish limited liability company in the telecommunications area and with more than 4 000 employees. Company D is a global manufacturing company with almost 20 000 employees in over 80 countries. All the interviewees in all the benchmarked companies were working in HR department. Table 6 summarizes the background facts of the benchmarked companies.

Table 6 Background facts of the benchmarked companies

	Company A	Company B	Company C	Company D
Government org.	Yes	No	No	No
No of employees	5 300	25 000	4 000	20 000
SAP utilized	No	Yes	Yes	Yes
Interviewed	HR Specialist	HR Development Manager	HR Development Manager	HR Director

All the interviews were done between May and September 2014. Present in the interviews from Kela side was Elisa Saarela (IT project manager and author of this thesis) and Sanna Norra (project manager of the combination project).

5. EMPIRICAL STUDY

In this chapter the benchmark results are introduced. All the material in this chapter is based on the interviews with the company representatives. Since the companies and interviewees wished to stay anonymous, obviously the sources have been not added to this chapter. Interview questions are listed in APPENDIX 1.

5.1. Company A - From combined performance appraisal and payment discussions to separate discussions

Previously in Company A the payment discussion and performance appraisal discussion have been held in a one combined discussion, but starting from the discussion round in 2015, these discussions are separated in Company A. Company A felt urge to update and modify their performance appraisal form and felt that separating the two discussions also in IT-system is worthwhile doing in parallel. The separation means in practice that the discussions are held in separate occasions and both topics have own separate forms and tabs in the IT-system. Reasons for separating these two discussions were that in barometer results the satisfaction towards performance discussions had been poor and there had been feedback that these two discussions should be separated. Comments from the personnel were that the payment is having too big role

in the combined discussions and that the combined discussions included overall too many topics. It was felt that the performance appraisal topics were easily left as the final issue to be discussed and did not receive enough attention and time in the discussions.

In Company A payment discussion and performance appraisal discussions are held by utilizing their own e-HR-system which provides forms for both of the discussions. This IT-system is tailor-made for the needs of Company A. Previously the time period for having performance appraisal discussion had been from October to mid-January. In addition to individual performance appraisal discussions, there has also been group discussions quite often related to some specific theme, eg. strategy. In the new process the payment discussion is held during Autumn but the timing of the performance appraisal can be decided independently by each unit. However, the majority of the discussions will most likely be held during spring. Units can decide independently the best timing. In addition, there are at least 1-2 follow-up / situational discussions during the year.

As discussed, previously performance appraisal, payment and job-well-being were discussed once a year in the same combined discussion. Although Company A in the new process has separate discussions for performance appraisal and payment, there exists still strong link between performance and payment since the targets are set in the payment discussions. Topics in the payment discussion include performance evaluation of the previous period, setting targets for the coming period, job description and discussion about the level of demand of the work. In other words, the payment discussion in Company A is very much focused on performance management. In the performance appraisal discussions the emphasis is more on job well-being, motivation and other non-money related issues. It is felt in Company A that separating especially development needs and feedback from employees to supervisors from payment discussions ensures honest and direct communication between employee and manager when discussing these topics.

In Company A following items are included in the new performance appraisal discussions form in IT-system:

- Joy of working – what makes employee excited in his/her work? What works well and helps employee to succeed? What hinders the experience of achievement? How these issues could be eased and improved?

- Pre-requisites for work and job well-being – does the employee feel that he/she masters his own work? How job well-being could be improved?

- Work community and supervisory work – how the employee feels that the collaboration in his/her group and work community is working? How the collaboration with supervisor is seen? How these issues could be improved?

- Feedback to supervisor

- Own / unit topics – This field can be used in case there is some additional topic to be discussed.

- Future plans – what kind of work-related objectives the employee has for next 1-3 years? What kind of expertise is seen to be needed in the future to master the work? What kind of actions should be taken to support the objectives and reassuring the expertise?

- Other information and wishes for the next 2 years – in case employee has interest for example towards job rotation, supervisory work, project work etc. this can be documented and reported in the system.

In addition, in the IT-system there exists also information of all Company A's training and education.

According to the Company representative some managers in Company A feel that the change means more work for them since instead of one discussions they should held two discussions according to the new process. It will be seen what is the opinion of personnel about the new performance appraisal process. In Company A two people from HR department work with the process and system as sort of super users. In addition, one IT person has been involved in the system development by taking part in the negotiations with the system provider. IT support is provided by the IT-system provider. Number of employees whose performance appraisal and payment discussion information is in the IT-system is 5100. When designing the process change and system update Company A used their current process and system as base and did also benchmarking. Both employee and manager have access to the forms in the IT-system. There

does not exist separate workflow in the system, but when the manager has signed off the performance appraisal form the employee receives an email and goes to the system to sign off the form as well. After payment discussions, the head of the unit prints payment report from the system and signs it.

5.2. Payment determination in Company A

Payment in Company A is determined so that it consists of personal performance-related component and job-related component. Performance-related component is max 48% of the payment. In addition, an employee can get transfer allowance. Job-related component is based on three parts:

1. Expertise and collaboration environment; expertise, skills and experience needed and difficultness of the collaboration environment
2. Guidance and decision-making environment; received feedback and guiding as well as difficultness of the decision-making needed
3. Responsibility and role in the decision-making; effect and relationship of the task with the outcome

Job-related component is based on job description done by employee and manager by utilizing job-description form in the IT-system. Personal performance-related component is based on effectiveness and quality of the work, collaboration skills, special skills and broadness of the skills, and activeness as well as development spirit.

In the payment determination, form there exists no workflow in the system, but after the discussion round is over, the head of the unit prints payment report from the system and signs it.
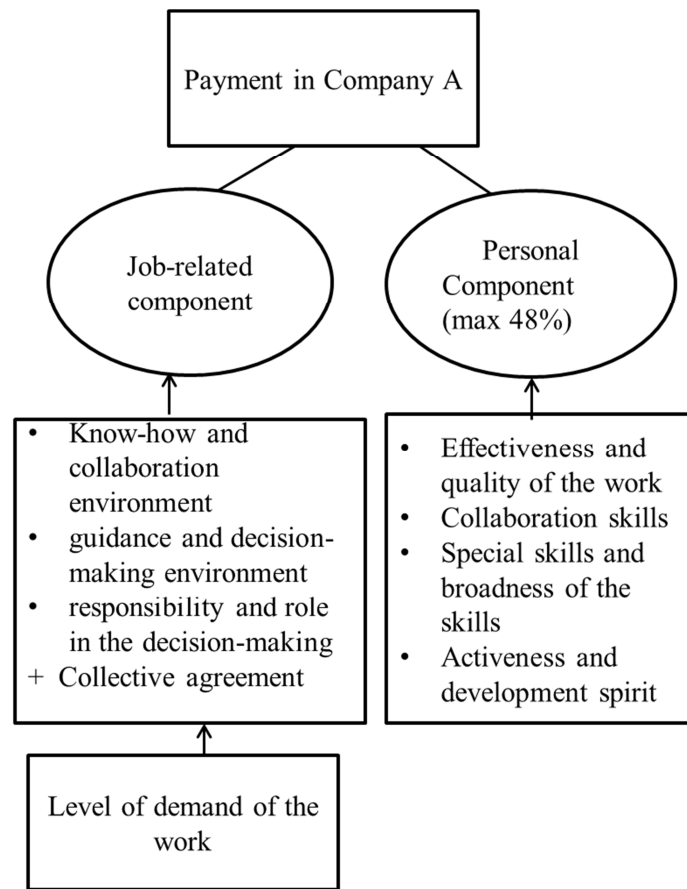
Figure 21 Payment determination in Company A

5.3.Performance appraisal in Company B

In 2010, Company B started a project in order to implement performance appraisal functionality in SAP. When designing the new process and system Company B did a lot of benchmarking and considered also cloud services as alternative option. New functionality was piloted with certain units in 2011 and since 2012, all units in Company B are handling performance appraisal in SAP. This procedure and SAP functionality is used with approximately 4000 employees, consisting of 20% of the total personnel of the company. The process and IT-tool is same for all of these 4000 employees, including top management. Rest of the personnel performs production work and is having different kind of a process with group discussion without utilizing SAP system.

Performance appraisal process of Company B is called Target & Development and consists of two discussions:

1. Target and performance discussion, which is held in the beginning of the year consisting of target setting and closing previous year. This discussion is heavily related to performance management and includes discussion of the actions of previous year and the targets for the coming year.
2. Development and well-being discussion / Mid-term discussion, which is held at the end of the summer or in the beginning of autumn. In this discussion the situation regarding targets, plans and development actions are evaluated. In addition, job well-being and personal development is discussed.

In SAP the functionality is handled so that Manage Business Objectives (MBO) -module is used in Performance Management and this organization and personnel information is utilized in the performance appraisal. Only the managers use the IT-tool, since employees do not have Employee Self Service (ESS) functionality available. In Company B there has been discussions about taking the ESS functionality into use and also could services are being considered as an option to give easy access to the performance appraisal form to employees.

In target setting the system enables altogether 8 targets to be defined but the guideline is that everyone should have only maximum of 5 targets. The approval of the targets is done by the second level manager (one-over-principle) and the workflow functionality is in use so that the approver gets information about targets to be approved in the system. There is also a possibility for the approving manager to approve all the forms as a mass approval. This is tailor-made functionality for the Company B. Other tailor-made solution is that the target setting by cascading targets from top layers to lower levels can be done by HR so that they are able to choose certain criterions (eg. certain personnel numbers) according to which the target cascading can be done despite of the organization structure. In the standard functionality the target cascading can be done only based on the organization structure. In addition Company B has done quite a lot of custom programs to ease the system maintenance. For example they have custom program to close all documents in the system in case the employee leaves the company.

What comes to the performance appraisal documents, in Company B there is two new templates created each year for each employee involved in the process. These two documents based on below-mentioned templates are following the structure of the discussions:

1. Target and performance template, which is in the workflow approval process
2. Development and well-being template, which is more of a discussion between employee and manager without approval process

Manager creates the documents for his/hers subordinates and this can also be done by creating documents for all subordinates as a mass. Both documents are went through in both of the discussions (target & development discussions) since they are closely linked with one another, although the different discussions have different emphasized themes as stated before. The linkage between these two discussions and template can be eg. that targets are created based on identified development items.

SAP for performance appraisal in Company B is including per tab:

1. Job description, role and main responsibility areas'
2. My targets; targets, description of the targets, what are the prerequisites for target fulfillment, weighting of different targets, team targets, service time, multiplier. In this tab the Company B wishes to have target library but that is not available in the SAP standard.
3. Overall performance; efficiency, attitude, collaboration, competencies, leadership (if in management position)

Representatives of Company B find SAP very reliable and efficient and no negative feedback about the IT-tool is received from the users. Biggest problem at the time of the interview was related to team targets and how they are related to the organization set-up. In case organization changes so that the team seizes to exist or management position does no longer exist the team targets are left without owner and cascading the targets is no longer possible.

Company B has created also easy-to-use reports to managers and HR who can monitor the discussions from the reports. Altogether the Company B has 6 SAP BW reports related to the target & development discussions:

- Status summary; showing the number of documents and their status
- Target summary; listing personnel and their targets in heading level
- Target fulfillment; showing how well the targets were fulfilled
- Overall performance; showing in a summary level per unit how targets were fulfilled
- Development plans; listing the career aspirations and development actions of personnel
- Well-being summary; showing the average evaluations of respondents per unit and area

What comes to administration and IT support, in Company B the HR department has the process ownership and the concept ownership regarding the performance appraisal process and system. Process owner is responsible of the process and it includes for example planning training and instructions for managers and guiding the target setting. Concept owner on the other hand is responsible for the system and how it functions. In addition in the system development issues Company B has one resource in the ICT department working as SAP Solution Manager with whom the HR discusses the development needs and actions, technical solutions and possible vendor options. Company B has outsourced their IT and in problem situations the error ticket is opened in the IT support which acts as a Service Center. In addition the local HR is proving process support and by some means also system support for the managers.

5.4.Payment determination and merit discussion in Company B

Company B does not have separate payment determination discussion but merit discussion instead. Merit discussion round starts in the early spring and lasts couple of months. Merit discussion is separate discussion from the target and development discussions and is held only with personnel fulfilling certain criterions (eg. in case overall performance is in high enough level). Being invited to merit discussion usually implies that there will be merit raise for the employee. In case employee states during the year his/hers wishes to get payment raise, there exists certain procedure for that but the guideline is that all the payment raises and merit raises are to be handled during the merit discussion round.

Before merit discussion round the available increase is budgeted and managers are informed about the criterions by which the increases can be given. Overall performance plays important role and also payment statistics are used in order to evaluate the employee's payment in relation with others doing the same job in the same territory. HR department is active in monitoring are the increases given to the right people by following eg. the overall performance. The performance of an employee is evaluated based on fulfilment of concrete targets (company level, team level or personal targets) and overall performance. In case the overall performance does not exceed certain level, merit increase cannot be considered. It can be also so that the employee does not fulfill concrete targets but the overall performance is so good that he/she can be invited to the merit discussion round. In the merit discussion round it is also evaluated how much the employee is below or over the median salary in that specific job he or she does.

Based on their position (job and grade) major part of non-production employees of Company B have also possibility to receive bonus in a form of incentives. The amount of target incentive (in % of yearly wage) is determined automatically based on the job grade. Target & Performance functionality in SAP can read job and grade from the employee's basic information and save the information of the incentive program to the Target & Performance document. From the document selected targets are connected to the incentive and the final incentive percentage is calculated based on how well the incentive targets were reached.

There have not been plans or considerations to combine merit discussion and performance appraisal discussions at least not during the SAP implementation project. Representatives of Company B are not able to say why exactly the merit discussion is separate from performance appraisal discussions but most probably the reason is that as stated before, unlike with performance appraisal, not all employees are involved in the merit discussion round. Although the discussions are separate, the target and development discussions serve as stimulus to the merit discussion round.

What comes to actual payment determination process in Company B, there exists no system support for it and eg. SAP's Compensation & Benefits –module is not in use in the company. However the payment info type and payment changes are done in SAP. For new employee, the

payment is determined based on the actual job, job grade, person's capabilities, location country and territory. Payment determination in Company B is described in Figure 22.
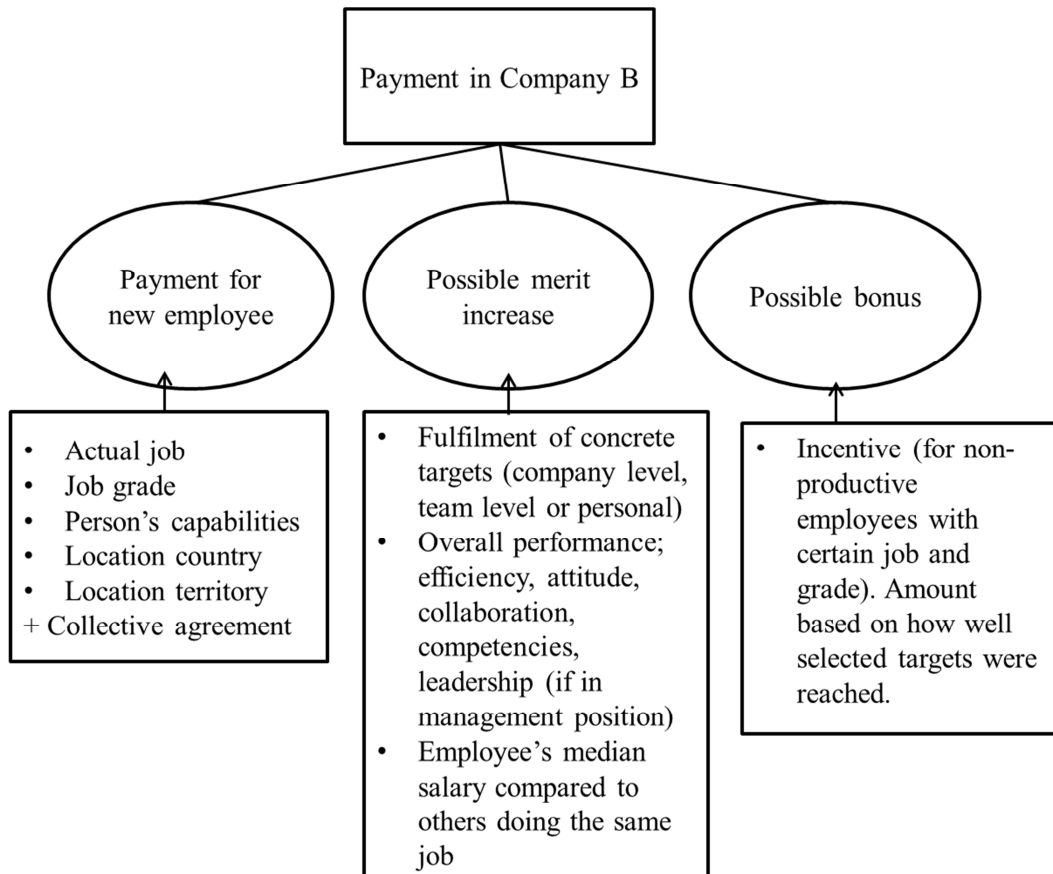
Figure 22 Payment determination in Company B

5.5.Performance appraisal in Company C

Company C calls performance appraisal discussion as target and development discussion, which is held twice a year with almost the same content. In both of these half-year discussions, personal objectives are agreed for the next 6 months. First half-year discussion covers time period from 1st Jan-30th June and second half-year discussion 1st July-31st Dec. The discussions are held in the beginning of these periods.

Company C has had SAP in use in target and development discussions since 2008. In the development phase, a user interface designer designed the interface with the feedback from the users and the SAP consultants built the functionality based on the design. In 2013, they changed from PSP-forms to Web Dynpro Apab -forms, but the process as such remained the same. The number of employees whose performance appraisal is mastered in SAP is approximately 2800.

Feedback from employees regarding two discussions per year has been positive and the quality of the discussions has been seen as very good. Managers who have large teams (eg. 20 subordinates) have felt that two discussions per year is quite a heavy work load for them and there has been pilot on-going in the Company C where large teams working with customer service have done the target discussion as a group discussion and only the development part as one-on-one discussion.

Before implementation of SAP, the Company C had payment related discussion included in the target and development discussions but that was changed since there was willingness to focus to the target and development topics without payment issues taking too much time and attention in the discussions. However, also in the current process, the payment can be mentioned in "Other matters" part but the manager at that point cannot promise any actions. In case manager sees grounds for payment raise, he/she can take the issue up in the following merit round. Merit ground is explained in details later.

SAP functionality for target and development discussions in Company C consists of following tabs:

1. Task; main responsibilities
2. Performance; 8 criterions measured in scale of good, excellent, in the right direction, insufficient
3. Job rotation interest (this is part of the second half-year discussion only)
4. Main objectives for the period; 3 goals as default but number can be increased or decreased and under each goal their fulfillment is documented
5. Development plan
6. Work community and well-being
7. Other matters; eg. payment related topics can be mentioned here

8. Feedback to supervisors (only employee can fill)

What comes to the "Performance"–tab, in second half-year discussion only the general performance is discussed and documented but in the first half-year discussion all the eight criterions are touched and both the manager and employee can insert note below each criterion. The criterions are grouped into two categories and are as follows:

- Potential
    - Commitment; following values, principles and management theses (supervisors)
    - Versatility; will & ability to learn & transform
    - Competence; knowledge, skills, professional competence
    - Inspiration; attitude towards work
- Performance
    - Investment; willingness to work and perform in order to reach objectives
    - Results; ability to reach objectives
    - Cooperation; ability to work with different stakeholders
    - Customer-orientation; ability to take the customer's position and understand what's important to customers

All the data from the documented target & development discussion can be taken into Excel but actual reports are not available in the system. Training calendar is not implemented in SAP so there is no link from the target & development functionality to trainings. In general the target & development functionality in SAP is following the standard functionalities. Only tailor-made solution is that there exists automatic saving. There exists no workflow in the system for approving objectives or other items agreed in the target & development. In addition to the manager, also the employee has possibility to view and insert text to the target & development forms in SAP.

In Company C there is two people working with the target & development process and IT-system; one responsible for the HR IT development and one responsible for the process but who does also configuration in the system. These people are acting also as super users. Actual IT support is outsourced, but first level support is provided by the HR help center. In general quite a lot of problems and issues are solved internally by the two super users / responsible persons.

5.6.Payment determination and merit round in Company C

When new employee is hired to Company C, his/her payment is determined based on collective agreement, level of demand of the work and possible previous experience. Upper white collar workers of Company C have contractual salary and in case of switching tasks, the payment does not automatically change immediately but is affected by the performance and capability of the person in the new position.

All employees of the Company C are also part of either bonus, incentive or commission payment system that is based on performance in the job. Employees working in customer service or service center are part of incentive system. Employees working in business-to-consumer sales are part of commission system. All the rest of the employees are part of bonus system, which is based on company-level Balanced Score Card without any personal key performance indicators.

It has been considered in Company B that bonus system could involve also personal performance as it did before implementation of SAP in 2008, but back then it was felt that the managers' capability to evaluate performance was quite diverse.

Once a year the payment level in Company C is examined in general, a certain merit increase limit is defined as a whole and managers can nominate their subordinates as receivers of the merit increase. Decisions regarding the merit increases are done by the unit heads. There needs to be grounds for the merit increase and the HR manager goes through the grounds with the management before the increases are decided.

Grounds are based on the level of the employee's payment in relation to median payment in the company, the level of employee's payment in relation to the median payment in the market (Compay C is part of market payment study on a yearly basis) and in addition the personal performance of the employee needs to be on an excellent level (8 criterions as described in relation to performance). In addition to these grounds and criterions, Company C can have additional pre-defined criterions per year. These can be eg. has the employee received payment increase within last few years, has the employee changed job within last few years without payment increase etc. What comes to the main objectives defined in the target and development discussion, the fulfillment of them does not have direct impact to payment. However, in case the

objectives are fulfilled, the probability for merit increase is higher than in case the objectives are not met.

Merit round is not handled in SAP, but Excel is used instead. What comes to approving the merit increases, HR makes Excel format list to approvers who perform the approval outside SAP. However, it is technically possible to handle merit increases system-wise, but HR department wants to provide customer service to managers and avoid situations where managers need to handle the merit increase procedure in SAP one-by-one.In case there shall be need for merit increase during the year outside the merit round time period, the manager can handle the merit increase process in SAP involving workflow from manager to HR and unit head.

In the merit round, which is held during April, there are no actual merit payment discussions between manager and employee but the manager informs the receivers of the merit increase. In case there is payment amendments needed after the merit increase round, there is possibility to do payment changes still during November, in case the increase is related to payment inequality due to changed tasks. Payment determination in Company C is described in Figure 23.
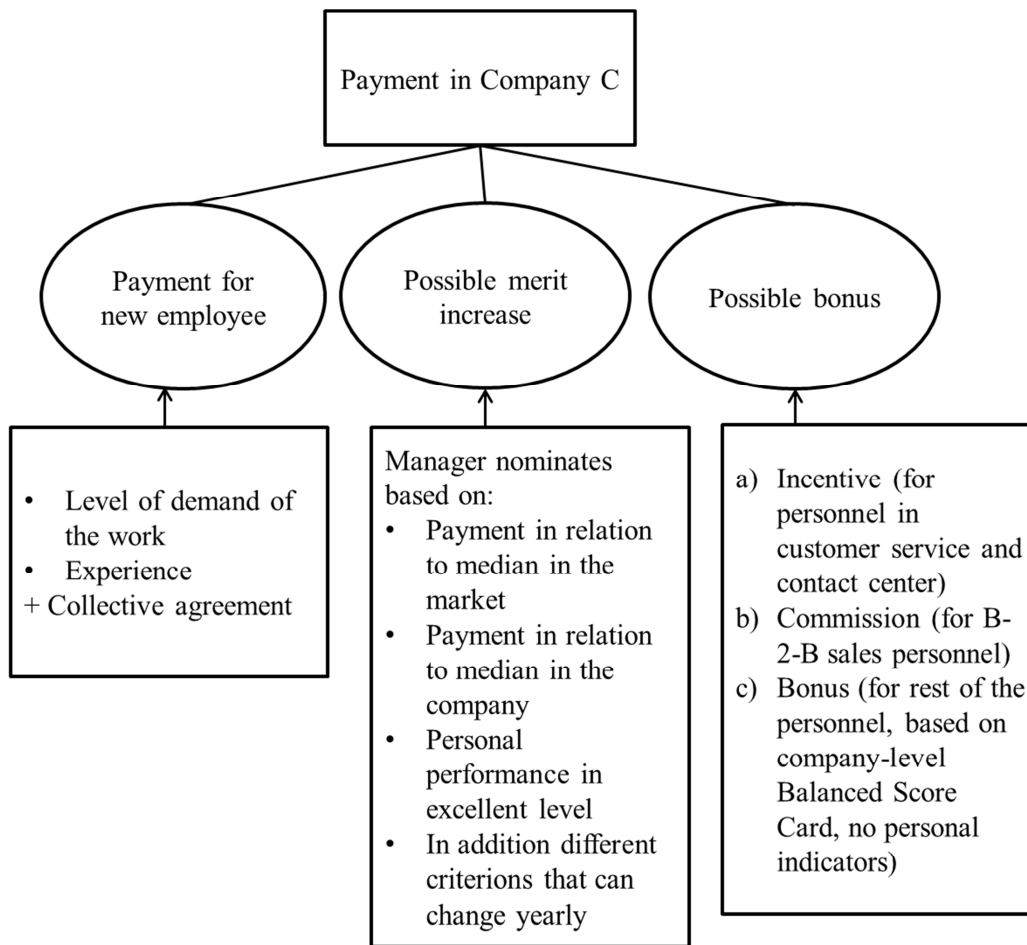
Figure 23 Payment determination in Company C

5.7. Performance appraisal in Company D

Company D is a global manufacturing company with almost 20 000 employees in over 80 countries. SAP HR has been in use in the company since 2002. Enterprise compensation management (Compensation & Benefits) has been in use for 4 years at the time of the interview and SAP Performance Management for 8 years. The performance appraisal called development discussion is held individually with each of the employees. Even the blue-collar workers at the mill have own login to use employee self-service (MSS) for the purpose even though they do not have own computers. All the employees use Employee Self Service (ESS) functionality, managers and HR the Manager Self Service (MSS) functionality.

Company D has global Processes & Projects -team in HR who is centrally responsible for the SAP HR concepts and how the SAP HR should be developed to support the people processes. According to HR Projects & Processes Director, the strong concept ownership is the key issue for functioning HR tools. The principle is that as little customizing as possible is done; if the solution fits 70-80% it is good enough and the process is rather changed than system customized to meet the exceptional cases.

Technical system development, including coding and configuration is outsourced to external service providers who perform the development based on the specifications from Concept owners. HR supports managers every year before the Development Discussions by offering management training where for example good target setting is discussed. In Company D the IT department is involved what comes to IT architecture and platform issues and IT supplier management but the actual development work is outsourced, as previously described. In the HR organization, there are approximately 120 key users covering all locations and they locally maintain the data of all HR applications and support line managers in the tool usage.

The Development Discussions are held typically at the beginning of the year. The Development Discussion consists of two parts; Achievement Review and Target Setting. Competence Assessment is recommended to be done prior of the Development Discussion as it gives good input to the Personal Development Plans.

Technically the Development Discussion and Competence Assessment templates need to be ready by mid-November so that the discussions can start in time. Once the templates are released to the Production environments, it is possible for the employees and line managers to start the target setting for the following review period. Competence assessment, meaning employee skills assessment for competence development purposes is done before or during the development discussion. Items in the competence assessment include general skills, management & leadership competences and professional skills. Competence assessment gives input to the development discussion, especially to the personal development plan and therefore at least the employee self-assessment part of the competence assessment is advised to be done before or during the development discussion.

The development discussion begins with achievement review, which means the evaluation of how the targets of the previous year where met. Person having a manager role in SAP HR can do the target setting to whomever even though the employee is not directly reporting to the manager. This enables that in this matrix organization, also other managers than line managers can give input to the target setting and at the achievement review for example based on project work where the employee has reported to a project manager other than his/hers line manager. This possibility is widely used especially in project work.

In case the targets have not been set with a thought, it is very challenging to do the achievement review. That is why the importance of good target setting is highlighted in by HR and also supported by management training, as described earlier.

Development discussion in SAP in Company D has following tabs and contains following topics:

1. Performance targets
2. Behavioral targets; 8 behavioral expectations based on Company's value-based behaviors (scale 1-5 and none) Number of the behavioral targets can be added or deleted to suit the position of the employee. In this section, the target behavioral level in chosen areas is set.
3. Personal development plan; learning plan, training plan (link to training calendar where courses can be booked), other development remarks
4. Other; job satisfaction, values, teamwork, cooperation, motivation, career aspiration, other. Also feedback to managers can be given in this field but it is not separately asked.

Achievement review has the same tabs as development discussion but in addition the Overall performance evaluation -tab. The targets are evaluated one by one in terms of where the targets met, exceeded etc. In practice this means five point scale (1-5, plus additional "too early to evaluate") and in the Overall Performance Evaluation tab the employee's overall performance is evaluated.

There should be strong correlation between performance targets and behavioral targets but one need to take into consideration the whole performance. There is no pre-defined amount of targets that should be set for each employee, but the guideline is that there should not be too many targets but few well-thought targets instead.

There is workflow procedure in place for the development discussion and competence assessment templates. When either of them is held and the template filled, manager submits the template to the employee who approves or rejects the discussion in SAP HR. In case employee rejects the outcome, there will be new discussion between the manager and the employee. Second level manager can see the development discussion templates and outcome but are not part of the approval process.

Development Discussions are encouraged to do more often than once a year and there is mid-year review option available for that in SAP HR. The guideline in the Company D is that the performance management process should be continuous rather than once-off. Mid-year review can be done during the year as many times as seen appropriate by the manager.

There is Business Warehouse (BW) in use and HR employees, Line managers as well as Finance users have wide range of different reports available. Line managers and HR users have for example development discussion and competence assessment status reports as well as on-time reports.

5.8. Payment determination and merit round in Company D

In Company D the payment discussion is not part of the performance appraisal discussion and no separate payment discussion is held with the employees. What comes to payment determination, when the position opens, it has certain grade and range that are locally set and compared to market data.

There is a yearly merit planning process in case the Board of Directors decides that the business situation in that year allows merit increases. The overall performance evaluation gives input to merit planning. Depending on the merit budget, HR creates merit matrix. If the country merit budget then allows, the manager can plan merit increases based on the matrix. This planning is done in SAP. Timing of the merit planning can be different each year but it is always after the achievement review since the overall performance information is needed when deciding about merit increases. Compensation planning and compensation approval section in SAP related to merit planning is open to the management only during the time window of the merit round.

In addition, approximately 10% of the employees in Company D is part of a group who can also receive bonus. Bonuses are also handled in SAP. Issues affecting the bonus are company performance, business performance as well as individual elements. Based on recent satisfaction survey, the employees of Company D are very satisfied with the supporting tools what comes to development discussion and merit planning functionalities. There have not been discussions or plans to combine development discussion and merit round. Payment determination in Company D is described in Figure 24.
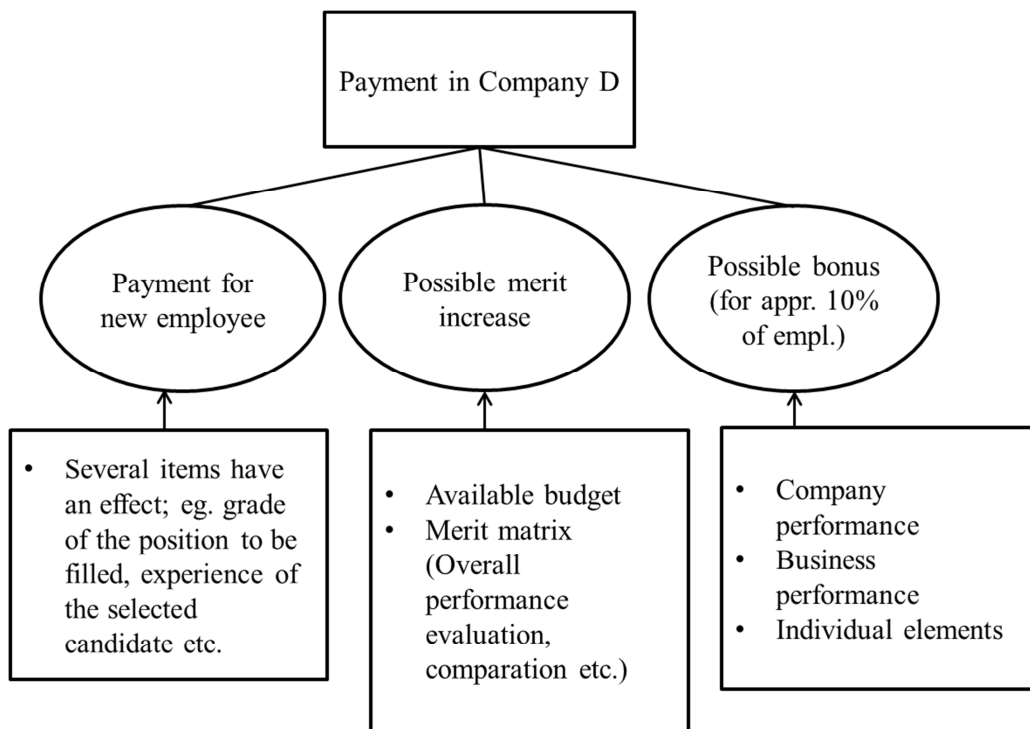

Figure 24 Payment determination in Company D

6. SUMMARY AND DISCUSSION

The research problem of this study was to examine how performance appraisal and payment determination processes can be combined as a process and as an IT-tool in SAP. In addition, the aim of the benchmark study was to give to Kela's IT and HR management further information regarding whether benchmarked companies are combining appraisal and payment determination processes, and what are their experiences regarding the combination / non-combination as well as how the case companies have built the technical solution in relation to this process.

Concerning discussion of should payment issues be linked with performance, based on the literature review, there exists both support and resistance to the topic. It seems that the success of the combination is also heavily related to the payment system and organization. Research by Lawner (2003) revealed, that performance appraisals where considered to be more effective in cases where the outcome of the results were linked to payment determination. On the other hand, research by Heneman and Werner (2005) found out that merit pay was more related to improved employee attitudes than improved performance. There exist both psychological and economic theories supporting the linkage of performance and pay. Both economic and psychological theories supporting the linkage imply that the combination of the payment and performance would enhance the individual employees' performance and by that increase the overall performance of the organization (Maanieniemi, 2013).

As well as support, also criticism is found towards linking pay-to-performance. Critics regarding linking pay to performance are arguing eg. that payment is not the main motivator for employees, but job satisfaction can be derived from eg. responsibility, recognition or optimal amount of challenges. (Maaniemi, 2013). It seems that no single truth is available to the questions whether pay should be linked to performance.

What comes to the fit of pay-for-performance systems in public sector, based on this earlier research, linking pay to performance in public sector seems to be more challenging than in private sector. The challenges with linking pay to performance in public sector include lacking of clear linkage between performance and outcome, and lack of funding for rewarding good performance (Ingraham, 1993). In addition according to Ingraham (1993) in public sector

managers do not have enough flexibility, legitimacy and control over the budged, and employees in the public sector may be motivated better by other means than actual monetary payment.

Since the topic of the study relates to issue of combining the performance appraisal and payment determination processes, naturally the experiences of the benchmark companies regarding combining these two issues and reasoning for the separation is utmost interesting.

Company A, which is a public organization had separated their payment determination and performance appraisal discussions that used to be held as one combined discussion. Reasons for separating the discussions were that the satisfaction towards performance discussions had been poor and there had been feedback that these two discussions should be separated since it was felt that the payment was having too big role in the combined discussions and that the combined discussions included overall too many topics. This led to the situation where performance appraisal topics did not receive enough attention and time in the discussions. This item was also one of the arguments in the literature against linking pay to performance. It is felt in Company A that separating especially development needs and feedback from employees to supervisors from payment discussions ensures honest and direct communication between employee and manager when discussing these topics.

It is to be noted that even though the two discussions are now separated in Company A, there exists still strong link between performance and payment since the targets are set in the payment discussions. Topics in the payment discussion in Company A include performance evaluation of the previous period, setting targets for the coming period, job description and discussion about the level of demand of the work. In other words, the payment discussion in Company A is very much focused on performance management. In the performance appraisal discussions, however, the emphasis is more on job well-being, motivation and other non-money related issues.

Before implementation of SAP, also the Company C had payment related discussion included in the target and development discussions but that was changed since there was willingness to focus on the target and development topics without payment issues taking too much time and attention in the discussions. However, also in the current process, the payment can be mentioned in "Other matters" part but the manager at that point cannot promise any actions since payment issues are normally handled during merit round.

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Table 7 summarizes the main findings from the benchmark study what comes to performance appraisal discussion and Table 8 what comes to payment discussion and merit round. What can be interpreted is that private sector companies (B, C, D) have quite the same kind of performance appraisal discussions content/topic wise as well as quite similar merit round procedures. However it is interesting how differently the private sector companies have divided the performance discussions; Company B has two discussions with different topics, Company C has two similar discussions, and Company D only one discussion but possible but not mandatory mid-year reviews. One common feature for all benchmarked companies is the resourcing related to the process and system; in all companies the process and system is owned by HR and IT development as well as support outsourced to external companies.

Main finding of this research, based on the benchmark study is that there seems to exists more support for keeping payment and performance as separate topic and process, including separate discussions. This finding is based on the experiences of the case companies regarding separate and joint discussions. It should be however noted, that even though the performance appraisal and payment discussions were separated into two discussions in one of the case companies, there exists still strong link between performance and payment since the targets are set in the payment discussions.

Table 7 Performance appraisal discussions in benchmarked companies

	Company A	**Company B**	**Company C**	**Company D**
What kind of performance appraisal discussions	• Performance appraisal discussion • At least 1-2 follow-up / situational discussions during the year	• *Target and performance discussion* (target setting and closing previous year) • *Development and well-being discussion* / mid-term discussion (mid-term situation, job well-being and personal development)	*Target and development discussion* twice a year covering periods of 1.1-30.6 and 1.7-31.12	• *Development discussion* (Achievement Review & Target Setting) Note: Competence assessment done before or during the development discussion (general skills, management & leadership competences and professional skills) • mid-year review option available (can be done during the year as many times as seen appropriate)
Timing of the discussions	Decided independently by each unit (normally spring)	• Target and performance discussion beg. of the year • Development and well-being discussion end of the summer / beg. of Autumn	Discussions held in the beginning of the periods	Beginning of the year

Topics in performance appraisal / IT-tool	• Joy of working • Pre-requisites for work and job well-being • Work community and supervisory work • Own / unit / additional topics • Future plans • Other information and wishes for the next 2 years • Training & education	• Job description (role and main responsibility areas) • My targets • Overall performance; efficiency, attitude, collaboration, competencies, leadership (if in management position)	• Task; main responsibilities • Performance (8 criterions) • Job rotation interest • Main objectives for the period (3 goals as default) • Development plan • Work community and well-being • Other matters (eg. payment related topics) • Feedback to supervisors	• Performance targets • Behavioral targets (8 behavioral expectations) • Personal development plan • Other (job satisfaction, values, teamwork, cooperation, motivation, career aspiration, other, also feedback to managers can be given) • Overall performance evaluation
Resources working with process and/or system	• 2 super users/ process owners from HR department • 1 IT person involved in IT supplier management • IT support provided by the IT-system provider	• 1 process owner from HR (process, training, instructions) • 1 concept owner from HR (system) • 1 SAP Solution Manager from IT • Outsourced IT Service Center • Also local HR gives support for managers	• 2 super users (1 responsible for the HR IT development, 1 responsible for the process)) • Outsourced IT support but first level support provided HR help center.	• Process owner in HR • Technical system development outsourced to external service providers • IT involved in IT supplier management • Key users in local HR units supporting managers
IT-tool	Own tailor-made	SAP	SAP	SAP

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How many employees' discussions mastered in IT system	5 100	4 000	2 800	20 000
Who uses IT-tool	Both employee and manager	Only manager (no ESS available but has been under discussion)	Both employee and manager (ESS & MSS)	Both employee and manager (ESS & MSS)

Table 8 Payment discussions or merit rounds in benchmarked companies

	Company A	Company B	Company C	Company D
Type of discussion	Payment discussion	Merit discussion round	Merit round; yearly general payment level examination (a certain merit increase limit is defined as a whole and managers can nominate their subordinates as receivers of the merit increase.)	Merit round, yearly merit planning process in case the Board of Directors decides that the business situation in that year allows merit increases
Timing	During Autumn	Starts early spring and lasts couple of months	April	NA
Employees involved	All	Manager nominates based on criterions	Manager nominates based on criterions	Manager nominates based on criterions
Topics discussed / topics affecting the raise	• Performance evaluation of the previous period • Setting targets for the coming period • Job description • Discussion about the level of demand of the work.	• Fulfilment of concrete targets • Overall performance (efficiency, attitude, collaboration, competencies, leadership) • Employee's median salary compared to others doing the same job	• Payment in relation to median in the market • Payment in relation to median in the company • Personal performance in excellent level • In addition different criterions that can change yearly	• Merit matrix (Overall performance evaluation, comparation etc.) • Available budget
System support for the payment discussion	Yes, handled in same system than performance appraisal	No	No	Yes, SAP

6.1. Limitations

It must be noted, that the empirical study conducted has certain limitations. First of all, the sample size of the empirical study is rather small, consisting of four benchmarked companies. However the more crucial limitation what comes providing information to Kela's management is the fact that the optimal benchmark company was not found.

As discussed earlier in chapter 4.1 when the benchmark company selection was introduced, the optimal benchmark company would have been a public organization which has combined performance appraisal and payment determination processes both as a process and as system wise and which utilizes SAP in this purpose. Instead, in the end the companies were chosen based on that the criterions that they should use SAP in performance appraisal OR they should have experience of combining performance appraisal and payment discussions.

Introducing the new performance appraisal and payment determination process and SAP functionality of Kela has also certain limitations what comes to the generalizability of that information. As discussed, Kela is a public sector organization having its own collective agreement and very Kela-specific payment determination including tailor-made system for handling it. Therefore the process and IT solution may not be generalized to other, mainly private sector companies.

6.2. Recommendations for future research

Recommendations for further research divide into two categories; further research regarding the topic in general, and further research regarding Kela's solution. As discussed earlier, there is a lot of support and criticism available towards linking pay to performance, but no actual outcome to this dispute seems to be available. This topic needs more investigation and further search, even if it might be that there exists no one truth. Finding companies who have combined performance appraisal and payment discussed processes and preferably, also the IT-tools and collecting data based on their experiences is recommended.

What comes to Kela and their experiences, further research is also recommended. As discussed, the new process and IT functionality has been in use since January 2015. It would of interest to collect experiences after few years from the implementation of the process and functionality.

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APPENDIX 1: BENCHMARK QUESTIONS

Note: The questions are translated from Finnish to English

Process

- What kind of a payment determination process you have in your company?
- What kind of a performance appraisal process you have in your company?
- Are payment discussions and performance appraisal discussions held together or separately? Why?
- Has there been plans to combine/separate these discussions? Why?
- What kind of experiences your company has from combined/separated processes? (feedback from managers, employees)

IT-system

- What IT-system you have in your company for payment determination and performance appraisal discussions purposes?
- How payment determination is handled in the IT-system?
- How performance appraisal is handled in the IT-system?
- How much in your company you rely on standard processes and how much you have tailored them? Has it paid off?
- How many IT people in your company works with the payment determination and performance appraisal IT-system?