Managing Human Capital Through the Use of Performance Improvement Plans

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Management of human capital through the use of performance management systems and performance improvement plans is of the utmost importance to managers. Employees are the most valuable assets companies possess. Effective management of human capital can have a direct impact on individual and team performance, as well as the success of the business. This paper focuses on the use of the performance improvement plan and its impact on employee performance outside of the progressive disciplinary process. In this paper, we review the existing literature on human capital and performance improvement plans, and make managerial recommendations for the use of performance improvement plans going forward.

Keywords: human capital, performance improvement plan, performance management

INTRODUCTION

From an economic perspective, the management of human capital is a critical concern as it relates to overall business performance (Samson & Bhanugopan, 2022; Thuda & Maharani, 2019). Employees are arguably the most valued resource in business, while also being the most volatile (Hall, 2008; Mehale et al., 2021). There are many factors that influence the overall volatility of human performance in the employment setting. For this paper, the focus will be on the performance management strategy known in the human resources discipline as “Performance Improvement Plans (PIP)” and the use of performance management strategies in the organizational setting.

HUMAN CAPITAL MANAGEMENT & PERSONNEL ECONOMICS

Labor economics broadly focuses on various factors in labor markets. This includes personnel economics, which centers on “the set of marketable skills of workers as a form of capital in which workers [and employers] make a variety of investments” (Acemoglu & Autor, 2011, p. 3). It is important to differentiate the greater labor economics from personnel economics in that “personnel economics is a branch of labor economics but there is a great deal of labor economics that is not [part of] personnel economics” (Lazear & Oyer, 2007, p. 2). This paper focuses on the latter with respect to the “interactions between firms and workers” in the context of performance management (Lazear & Oyer, 2007, p. 2).

Human Capital Theory emerges in the study of labor economics as the recognition that "people's learning capacities are of comparable value to other resources involved in the production of goods and services" (Nafukho, Hairston & Brooks, 2004, p. 546). The research of human capital scholars helps quantify the returns on investing in professional development opportunities for employees as part of operational costs, though this can be difficult to specify due to the variability or even lack of "systematic plans for growing human capital" within organizations (Hall, 2008, p. 20; Nafukho et al., 2004). Still, through the lens of labor economics, specifically the branch of personnel economics, the business world knows that focusing on human capital creates competitive advantage in the greater labor market (Hall, 2008). Employee costs may "exceed 40 percent of corporate expense" which necessitates careful attention to the ROI of human capital by organizational leaders (Fitz-Enz, 2000, p. 3). There are many strategies organizations may employ to advance human capital in accordance with the principal objectives of personnel economics, which is to improve market gains and production/service delivery (Zeb et al., 2018). Addressing employee development and performance is especially vital and a sound starting point since investing in the knowledge, skills, and abilities of employees is critical for strategic positive organizational performance (Zeb et al., 2018). Like any resource, when optimized, individual and group performance leads to business gains (Nafukho et al., 2004). Additionally, a strategic human capital investment plan may help mitigate adverse and costly business outcomes and increase worker commitment (Galunic & Anderson, 2000).

HUMAN CAPITAL MANAGEMENT & EMPLOYEE PERFORMANCE MANAGEMENT

The focus of human capital management is the management of people within an organization as a resource (Ward, 2009; Thuda & Maharani, 2019). Features of human capital management focus on optimizing the workforce. This includes a full workforce performance and employment life cycle focus, which includes many factors like recruitment/retention, training and development, employee relations, and performance management (Hall, 2008).

This paper focuses on the impact of performance management as it relates to contributing to individual employee performance advancements when lagging in accordance with legitimate business prescribed performance expectations. This is a risky approach from a personnel economics perspective, as existing research supports that team productivity is often greater than individual productivity, making the emphasis on managing team performance a more attractive investment (Lazear & Shaw, 2007). That said, poor individual performance is disruptive to team performance, as "organizational performance accrues from the performance of individuals" even if the adverse observable outcome is insidious (Aguinis et al., 2011; Kurz & Bartram, 2002, p. 229). To address this, the authors focus on the Performance Improvement Plan (PIP), a commonly used strategy in employee disciplinary stages of performance management practices for individuals (Sahoo & Mishra, 2012).

PERFORMANCE IMPROVEMENT PLANS

Performance improvement is a continuous process of improving that uses "a systematic methodology to find the root cause of a performance problem, and then implement an intervention that applies to that specific performance deficit" (El-Daghar, 2018, p.1). From an employee relations perspective, performance improvement plans (PIPs) are a feature of an organization's performance management strategy (Nordli, 2021; shrm.org, n.d.). PIPs may be used in accordance with standard performance appraisal processes, such as annual performance reviews and are most impactful when employees are given the opportunity to take a participatory approach for goal setting (Wilder et al., 2011). Designing and implementing a PIP helps to outline performance goals for employee professional development as well as track employee progress of same. Promotions or other material changes of job duties may also trigger the need for a PIP (Kirkpatrick, 1982). The aforementioned examples of the PIP are often included as part of employee training and development practices and do not necessarily signal performance related issues or deficiencies.

Conversely, PIPs may be embedded within an organization's employee disciplinary process (McConnell, 2011; Nordli, 202; Miller-Merrell, 2021). The disciplinary process is the managerial procedure in which unfavorable employee behavior and/or poor performance is documented and addressed by management (Chai et al., 2021). When used in this way, the PIP is generated to demonstrate the organization's attempts at clearly communicating performance expectations and documenting performance failures. Providing a PIP to poorly performing employee is often a collaborative effort between the employee's direct supervisor with guidance from human resources (shrm.org, n.d.). In these instances, the PIP is commonly associated with consequences, such as demotion or termination, if the poorly performing employee fails to meet the objectives outlined within the PIP in the prescribed timeframe. The PIP is intended to be a concise tool to help assess the individual performance of employees in relationship to specific performance objectives as "measuring the output of individual workers is often difficult" (Lazear & Shaw, 2007, p. 110).

Unfortunately, PIPs are more often used in the disciplinary process instead of the more positively perceived performance appraisal process (Nordli, 2021). This comes from the fact that historically, organizations tend to have more precise disciplinary processes than formal professional development processes (Kirkpatrick, 1982). This is a missed opportunity, as training and development is worthy human capital investment which leads to higher performance rates and ultimately greater production and service (Martins, 2022; McConnell, 2011).

Employee perception of PIPs matters for the effectiveness of this performance management tool (Miller-Merrell, 2021). If the organization only uses PIPs as part of the disciplinary process, employees may associate this professional development opportunity with negative outcomes only (Nordli, 2021). Negative associations with performance improvement interventions may impact employee commitment and reduce trust in the supervisory relationship (Nordli, 2021). This is problematic because "obtaining higher levels of employee commitment is important in markets in which quality and customer satisfaction are key to competitive success" (Osterman, 2011, p. 645). This negates the purpose of investing expensive time and resources into the PIP as employees are unlikely to meet the demands under such circumstances. The effectiveness of the PIP is reduced, potentially leading to unintended adverse outcomes for the employee. Investing in a process with little potential for a positive outcome detracts from human capital growth potential.

Employees undergoing a PIP, in conjunction with the disciplinary process, may be quicker to experience poor states of wellness, such as stress, a leading cause of burnout (Knight & Ukpere, 2014; Miller-Merrell, 2021). Motivation may also be disrupted or skewed during the PIP under duress of looming consequences or experiences of fear (Ryan & Oestreich,1998). Intrinsic factors, such as personality may influence the employee's job performance and behaviors during the performance management process (Chefu, 2022). Extrinsic factors, such as the general work environment, or interpersonal factors, like relationships with leadership or peers, may also influence the success of performance management interventions (Ahuja et al., 2018). Due to the variability of related factors that potentially impact the success of performance interventions, such as PIPs, causality requires additional research. That said, it is reasonable to imagine there may be the potential for poor outcomes associated with PIPs when embedded in the disciplinary process.

Employees are not the only ones that may suffer unintended adverse outcomes associated with PIPs embedded within disciplinary structures due to the emotional nature of the exchange (Miller-Merrell, 2021). Managers who supervise the PIP process may also suffer poor work outcomes such as stress related burnout and emotional dissonance if they experience a conflict of emotion (Humphrey, 2012; Pugh et al., 2011; Riforgiate et al., 2022). As an occupational requirement, emotional labor requires the employee (in this example, the manager) to look and act in specific ways to meet the demands of the job (Grandey et al., 2015; Grandey, & Sayre, 2019; Humphrey et al., 2008). This is most likely in instances where the manager is using the PIP as a way to manage the employee to termination because the manager is simultaneously navigating their own emotions while also attempting to manage the emotions of others, a key aspect of emotional labor (Humphrey et al., 2008). Committing to the development of the employee, as required by the PIP process, may result in emotional dissonance (a conflict between how they are supposed to feel and how they genuinely feel) if management does not feel the employee's performance is salvageable (Pugh et al., 2011; Van Dijk & Brown, 2006). Additionally, prolonging the inevitable termination of the employee may disrupt general business performance or influence the workflow of others in a negative way. Poor performance generates losses (Thuda & Maharani, 2019). Dedicating additional resources (time, supervision, attention, training etc.) to a poor performer increases and compounds the expense associated with these losses.

MANAGERIAL RECOMMENDATIONS REGARDING PIPS

Personnel economic theories and practices help shape and inform human capital management strategies and human resources practices (Thuda & Maharani, 2019). Performance management is integral to this as a means of addressing human capital, as "all forms of capital must be evaluated and analyzed in context to understand how people drive business performance" (Baron, 2011, p. 30). PIPs are a tool to help management evaluate individual performance (McConnell, 2011). The following managerial recommendations offer insights on how to effectively use PIPs while striving for strategic human capital strategy. Based on this, it is recommended that managers and organizational leaders consider the following:

- Review existing performance appraisal strategies. How does the organization use them? "Performance appraisals may have other uses, but the main justification for having them is to motivate employees to perform their jobs well" (Cappelli & Conyon, 2018, p.97).
- Do not use PIPs solely for disciplinary purposes. PIPs can be valuable training and development agendas (Kirkpatrick, 1982). Focus on initiatives that serve the organization overall and not professional development that solely benefits the employee. This will help protect the human capital investment for the organization. "Effective performance management would enable employee engagement and also ensure that employees have clarity on their goals" (Luthia, 2022, p.116).
- Use progressive discipline to address performance failures in real time with no prolonged periods of sustained poor performance. Durbin (2021) defines progressive discipline as "corrective action that involves a progression of steps to help guide an employee from inappropriate or undesired behavior to behavior that supports organizational goals" (p.30). Provide employees with clear feedback regarding their performance and the associated consequences as part of the progressive discipline process.
- Identify whether or not it is skill/professional capability or will causing performance issues. If it is behavioral, PIP is not appropriate as this is a tool directed at business goals. If the employee is not salvageable do not waste organizational resources (Nordli, 2021). However, it is the manager's responsibility to encourage employees to have open lines of communication, to be involved and convey their views, and to assist employees in achieving their goals before making that determination (Ravesangar & Fauzi, 2022).
- Maintain a human capital growth mindset as it relates to performance management. Identify how this performance intervention contributes to human capital growth for the organization. Use the guiding question of how does this performance intervention at the individual level help to contribute towards optimal productivity and service delivery for the organization at large (Luthia, 2022).
- Differentiate between employee benefits and human capital investments and adjust policies to align with this. For example, offering tuition reimbursement programs that do not have pay back conditions associated with company separation, or are not specifically related to the type of work the employee is doing for the employer, is an employee benefit. Adjusting this same offering to include time in job commitments and with clearly defined ways this additional education will benefit the organization may be a worthy human capital investment. The idea is to design your human capital strategy and implement your policies to create a continuous benefit to the organization. For example, paying for education that will help employees build a

much-needed technological advancement or program for the company will remain a benefit long after the departure of the existing employee.

CONCLUSION

PIPs are a powerful tool that when utilized correctly can mitigate employee performance issues and contribute to strategic human capital management (Lee, & Rhee, 2020). If not used strategically, PIPs provide little value for the employee or the organization (Nordli, 2021). The focus of performance management initiatives should remain on improving the organization through increasing productivity, service delivery and should result in measurable gains over time. By using performance management tools such as PIPs correctly, managers can work to improve employee performance and minimize the need for progressive discipline by assisting and engaging employees in their own improvement and development in a systematic way. Changing the way PIPs are used with regards to a focus on improving performance, as opposed to a precursor to termination, can drastically improve the way employees perform at work.

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