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# Goal Setting: What Has Gone Wrong and What Can Be Done?

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One does not need to read a great deal in the media to understand that many companies have made large bonus payouts for results that were of questionable value. Many bonus or incentive pay plans have become entitlements. Sometimes employees receive performance ratings or bonus payouts that do not reflect their actual performance or that of the organization. And frequently performance ratings show that most people are "above average," even when business unit or organizational performance does not justify this rating. Goals are dictated to people in some organizations with little involvement or basis on realistic business conditions. Organizations that are concerned about losing talent frequently provide performance ratings or bonus payouts despite the performance facts. It is no wonder that when performance reviews, merit increases or bonus payouts are made in this context, goal setting lacks real credibility with the employees these processes are intended to inspire.

This paper examines the tasks that lead to effective (or ineffective) goal setting for organizations and individuals. There is a great deal of research now available on goal setting and the factors that make it effective. Unfortunately, many managers, executives and board members have their own beliefs about what makes goal setting effective. This is often based on their prior experience with little understanding of the reasons why a particular experience was successful or unsuccessful. Therefore, this paper also examines the fundamental principles that create best practices and reviews some of the common practices in the marketplace regarding goal setting. It is time to employ a process of goal setting that will result in strong commitment and high performance. This paper can serve as a guide for developing the approach that will enable employees and the organization to create strong competitive advantages and achieve high performance.

## 10 KEY TASKS

When one examines goal setting and seeks to improve the process, there are 10 key tasks to make it effective. These tasks are based on well-documented and researched principles of human motivation and performance. Following are the 10 key tasks:

### 1 | Determine the most meaningful measures on which goals will be based.

There were times when the only measures used by companies were financial results – revenues and profits. Over time, the types of measures have expanded to include the long-term value created by the results and the actions that produce these results. Long-term metrics reflect the value of the enterprise in the market or to its mission over time. Measures such as total shareholder return (TSR), return on invested capital and growth in marketshare are some of the most common. They reflect how an organization utilizes its resources and assets to expand its market leadership, improve its profitability and increase the value to shareholders and other stakeholders. Further, by understanding the determinants of financial results, companies are better able to focus on measures that are leading determinants of desired performance. Profits reflect what was done in the past. To improve the results, people need to understand and focus on the most important drivers of financial success, such as customer satisfaction, employee engagement, operating or gross margins, on-time-delivery or lead time, quality, productivity, etc. By focusing only on end result financial measures such as revenues and profitability, the drivers of this performance are generally left unmanaged.

Table 1 shows the types of measures used by organizations for different levels of employees (Mercer 2008-2009). It shows both the types of measures that are used and the relative weighting of them to determine bonus payouts.

The measurement and goal setting process needs to define *what* needs to be achieved, *how* it should be done and why this performance is important — it creates a path from mission and strategy to milestones and actions.

### 2 | Identify the frame of reference for setting goals.

Perhaps one of the most difficult aspects of setting goals is to determine what should be the actual goal. At the heart of this issue is the level of confidence people have in achieving the goal and the level of desired performance

**TABLE 1** Types of Measures

| Employee Category | Financial Measures | Operational Measures | Customer Based Measures | People Based Measures |
|---|---|---|---|---|
| Senior Executives | 94% | 57% | 30% | 25% |
| Directors and Managers | 92% | 61% | 31% | 28% |
| Professional (non-sales) | 88% | 59% | 29% | 20% |
| Professional Sales | 89% | 50% | 30% | 14% |
| Office/Clerical and Administrative | 85% | 61% | 32% | 18% |
| Production/Service and Operational | 84% | 64% | 33% | 14% |

improvement. Successful companies define the basis for the goals (actually and philosophically) as:

- Improvements in performance from the prior year (or period)
- A comparison to external benchmarks, such as peer companies or objective standards as one finds with industry standards
- Forecasts of expected revenues, spending plans, cost, etc.
- What people believe is important and achievable (bottom up plans)
- Strategic, long-term requirements (top down plans), milestones or other performance requirements to meet long-term goals.

There is little data on which reference point is most prevalent or reliable. This depends on the type of measures used, the level in the organization for which the goal is being set and the availability and relevance of existing data. The important message here is to identify and understand the comparisons and assumptions that are used to establish the goal. Much conflict and confusion can be avoided by clarifying this task.

**3 | Establish the framework and mechanism for measuring goal performance.**
The simplest form of goal is a "binary goal" — Did you meet this goal, yes or no? This means that only one level of performance needs to be established, and if one does not meet this goal, there is no payout. Further, if one exceeds the goal, then there is no additional payout. The rules are simple and clear, but *ineffective*. Defining the desired performance often requires critical thought and an understanding of the context — strategy, current priorities, interdependencies and capabilities. If the measure has a range of goals associated with it, then the pressure to manipulate the level of challenge or the assessment of performance can be minimized. This means, however, that a range of goals needs to be discussed and different payout opportunities need to be determined based on the importance, probability of achievement and reliability of the measure.

**4 | Determine the level of "stretch" required by the goal.**
The important principle that underlies this task is the *probability of achievement*. How likely is the goal to be achieved at X, Y or Z level? David McClellan, one

of the early founders of modern theories on human motivation, concluded from his research that the level of achievement desired for maximizing performance is one where the goals were seen as both challenging and achievable (1961). While this criterion is obvious, it reflects an important balance in the level of difficulty of a goal. The most common practice of companies is one that utilizes the following framework:

- **Threshold** — Minimum level of *acceptable* performance – 80 percent probability of achievement
- **Target** — The *desired* level of performance – 60 percent to 70 percent probability of achievement
- **Exceptional** — Performance that is *clearly beyond* established expectations and reflects outstanding performance — 30 percent probability of achievement.

This provides a range of goals associated with a measure as described in the previous task. So the question is: What is the probability of achieving each level of performance? A study completed by Hewitt Associates found that 83 percent of high performance company leaders believed their companies will achieve their target performance, but only 54 percent of low performance companies felt their goals were achievable (2003). Does the belief in target achievement lead to high-performing companies or do low-performing companies have less confidence in their ability to achieve their goals? Which is the cause and which is the effect?

The degree of difficulty often reflects a company's culture, standards and experience with goal achievement. If goals are seen as too easy, achieved consistently and require little extra effort, then they are simply not motivating. Employees become complacent and the payouts become an entitlement. If the goals are seen as unachievable, they create a different, but similar low-motivation environment. Employees give up, see little chance for success and may set lower personal goals they perceive as more realistic in order to gage their own performance. Or, they may simply regard the goal-setting process as a useless exercise, further undermining the credibility of the organization's leaders.

To reflect the likelihood of goal achievement, the Hewitt study noted above found the following in companies that believed their target performance would be achieved. (See Table 2).

Companies that see target performance as requiring a significant stretch (such as less than 30 percent probability of achievement) should probably ignore goal

**TABLE 2** Probability of Achievement

| Likelihood of Target Achievement | % of Companies |
|---|---|
| 10% — 40% | 4% |
| 50% — 60% | 30% |
| 70% — 80% | 42% |
| 90% — 100% | 24% |
| 71% | Overall Average |

setting and find some other means to guide performance. They are not likely to be a sustainable high-performance company. Equally, companies that set goals that are easily and consistently achieved or exceeded are not challenging their employees sufficiently; they will also not likely be a high performer in the marketplace.

**5 | Determine if the goal is based on an absolute or relative level of achievement.** This task is similar to the frame of reference with an important difference. An *absolute* type goal implies that if X is achieved, then $Y will be made as a payout. It shows a clear quid-pro-quo relationship. The task then focuses on what is measured and how reliable is the information on which assessment of performance is based. A *relative* type goal implies that actual performance is based on a comparison to an external index or reference to determine the level of performance and payout. Examples of this are most common in executive and investment management positions. For some executives, a portion of their variable pay (cash or long-term incentive or equity awards) is based on how well the company's financial performance compares to a set of peer-group companies or a market index, such as Standard & Poor's 500 or Russell's 2000 companies. In investment management, a bonus may be earned if the returns on one's investment portfolio meet or exceed a comparable market index as opposed to an absolute return on investment percentage. If the company does well, but so do similar organizations in the same market, has the company truly achieved desired performance? If the company's profitability declines dramatically, but is higher than the comparator group, did the company really fail in meeting its goals? Depending on who and what measures are being considered, this issue may be important to consider when setting goals.

**6 | Determine the effective balance between quantitative and qualitative goals.** As discussed above, financial and operational metrics are usually very quantitative. The level of achievement can be objectively determined, at least that is the prevailing assumption. Qualitative goals are usually based on judgment and require discussion and analysis. The primary issue here is what makes the goal and the performance assessment verifiable? Most astute financial executives know that financial results can be manipulated to reflect desired performance achievements. Although new Securities and Exchange Commission (SEC) regulations have increased the transparency of financial reporting and placed significant accountability on the CEO and CFO for the accuracy, financial and operational results can often be interpreted. Further, if a group of independent individuals examined certain qualitative information and reached the same conclusion about performance, then isn't the assessment reliable? Who (with the knowledge and authority) can say the goal was not achieved?

The forces that influence the desire to manipulate results are usually related to the level of risk of failure and the payout opportunity associated with the results. If either is too high, then individuals are tempted to distort the results in order to achieve a personal gain (or protection). Once again the principle is to establish a series of goals that are meaningful and verifiable to the individuals and organization. Goals should not be limited to only what can be counted; they should define what the organization needs to do to be successful. This enables the performance and the associated payouts to reflect the full picture of performance of the organization, business unit and individual.

**7 | Determine the right balance between individual and group performance.** One of the most challenging tasks that need to be resolved in setting goals is the relationship between the performance of the individual employee and the group — team, department, region and company. When individual goals are emphasized, the organization creates a clear alignment between the performance of the employee and his/her resulting rewards (e.g., bonus payouts). This reinforces accountability and individual initiative. However, it discourages collaboration, communication and resource optimization. This approach creates silos; employees may tend to engage others when they know that they have achieved their own goals or these actions will benefit them personally. When group goals are emphasized, the organization reinforces a common fate, collaboration and optimization of shared resources. Desired performance is often achieved only by the combined efforts and talents of many employees. However, the approach reduces the ability to recognize and reward high-performing individuals, and may discourage employees from taking initiatives or actions where they will see little personal benefit. In fact, in some organizations employees that exercise high personal initiative are treated as "rate busters." Their behaviors will soon return to the "norm" or the person will leave the organization.

One of the key elements of effective goal setting is to identify the unit for which the performance goal is established: individual employee, department/team, region/division or overall company, and the weight when assessing overall performance. Most companies resolve this issue by using multiple measures or funding mechanisms for bonus plans that reflect the appropriate balance. The discussion of weighting these measures should determine the optimal balance. Table 3 shows the percentage of companies in a recent Wilson Group survey that uses measures from different segments of the organization by employee group (2007-2008).

One interesting observation about this table is that is shows relatively few organizations that focus their performance measures on business units and departments or divisions, particularly at lower levels where employees would most likely have the greatest impact. This survey data shows common practice, but is it best practice? The important question for the organization seeking to improve the goal-setting process is how to resolve the inherent paradox between measuring and rewarding individual employee versus group performance. What is the right

**TABLE 3** Weighting of Measures

| Employee Group | Corporate Measures | Business Unit Measures | Dept/Div'l Measures | Individual Measures |
|---|---|---|---|---|
| Senior Executives | 88% | 19% | 4% | 38% |
| Directors and Managers | 65% | 31% | 8% | 38% |
| Professionals (non-sales) | 50% | 8% | 4% | 31% |
| Sales Professionals | 12% | 0% | 0% | 77% |
| Office/Clerical Administrative | 35% | 8% | 0% | 23% |
| Operational and Service | 27% | 12% | 0% | 19% |
| Production/Service and Operational | 84% | 64% | 33% | 14% |

balance of different business units that will encourage individuals to maximize performance? How can different rewards be used to reinforce the company, group and individual performance? Expecting a single bonus plan to create this balance may be asking too much of this program. Perhaps the organization can utilize a variety or portfolio of rewards systems, integrated with the different goals, to create the desired balance for achieving optimal performance.

**8 | Determine the right payout-to-performance ratio to be meaningful to the individual and to provide the desired return on investment for the organization.** Goals that have little positive or negative consequences (e.g., bonus payouts, pay increases, recognition awards, promotions or getting fired) associated with them, often become ignored. Companies measure many things, only a few of them are associated with rewards. There are often detailed financial metrics (e.g., cost per unit, actual expenses to budget, etc.), operational metrics (e.g., on-time-delivery, scrap ratios, productivity, safety, and quality, etc.) and customer satisfaction (e.g., customer retention, profitability and satisfaction, etc.). The goals that make a difference in the bonus payout or other forms of rewards therefore, tend to get the attention. Research (and experience) clearly shows that goals paired with meaningful rewards have more influence on behavior than either the goals or the rewards do independently (Milkovich 1992). The task is to define the right rewards to be associated with the selected measures and desired performance. There are many factors that influence this ratio. The primary factors are as follows:

- **The level of influence** one has on the factors that create desired results (the reason executives and professional sales people have higher variable pay associated with their compensation than others in an organization). This is often referred to as the "line of sight."
- **The value of the performance** achieved in relation to the amount of payouts associated with the outcomes (i.e., the cost of the payouts in relation to the value of the performance — the ROI).
- **The level of risk** associated with the performance and its importance to the organization from short- and long-term perspectives.

- **The customary market practices** associated with the compensation of these jobs. The market practices often set the expectations of individuals the company seeks to hire and what is generally known and acceptable by human resources, corporate executives and the board of directors.
- **The probability of achieving the target** often reflects the level of payout one will receive. If the payout is infrequent, then the payout needs to be higher than standard practices so that the *expected* value — amount of award multiplied by the percent probability of achievement — results in total compensation that achieves the desired level of competitiveness.

When one establishes goals for a given position, one needs to understand the ratio between the amount of the payout and the probability of the payout so the opportunity for the additional income is meaningful to the employee. If the expected value is low, the importance of the goal will be minimized. In contrast, if the expected value is high, then the individual may focus more on that goal than on other goals or accountabilities for which one is responsible. Further, the bonus payouts that are paid need to reflect a meaningful ROI by the company. If the company can achieve the same results without making this payment, then it should simply do so. In most cases, it cannot. Therefore, the costs associated with the bonus payouts need to be considered in relation to the value of the results – hence the pay-to-performance ratio is a critical ingredient to effective goal setting. Without the proper balance between goals and rewards, the organization risks it ability to retain desired talent or motivate work that aligns with the strategy and the desired culture of the organization. The simple message is that organizations often get what they pay for in relationship to the expected value.

### 9 | Calibrate goals in order to reinforce accountability, initiative and collaboration.

In traditional goal-setting practices, the individual and the manager reach agreements (usually in private) on the goals for a given time period. This may be part of the performance management or business planning process. In many organizations the manager's or company's goals provide the context for setting individual goals, and the goal-setting process cascades down through the organization. When done effectively, this process both translates and aligns sub-unit goals (i.e., department, team or individual) with the larger enterprise (e.g., division or overall company). The challenge is to make sure the goals that are set for one group of employees reflect a similar focus and challenge for other groups, particularly for those that are related to each other. Public display and discussion of goals adds a powerful self-correcting and quality assurance dynamic to the process. For example, some companies use a planning process where managers discuss and calibrate the goals in one's area with peer or related groups. Imagine a meeting where a manager of one department presents the goals he/she established for each individual in the group and displays both the goals and the progress that is being made on a monthly or quarterly basis. The discussion and display of goals fosters a more disciplined approach to setting goals, better calibration of the goals (i.e., level of stretch), and stronger interdependencies and collaboration where they are needed. In short, the process of goal setting can often address many of the inequities and issues that companies have with their goals.

**10 | Learn from experience and continually improve the goal-setting process.** Like many systems in organizations, goal setting is a process. It is seldom perfect and can always be improved. Even though organizations link important decisions to the process – investment decisions, staffing, talent management, bonus awards, merit pay decisions, etc. — the process has to be one that creates credible and effective focus on performance. As information systems, individual and group capabilities improve, so should the clarity, rigor, confidence and value of the goals. The communication process should be frequent, engaging and fact-based. When goals need to change, people understand why and by how much. When performance issues need to be addressed, goals provide the focus for the discussion so that both the "what" and "how" can be accurately, effectively determined. One only needs to observe how goals, performance feedback and rewards (formal and informal) are applied in highly effective sports teams to see the power of this process.

## CONCLUSION

This paper has examined one critical element of the performance management and variable compensation – the goal setting process. There are many attributes of highly successful organizations, and the effectiveness of their goal setting is but one of the common ingredients. There is substantial data on the importance of effective goals and the association they have with meaningful rewards. Some believe you get what you measure, but in reality, you get what you measure and reward. It is the relationship between the nature of the goals and the positive (or negative) consequences that are associated with them that influences human behavior. People create performance by their actions. By utilizing goals that work and rewards that work, an organization can achieve remarkable performance.

One of the primary challenges to executives and leaders of organizations is to engage employees so they care as much about their individual and the organization's performance as the executives themselves do. This article provides some of the factors that highly successful companies employ to achieve this culture. The most important message is to understand the principles that create highly effective goal setting, and employ the practices the organization needs to build the commitment and discipline needed to be successful. The organization will then have multiplied the power of talented people to focus on common goals and achieve remarkable results. This provides personal rewards and creates outstanding value for the organization and the customers and shareholders it serves. Yes, this is an idealistic statement. Performance is the result of many things, and the effectiveness of the goals is determined by how well principles outlined in this paper are employed. This paper should enable one to identify where the strengths and weaknesses exist and what can be done about them, so the organization and its employees can truly do their very best. ∎

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Whether you're setting personal goals or professional goals, this guide reveals the science and strategy behind smart goal setting.Â  This is where setting an upper limit can be useful. Upper limits make it easier for you to sustain your progress and continue showing up. This is especially critical in the beginning. Whenever you set a new goal and begin working toward it, the single most important thing is showing up.Â  This has an important impact when it comes to achieving goals. Whether or not you achieve your goals in the long-term has a lot to do with what types of influences surround you in the short-term. Itâ€™s very hard to stick with positive habits in a negative environment. Here are a few strategies I have found useful when trying to design better default decisions into my life Many people have become â€œanti-goal setting,â€ because they have seen a lack of proper results. Well, we know why: goal setting can be quite arbitrary and can oftentimes go wrong if not done correctly. Setting goals can be a miraculous thing, though, if done properly. For that, it is our mission to re-examine goal setting theory in order to correct these problems. First, we will discuss why setting goals is still awesome. So what should you do when you fail to achieve the goals you have set? Here are 7 things you should do when you fail to reach your targets.Â  First, you have to understand that failing to achieve your goals does not mean that you have failed. It just means that something is wrong and you need to change your strategies. You need to change your approach. And you need to change the way you do things.