Is Your HR Department Friend or Foe? Depends on Who's Asking the Question

Published : August 10, 2005 in Knowledge@Wharton

Talk to human resources professionals, consultants and scholars who study the workplace and you will find two different views of HR.

According to its critics, HR departments can be needlessly bureaucratic, obstructionist, stuck in the "comfort zone" of filling out forms and explaining company benefits, and too closely aligned with the interests of management yet lacking the business knowledge to be effective strategic partners. Dealing with these types of HR departments "is like going to the dentist," says David Sirota, author of *The Enthusiastic Employee: How Companies Profit by Giving Workers What They Want* (Wharton School Publishing). When people are asked to rate the quality of different functions within their company, he adds, "IT and HR are repeatedly rated the lowest."

The more positive view of HR is that it works directly with senior management, providing crucial input into major business transactions such as mergers and acquisitions and restructurings. In this scenario, HR departments have moved away from the traditional role of administrators -- many of those responsibilities are now outsourced -- to a more creative focus on their prime role, which includes recruiting talent, promoting mobility and career development, and improving organizational effectiveness. "I would not choose HR as a career if we couldn't be a strategic partner with the business," says Kathy Gubanich, managing director of HR at The Vanguard Group. "HR is fortunate to report to the CEO of Vanguard.... If we didn't, it would mean HR's priorities are being set differently."

Peter Cappelli, director of Wharton's Center for Human Resources, recently led a discussion at the Center focused on the question: "What is the role of HR now?" From the 1920s on, Cappelli says, HR was seen as a way to advocate for, and protect, employees -- an orientation that became "quite explicit in the 1950s and beyond as part of an effort by management to prevent unionization." But more recently, and especially over the past decade, the threat of unionization is much less widespread even as technological advances have made employees more expendable. The "social contract" between employee and employer -- in which companies provided lifetime employment to its workers in return for loyalty and commitment to company goals -- has ended.

These days, employees are afraid to quit because of the tight labor market and reluctant to complain about increased work loads for fear of being laid off, says Cappelli. "Companies are pushing more and more work onto employees, and HR departments are becoming the mechanism for doing that. As a result, the idea that HR people are there to represent workers -- or at least deal objectively with their concerns -- is pretty much gone." In addition, with companies continuing to cut back employee benefits such as healthcare and pensions, HR departments have found themselves "increasingly the bearer of bad news to employees."

Meanwhile, HR issues are very much a part of the press's business coverage, whether it's Hewlett-Packard's recent announcement that it is laying off 14,500 employees (including a number of HR positions) or the breakdown of talks between Citigroup chairman Sandy Weill and Citigroup's board over the retirement perks available to him under his contract. Weill, who is reportedly interested in starting a private equity fund, had earlier committed to staying on as chairman until April 2006.

Strategy-driven HR: Reality or Goal?

If you look at the history of HR, says James Walker, a consultant on strategic human resources based in La Jolla, Ca., trends in HR -- such as outsourcing, the establishment of call centers and service centers, and the integration of work-life balance issues -- usually require about a decade to take hold.

For example, "most of us would like to see HR be transformed more rapidly into a business partner, with less emphasis on administrative functions that can now be outsourced," Walker says. "To achieve that, it's vital to help key HR individuals accelerate their development of business skills. I think many companies are, in fact, doing this, but not as fast as I would like. There is still a tremendous attraction within HR to the comfort zone of more traditional and functional support-service kinds of relationships."

The classic area where HR leaders can provide strategic input is "anticipating a merger," says Walker. "A very well-defined set of opportunities and experiences exists, including assistance in valuing the merger, developing the integration plan, communicating with employees, matching talent, and so forth. Some company HR departments play a key role here. In others, they are still observers, cleaning up the mess afterwards." HR executives who serve as business partners, he adds, are more likely to be in strategy-driven organizations -- professional services firms, financial services firms, high-tech companies and "to some extent pharmaceuticals, the opposite end of the continuum from healthcare companies and manufacturers." The most talented HR leaders, he says, tend to work "in pockets within a business. They have established a relationship with their client executive in which they are able to have a dialogue and push back as appropriate."

Over the last 10 to 15 years, HR has begun to have a much bigger impact on how a company operates, says J. Steele Alphin, global personnel executive at Bank of America. "To put this in perspective: At Bank of America, we have $28 billion of non-interest expenses. Of that, $15 billion is related to personnel" -- everything from salaries, incentive plans and fringe benefits to talent retention programs and risk management strategies. "If you can effectively manage those dollars, trying to get as high a return on investment as possible, then you approach the opportunity a lot differently."

To fulfill his mandate of growing revenue, increasing productivity and developing leadership in the company, Alphin, who reports directly to CEO Ken Lewis, has assembled an HR team that includes managers with degrees in business, HR, psychology and engineering. "Our team looks very similar to any other high-level team in Bank of America," he says. So when HR sits around the table with other departments, "we don't talk HR; we talk about the business."

Lewis, he adds, "looks to us to be business leaders, business partners, the person at the table who will always bring up the critical fact that no one else does." Alphin, who has 10 direct reports, says that most of those 10 people show up "on replacement charts for other areas of the company. One of our goals is to be a net supplier of talent to Bank of America. We have had personnel executives move into running real estate, branding and transition on acquisitions."

According to Mark Bieler, a human resources consultant who was executive vice president of HR at Bankers Trust from 1985 to 1999, "without the direct tie to strategy, there is no context for HR work. You have to be completely focused on aligning HR practice, policies and procedures to the overall strategy of the organization." In the mid-1980s, when Bieler was at Bankers Trust, chairman Charles Sanford converted the company from a commercial bank to an investment bank -- "about as radical a cultural shift as one could imagine," says Bieler. "My role was taking a set of HR practices that I had inherited and making sure they were consistent with where we were trying to take the firm. At the simplest level, that means redesigning pay systems, not so much to pay people more -- although investment bankers do tend to make more -- but to restructure the system to include smaller amounts of fixed compensation and to put more of people's pay at risk.

"In addition, we became the first bank in the mid-1980s to offer a cafeteria style benefits approach because we wanted people to take charge of their lives, to be more entrepreneurial. Cafeteria benefits were more suited to the type of organization we wanted to be.... We shifted our recruiting goals, changed the way new employees were socialized .... and bit by bit, brick by brick, aligned what we did from the people point of view with the strategy of the company."

Jack Welch, former CEO of General Electric and author of a book entitled *Winning*, noted in a recent interview that "outside of the CEO, HR is the most critical function in any company. Development of leaders is the ultimate responsibility of every CEO and thus is an integral part of HR. I saw my job as allocating people and dollars to opportunities. I wasn't designing products. I was putting people where I thought they were right for the job. I did that with my partners in HR." HR evaluation systems, he says, "should be rigorous and nonbureaucratic" and monitored as closely as financial reporting is now monitored under Sarbanes-Oxley.

While many HR professionals say their role is to be a strategic partner with senior management, critics question whether this is possible given that HR people often lack the business skills to understand strategy or their role in implementing it. Furthermore, some senior managers aren't interested in having HR as a strategic partner; they just want the department to go out and hire the people they (the managers) want.

"If top management doesn't see value in having HR as a strategic partner -- and if HR can't think out of the box in that role -- then the partnership is probably not going to happen," says Wharton management professor Nancy Rothbard. She cites the case of a woman who heads HR at an in-house call center for a large financial services firm who is "constantly experimenting with new ways to help the company achieve its overall goals," such as trying out new tools to better select employees and sitting through hours of training sessions to test their effectiveness. Overall, says Rothbard, such an approach "means committing resources -- in terms of top management's time as well as the time of managers a level below." The effort, she says, "took guts on HR's part because it wasn't clear there was going to be a definite payoff."

Of course becoming a "partner" with senior management doesn't always happen. At Vanguard, says Gubanich, "you have to earn your way to the table. I might also say that rather than a strategic partner, we are more of a strategic enabler. We need to understand the business deeply -- where it is now and where it wants to go. This is important because sometimes I think we get caught up in, 'What is the coolest program?' or 'Should we be designing something new?' The key question has to be: 'Was HR successful at moving the company in the direction it wanted to go?'"

HR at Vanguard has a number of strategic imperatives, Gubanich adds, "such as hiring the right people in the right place in the right time; looking for breadth and depth of leadership talent; maintaining the right culture for the organization; risk mitigation and operational excellence.... For example, if someone at Vanguard wants to create a new business, we talk about the people and programs needed to get there. Do you have the leadership necessary for that? Do you have the training programs? Do you know how to take a group and say, 'We are now going to do things this way instead of that way'? What do you want to accomplish? Will you be sales oriented or service oriented? What are the competencies required for the job? Will you focus on external or internal hiring or a combination of the two? And so forth."

The same orientation exists at Air Products, an $8 billion industrial gas, chemical and home health care company headquartered outside of Allentown, Pa. Vince Kraft, director of industrial relations, reports to the vice president of human resources. "When people say HR is non-strategic and does not understand the business, here it is just the opposite," Kraft says. "We are imbedded in a variety of operational issues especially in the field. We are out there among the employees, customers and the distribution network, and we are seen by senior management as very valuable, especially when it comes to areas like professional development and succession plans."

In some companies, HR's influence extends beyond their own departments. "Outside of the marketing function," notes Bank of America's Alphin, "the personnel function at Bank of America has one of the biggest responsibilities relating to brand. For example, every year we hire about 40,000 people externally. Each time we interview someone, we are looking for talent. That person, in turn, has a chance to see our company. That's a branding opportunity. If you interview people, even if you do not hire them, the experience should be such that they would want to bank with us."

A Two-Tiered System

Critics of the way HR has developed over the past decade suggest that HR has become a "handmaiden of management," more concerned with carrying out directives from above than supporting the needs of employees.

Bieler sees "some truth" to that claim but says it's "largely because of the decentralization of the functions. The most common model today in large corporations is a smaller, highly expert central staff and then masses of HR people in distributed HR organizations throughout the company. Their reporting relationship may either be dual -- to the head of the line operating office and to the head of HR -- or may be direct. But at the end of the day, the power dynamic seems to favor HR's relationship to their senior line executive. This distribution of the HR function has many advantages but one of the downsides is a decrease in the view of HR as playing an ombudsperson role in the organization."

According to Air Products' Kraft, "the climate change" toward HR being perceived as pro-management "began when we started to outsource what is generally described as administrative duties, but what are generally regarded by employees as positive employee relations -- such as help with medical insurance, leave and vacation issues. The day-to-day contract between employees and management of keeping each other informed has been relegated to either voicemail or email as opposed to conversations. HR began to be perceived by the employee base as a necessary evil."

Kraft also notes a tendency to treat people as "numbers rather than as individuals, which is not the fault of the company but really the fault of financial pressure from Wall Street. It's very hard not to feel the pressure to cut costs...."

When Leon Cornelius, a director of GM's labor relations staff, first started at a GM plant in 1978, "all the HR issues were handled right there, in the plant," he says. Employees could ask questions about benefits, compensation, and "if you were sick or somebody passed away, there were people who you could talk to about it and find a sympathetic ear. It wasn't strategic; it was more transactional, but it had that personal touch. Now it's all about going to the web and calling 1-800."

The system could be better if it were two-tiered, Kraft suggests. "Somebody has to develop an alternative dispute resolution system or some mechanism that allows employees a voice.... I still view that as a part of the HR function, although it doesn't seem to be happening."

Kevin Sullivan, an employee relations consultant at IBM, acknowledges allegations of HR bias towards management, but points to the company's appeals process as an effort to "maintain the integrity of the system." Once employees exercise their right to challenge a performance appraisal, salary decision or other personnel matter, that challenge is handled in one of two ways -- either through the appointment of an investigator, assigned by management, to look into the complaint, or through a panel review. The panel, which is available to U.S.-based employees, consists of five individuals -- three employees and two managers, all of them randomly selected -- who hear the case and make a decision. "That system gets used. Our employees are not shy about coming forward."

In many companies, Sullivan adds, employees feel that the social contract between the company and its workforce no longer exists and that "employees are on their own. What companies must do is offer a compelling case to the individual as to why he or she would want to work there. In our case, we emphasize our skills training, our workplace flexibility options (including work-at-home), our commitment to diversity, our focus on performance differentiation, our leading-edge technology and our leadership development.... You have to show employees that opportunities exist."

For Mark Bieler, the bottom line is that "the quality of HR functions correlates more than anything to the quality of culture and management they are supporting. If you put me in an environment as head of HR in a company that fundamentally doesn't respect people and has a short term orientation toward them, I would have a difficult time either championing the needs of the people or furthering the objectives of the organization through HR policy or practice."

Seeing the Employee as Customer

According to the August 2005 cover story in *Fast Company* magazine, entitled "Why We Hate HR," HR people are not interested in an "open-minded approach" when it comes to making exceptions to company policies, including pay schedules. "Instead, they pursue standardization and uniformity in the face of a workforce that is heterogeneous and complex.... Bureaucrats everywhere abhor exceptions -- not just because they open up the company to charges of bias but because they require more than rote solutions."

Rather than sending the message that the company values "high-performing employees and is focused on rewarding and retaining them," the article says, "HR departments benchmark salaries, function by function and job by job, against industry standards, keeping pay -- even that of the stars -- within a narrow band determined by competitors. HR, in other words, forfeits long-term value for short-term cost efficiency." The article poses this question: "Who does your company's vice president of human resources report to? If it's the CFO -- and chances are good it is -- then HR is headed in the wrong direction."

Sirota has a different way of getting at the same issue: If you think of HR as having three roles, says Sirota, the first is to carry out administrative functions. The second is to serve as strategic partner, and the third is to see the employee as customer. The most important part of that customer-centric view involves "working with management to develop policies, practices and philosophies geared toward creating a truly motivated and dedicated workforce," says Sirota. Generally speaking, "in many organizations, that role is more notable by its absence."

When HR managers "say they want to be business partners," suggests Sirota, "what they mean is they want to work for management. Most companies say employees are our greatest asset, but what they really mean is they are our biggest cost." HR should "be proactive. Walk around the company, find out the issues, just as you would do with customers. External customers are surveyed regularly. HR should be surveying their internal customers as well."

GM's Cornelius agrees that "what's missing in today's workplace is the view that HR is there for the employees. When younger people in the organization come to me for advice I say, 'Have you talked to anybody in HR about this?' and they roll their eyes and say, 'Why should I bother to do that?'" But it doesn't have to be that way, Cornelius adds. "An HR person can handle a hard conversation with an employee about what he or she needs to do to improve, but that employee can still walk away thinking: 'If I do these things, I will have somebody there who will help me move around the company or get me positioned for a promotion.'"

HR also tends to push onto managers a number of functions that could be done by HR staff, such as finding and downloading the forms needed when an employee retires. "HR has dumped a number of jobs on other functions that they used to do themselves," Cornelius says. But he also has praise for specific HR policies including, for example, those dealing with layoffs. "I give GM credit in situations where there is a downsizing. They stand tall when it comes to the employees. The situation is handled in a very humane way." And where major long-term issues are involved, such as restructurings and joint ventures, "HR is actively a part of those strategic discussions, along with labor relations. HR brings value" to the table.

Bank of America is taking the idea of serving employees one step further. The company just opened a facility near Charlotte, N.C., which provides a flexible work environment and allows people who live in nearby communities to spend a day or two every week at that location, rather than commuting an hour or more each way into the city. "It's a new concept and we have gotten very good response to it," says Alphin. "In addition, we are already seeing increases in productivity among employees who use this option." Alphin points to another initiative at Bank of America instituted this year -- a broad-based incentive plan that will pay out between $500 and $3,000 to eligible employees from mid-level managers to their associates, in addition to existing incentive programs already in place.

He predicts that some companies will start insourcing HR functions that they previously outsourced. "We have about 1,200 people in HR now but that number will soon grow to 1,500 because we are bringing some staffing back in house -- including recruiting -- that we had outsourced. We liked the pricing but we didn't like the quality," Alphin says. "You always have to look at that tradeoff."

Performance-based Pay

Given the recent controversies over huge compensation packages at public companies, pay-for-performance continues to be a hot-button issue for everyone from CEOs down to lower level employees. According to Walker, "the leading-edge thinking now is much more on segmenting work across the company and also segmenting the work force" in ways that let differences be defined and valued. "This allows HR to move away from a system of 'everyone is treated the same' to one where people can be treated differently according to business needs, individual preferences and performance. That's a trend, starting with IBM and working through a lot of companies."

IBM's Sullivan would agree. The philosophy of the company toward its 330,000 employees "is to pay our best people like the best people in the industry are paid. The rest of our employees get paid competitively. We also have a performance appraisal system in which we hold people accountable. That's the underpinning of the system, whether it is pay, promotions or the opportunity for stock options and other awards and recognition. It is all based on performance."

At Vanguard, with its 11,000 employees, "we describe ourselves as a pay-for-performance organization," adds Gubanich. "As such, we believe that the top performers should be rewarded more. We do all kinds of analysis on pay and total compensation -- where it should fall on the individual level as well as the job aggregate level. In addition, it can't just be all about the individuals. It is valuable to also have team and company incentives."

Issues of pay and performance are now reaching boards of directors as well, says Bieler. "One key factor in the evolution of HR departments has been Sarbanes-Oxley. At least for the head of HR, this has radically changed the relationship with the board's compensation committee. Recently, as part of my work redesigning two companies' compensation systems, I dealt with consultants hired by the compensation committee. That hadn't happened before. So issues around pay -- including sensitivity to full disclosure of executive perks, for example -- are in the forefront these days, as are issues of management development and succession. Sarbanes-Oxley has had a profound effect on the relationship between the board and the company, in which the HR function plays a key role."

The question arises, adds Walker, as to where a board gets guidance on matters of corporate pay, perks, etc. "Is it from corporate HR or does the board hire its own consultants directly?" With regards to compensation, "HR executives should be doing the analysis and bringing information and advice to the board. If you want HR to be a strategic partner, it can't be just with the CEO; it has to be with the board as well."

But pay issues are not always easy to administer, especially at places like universities and hospitals, where, as Bieler says, "there are numerous constituencies, all of whom think they are in charge. It is hard to get your arms around a clear cut strategy." Cappelli suggests that one approach to setting pay, "left over from this idea of looking out for employees, is to have a model of equality: Treat everyone roughly the same, especially in issues of pay. Of course places that do this get complaints from top managers saying, 'I lost these people because HR wouldn't let me pay them enough.' Top managers, who for the most part are high achievers, believe people should be paid based on their own performance."

The problem, says Cappelli, "is that perceived inequities drive people crazy. It's one thing to say, 'This person is a star, pay him or her more or he might quit.' What happens next? People who discover this person is being paid more [within an equal pay system] start to complain. So you move to a model where everyone is paid based on performance. But this approach requires an objective assessment of performance that everyone must be willing to buy into. That's the hard part."