Harvard Business Review OnPoint ARTICLE

BEST OF HBR

Fair Process
Managing in the Knowledge Economy

by W. Chan Kim and Renée Mauborgne

Included with this full-text *Harvard Business Review* article:

Fair Process

Managing in the Knowledge Economy

The Idea in Brief

In just months, a model workforce degenerated into a cauldron of mistrust, resistance, and plummeting performance. Why? Management launched a major change effort without inviting employees' input, without explaining the reasons for the change, and without clarifying new performance expectations.

In other words, the company ignored **fair process**—a decision-making approach that addresses our basic human need to be valued and respected. When people feel a decision affecting them was made fairly, they trust and cooperate with managers. They share ideas and willingly go beyond the call of duty. Corporate performance soars.

In knowledge-based organizations— whose lifeblood consists of employees' trust, commitment, and ideas—fair process is essential. It enables companies to channel people's energy and creativity toward organizational goals.

The benefits of fair process may seem obvious—yet most organizations don't practice it. Why? Some managers find it threatening, assuming it will diminish their power. They keep employees at arm's length to avoid challenges to their authority. Others believe employees are concerned only with what's best for themselves. But evidence shows that most people will accept outcomes not wholly in their favor—*if* they believe the process for arriving at those outcomes was fair.

The Idea in Practice

Fair process isn't decision by consensus or democracy in the workplace. Its goal is to pursue the best ideas, not create harmony. Fair process consists of three principles:

- *Engagement*—**involving individuals in decisions by inviting their input and encouraging them to challenge one another's ideas.** Engagement communicates management's respect for individuals and their ideas and builds collective wisdom. It generates better decisions and greater commitment from those involved in executing those decisions.

- *Explanation*—**clarifying the thinking behind a final decision.** Explanation reassures people that managers have considered their opinions and made the decision with the company's overall interests at heart. Employees trust managers' intentions— even if their own ideas were rejected.

- *Expectation clarity*—**stating the new rules of the game, including performance standards, penalties for failure, and new responsibilities.** By minimizing political jockeying and favoritism, expectation clarity enables employees to focus on the job at hand.

▶ Example:
Facing decreasing demand, an elevator manufacturer we'll call Elco decided to design a more efficient manufacturing system. It would introduce the system at its Chester plant, a model operation with such positive employee relations that it decertified its own union. Then it would incorporate the new system at High Park, a strongly unionized plant highly resistant to change.

Seeking minimal workforce disturbance, managers didn't involve the Chester employees in the system design process, explain why change was necessary, or clarify new performance expectations. Soon rumors about layoffs proliferated, trust and

commitment deteriorated, and fights erupted on the shop floor. Quality sank.

Rattled but wiser, Elco took a different tack at their High Park site. Managers held ongoing plantwide meetings to explain the need for the new system, encouraged employees to help design the new process, and laid out new expectations. The anticipated resistance never came—and trusting employees embraced the new system.

People care about the decisions you make, but they care even more about the process you used along the way.

Fair Process
Managing in the Knowledge Economy

by W. Chan Kim and Renée Mauborgne

When employees don't trust managers to make good decisions or to behave with integrity, their motivation is seriously compromised. Their distrust and its attendant lack of engagement is a huge, unrecognized problem in most organizations. This issue has always mattered, but it matters now more than ever, because knowledge-based organizations are totally dependent on the commitment and ideas of their employees.

Unfortunately, neither integrity nor good judgment can be magically conferred on all the managers in an organization. But it is possible for top executives to create processes that help keep managers honest—and that also help build employees' trust. In this article, W. Chan Kim and Renée Mauborgne describe one such process, which grew out of their research into the links between trust, idea sharing, and corporate performance. Their central finding is that employees will commit to a manager's decision—even one they disagree with—if they believe that the process the manager used to make the decision was fair. Sounds simple, but most organizations don't practice fair process. And because they don't,

they never know what they've lost in the way of ideas and initiatives.

A London policeman gave a woman a ticket for making an illegal turn. When the woman protested that there was no sign prohibiting the turn, the policeman pointed to one that was bent out of shape and difficult to see from the road. Furious, the woman decided to appeal by going to court. Finally, the day of her hearing arrived, and she could hardly wait to speak her piece. But she had just begun to tell her side of the story when the magistrate stopped her and summarily ruled in her favor.

How did the woman feel? Vindicated? Victorious? Satisfied?

No, she was frustrated and deeply unhappy. "I came for justice," she complained, "but the magistrate never let me explain what happened." In other words, although she liked the outcome, she didn't like the process that had created it.

For the purposes of their theories, economists assume that people are maximizers of

utility, driven mainly by rational calculations of their own self-interest. That is, economists assume people focus solely on outcomes. That assumption has migrated into much of management theory and practice. It has, for instance, become embedded in the tools managers traditionally use to control and motivate employees' behavior—from incentive systems to organizational structures. But it is an assumption that managers would do well to reexamine because we all know that in real life it doesn't always hold true. People do care about outcomes, but—like the woman in London—they also care about the processes that produce those outcomes. They want to know that they had their say—that their point of view was considered even if it was rejected. Outcomes matter, but no more than the fairness of the processes that produce them.

Never has the idea of fair process been more important for managers than it is today. Fair process turns out to be a powerful management tool for companies struggling to make the transition from a production-based to a knowledge-based economy, in which value creation depends increasingly on ideas and innovation. Fair process profoundly influences attitudes and behaviors critical to high performance. It builds trust and unlocks ideas. With it, managers can achieve even the most painful and difficult goals while gaining the voluntary cooperation of the employees affected. Without fair process, even outcomes that employees might favor can be difficult to achieve—as the experience of an elevator manufacturer we'll call Elco illustrates.

Good Outcome, Unfair Process

In the late 1980s, sales in the elevator industry headed south as overconstruction of office space left some large U.S. cities with vacancy rates as high as 20%. Faced with diminished domestic demand for its product, Elco knew it had to improve its operations. The company made the decision to replace its batch-manufacturing system with a cellular approach that would allow self-directed teams to achieve superior performance. Given the industry's collapse, top management felt the transformation had to be made in record time.

Lacking expertise in cellular manufacturing, Elco retained a consulting firm to design a master plan for the conversion. Elco asked the consultants to work quickly and with minimal dis-turbance to employees. The new manufacturing system would be installed first at Elco's Chester plant, where employee relations were so good that in 1983 workers had decertified their own union. Subsequently, Elco would roll the process out to its High Park plant, where a strong union would probably resist that, or any other, change.

Under the leadership of a much beloved plant manager, Chester was in all respects a model operation. Visiting customers were always impressed by the knowledge and enthusiasm of Chester's employees, so much so that the vice president of marketing saw the plant as one of Elco's best marketing tools. "Just let customers talk with Chester employees," he observed, "and they walk away convinced that buying an Elco elevator is the smart choice."

But one day in January of 1991, Chester's employees arrived at work to discover strangers at the plant. Who were these people wearing dark suits, white dress shirts, and ties? They weren't customers. They showed up daily and spoke in low tones to one another. They didn't interact with employees. They hovered behind people's backs, taking notes and drawing fancy diagrams. The rumor circulated that after employees went home in the afternoon, these people would swarm across the plant floor, snoop around people's workstations, and have heated discussions.

During this period, the plant manager was increasingly absent. He was spending more time at Elco's head office in meetings with the consultants—sessions deliberately scheduled away from the plant so as not to distract the employees. But the plant manager's absence produced the opposite effect. As people grew anxious, wondering why the captain of their ship seemed to be deserting them, the rumor mill moved into high gear. Everyone became convinced that the consultants would downsize the plant. They were sure they were about to lose their jobs. The fact that the plant manager was always gone—obviously, he was avoiding them—and that no explanation was given, could only mean that management was, they thought, "trying to pull one over on us." Trust and commitment at the Chester plant quickly deteriorated. Soon, people were bringing in newspaper clippings about other plants around the country that had been shut down with the help of consultants. Employees saw themselves as imminent victims of yet another

W. Chan Kim is the Boston Consulting Group Bruce D. Henderson Chair Professor of International Management at Insead in Fontainebleau, France. **Renée Mauborgne** is the Distinguished Fellow and Affiliate Professor of Strategy and Management at Insead and the president of ITM, a strategy research group in Fontainebleau. Their last HBR article, "Charting Your Company's Future," appeared in the June 2002 issue. They can be reached at chan.kim@insead.edu and renee.mauborgne@insead.edu.

management fad and resented it.

In fact, Elco managers had no intention of closing the plant. They wanted to cut out waste, freeing people to enhance quality and produce elevators for new international markets. But plant employees could not have known that.

The Master Plan. In March 1991, management gathered the Chester employees in a large room. Three months after the consultants had first appeared, they were formally introduced. At the same time, management unveiled to employees the master plan for change at the Chester plant. In a meeting that lasted only 30 minutes, employees heard how their time-honored way of working would be abolished and replaced by something called "cellular manufacturing." No one explained why the change was needed, nor did anyone say exactly what would be expected of employees under the new approach. The managers didn't mean to skirt the issues; they just didn't feel they had the time to go into details.

The employees sat in stunned silence, which the managers mistook for acceptance, forgetting how many months it had taken them as leaders to get comfortable with the idea of cellular manufacturing and the changes it entailed. The managers felt good when the meeting was over, believing the employees were on board. With such a terrific staff, they thought, implementation of the new system was bound to go well.

Master plan in hand, management quickly began rearranging the plant. When employees asked what the new layout aimed to achieve, the response was "efficiency gains." The managers didn't have time to explain why efficiency needed to be improved and didn't want to worry employees. But lacking an intellectual understanding of what was happening to them, some employees literally began feeling sick when they came to work.

Managers informed employees that they would no longer be judged on individual performance but rather on the performance of the cell. They said quicker or more experienced employees would have to pick up the slack for slower or less experienced colleagues. But they didn't elaborate. How the new system was supposed to work, management didn't make clear.

In fact, the new cell design offered tremendous benefits to employees, making vacations easier to schedule, for example, and giving them the opportunity to broaden their skills and engage in a greater variety of work. But lacking trust in the change process, employees could see only its negative side. They began taking out their fears and anger on one another. Fights erupted on the plant floor as employees refused to help those they called "lazy people who can't finish their own jobs" or interpreted offers of help as meddling, responding with, "This is my job. You keep to your own workstation."

Chester's model workforce was falling apart. For the first time in the plant manager's career, employees refused to do as they were asked, turning down assignments "even if you fire me." They felt they could no longer trust the once popular plant manager, so they began to go around him, taking their complaints directly to his boss at the head office.

The plant manager then announced that the new cell design would allow employees to act as self-directed teams and that the role of the supervisor would be abolished. He expected people to react with excitement to his vision of Chester as the epitome of the factory of the future, where employees are empowered as entrepreneurial agents. Instead, they were simply confused. They had no idea how to succeed in this new environment. Without supervisors, what would they do if stock ran short or machines broke down? Did empowerment mean that the teams could self-authorize overtime, address quality problems such as rework, or purchase new machine tools? Unclear about how to succeed, employees felt set up to fail.

Time Out. By the summer of 1991, both cost and quality performance were in a free fall. Employees were talking about bringing the union back. Finally, in despair, the plant manager phoned Elco's industrial psychologist. "I need your help," he said. "I have lost control."

The psychologist conducted an employee opinion survey to learn what had gone wrong. Employees complained, "Management doesn't care about our ideas or our input." They felt that the company had scant respect for them as individuals, treating them as if they were not worthy of knowing about business conditions: "They don't bother to tell us where we are going and what this means to us." And they were deeply confused and mistrustful: "We don't know exactly what management expects of us in this new cell."

What Is Fair Process?

The theme of justice has preoccupied writers and philosophers throughout the ages, but the systematic study of fair process emerged only in the mid-1970s, when two social scientists, John W. Thibaut and Laurens Walker, combined their interest in the psychology of justice with the study of process. Focusing their attention on legal settings, they sought to understand what makes people trust a legal system so that they will comply with laws without being coerced into doing so. Their research established that people care as much about the fairness of the process through which an outcome is produced as they do about the outcome itself. Subsequent researchers such as Tom R. Tyler and E. Allan Lind demonstrated the power of fair process across diverse cultures and social settings.

We discovered the managerial relevance of fair process more than a decade ago, during a study of strategic decision making in multinational corporations. Many top executives in those corporations were frustrated—and baffled—by the way the senior managers of their local subsidiaries behaved. Why did those managers so often fail to share information and ideas with the executives? Why did they sabotage the execution of plans they had agreed to carry out? In the 19 companies we studied, we found a di-

Making Sense of Irrational Behavior at VW and Siemens-Nixdorf

Economic theories do a good job of explaining the rational side of human behavior, but they fall short in explaining why people can act negatively in the face of positive outcomes. Fair process offers managers a theory of behavior that explains—or might help predict—what would otherwise appear to be bewilderingly noneconomic, or irrational, behavior.

Consider what happened to Volkswagen. In 1992, the German carmaker was in the midst of expanding its manufacturing facility in Puebla, Mexico, its only production site in North America. The appreciation of the deutsche mark against the U.S. dollar was pricing Volkswagen out of the U.S. market. But after the North American Free Trade Agreement (NAFTA) became law in 1992, Volkswagen's cost-efficient Mexican facility was well positioned to reconquer the large North American market.

In the summer of 1992, a new labor agreement had to be hammered out. The accord VW signed with the union's secretary-general included a generous 20% pay raise for employees. VW thought the workers would be pleased.

But the union's leaders had not involved the employees in discussions about the contract's terms; they did a poor job of communicating what the new agreement would mean to employees and why a number of work-rule changes were necessary. Workers did not understand the basis for the decisions their leaders had taken. They felt betrayed.

VW's management was completely caught off guard when, on July 21, the employees started a massive walkout that cost the company as much as an estimated $10 million per day. On August 21, about 300 protesters were attacked by police dogs. The government was forced to step in to end the violence. Volkswagen's plans for the U.S. market were in disarray, and its performance was devastated.

In contrast, consider the turnaround of Siemens-Nixdorf Informationssysteme (SNI), the largest European supplier of information technology. Created in 1990 when Siemens acquired the troubled Nixdorf Computer Company, SNI had cut head count from 52,000 to 35,000 by 1994. Anxiety and fear were rampant at the company.

In 1994, Gerhard Schulmeyer, the newly appointed CEO, went out to talk to as many employees as he could. In a series of meetings large and small with a total of more than 11,000 people, Schulmeyer shared his crusading mission to engage everyone in turning the company around. He began by painting a bleakly honest picture of SNI's situation: The company was losing money despite recent efforts to slash costs. Deeper cuts were needed, and every business would have to demonstrate its viability or be eliminated. Schulmeyer set clear but tough rules about how decisions would be made. He then asked for volunteers to come up with ideas.

Within three months, the initial group of 30 volunteers grew to encompass an additional 75 SNI executives and 300 employees.

These 405 change agents soon turned into 1,000, then 3,000, then 9,000, as they progressively recruited others to help save the company. Throughout the process, ideas were solicited from managers and employees alike concerning decisions that affected them, and they all understood how decisions would be made. Ideas would be auctioned off to executives willing to champion and finance them. If no executive bought a proposal on its merits, the idea would not be pursued. Although 20% to 30% of their proposals were rejected, employees thought the process was fair.

People voluntarily pitched in—mostly after business hours, often until midnight. In just over two years, SNI has achieved a transformation notable in European corporate history. Despite accumulated losses of DM 2 billion, by 1995 SNI was already operating in the black. In the same period, employee satisfaction almost doubled, despite the radical and difficult changes under way.

Why did employees of Volkswagen revolt, despite their upbeat economic circumstances? How, in the face of such demoralizing economic conditions, could SNI turn around its performance? What is at issue is not *what* the two companies did but *how* they did it. The cases illustrate the tremendous power of fair process—fairness in the process of making and executing decisions. Fair process profoundly influences attitudes and behavior critical to high performance.

rect link between processes, attitudes, and behavior. Managers who believed the company's processes were fair displayed a high level of trust and commitment, which, in turn, engendered active cooperation. Conversely, when managers felt fair process was absent, they hoarded ideas and dragged their feet.

In subsequent field research, we explored the relevance of fair process in other business contexts—for example, in companies in the midst of transformations, in teams engaged in product innovation, and in company-supplier partnerships. (See the sidebar "Making Sense of Irrational Behavior at VW and Siemens-Nixdorf.") For companies seeking to harness the energy and creativity of committed managers and employees, the central idea that emerges from our fair-process research is this: Individuals are most likely to trust and cooperate freely with systems—whether they themselves win or lose by those systems—when fair process is observed.

Fair process responds to a basic human need. All of us, whatever our role in a company, want to be valued as human beings and not as "personnel" or "human assets." We want others to respect our intelligence. We want our ideas to be taken seriously. And we want to understand the rationale behind specific decisions. People are sensitive to the signals conveyed through a company's decision-making processes. Such processes can reveal a company's willingness to trust people and seek their ideas—or they can signal the opposite.

The Three Principles. In all the diverse management contexts we have studied, we have asked people to identify the bedrock elements of fair process. And whether we were working with senior executives or shop floor employees, the same three mutually reinforcing principles consistently emerged: engagement, explanation, and expectation clarity.

Engagement means involving individuals in the decisions that affect them by asking for their input and allowing them to refute the merits of one another's ideas and assumptions. Engagement communicates management's respect for individuals and their ideas. Encouraging refutation sharpens everyone's thinking and builds collective wisdom. Engagement results in better decisions by management and greater commitment from all involved in executing those decisions.

Explanation means that everyone involved and affected should understand why final decisions are made as they are. An explanation of the thinking that underlies decisions makes people confident that managers have considered their opinions and have made those decisions impartially in the overall interests of the company. An explanation allows employees to trust managers' intentions even if their own ideas have been rejected. It also serves as a powerful feedback loop that enhances learning.

Expectation clarity requires that once a decision is made, managers state clearly the new rules of the game. Although the expectations may be demanding, employees should know up front by what standards they will be judged and the penalties for failure. What are the new targets and milestones? Who is responsible for what? To achieve fair process, it matters less what the new rules and policies are and more that they are clearly understood. When people clearly understand what is expected of them, political jockeying and favoritism are minimized, and they can focus on the job at hand.

Notice that fair process is not decision by consensus. Fair process does not set out to achieve harmony or to win people's support through compromises that accommodate every individual's opinions, needs, or interests. While fair process gives every idea a chance, the merit of the ideas—and not consensus—is what drives the decision making.

Nor is fair process the same as democracy in the workplace. Achieving fair process does not mean that managers forfeit their prerogative to make decisions and establish policies and procedures. Fair process pursues the best ideas whether they are put forth by one or many.

"We Really Screwed Up." Elco managers violated all three basic principles of fair process at the Chester plant. They failed to engage employees in decisions that directly affected them. They didn't explain why decisions were being made the way they were and what those decisions meant to employees' careers and work methods. And they neglected to make clear what would be expected of employees under cellular manufacturing. In the absence of fair process, the employees at Chester rejected the transformation.

A week after the psychologist's survey was completed, management invited employees to meetings in groups of 20. Employees surmised that management was either going to pretend that the survey had never happened or accuse employees of disloyalty for having voiced their

complaints. But to their amazement, managers kicked off the meeting by presenting the undiluted survey results and declaring, "We were wrong. We really screwed up. In our haste and ignorance, we did not go through the proper process." Employees couldn't believe their ears. There were whispers in the back of the room, "What the devil did they say?" At more than 20 meetings over the next few weeks, managers repeated their confession. "No one was prepared to believe us at first," one manager said. "We had screwed up too badly."

At subsequent meetings, management shared with employees the company's dismal business forecast and the limited options available. Without cost reduction, Elco would have to raise its prices, and higher prices would further depress sales. That would mean cutting production even more, perhaps even moving manufacturing offshore. Heads nodded. Employees saw the bind the company was in. The business problem was becoming theirs, not just management's.

But still there were concerns: "If we help to cut costs and learn to produce elevators that are twice as good in half the time, will we work ourselves out of a job?" In response, the managers described their strategy to increase sales outside the United States. They also announced a new policy called *proaction time:* No one would be laid off because of any improvements made by an employee. Instead, employees could use their newly free time to attend cross-training programs designed to give them the skills they would need to work in any area of operations. Or employees could act as consultants addressing quality issues. In addition, management agreed not to replace any departing employees with new hires until business conditions improved. At the same time, however, management made it clear that it retained the right to let people go if business conditions grew worse.

Employees may not have liked what they heard, but they understood it. They began to see that they shared responsibility with management for Elco's success. If they could improve quality and productivity, Elco could bring more value to the market and prevent further sales erosion. To give employees confidence that they were not being misled, management pledged to regularly share data on sales, costs, and market trends—a first step toward rebuilding trust and commitment.

Elco's managers could not undo past mistakes, but they could involve employees in making future decisions. Managers asked employees why they thought the new manufacturing cells weren't working and how to fix them. Employees suggested making changes in the location of materials, in the placement of machines, and in the way tasks were performed. They began to share their knowledge; as they did so, the cells were redesigned and performance steadily improved, often far exceeding the expectations originally set by the consultants. As trust and commitment were restored, talk of bringing the union back died out.

High Park's Turn. Meanwhile, management worried about introducing the new work methods at Elco's High Park plant, which, unlike the Chester plant, had a history of resisting change. The union was strong at High Park, and some employees there had as much as 25 years' service. Moreover, the plant manager, a young engineer new to High Park, had never run a plant before. The odds seemed to be against him. If change had created animosity at Chester, one could only imagine how much worse the situation could become at High Park.

But management's fears went unrealized. When the consultants came to the plant, the young manager introduced them to all employees. At a series of plantwide meetings, corporate executives openly discussed business conditions and the company's declining sales and profits. They explained that they had visited other companies' plants and had seen the productivity improvements that cellular manufacturing could bring. They announced the proaction-time policy to calm employees' justifiable fears of layoffs. At the High Park plant, managers encouraged employees to help the consultants design the new manufacturing cells, and they encouraged active debate. Then, as the old performance measures were discarded, managers worked with employees to develop new ones and to establish the cell teams' new responsibilities.

Every day, the High Park plant manager waited for the anticipated meltdown, but it never came. Of course, there were some gripes, but even when people didn't like the decisions, they felt they had been treated fairly and, so, willingly participated in the plant's eventual performance turnaround.

Three years later, we revisited a popular

local eatery to talk with people from both plants. Employees from both Chester and High Park now believe that the cellular approach is a better way to work. High Park employees spoke about their plant manager with admiration, and they commiserated with the difficulties Elco's managers had in making the changeover to cellular manufacturing. They concluded that it had been a necessary, worthwhile, and positive experience. But Chester employees spoke with anger and indignation as they described their treatment by Elco's managers. (See the sidebar "The Price of Unfairness.") For them, as for the London woman who had been unfairly ticketed, fair process was as important as—if not more important than—the outcome.

Fair Process in the Knowledge Economy

Fair process may sound like a soft issue, but understanding its value is crucial for managers trying to adapt their companies to the demands of the knowledge-based economy. Unlike the traditional factors of production—land, labor, and capital—knowledge is a resource locked in the human mind. Creating and sharing knowledge are intangible activities that can neither be supervised nor forced out of people. They happen only when people cooperate voluntarily. As the Nobel laureate economist Friedrich Hayek has argued, "Practically every individual . . . possesses unique information" that can be put to use only with "his active cooperation." Getting that cooperation may well turn out to be one of the key managerial issues of the next few decades. (See the sidebar "Fair Process Is Critical in Knowledge Work.")

Voluntary cooperation was not what Frederick Winslow Taylor had in mind when at the turn of the century he began to develop an arsenal of tools to promote efficiency and consistency by controlling individuals' behavior and compelling employees to comply with management dictates. Traditional management science, which is rooted in Taylor's time-and-motion studies, encouraged a managerial preoccupation with allocating resources, creating economic incentives and rewards, monitoring and measuring performance, and manipulating organizational structures to set lines of authority. These conventional management levers still have their role to play, but they have little to do with encouraging active cooperation. Instead, they operate in the realm of outcome fairness or what social scientists call *distributive justice,* where the psychology works like this: When people get the compensation (or the resources, or the place in the organizational hierarchy) they deserve, they feel satisfied with that outcome. They will reciprocate by fulfilling to the letter their obligation to the company. The psychology of fair process, or *procedural justice,* is quite different. Fair process builds trust and commitment, trust and commitment produce voluntary cooperation, and voluntary cooperation drives performance, leading people to go beyond the call of duty by sharing their knowledge and applying their creativity. In all the management contexts we've studied, whatever the task, we have consistently observed this dynamic at work. (See the exhibit "Two Complementary Paths to Performance.")

Consider the transformation of Bethlehem Steel Corporation's Sparrows Point, Maryland, division, a business unit responsible for marketing, sales, production, and financial performance. Until 1993, the 106-year-old division was managed in the classic command-and-control style. People were expected to do what they were told to do—no more and no less—and management and employees saw themselves as adversaries.

That year, Bethlehem Steel introduced a

The Price of Unfairness

Historically, policies designed to establish fair process in organizations arise mainly in reaction to employees' complaints and uprisings. But by then it is too late. When individuals have been so angered by the violation of fair process that they have been driven to organized protest, their demands often stretch well beyond the reasonable to a desire for what theorists call *retributive justice:* Not only do they want fair process restored, they also seek to visit punishment and vengeance upon those who have violated it in compensation for the disrespect the unfair process signals.

Lacking trust in management, employees push for policies that are laboriously detailed, inflexible, and often administratively constricting. They want to ensure that managers will never have the discretion to act unjustly again. In their indignation, they may try to roll back decisions imposed unfairly even when the decisions themselves were good ones—even when they were critical to the company's competitiveness or beneficial to the workers themselves. Such is the emotional power that unfair process can provoke.

Managers who view fair process as a nuisance or as a limit on their freedom to manage must understand that it is the violation of fair process that will wreak the most serious damage on corporate performance. Retribution can be very expensive.

management model so different at Sparrows Point that Taylor—who was, in fact, the company's consulting engineer about 100 years ago—wouldn't have recognized it. The new model was designed to invoke in employees an active sense of responsibility for sharing their knowledge and ideas with one another and with management. It was also meant to encourage them to take the initiative for getting things done. In the words of Joe Rosel, the president of one of the division's five unions, "It's all about involvement, justification for decisions, and a clear set of expectations."

At Sparrows Point, employees are involved in making and executing decisions at three levels. At the top is a joint-leadership team, composed of senior managers and five employee representatives, that deals with companywide issues when they arise. At the department level are area teams, consisting of managers like superintendents and of employees from the different areas of the plant, such as zone committee people. Those teams deal with day-to-day operational issues such as customer service, quality, and logistics. Ad hoc problem-solving teams of employees address opportunities and obstacles as they arise on the shop floor. At each level, teammates share and debate their ideas. Thus, employees are assured a fair hearing for their points of view on decisions likely to affect them. With the exception of decisions involving major changes or resource commitments, the teams make and execute the decisions themselves.

Sparrows Point uses numerous processes and devices to ensure that all employees can understand why decisions have been made and how such decisions need to be executed. There is, for example, a bulletin board where decisions are posted and explained, allowing

Fair Process Is Critical in Knowledge Work

It is easy to see fair process at work on the plant floor, where its violation can produce such highly visible manifestations as strikes, slowdowns, and high defect rates. But fair process can have an even greater impact on the quality of professional and managerial work. That is because innovation is the key challenge of the knowledge-based economy, and innovation requires the exchange of ideas, which in turn depends on trust.

Executives and professionals rarely walk the picket line, but when their trust has not been won, they frequently withhold their full cooperation—and their ideas. In knowledge work, then, ignoring fair process creates high opportunity costs in the form of ideas that never see daylight and initiatives that are never seized. For example:

A multifunctional team is created to develop an important new product. Because it contains representatives from every major functional area of the company, the team *should* produce more innovative products, with less internal fighting, shortened lead times, and lower costs. The team meets, but people drag their feet. Executives at a computer maker developing a new workstation, for example, thoughtfully deploy the traditional management levers. They hammer out a good incentive scheme. They define the project scope and structure. And they allocate the right resources. Yet the trust, idea sharing, and commitment that everyone wants never materialize. Why? Early in the project, manufacturing and marketing representatives on the team propose building a prototype, but the strong design-engineering group driving the project ignores them. Subsequently, problems surface because the design is difficult to manufacture and the application software is inadequate. The team members from manufacturing and marketing are aware of these issues all along but remain passive in sharing their concerns with the powerful design engineers. Instead, they wait until the problems reveal themselves— at which time they are very expensive to fix.

Two companies create a joint venture that offers clear benefits to both parties. But they then hold their cards so close to their chests that they ensure the alliance will create limited value for either partner. The Chinese joint-venture partner of a European engineering group, for example, withholds critical information from the field, failing to report that customers are having problems installing the partner's products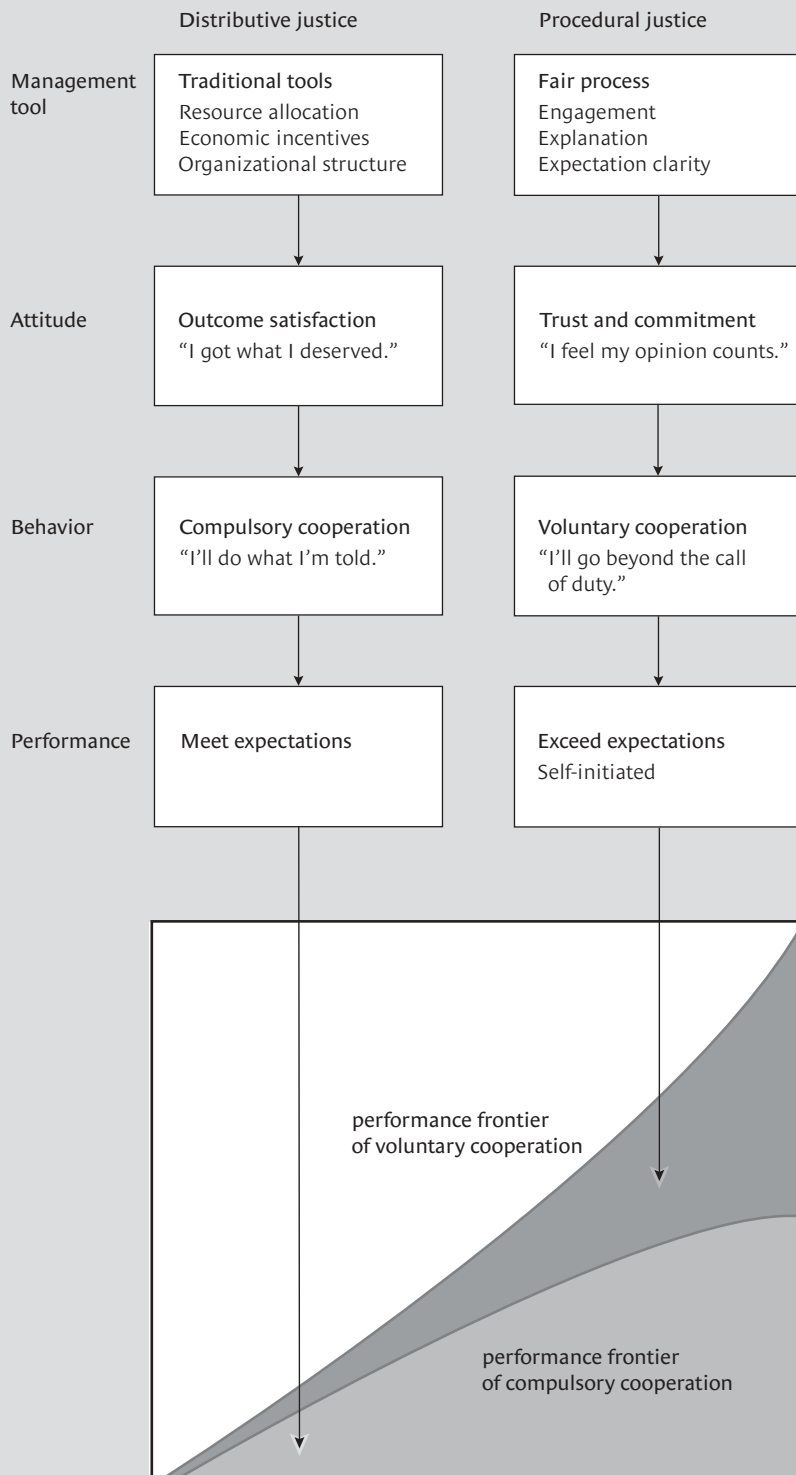 and sitting on requests for new product features. Why do the Chinese fail to cooperate fully, even if it means hurting their own business?

Early in the partnership, the Chinese felt they had been shut out of key product and operating decisions. To make matters worse, the Europeans never explained the logic guiding their decisions. As the Chinese withhold critical information, the increasingly frustrated European partner responds in kind by slowing the transfer of managerial know-how, which the Chinese need badly.

Two companies create a supplier partnership to achieve improved value at lower cost. They agree to act in a seamless fashion, as one company. But the supplier seems to spend more energy on developing other customers than on deepening the partnership. One consumer goods manufacturer, for example, keeps delaying the installation of a joint electronic consumer-response data system with a major food retailer. The system will substantially improve inventory management for both partners. But the supplier remains too wary to invest. Why? The retailer has a history of dropping some of the supplier's products without explanation. And the consumer company can't understand the retailer's ambiguous criteria for designating "preferred suppliers."

Two Complementary Paths to Performance

	Distributive justice	Procedural justice
Management tool	**Traditional tools** Resource allocation Economic incentives Organizational structure	**Fair process** Engagement Explanation Expectation clarity
Attitude	**Outcome satisfaction** "I got what I deserved."	**Trust and commitment** "I feel my opinion counts."
Behavior	**Compulsory cooperation** "I'll do what I'm told."	**Voluntary cooperation** "I'll go beyond the call of duty."
Performance	**Meet expectations**	**Exceed expectations** Self-initiated

performance frontier of voluntary cooperation

performance frontier of compulsory cooperation

employees who haven't been directly involved in those decisions to understand what's going on and why. In addition, in more than 70 four-hour seminars, groups ranging in size from 50 to 250 employees have met to discuss changes occurring at the division, learn about new ideas under consideration, and find out how changes might affect employees' roles and responsibilities. A quarterly newsletter and a monthly "report card" of the division's strategic, marketing, operational, and financial performance keeps each of the unit's 5,300 employees informed. And the teams report back to their colleagues about the changes they are making, seeking help in making the ideas work.

Fair process has produced significant changes in people's attitudes and behavior. Consider, for example, the tin mill unit at Sparrows Point. In 1992, the unit's performance was among the worst in the industry. But then, as one employee explains, "People started coming forward and sharing their ideas. They started caring about doing great work, not just getting by. Take the success we've had in light-gauge cable sheathing. We had let this high value-added product slip because the long throughput time required for production held up the other mills in the unit. But after we started getting everyone involved and explained why we needed to improve throughput, ideas started to flow. At first, the company was doubtful: If the product had created a bottleneck before, why should it be different now? But people came up with the idea of using two sequential mills instead of one to eliminate the bottleneck. Did people suddenly get smarter? No. I'd say they started to care."

The object in creating this new way of working at Sparrows Point was to improve the intellectual buy-in and emotional commitment of employees. It has apparently been successful. Since 1993, Sparrows Point has turned a profit three years in a row, the first time that has happened since the late 1970s. The division is becoming a showcase demonstrating how a declining industry can be revitalized in today's knowledge economy. In the words of one Sparrows Point employee, "Since we know now everything that's going on in the company, we have more trust in management and are more committed to making things happen. People have started doing things beyond the normal call of duty."

Overcoming Mental Barriers

If fair process is such a simple idea and yet so powerful, why do so few companies practice it? Most people think of themselves as fair, and managers are no exception. But if you ask them what it means to be a fair manager, most will describe how they give people the authority they deserve, or the resources they need, or the rewards they have earned. In other words, they will confuse fair process with fair outcomes. The few managers who focus on process might identify only one of the three fair-process principles (the most widely understood is engagement), and they would stop there.

But there are two more fundamental reasons, beyond this simple lack of understanding, that explain why fair process is so rare. The first involves power. Some managers continue to believe that knowledge is power and that they retain power only by keeping what they know to themselves. Their implicit strategy is to preserve their managerial discretion by deliberately leaving the rules for success and failure vague. Other managers maintain control by keeping employees at arm's length, substituting memos and forms for direct, two-way communication, thus avoiding challenges to their ideas or authority. Such styles can reflect deeply ingrained patterns of behavior, and

rarely are managers conscious of how they exercise power. For them, fair process would represent a threat.

The second reason is also largely unconscious because it resides in an economic assumption that most of us have grown up taking at face value: the belief that people are concerned only with what's best for themselves. But, as we have seen, there is ample evidence to show that when the process is perceived to be fair, most people will accept outcomes that are not wholly in their favor. People realize that compromises and sacrifices are necessary on the job. They accept the need for short-term personal sacrifices in order to advance the long-term interests of the corporation. Acceptance is conditional, however, hinged as it is on fair process.

Fair process reaches into a dimension of human psychology that hasn't been fully explored in conventional management practice. Yet every company can tap into the voluntary cooperation of its people by building trust through fair processes.

Reprint R0301K
Harvard Business Review OnPoint 407X
To order, see the next page
or call 800-988-0886 or 617-783-7500
or go to www.hbr.org

Fair Process

Managing in the Knowledge Economy

Further Reading

A R T I C L E S
The Smart-Talk Trap
by Jeffrey Pfeffer and Robert I. Sutton
Harvard Business Review
May–June 1999
Product no. 4061

Knowledge is a resource that can't be forced out of people. In "Fair Process," authors Kim and Mauborgne urge managers to build trust and create an environment where employees freely share their creativity and expertise. Pfeffer and Sutton explore another obstacle to sharing knowledge: smart talk, a type of inertia. An organization is plagued by smart talk when its employees let talk substitute for action, when they know too much and do too little. Confronted with a problem, people act as though discussing it, formulating decisions, and hashing out plans for action were the same as fixing it. People who engage in such talk generally sound confident and articulate; they can spout facts and may even have interesting ideas. But they also often exhibit a more insidious aspect of smart talk: focusing on the negative and favoring unnecessarily complex or abstract language. The former tendency lapses into criticism for criticism's sake; the latter confuses people and decreases their level of trust. Both tendencies can stop an action plan in its tracks. Pfeffer and Sutton offer five strategies for avoiding the smart-talk trap, rebuilding trust, and creating a more decisive organization.

Putting Your Whole Company's Brain to Work
by Dorothy Leonard and Susaan Straus
Harvard Business Review
July-August 1997
Product no. 4088

Leonard and Straus articulate another important aspect of building trust: creative abrasion, or colliding different ideas, perceptions, and ways of thinking so that they "grate" against one another productively. When people who see the world differently (abstract versus concrete thinkers, analytical versus intuitive problem solvers) try to collaborate, constructive conflict often degenerates into personal disputes, the creative process breaks down, and mistrust flourishes. But when managers put their company's "whole brain to work," they actively manage a team's collaborative process to ensure trust and greater creativity. They do so by taking time at the outset to acknowledge team members' differences. Before problems arise, they devise clear, simple guidelines for working together. For example, no one can disagree without stating the reason. Managers also schedule time for both divergent thinking (uncovering imaginative alternatives) and convergent thinking (focusing in on one option and then implementing it). And finally, they depersonalize conflict by acknowledging that other approaches are not wrongheaded, just different.

To Order

For reprints, *Harvard Business Review* OnPoint orders, and subscriptions to *Harvard Business Review:* Call 800-988-0886 or 617-783-7500. Go to www.hbr.org

For customized and quantity orders of reprints and *Harvard Business Review* OnPoint products: Call Rich Gravelin at 617-783-7626, or e-mail him at rgravelin@hbsp.harvard.edu