



What does the Design of your Organisation say about your Strategy?

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The design of your organisation is an important part of its effectiveness – yet it doesn't always get the attention it deserves. Management is not always aware of the linkages between design and strategy. And we often neglect the key principles when making decisions about it.

So, what is Organisation Design?

Organisation design deals with the structure and processes of the organisation. It focuses the organisation - allowing it to achieve the purposes for which it was created. As such, organisation design addresses three key issues:

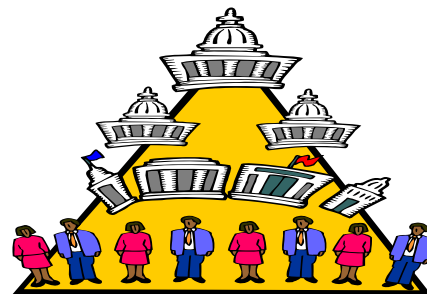
- How do we set up and manage the interface between the organisation and its customer groups?



- How do we configure resources so we get the best value-creating process?



- How do we integrate and support the various parts of the organisation to create synergy?



Why is Organisation Design so often neglected?

The reasons for apparently neglecting organisation design often revolve around a number of misconceptions that managers hold. These include:

Misconception 1: “A positive attitude is more important than organisation design or structure”

Managers often hold that staff can work “through” the design or structure and that their attitude and willingness to collaborate will drive their behaviours.

Our research (Chorn 1991, 2004) has shown that people can certainly overcome the limitations of the design and structure, *but they do so at a cost to themselves and the organisation*. Consequences of this include:

- Stress and tension within the organisation as people work outside some of the required lines of reporting and communication
- Certain elements of the organisation, such as autonomy and performance measurement, will be out of “synch” with the required behaviours – i.e. staff will not be measured or rewarded for the work they are required to do
- The organisation will be difficult to understand – particularly for outsiders and newcomers. The levels of uncertainty and complexity rise with a resultant fall in efficiency and increase in risk.

Misconception 2: “Good process can overcome the inadequacies of an inappropriate structure”

Sometimes when a structure does not deliver all that the strategy requires, management set up processes to correct the deficiencies. Examples here include the TQM processes designed to “integrate” the outputs and inputs of various divisions within the organisation.

Why is this a problem?

- Structure is more “powerful” than process. Because structure determines who you work with, the reporting relationships and the way your performance is measured, it tends to have a greater

impact on shaping behaviour than any process that has been implemented (Chorn 1991, 2004)

- Processes that are designed to “cut across” the organisation can cause tension and confusion as a result of the additional lines of reporting. These can often be in conflict with each other and result in sub-optimum outcomes
- The primary shaper of outcomes will be the structure of the organisation. At best, processes such as TQM and “coordinating committees” can only moderate the behaviour of the organisation. “Quality” and “integration” are outcomes that should be designed *into* what the organisation does, rather than being added as a secondary process.

Misconception 3: Flexibility is a lack of structure

In changing and uncertain environments, managers want to retain maximum flexibility in their repertoire of strategies and responses. And so they resist explicitly defining the organisation design or structure in the belief that this will allow them to retain maximum flexibility.

But flexibility is *not* produced by a lack of structure. Flexibility is produced when the design and structure adequately reflect the complexity and uncertainty in the environment. A lack of structure generally results in uncoordinated effort and a lack of focus in the way resources are deployed. Research shows that unstructured organisations usually under-perform (Miles & Snow, 1978, 1984; Stace & Dunphy, 2001; Cunningham, 2002).

How does Organisation Design impact on behaviour?

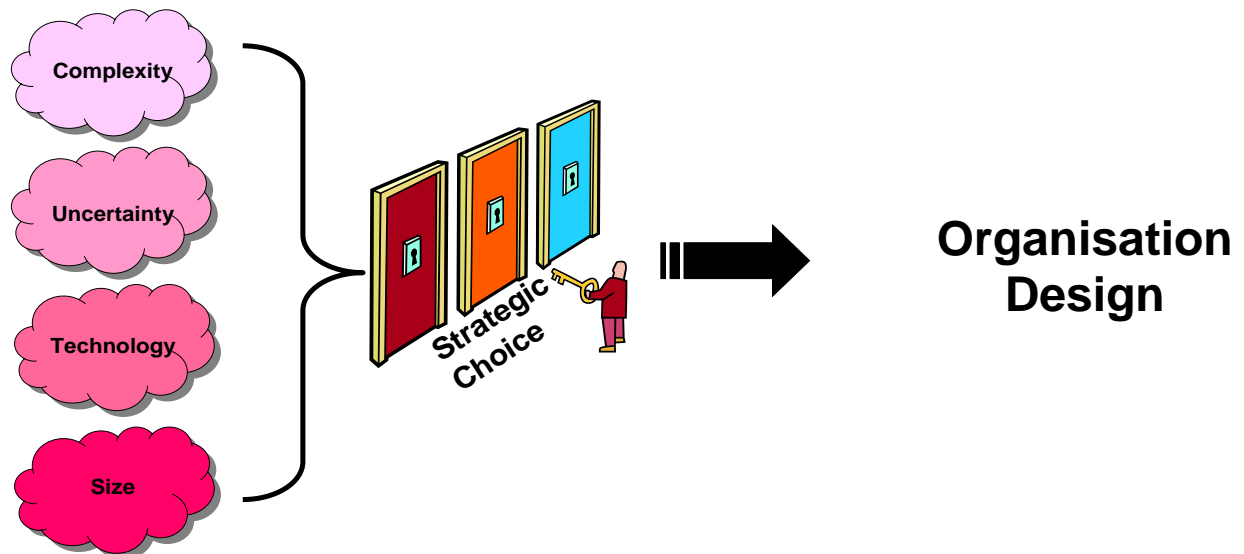
Organisations involve social interactions between the members – but these interactions are not simply random contact. The organisation imposes a certain “structure” to the way the interactions occur – by grouping people together in certain ways and by giving them specific objectives to meet.

The way these interactions are designed and structured reflects the way we have chosen to control and coordinate the resources of the organisation – and the way we have chosen the desired outcomes of the organisation.

So, the design and structure of the organisation will shape its behaviour and strategy. In many ways, it could be said that the design and structure of the organisation is the ultimate expression of the organisation's strategy!

What are the key influences on Organisation Design?

Five key influences shape the design of organisations:



- The level of *uncertainty* within the environment and the organisation
- The extent of the *complexity* and fragmentation in the environment and organisation
- The *technology* that is used in the value-creating process
- The *size* of the organisation -although size on its own is not a key determinant
- The *strategic choice* made by management – although this is often affected by the “bounded knowledge” that they possess.

1. Levels of uncertainty

In general, the greater the level of uncertainty in the environment or organisation, the more we have to rely on a range of *indirect* and *subjective* means to achieve coordination and control of the behaviours and patterns of interaction:



Low uncertainty



Direct control

- Control by objective measures
- Explicit and formal standards
- Coordination by rules, regulations and standard operating procedures
- Roles and decision authority precisely defined

High uncertainty



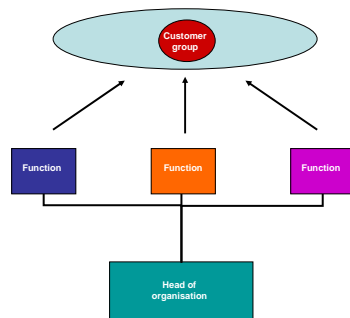
Indirect control

- Control by subjective measures
- Implicit and informal standards
- Coordination by staff participation in a common set of values and vision of the future
- Roles and decision authority broadly and generally defined

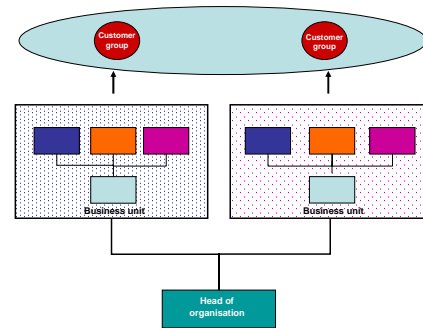
2. Complexity and fragmentation

In most cases, this is about the number of different “parts” that make up the organisation and its environment. Complexity generally refers to the number of occupational or process specialties within the organisation, whereas fragmentation usually refers to the number of different segments or customer groupings in the market.

Single organisation Single market



Complex organisation Fragmented market



Complexity and fragmentation is dealt with by introducing *differentiation* into the design – i.e. where the organisation creates additional functions and /or processes to deal with these different aspects. Importantly, the more differentiation that is created in the design, the more *integration* has to be created.

3. Different forms of technology

Technology refers to more than the “IT” component – we are concerned with the value-creating processes in the organisation.

Generally, we can identify five broad technology types as follows:



Continuous production: Ongoing process for converting materials or information to a higher state. Eg - chemical plant



Mass production: Production of large volumes of a standard unit. Eg – a vehicle assembly plant



Engineering: Using physics and mathematics to convert materials to another state. Eg – building bridges / equipment

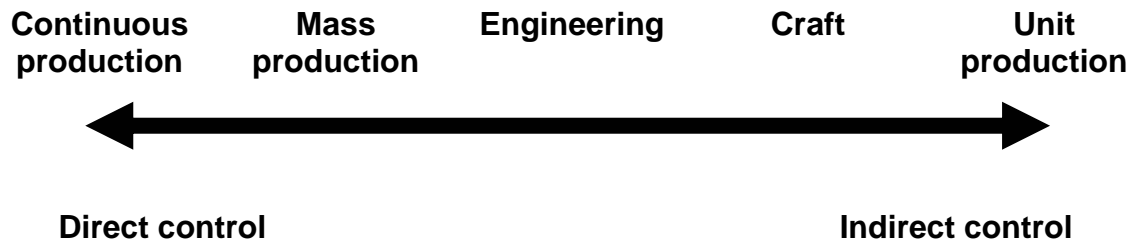


Crafts: Skills used in individualistic ways to produce non-standard outcomes. Eg – jewellery making



Unit production: Production of one-off or one-at-a-time products and services. Eg – prototypes / consulting assignments

Depending on the type of technology to be used, we can identify the most appropriate form of organisation design. Once again, this refers to the nature of the controls and decision authority we defined earlier:



As we can see, this means that we should design different parts of the organisation in different ways – depending on the nature of the technology being used. As we move along the continuum from continuous production towards unit production, we would be replacing the objective and explicit structures with more subjective and implicit controls.

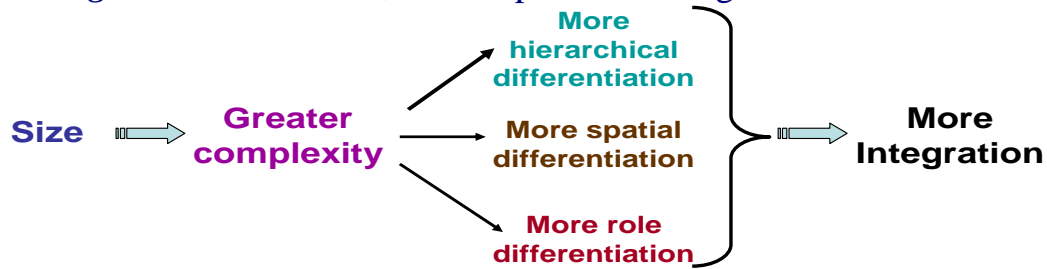
4. Organisation size

Clients often tell me that they prefer keeping their organisations small so that they can remain flexible and nimble. The implication is that with size comes additional complexity and bureaucracy. It's an interesting argument – but it's not entirely correct!

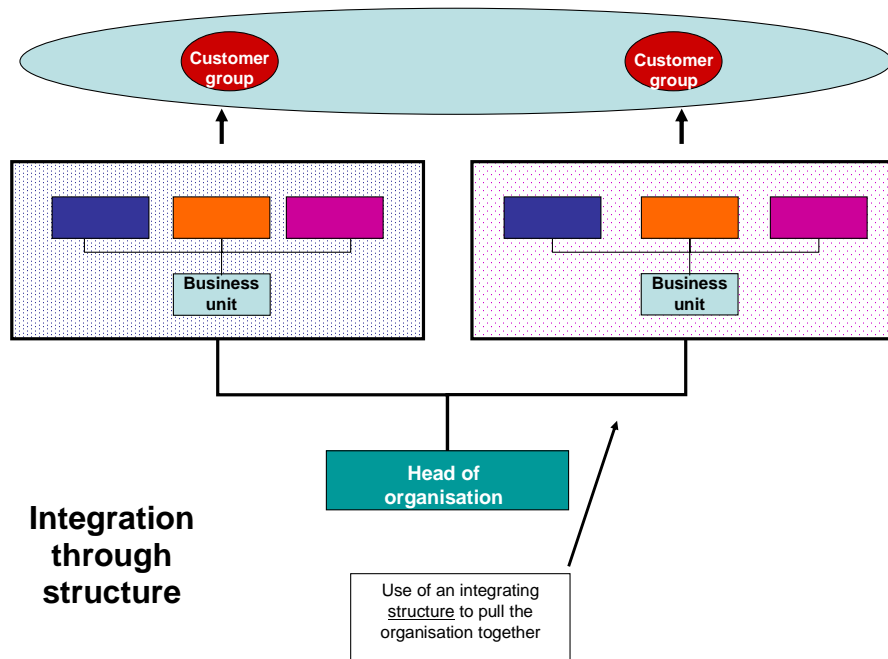
Size is often associated with greater complexity, but research shows no necessary link with being cumbersome and rigid. Size impacts on the organisation in three ways:

- **Size → more hierarchical differentiation**, i.e. more levels in the organisation to cope with the additional people and resources
- **Size → more spatial differentiation**, i.e. more units and departments to deal with the business of the organisation
- **Size → more role differentiation**, i.e. greater division of labour and use of specialists in the organisation.

But as we know from the earlier discussion, more differentiation requires more *integration*¹. Therefore, we can present the argument as follows:



And the integration can be achieved through various structures and processes – we need this to “pull the parts of the organisation together”.

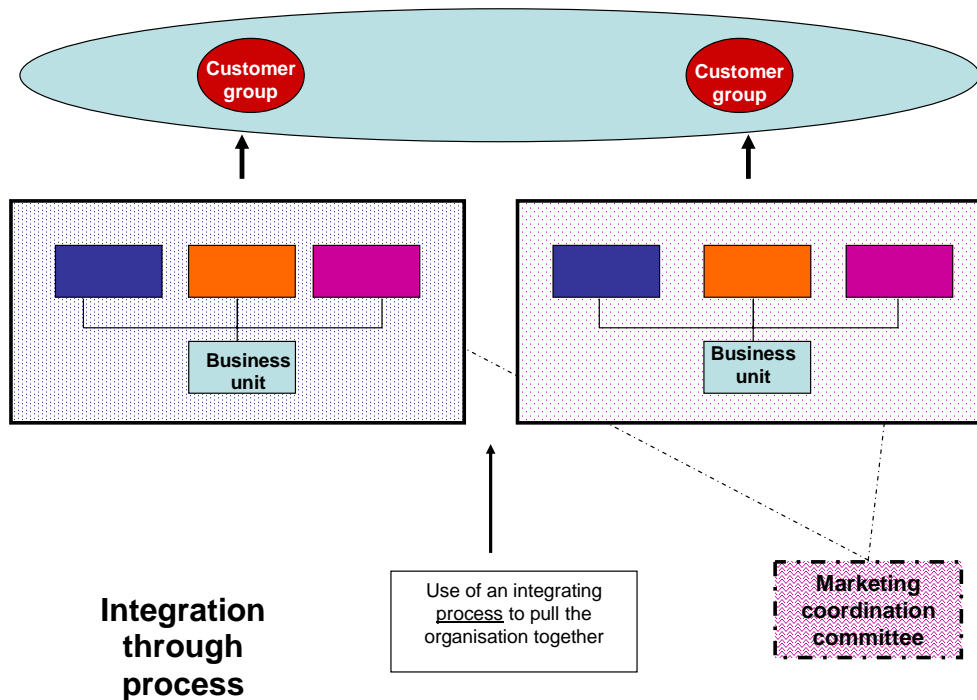


In the example above, we show the use of an integrating *structure* – the appointment of an overall “head of organisation”. This role has the responsibility of integrating the efforts of the two business units.

In the example below, we show the use of a “marketing coordinating committee” – an integrating *process* where the marketing managers in the two business units attempt to coordinate their marketing efforts.

¹ We need to be careful of making generalisations about these relationships. Larger organisations are not necessarily more complex than smaller organisations. For example, it may be more complex to manage a small, multi-technology organisation than a larger, single-technology one.

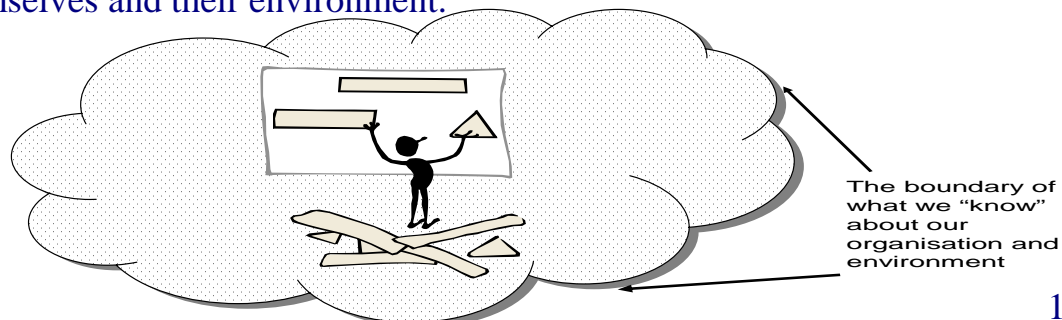
We mentioned earlier that structure is more “powerful” than process. Usually, this means that the integrating efforts via the structural solution will be more effective than that via the process. So, putting one manager above both business units is likely to be more effective at integrating their marketing efforts than creating a coordinating marketing committee.



5. Strategic choice

While all the factors mentioned above place constraints on the final organisation design, management still has to exercise some choice. Strategy is about choice, and management will choose the design that best meets their needs.

But why do designs and structures emerge that are obviously NOT the optimum solutions – at least to the outside observer? The major reason seems to be that management operates within what is known as “bounded rationality” (Simon 1957, Johnson & Scholes, 2002). This is, quite literally, a boundary that defines the limits of knowledge and understanding of themselves and their environment.



They attempt to make rational and logical decisions in the best interests of the organisation – but they do so within the limits of what they know and understand at that point in time.

These boundaries are determined by many factors, including:

- Political and power factors – where a powerful individual retains control of certain functions even though there is no logic for it
- Cultural factors – where the organisation “believes” in a particular approach and always follows it – eg “we always have an engineer heading up our organisation”
- Knowledge limitations – where the organisation’s information systems are designed to emphasise certain information only.

What are the principles worth keeping in mind when designing organisations?

We’ve done all the analysis and considered all the external and internal factors. We now want to design the organisation and its structure. Where do we start? What are the key principles to keep in mind?

I have identified some seven general principles that have served me well over the years. They are based on research – both mine and others’ – and include the experience I have had in working on many such assignments:

1. Beware of generalised principles!

This may be a strange principle to start with; given this is exactly what I am doing! But one of my major gripes is the crude checklists that some leaders carry around with them. They often include simplistic slogans such as:

- *“Never have more than five layers between the customer and CEO”*
- *“Keep your number of direct reports to below seven”*
- *“Don’t have more than 100 people in the organisation.”*

While these principles may apply in certain situations, they are dangerous to apply across the board. Our discussion above suggests that the appropriate design depends on the situation on hand.

2. The organisation design should be understandable to most people in the organisation

I often come across organisations with such complicated designs and structures that staff don't know how the whole thing works. This is usually a good indication that the organisation is not operating as effectively as it could.

When people don't understand how the organisation works, they operate within a severely bounded rationality. They will be making decisions based on an incomplete understanding of the organisation and its strategy. There will be many "irrational" and sub-optimum decisions being made.

3. The organisation design should reflect the "strategic intent" of the organisation

The debate about whether strategy leads structure, or vice versa, is not of concern here. What is important, however, is that organisation design and structure give effect to the strategy.

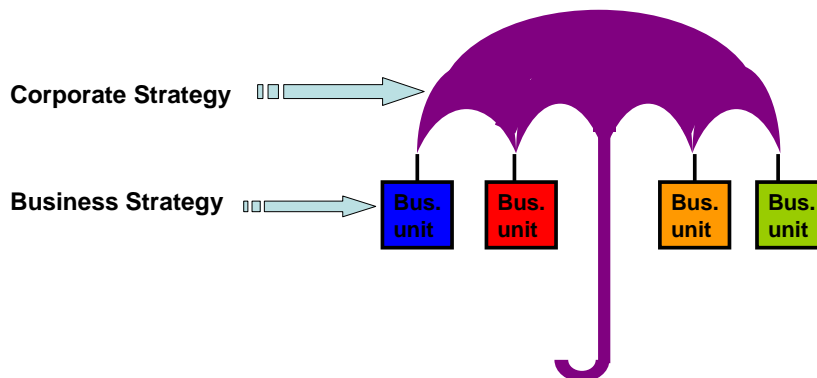
For example, if your strategy is to offer the customer a totally seamless and one-stop experience, then your structure should reflect this. The design should, for example, integrate all the elements of your offer and manage the various linkages inside the organisation, rather than expecting the customer to speak to several different departments in order to have their problem solved or query answered.

4. The organisation design should reflect appropriate levels of uncertainty and complexity

The internal structure of the organisation should reflect the conditions of the operating environment in which it operates. One cannot expect a highly routine set of processes to work effectively in a highly uncertain and complex environment.

As the levels of uncertainty and complexity rise, so the nature of the controls and systems within the organisation should shift towards a more indirect / subjective approach. We have to forgo some of our *efficiency* concerns in favour of a focus on *effectiveness*.

5. Don't confuse responsibility for Corporate Level strategy and Business Level strategy



Corporate strategy involves the integration of the whole organisation, while *business strategy* focuses on the performance of a single business unit within its market or customer group.

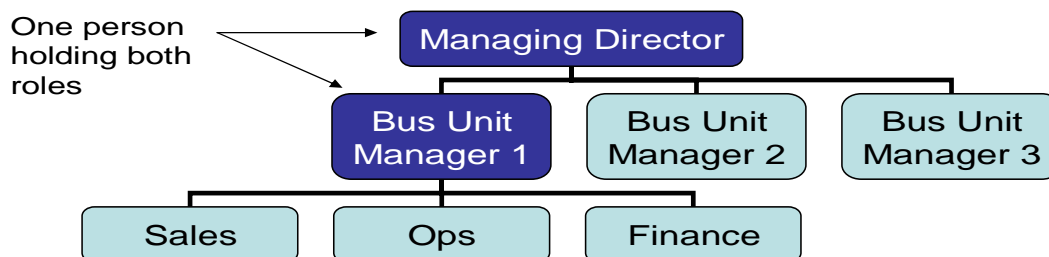
Corporate strategy

- Defines the shape of the overall portfolio of businesses and activities within the organisation – *what business are we in?*
- Allocates and deploys resources across the whole organisation so as to optimise performance of the whole organisation

Business strategy

- Focuses on competing / operating within the defined “space” of the business
- Addresses the customers / stakeholders within its operating environment

They have different focuses and types of responsibility. It is not a good idea to create a structure that gives someone responsibility for both areas at the same time. In my experience, the breadth of the dual role is too great for most people – no matter how talented they are! The timing, pace and skills required at the corporate level are quite different to those at the business level. This situation almost inevitably results in one of the two roles being performed inadequately.



6. In order for federal structures to work, important conditions apply

Federal designs are popular in complex organisations that address several different markets. In these designs, the organisation is formed by several semi-autonomous business units with a head office that performs an overall integrating function. (The business units focus on “business strategy” while the head office deals with “corporate strategy”).

However, the success of these designs is dependant on several important conditions (see Handy 2002), including:

- a) **Subsidiarity**: All the supporting functions that are necessary to make a business unit effective should be included *within* the business unit. That is, the manager responsible for the unit should have direct influence over the resources needed to operate effectively.

The obvious exceptions are those functions that have a vital corporate role or where the resources are extremely scarce. Even so, head office roles should be confined to policy – the application and implementation is the responsibility of the business unit wherever possible.

In my opinion, this is the most misunderstood and abused principles in federal structures. Under the guise of “sharing costs”, many organisations set up support centres / units whose role it is to “serve” the needs of the business units. There is a limited case for “shared services”, and this includes issues such as lack of critical mass, low value-add of the service, and a similar need by the various “internal customers”.

In many cases, however, the setting up of support units creates the dilemma of the “internal customer” that sub-optimises the organisation’s overall effectiveness by confusing roles and creating an overly internal focus.

- b) **Twin citizenship**: Managers need to adopt a corporate perspective for major decisions. Although they are a “citizen” of their business unit and have to operate with their business unit’s interest in mind, they are also a “citizen” of the overall corporate entity – and it is at this level that their primary loyalty should lie.

Decisions should be made in the long-term interests of the whole organisation – even though the short term interests of the business unit may be compromised. Often, incentives within the organisation will prevent this from happening, and to this extent, the federal structure fails to deliver optimum effectiveness.

7. Outsource with care

The last decade has seen a rise in outsourcing, whereby organisations contract out processes that can be delivered more efficiently elsewhere. This has certainly delivered short-term cost savings in many cases, but the rising number of policy reversals in this practice has led some to rethink the initial approach.

From my consulting experience I have identified five key pointers to keep in mind when considering outsourcing:

- **Make sure you understand the true cost of the service:** This is actually a good argument in favour of going through the outsourcing process, since organisations rarely understand the future cost of the service until they explore the outsourcing option.
- **Protect the core elements of your value-creating process:** If possible, those parts of the organisation that create the real value proposition to customers should be protected from outsourcing.

For example, if your proposition is that you offer “24-hour professional advice”, then you should not outsource your after-hours telephone answering.

- **Ensure that variations in the quality of the outsourced service will not impair the customer’s experience:** A good example here are furniture retailers who outsource the delivery of their product to transporters who serve several retailers. I can certainly recall a number of situations where I had purchased an item of furniture in the pleasant surroundings of a furniture store – only to have the illusion well and truly shattered by the experience of “rough and tough” delivery people.
- **Ensure that you retain enough “space” in the value chain to justify your position as the “supplier”:** In most cases, the outsourcing takes place “behind the scenes” – you still offer and take responsibility for the whole proposition to your customers.

However, if you have outsourced large parts / components of the value

chain and this is apparent to outsiders, you may lose the ability to legitimately represent the offer to customers. In addition, you may limit your ability to add value and charge an acceptable price / fee for your services.

- **Remain as close to the customer interface as possible:** The research on customer value management (Gale, 1994; Johnson & Scholes 2002) suggests that, in general, value migrates to the point of interface with customers. The most valuable position for an organisation is to control and manage the relationship with the customer.

In general, therefore, it is preferable not to outsource those functions that allow you to do so. This may erode your ability to add value in the long run.

- **Never outsource your vision, leadership or values:** This may seem obvious, but you should avoid outsourcing the thinking and interactions that are needed to develop strategic direction and what the organisation stands for! Consultants provide an important external perspective, but they only assist and advise. These must be you decisions and positions.

Organisation Design is an important driver of effectiveness

We have seen the influence that design and structure have on the effectiveness of the organisation. Often, this influence is ignored due to popular misconceptions.

In general, management should see design as a tool that can be purposefully used in planning organisational outcomes. Uncertainty, complexity and technology need to be considered when structuring or re-engineering the organisation, as do some of the principles inherent in the ever-popular federal structures we use in our organisations.

In the final analysis, I hope that we can recognise the important contribution made by organisation design and structure in the overall success of the organisation.

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