Frameworks for Organizational Design

Executive Brief

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This report five leading frameworks companies can use when approaching organizational design. Although there is no universal or ideal organizational structure, the most notable common thread connecting these top approaches is organizational strategy. Each framework emphasizes that considerations of the organization's strategy should be the key determinant of how the business will be structured. Different strategies lead to different organizations; the chosen design best meets the criteria derived from an organization's unique strategy.

JAY GALBRAITH'S STAR MODEL

Jay Galbraith's star model is one of the most widely-used and accepted organizational design frameworks. This model relies on the following five categories of design policies: strategy, structure, processes, rewards, and people. These categories determine the direction of the organization, the location of decision-making power, the flow of information, the motivati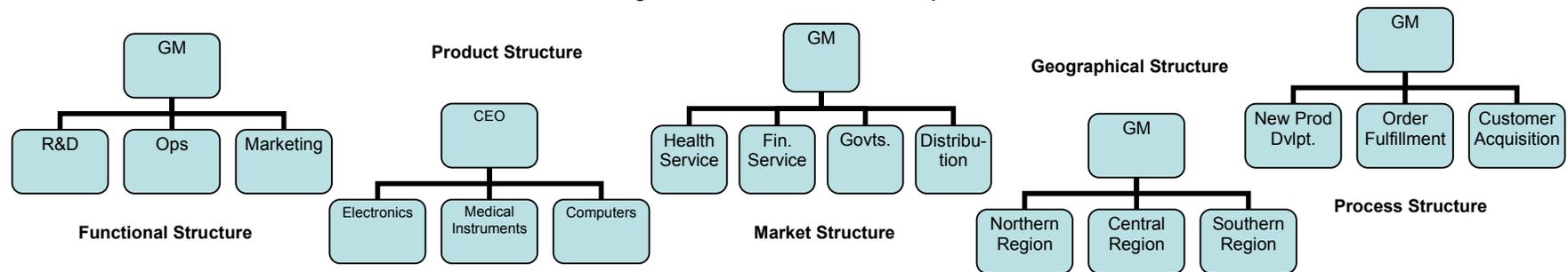on of people to perform, and employee mindset and skills. In other words, strategy drives structure; processes are based on structure; and structures and processes define the implementation of reward systems and people policies. Figure 1 below depicts Galbraith's Star Model and provides an overview of the components included within each category of his framework:[1]

Figure 1: Galbraith's Star Model

5. HR policies produce the talent that is required by the strategy and structure of the organization, generating the skills and mind-sets to implement the company's chosen direction.

1. Strategy is the first component of the star model to address and establishes the criteria for choosing among alternative organizational forms. Each organizational form enables some activities while hindering others; strategy dictates how to make these trade-offs.

2. Structure determines the placement of power and authority in the organization.

4. Rewards align goals of employees with organizational goals. Rewards must be congruent with structure and processes to influence strategic direction.

3. Processes cut across an organization's structure and determine its functioning. Vertical processes allocate scarce resources while lateral processes enable work flow.

Strategy and structure are the first design policies to be addressed through this model. Figure 2 below introduces the five basic structures that can be derived from various strategies; refer to page 4 for additional information on each structure type.

Figure 2: The Five Basic Structure Options

Functional Structure
GM — R&D, Ops, Marketing

Product Structure
CEO — Electronics, Medical Instruments, Computers

Market Structure
GM — Health Service, Fin. Service, Govts., Distribu-tion

Geographical Structure
GM — Northern Region, Central Region, Southern Region

Process Structure
GM — New Prod Dvlpt., Order Fulfillment, Customer Acquisition

JAY GALBRAITH'S STAR MODEL (CONTINUED)

Galbraith's Star Model design requires organizations to use a chosen strategy to inform structure decisions. Figure 3 below highlights the five basic structure options introduced on the previous page and connects them with the strategy characteristics they facilitate. Organizations can use this figure to make design trade-offs depending on the strategy characteristics and goals they find most critical:

Figure 3: Strategies Associated With the Five Basic Structure Options

Structure Type	Description	Advantages	Disadvantages	Characteristics of Strategy Supported by this Structure
Functional Structure	Organized around activities or functions	▪ Gathering workers of one type allows them to transfer ideas and knowledge ▪ Allows for greater scale, specialization, and standardization ▪ Presents a single face to vendors to exercise buying leverage	▪ Creates barriers between different functions ▪ Overwhelming if there are a variety of products, channels, or customers	▪ Small-size, single-product line ▪ Undifferentiated market ▪ Scale or expertise within the function ▪ Long product development life cycles ▪ Common standards
Product Structure	Multiple functional organizations, each with its own product line	▪ Compresses the product development cycle because each unit focuses on a single product line	▪ Divisions want autonomy, so they reinvent the wheel and duplicate resources ▪ Organization loses economies of scale ▪ Challenging when customers buy from more than one product division	▪ Product focus ▪ Multiple products for separate customers ▪ Short product development life cycle
Market Structure	Organized around customers, markets, or industries	▪ Companies with superior knowledge and information about market segments have a competitive advantage ▪ Helps service businesses that must focus on market segments	▪ Tendency to duplicate activities and develop incompatible systems ▪ Difficulty sharing common products or services	▪ Important market segments ▪ Product or service unique to segment ▪ Buyer strength ▪ Customer knowledge advantage ▪ Rapid customer service and product cycles
Geographical Structure	Organized around districts, regions, or territories	▪ Minimize costs of travel and distribution when close to the customer ▪ Helpful if organization needs to be located near a source of supply	▪ Becoming less important now that technology allows companies to be anywhere and seek the best global location	▪ Low value-to-transport cost ratio ▪ Service delivery on-site ▪ Closeness to customer for delivery or support ▪ Perception of the organization as local
Process Structure	Organized around a complete flow of work	▪ Allows a renewed look, from end to end, at an entire process ▪ Processes with end-to-end coverage lend themselves to measurement more easily than other functions	▪ Creates barriers in handoffs between various process groups	▪ Potential for new processes and radical change to processes ▪ Reduced working capital ▪ Need for reducing process cycle times

BOSTON CONSULTING GROUP'S BUILDING BLOCKS FRAMEWORK

The Boston Consulting Group presents four building blocks that help a company avoid the pitfalls of organizational redesign and create the most successful structures. These include identifying the right business issues, pinpointing the right underlying obstacles, adopting the right design characteristics, and implementing change the right way. Figure 4 below provides additional details for each building block, while information regarding optimal design characteristics stemming from these building blocks is included on page 6.[2]

Figure 4: Boston Consulting Group's Four Building Blocks

BUILDING BLOCK	DESCRIPTION	GUIDING QUESTIONS
Right Issues	Because good design is based on good strategy, companies should translate business issues into goals for the redesign. Organizations must understand how they compete, where they make money, and what organizational levers enhance performance.	• How important is leveraging global opportunities? • How critical is cost to shareholder value? • Where are the synergies across the business portfolio?
Right Obstacles	Once business issues are identified, organizations must decide what it takes to address these issues. Obstacles to achieving solutions must be pinpointed accurately to ensure a redesign's success.	• How does your organization work today in terms of communication, workflow, and results? • Where are the obstacles in terms of goal alignment, resources, culture, and values?
Right Design Characteristics	Successful designs manage tradeoffs. They also respond to the global nature of today's economy, an evolving workforce, and the increasing role of speed and scale in competitive advantage.	• How does industry evolution, including globalization, information technology, and deconstruction, affect design options? • How will work force trends such as increased career mobility alter design options? • What design options will enhance speed and leverage scale?
Right Change	Successful redesigns are implemented organically rather than mechanically. Redesign efforts succeed when the organization has a clear vision for action, committed leadership, and exacting project management.	• Are key stakeholders involved in the redesign? • Have employee reactions and feelings towards change been taken into account?

Case in Point: Identifying Causes, Not Just Symptoms

This example highlights how one company pinpointed the cause of a problem in its marketing organization. Marketing units were not working well together, causing the sales forces they shared to be pulled in different directions. The initial thinking was that the marketing teams lacked an adequate common mechanism for coordination, although the underlying problem was that the teams had objectives and incentives that encouraged them to compete with one another rather than cooperate.
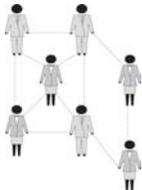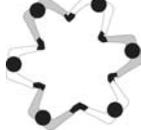
Questions	Marketing's Answers
Why don't the marketing teams work together?	We don't have time.
But when you do have time?	Our products are not related.
But you sell to a common set of customers?	We are all structured differently.
Would you work together if you were structured the same way?	No. We sell through the same sales force; I need to maximize my share of voice.
So if you win, others lose?	Yes. I want to sell my products, even at the expense of others.

Source: Boston Consulting Group

BOSTON CONSULTING GROUP'S BUILDING BLOCKS FRAMEWORK (CONTINUED)

The Boston Consulting Group framework also stresses the notion that successful designs respond to three major forces that drive the economy. First, the basic nature of business is evolving: industries are becoming increasingly global, companies are depending more and more on information gathering and exchange, and value chains are deconstructing at an accelerated pace. Second, the workforce is evolving—a development marked by more highly qualified staff, increasing career mobility, and greater career expectations. Third, the route to competitive advantage has changed, hinging on achieving greater speed, leveraging capabilities, and capturing scale in corporate knowledge and costs. These forces have produced a common set of characteristics, highlighted in Figure 5 below, that can guide any organization design initiative.[3]

Figure 5: Organization Design Characteristics

Orientation for Interactions	Hybrid Structures and Overlays	Rewards for Performance	Open-Source Approaches	Small But Active Corporate Center	An Organization Built to Change
Design should account for all the ways people work together, including objectives, capabilities, roles in key processes, and information flows. Interactions should occur across organizational boundaries and a good design will take into account the forces beyond structure that drive behavior.	Successful designs will include a variety of forms to reflect different business economics across the organization. For example, the heads of some business units may require more control or power than others, and network overlays may be needed to encourage functions within the organization to work together to improve the management of common processes or share best practices.	Redesigns should include highly-variable incentives for individuals through performance-based programs that extend down the corporate ladder. The importance of performance-based rewards also underscores the need for mechanisms to measure performance in any new design.	Effective designs often include close links with suppliers, allowing customers and suppliers to be integrated, redefining opportunities for outsourcing.	Well-designed organizations do not burden the corporate center with minor administrative tasks that can be better performed within business units or in a shared services center. The most effective corporate centers have the resources and capabilities to manage senior talent, disseminate best practices, and drive major change initiatives and strategy.	Organizational design should institutionalize the organization's capacity to remake itself by fostering ideas that are important for future growth (but potentially disruptive to existing businesses) and by implementing checks and balances through structures and processes that allow the status quo to be questioned.

BALANCED SCORECARD: MAKING TRADEOFFS BETWEEN CENTRALIZED AND DECENTRALIZED

The Balanced Scorecard is a model of business measurement and management designed not only to assess financial metrics that reflect past events, but also to incorporate measures related to the drivers of future performance. The objectives and measures of the scorecard are derived from an organization's vision and strategy and view organizational performance from the following four perspectives: financial, customer (external), internal business process (operational), and learning and growth (strategic).[4] The perspectives of the balanced scorecard may be adapted to assess tradeoffs between centralization and decentralization in the following manner:

- **Financial Perspective**—includes elements of resource allocation and scale economies. *How will the structure affect costs?*
- **Strategic Perspective**—includes elements of competence, culture, and leadership. *How will the structure affect human capital?*
- **Operational Perspective**—includes elements of process and coordination. *How will the structure affect key processes?*
- **External Perspective**—includes elements of customer service and marketing. *How will the structure affect market position?*

Each of these four perspectives can be linked to key decision points related to potential degree of centralization. By answering questions related to how structure should address these decision points and perspectives, organizations can make decisions around centralization and decentralization, as highlighted in Figure 6 below. While this presents a general example, the balanced scorecard framework is highly adaptable to individual organizations' missions, strategies, and environments. Organizations can customize this framework by breaking their unique mission and strategy statements into relevant perspectives and then assessing the resulting decision points with targeted questions.
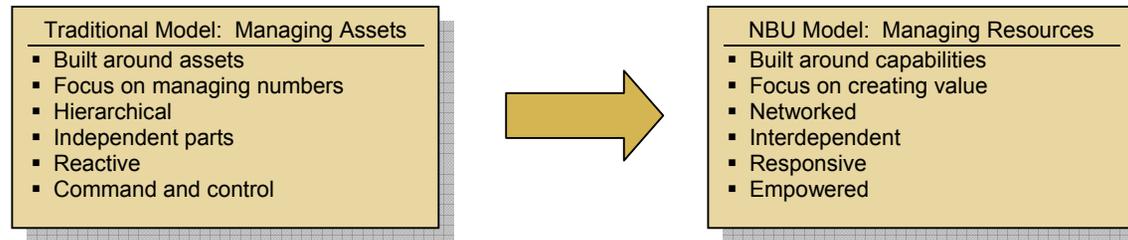
Figure 6: Assessing Tradeoffs from Four Organizational Perspectives

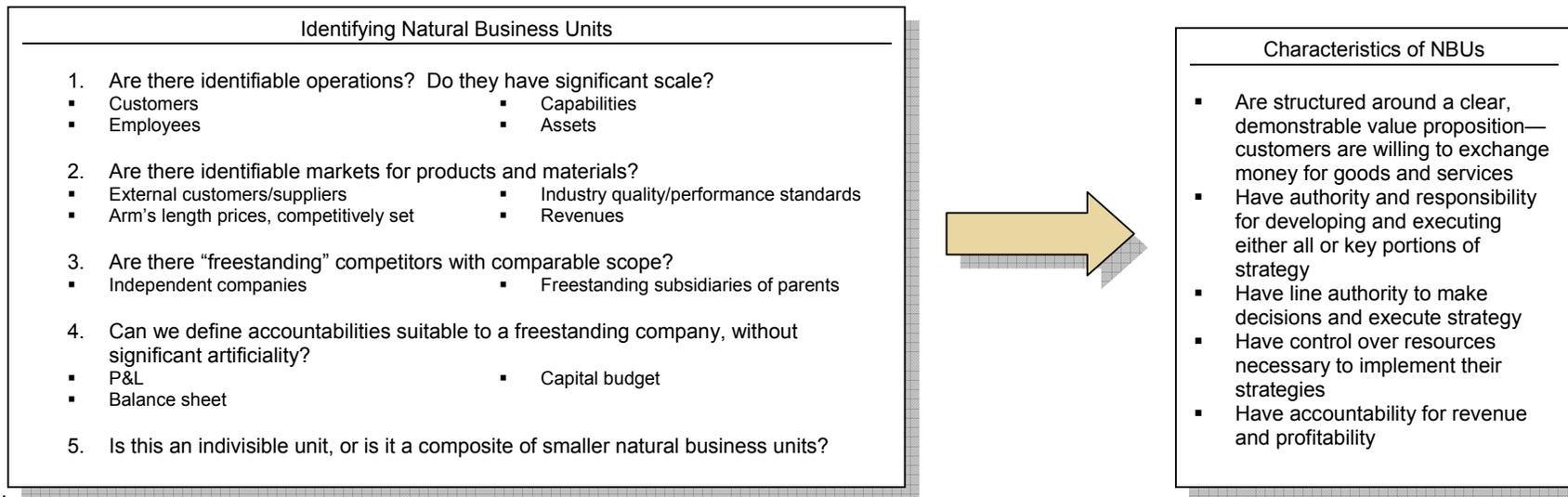| Perspective	Decision Point	Scale
		Decentralized ◄────────────► **Centralized**
Financial	**Scalability**—Which functions realize economies of scale? **Cost Structure**—What resources may be shared by all business units?	Small Economies of Scale------------------------------ Large Economies of Scale Charge-Back--Overhead
Strategic	**Innovation**—How rapidly must the company innovate to remain competitive? **Culture/Values**—How important is a common culture and shared values? **Competencies**—What core skills should be shared by all business lines? **Leadership Style**—Does the desired culture favor top-down or bottom-up leadership?	High Importance-- Low Importance Diverse---Shared Arise from Business Units--------------------------------------- Maintained at the Top Bottom Up---Top Down
Operational	**Oversight/Control**—Which processes should be monitored across business lines? **Speed of Business**—What types of decisions should be made on the line? **Internal Networks**—What functions must coordinate to accomplish goals?	Low Importance --High Importance Fast Moving --Slow Paced Low Level of Coordination --------------------------------High Level of Coordination
External	**Customer Proximity**—How important is proximity of customer to the line? **Market/Landscape**—How does the company gain customer knowledge? **Competitive Advantage**—Where does the company find competitive advantage? **Mission**—How does each function contribute to the company's mission?	Source of Advantage Near Market------------------ Source of Advantage Internal Highly Market-Driven-- Slightly Market-Driven

BOOZ ALLEN HAMILTON'S NATURAL BUSINESS UNITS

Booz Allen Hamilton's "Natural Business Units" (NBUs) approach is an organization design framework that involves bringing business units into closer alignment with their essential strengths and with ever-changing market demands. Organizing around natural business units and using NBUs to make decentralization decisions allows a company to be more customer-focused and agile through simplification. Traditional business unit configurations can hamper progress because they approach market challenges from an inside-out or top-down perspective. Companies should be structured around capabilities rather than a traditional definition of business lines or assets, as highlighted in Figure 7 below:[5]

Figure 7: Transitioning from Traditional Business Units to Natural Business Units

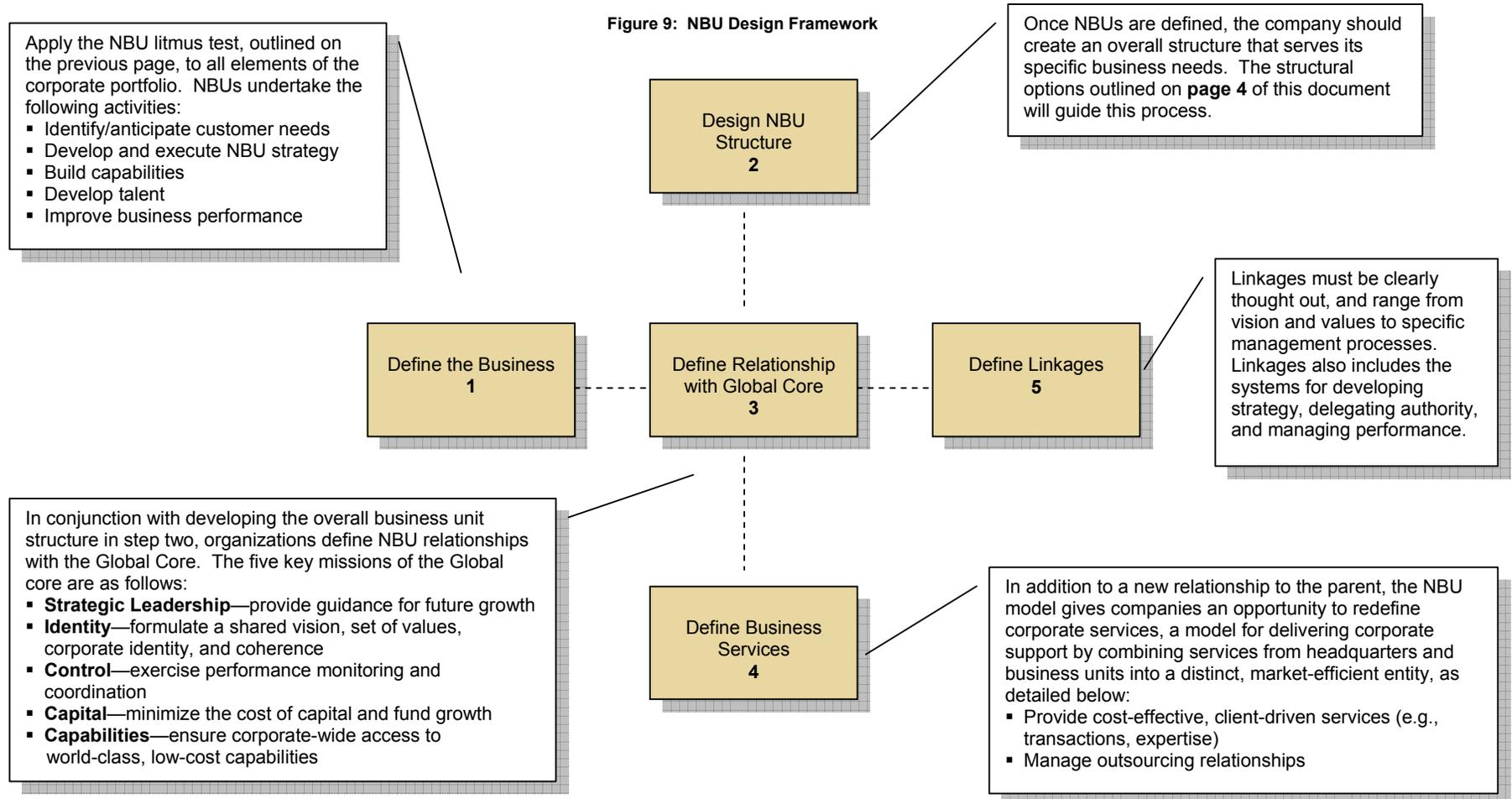| Traditional Model: Managing Assets	NBU Model: Managing Resources
▪ Built around assets ▪ Focus on managing numbers ▪ Hierarchical ▪ Independent parts ▪ Reactive ▪ Command and control	▪ Built around capabilities ▪ Focus on creating value ▪ Networked ▪ Interdependent ▪ Responsive ▪ Empowered

To achieve this transformation, businesses should be organized from the outside-in, or from a customer back perspective. Organizations can use the NBU litmus test, detailed in Figure 8, to identify whether or not they have the right business units.

Figure 8: NBU Litmus Test

Identifying Natural Business Units

1. Are there identifiable operations? Do they have significant scale?
   - Customers
   - Employees
   - Capabilities
   - Assets

2. Are there identifiable markets for products and materials?
   - External customers/suppliers
   - Arm's length prices, competitively set
   - Industry quality/performance standards
   - Revenues

3. Are there "freestanding" competitors with comparable scope?
   - Independent companies
   - Freestanding subsidiaries of parents

4. Can we define accountabilities suitable to a freestanding company, without significant artificiality?
   - P&L
   - Balance sheet
   - Capital budget

5. Is this an indivisible unit, or is it a composite of smaller natural business units?

Characteristics of NBUs

- Are structured around a clear, demonstrable value proposition—customers are willing to exchange money for goods and services
- Have authority and responsibility for developing and executing either all or key portions of strategy
- Have line authority to make decisions and execute strategy
- Have control over resources necessary to implement their strategies
- Have accountability for revenue and profitability

BOOZ ALLEN HAMILTON'S NATURAL BUSINESS UNITS (CONTINUED)

In addition to the litmus test for determining NBUs that will enhance organizational agility, Booz Allen also outlines a five-step framework to incorporate NBUs into a successful overall organization design. The process begins with an analysis of who the customers are, what they need, and what they are likely to pay for. After a company has defined the appropriate businesses, it develops a structure and defines its relationship to the corporate parent and to the supporting capabilities essential to operations. Finally, the linkages must be developed that glue the company together. This five part framework is detailed in Figure 9 below:[6]

Figure 9: NBU Design Framework

Apply the NBU litmus test, outlined on the previous page, to all elements of the corporate portfolio. NBUs undertake the following activities:
- Identify/anticipate customer needs
- Develop and execute NBU strategy
- Build capabilities
- Develop talent
- Improve business performance

Once NBUs are defined, the company should create an overall structure that serves its specific business needs. The structural options outlined on **page 4** of this document will guide this process.

Design NBU Structure 2

Define the Business 1

Define Relationship with Global Core 3

Define Linkages 5

Linkages must be clearly thought out, and range from vision and values to specific management processes. Linkages also includes the systems for developing strategy, delegating authority, and managing performance.

In conjunction with developing the overall business unit structure in step two, organizations define NBU relationships with the Global Core. The five key missions of the Global core are as follows:
- **Strategic Leadership**—provide guidance for future growth
- **Identity**—formulate a shared vision, set of values, corporate identity, and coherence
- **Control**—exercise performance monitoring and coordination
- **Capital**—minimize the cost of capital and fund growth
- **Capabilities**—ensure corporate-wide access to world-class, low-cost capabilities

Define Business Services 4

In addition to a new relationship to the parent, the NBU model gives companies an opportunity to redefine corporate services, a model for delivering corporate support by combining services from headquarters and business units into a distinct, market-efficient entity, as detailed below:
- Provide cost-effective, client-driven services (e.g., transactions, expertise)
- Manage outsourcing relationships

GOOLD AND CAMPBELL'S "FIT" AND "GOOD DESIGN" TESTS

Michael Goold and Andrew Campbell suggest that organizations use two types of tests to balance the right amount of hierarchy, control, and process in organizational structure, allowing the design to work smoothly while avoiding excessive structure that could dampen initiative, flexibility, and networking. These tests are highlighted in Figure 10 below:[7]

Figure 10: Fit and Good Design Tests

"Fit" tests—provide an initial screen for design alternatives, revealing whether the structures support the company's strategy, talent pool, and characteristics.	"Good design" tests—refine a chosen design by addressing potential problem areas, including the balance between empowerment and control.

"Fit" tests column:

The Market Advantage Test—assess a design's fit with the organization's market strategy and sources of competitive advantage. The test includes the three components and guiding questions depicted below:

Component	Guiding Question
Determine whether structure fits market strategy	Does the design reflect focus on key market segments?
Determine if structure directs enough attention to each market segment	Is every segment owned by at least one business unit?
Determine if structure supports key sources of market advantage	Does design support speed to market, solutions selling, etc.?

The Parenting Advantage Test—define corporate level ("parent") activities that add value to the entire organization and should be allocated to the corporate center.

The People Test—consider key players in the organization and determine if the design provides appropriate responsibilities and reporting relationships, solidifying key stakeholders' commitment. The two main components of this test and guiding questions are highlighted below:

Component	Guiding Question
Determine whether structure defines roles and responsibilities such that employees leverage their strengths	Are there employees who will forfeit power in the new structure?
Assess staffing needs	Have pivotal positions within the new structure been appropriately identified?

The Feasibility Test—consider the context in which the organization operates. Identify barriers to success due to any of the following constraints: government regulations, interests of company stakeholders, limitations of information systems, and corporate culture.

"Good design" tests column:

The Specialist Cultures Test—control for the new design's effect on groups where performance is contingent on their ability to operate outside the prevailing corporate culture (e.g., IT, product development). The two main components of this test and guiding questions are highlighted below:

Component	Guiding Question
Identify specialist cultures	Which groups think and work in ways that are different from organizational norms to maximize performance?
Assess vulnerability	Are these groups significantly different from and therefore at risk for domination by the units to which they report?

The Difficult Links Test—identify structural deficiencies that lead to inability to achieve coordination across business units through any of these six basic links: shared knowledge, shared tangible resources, pooled negotiating power, coordinated strategies, vertical integration, and new business creation.

The Redundant Hierarchy Test—control for inefficiencies resulting from unnecessary organizational layers.

The Accountability Test—ensure that each unit, especially if decentralized, has appropriate controls over its performance and that these controls suit the unit's responsibilities, are economical to implement, and motivate managers.

The Flexibility Test—ensure that future innovations will not face undue challenges because of the new design. The two components of this test and guiding questions are as follows:

Component	Guiding Question
Determine whether design supports innovation and adaptation to changing environments	Does the design support potential new opportunities?
Identify pockets of resistance to future change	Does the design pose a risk of entrenchment even if priorities change?

APPENDIX: ADDITIONAL RESOURCES

This appendix provides additional resources and information for each framework presented in this report.

JAY GALBRAITH'S STAR MODEL

Designing Your Organization: Using the STAR Model to Solve Five Critical Design Challenges, Amy Kates and Jay Galbraith, 2007
This workbook is a hands-on guide that provides managers with a set of practical tools to use when making organization design decisions. Based on Galbraith's Star Model, the book covers the fundamentals of organization design and offers frameworks and tools to help leaders execute their strategy.

Designing the Customer-Centric Organization, Center for Effective Organizations, 2006
http://www.marshall.usc.edu/assets/005/5484.pdf
This teleconference deck, written by Galbraith, provides examples of how organizations can use the star model to pursue customer-centric and solutions-oriented strategies.

BOSTON CONSULTING GROUP'S BUILDING BLOCKS FRAMEWORK

A Survivor's Guide to Organization Redesign, Boston Consulting Group, 2003
http://www.bcg.com/impact_expertise/publications/files/Survivors_Guide_Organization_Redesign_Jan2003.pdf
This link provides access to the full-text article.

BALANCED SCORECARD

The Balanced Scorecard, Robert S. Kaplan and David P. Norton, 1996
This book provides greater detail on and further implications for business inherent to the balanced scorecard methodology.

NATURAL BUSINESS UNITS

Organizing for Agility: Creating Natural Business Units, Booz Allen Hamilton, 1999
http://www.boozallen.com/publications/article/658369
This link provides access to the full-text article.

GOOLD AND CAMPBELL'S "FIT" AND "GOOD DESIGN" TESTS

Do You Have a Well-Designed Organization?, Harvard Business Review, 2002
(Due to copyright restrictions, we cannot provide a copy of this article. This document can be obtained from Harvard Business Publishing.)
This article includes examples and details regarding how organizations can conduct each test outlined in this brief.

NOTE TO MEMBERS: This project was researched and written to fulfill the research request of several members of the Corporate Executive Board and as a result may not satisfy the information needs of all member companies. The Corporate Executive Board encourages members who have additional questions about this topic to contact their research manager for further discussion. The views expressed herein by third-party sources do not necessarily reflect the policies of the organizations they represent.

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1 Galbraith, Jay, Designing Organizations: An Executive Briefing on Strategy, Structure, and Process, San Francisco: California: Jossey-Bass Inc., 2005.
2 Barber, Felix, D; Grant Freeland; and David Brownell, "A Survivor's Guide to Organization Redesign," *The Boston Consulting Group* (2003).
(Obtained through www.bcg.com/impact_expertise/publications/files/Survivors_Guide_Organization_Redesign_Jan2003.pdf). [Accessed 1 November 2008].
3 Barber, Felix, D; Grant Freeland; and David Brownell, "A Survivor's Guide to Organization Redesign."
4 Kaplan, Robert s. and David P. Norton, *The Balanced Scorecard*, Boston, Massachusetts: Harvard Business School Press, 1996.
5 Jones, John, Shelley Keller, Gary Nielson, and Eric Spiegel, "Organizing for Agility: Creating Natural Business Units," *Booz Allen Hamilton* (1999).
(Obtained through http://www.boozallen.com/publications/article/658369). [Accessed 11 November 2008].
6 Jones, John, Shelley Keller, Gary Nielson, and Eric Spiegel, "Organizing for Agility: Creating Natural Business Units."
7 Goold, Michael and Andrew Campbell, "Do You Have a Well-Designed Organization?," *Harvard Business Review* (March 2002). (Obtained through EBSCOHost).