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Organization Design

Aligning Organizational Structure With Business Goals

Is your organization well-designed, and how do you know? What does a well-designed organization look like? How does it feel to work there? And how is it different from a poorly-designed one?

These are the types of questions you need to explore when you look at organization design.

Many people equate organization design with an organization's structure: The words "lean" and "flat" are used to describe organization design as well as it's structure. In fact, organizational design encompasses much more than simply the structure: Organization design is the process of aligning an organization's structure with its mission. This means looking at the complex relationship between tasks, workflow, responsibility and authority, and making sure these all support the objectives of the business.

Good organizational design helps communications, productivity, and innovation. It creates an environment where people can work effectively.

Many productivity and performance issues can be traced back to poor organization design. A company can have a great mission, great people, great leadership, etc. and still not perform well because of poor organizational design.

Take the example of a company whose sales department and production department both work well as separate units. Yet they need to communicate about customer needs and have not been organized to do so: Company performance suffers as a result. Then take the example of a company that wants to grow by acquiring new customers. Yet its sales team is rewarded for customer retention instead: Again, company performance is compromised as a result.

How work is done, business processes, information sharing and how people are incentivized; all of these directly affects how well the organization performs. All of these factors are facets of the organization's design and each facet is important to organization's success.

Given the importance of organizational design, why is it so often to blame for inefficiency and ineffectiveness? The reason is because organizations often evolve rather than get designed. With little or no planning and intervention, the organization design that emerges is likely to be flawed with misaligned incentives, processing gaps and barriers to good communications.

Without due planning, an organization's design often takes on a hierarchical structure. This structure is common because business executives and managers are often reluctant to relinquish control. However, such structures can lack flexibility, soak up resources and under-use key people and skills. When it comes to good organization design, it's a question of getting the right balance – getting the right controls, the right flexibility, the right incentives; and getting the most from people and other key resources.

In this article, we first look at types of organization design and their uses. We then look in more detail at the key facets of organization design and offer some tips on how to ensure your organization is aligned with your business objectives.

Types of Organization Structure

Most organizations are designed, or evolve, to have elements of both hierarchy and more flexible, organic structures within. (Organic structures are more informal, less complex and more "ad-hoc" than hierarchical structures. They rely on people within the organization using their initiative to change the way they work as circumstances change.)

Before looking at some of the common types of organization structure, its worth looking at what characterizes a hierarchical structure and how it contrasts with an organic structure. It's worth saying that one type of structure is not intrinsically better than another. Rather, it's important to make sure that the organization design is fit for organization's purpose and for the people within it. And the section on **Making Organization Design Decisions** below discusses this in more detail.

Does your organization's design actually work?
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Characteristic	Hierarchical structure	Organic structure
Complexity	High – with lots of horizontal separation into functions, departments and divisions	Usually lower – less differentiation or functional separation
Formality	High – lots of well defined lines of control and responsibility	Lower – no real hierarchy and less formal division of responsibilities
Participation	Low – employees lower down the organization have little involvement with decision making	Higher participation – lower level employees have more influence on decision makers
Communication	Downward – information starts at the top and trickles down to employees	Lateral, upward, and downward communication – information flows through the organization with fewer barriers

Functional structures and divisional structure are both examples of hierarchical organization structures.

In a **functional structure**, functions (accounting, marketing, HR etc) are quite separate; each led by a senior executive who reports to the CEO. The advantage can be efficiency and economies of scale where functional skills are paramount. The main disadvantage is that functional goals can end up overshadowing the overall goals of the organization.

In a **divisional structure**, the company is organized by office or customer location. Each division is autonomous and has a divisional manager who reports to the company CEO. Each business unit is typically structured along functional lines. The advantage here relates to local results, as each division is free to concentrate on its own performance. The disadvantage is that functions and effort may be duplicated. For example, each division may have a separate marketing function, and so risk being inefficient in its marketing efforts.

More organic structures include: simple, flat structures, matrix organizations and network structures:

Simple Structure – Often found in small businesses, the simple organization is structure is flat. It may have only two or three levels; employees tend to work as a large team with everyone reporting to one person. The advantages are efficiency and flexibility, and responsibilities are usually clear. The main disadvantage is that this structure can hold back growth when the company gets to a size where the founder or CEO cannot continue to make all the decisions.

Matrix Structure – In a matrix structure, people typically have two or more lines of report. For example, a matrix organization may combine both functional and divisional lines of responsibility. For example, in this structure, a marketing manager may report both to the functional marketing director and the country director of the division he or she works in. The advantage is that the organization focuses on divisional performance whilst also sharing functional specialist skills and resources. The (often serious) downfall is its complexity – effectively with two hierarchies, and with the added complexity of tensions between the two.

Network Structure – Often known as a lean structure, this type of organization has central, core functions that operate the strategic business. It outsources or subcontracts non-core functions which, depending on the type of business, could include manufacturing, distribution, information technology marketing and other functions. This structure is very flexible and often can adapt to the market almost immediately. The disadvantage is inevitable loss of control, dependence on third parties and the complexity of managing outsource and sub-contract suppliers.

Making Organization Design Decisions

Given the many choices of structure, how do you go about making organization design decision for your business? Different organization structures have different benefits in different situations. What matters is the overall organization design is aligned with the business strategy and the market environment in which the business operates. It must then have the right business controls, the right flexibility, the right incentives, the right people and the right resources.

Here are just some of the many things that you can consider when thinking about the structure of your organization.

Strategy – The organization design must support your strategy. If your organization intends to be innovative then a hierarchical structure will not work. If however, your strategy is based on low cost, high volume delivery then a rigid structure with tight controls may be the best design.

Size – The design must take into account the size of your organization. A small organization could be paralyzed by too much specialization. In larger organizations, on the other hand, there may be economies of scale that can be gained by maintaining functionally specialist departments and teams. A large organization has

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more complex decision making needs and some decision making responsibilities are likely to be devolved or decentralized.

Environment – If the market environment you work in (customers, suppliers, regulators, etc.) is unpredictable or volatile, then the organization needs to be flexible enough to react to this.

Controls – What level of control is right in your business? Some activities need special controls (such as patient services in hospitals, money handling in banks and maintenance in air transport) whilst others are more efficient when there is a high degree of flexibility.

Incentives – Incentives and rewards must be aligned with the business's strategy and purpose. When these are misaligned, there is a danger that units within the organization become self-serving. Using the earlier example of a company that wants to grow by acquiring new customers, the sale team is incentivized on customer retention, and therefore is self-serving rather than aligned with the business purpose.

There is much more to organization design than deciding on its structure. This list shows just some of the facets organization design that can be taken into account in thinking about this. With each stage of growth or each change, the organization design needs to be reassessed and realigned as necessary. The list can also help you identify issues that might be causing team problems or holding back you business.

To learn more about organization design, we recommend three excellent books on the subject available at Amazon.com: **Designing Dynamic Organizations**, **Designing Organizations**, and **Designing Effective Organizations**.

Further articles at Mind Tools on the subject include: **RACI** ⊕ , (focusing on responsibilities and accountabilities); and the **Greiner Curve** ⊕ (more on the stage of business growth).

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Comments (9)

dhana wrote   Over a month ago

Designing an attractive motivational strategy is the key to making of a high performance driven organization

James wrote   Over a month ago

Hi Luxi

I'm quite fond of the Richard L Daft Organization Theory and Design book - it gives a clear, well-written overview of the topic, and it's well worth a browse to answer questions like these.

A lot of the high level design structures work at multiple levels within a business. (For example, we recently had a matrix structure operating within a four-person team at Mind Tools, and, thanks to the great attitude of all

involved, it worked really well.)

luxi wrote
Over a month ago

HI all

Very interesting article and written in a way that is east to understand. I had studied all of this in a very long strategy course with the OU but really it was written in an academic way that made it so hard to understand and really wasn't at all practical!
I am also looking for something more technical though. Once we have decide how we design the structure, how do we organize each segment of that structure? are there any models on how to organize each department internally?

Midgie wrote
Over a month ago

Hi Zuni,
Wow, I can't imaging going through an organizational restructuring on a yearly basis ... that much have caused a lot of stress and strain on employees, and as you said, impacted on their engagement!

You make a critical point about having a strategic plan/vision that gives everyone a sense of knowing and a sense of solid direction. At least employees can settle down and get going with their jobs, rather than being unsettled not knowing what was coming next and where they were going!

I hope that the future with the new CEO is more stable and solid!

Midgie

Dianna wrote
Over a month ago

Good point zuni - we have an upcoming article on how to create a strategy and I couldn't agree more that you don't want to be making major shifts all the time. It's far too disruptive to productivity and communication, not to mention the cultural ramifications of not knowing what direction you are headed in for any length of time. Your structure is meant to support all the core elements of your organization and you want to be able to give people a fighting chance to sort out how their role fits into the larger picture of corporate strategy and vision.

Thanks again zuni for sharing your experiences and insights. We all gain a great deal from your ideas.

Dianna

zuni wrote
Over a month ago

How many of you have been involved in a restructure of your business? I have been through so many I have lost count! In fact, until recently, my company would restructure each year. Employees could anticipate a reorganization in the late November time frame.

The most important element of organization design is having a solid business strategy; it is the foundation of good organization design. If your strategy shifts frequently, then so does your organization structure and this causes declines in productivity, as well as decreases in employee engagement. Not a great scenario when competition increases.

Thankfully, we have a new CEO who has set a solid course for the company. The strategy has a life, i.e., the core components of the strategy remain relatively stable for three to five years, as it should.We still have flexibility, but we are no longer redesigning the organization every year.

Zuni

Dianna wrote
Over a month ago

Fantastic! It's often not a clear cut decision to make and that's why the matrix structure is quite effective. Again, it

all depends on the organization and the issues facing it.

When you understand the basic concepts it makes the process of developing a deliberate organizational structure that much smoother. And since the process may involve change, the more issues you are aware of helps you communicate your decision and actions to others involved.

Dianna

kesadee wrote   Over a month ago

Thank you James and Dianna

This is a most helpful article and give me options.This article brings more clarity to my query onthe advantages and disadvantages of a functional vs process driven organisations.

Kez

Dianna wrote   Over a month ago

Here is a succinct description of the main organizational structures and why you'd choose to one versus the other. The typical hierarchy segregated by department works fine in some cases but it's good to know there are options that might make your organization and teams communicate better and operate better.

Dianna

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