

"Sheds light on the challenges of organization design in a complex enterprise and more importantly provides an insightful and practical roadmap for business decisions."

—**Randy MacDonald**, SVP, human resources, IBM

Leading Organization Design

HOW TO MAKE ORGANIZATION DESIGN DECISIONS
TO DRIVE THE RESULTS YOU WANT

GREGORY KESLER
AMY KATES

FOREWORD BY JAY GALBRAITH

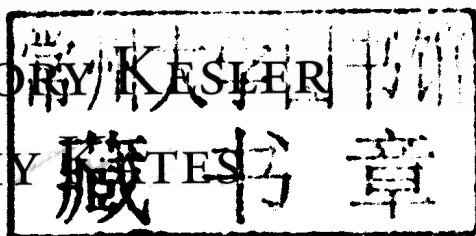
LEADING ORGANIZATION DESIGN

**How to Make Organization Design Decisions
to Drive the Results You Want**

GREGORY KESLER

AMY

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Foreword

It was not long ago when “doing what comes naturally” was sufficient for designing organizations. Leaders were advised to simply hire the best people. Everyone knew that good people could make any organization work. Whether these views were valid or not, they are not going to work today. We are now in a different era.

The overly simple views of organizing have gone away along with the mass market. That mass market was served by mass production and reached through mass media. Companies sold stand-alone products—and each one was based on its unique analogue standard. When faced with complexity, these companies divided themselves into multiple divisions, each of which was a separate profit-and-loss center. They created corporate centers that allocated investment funds to divisions based on various portfolio models. Those models further classified the profitability and growth potential of the divisions into dogs, cows, or stars. The international business climate was characterized by deregulation and privatization. The best performers under this set of rules were companies like Hewlett-Packard (H-P) and 3M. Their organization design approach was based on the biological process of cell division. That is, when a business

unit got to be too large, it was divided into two smaller divisions. And those two later became four, and so on. Each division was a fully functional and autonomous business. This model no longer works for H-P or 3M—or most other companies. H-P and 3M have gone outside for their last two CEOs as they attempt to transition to new models of organization.

This book, *Leading Organization Design* by Greg Kesler and Amy Kates, contains exactly the kind of advice that leaders need to navigate in today's business environment. Organization design requires the more thorough and more thoughtful approach that the authors demonstrate for us. Instead of serving a mass market with mass production, companies now face a fragmenting and segmented market that is served by mass customization. Instead of familiar Western markets, today's growth is in emerging markets with different cultures, active host governments, and state-owned enterprises acting as competitors, customers, and partners. Instead of stand-alone products and services, companies are being asked to integrate products, software, and services into solutions based on digital standards. Today everything can talk with everything else. Parts of companies that used to work separately now must work together.

So today leaders need to do what is required and not what comes naturally. The lessons that leaders learned—like “keep it simple” and “all you need is good people”—will not work anymore. What is required is the kind of explicit design process that Kesler and Kates present in this book. While growing up in the business, most leaders did not learn how to design and execute three- or four-dimensional matrix organizations. But by following the five-milestone process in the book, leaders can learn to design today's more complex and necessary organizations.

The book has some unique features that make it valuable. It is one of the few and certainly only recent books to take us through an explicit process to design modern organizations.

This is accomplished with the five-milestone process. The process is not a simple cookbook. Indeed, the authors have achieved a balance between process and content. They introduce the content at appropriate places in the design process. In so doing, the authors show us what to do as well as how to do it.

The other unique feature is the marriage of organization design with organizational change. Many of us believe that change begins with design. By following the Kates-Kesler process, companies can involve many key players in the design-change process. This is a good way for everyone to get his or her fingerprints on the design.

I recommend this book to all of the men and women who are charged with the stewardship of our institutions. The successful execution of leadership roles today requires an ability to design and change the organization. There is no more important and challenging task. *Leading Organization Design* should be one of the guidebooks for today's leaders.

October 2010
La Conversion, Switzerland

Jay Galbraith

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Introduction

Why Organization Design

A business leader can directly impact three levers of performance:

1. The *strategy*—where and how the firm competes, and where it chooses not to compete
2. The *talent* of the top team—the executive team that will build and direct the activities of the organization day-to-day
3. The shape of the *organization*—how power and resources are allocated to influence the decisions that are made and the work that is executed

Strategic decisions are first and fundamental. No amount of talent or organizational execution will overcome poor investment decisions. Talent and organization, however, equal strategy in importance. Strategy without a clear path to execution wastes the creative energy of the company's employees (Bossidy, Charan, and Burck, 2002).

The talent lever for strategy execution has garnered much research, writing, and attention over the past ten years. Although organization design and development have also grown as disciplines, there is often little connection made between talent and organization either in the academic or corporate arenas.

We have long believed that in order to reap the benefits of investments in talent, a company needs to create the organizational conditions in which all employees—from the front line to the CEO—can do their best work. In 2009, the Corporate Leadership Council launched a major research initiative to identify why so many leaders feel frustrated and unsuccessful despite the attention to selection and development of leadership in most companies. Its conclusion: “Leadership does not exist in isolation. Organizations must consider the organizational structure and macro and micro market situations in which leaders work. Strong leadership performance occurs when the right individuals and organization are available to address a given market situation” (2010, p. 11).

Good organization design enables effective business decisions to be made with a high degree of consistency. At the most basic level, aligned decision making (against a given strategy) is the test of an effective structure. It’s logical to believe, then, that great talent is helped or hindered by the organization in which it is asked to work. Even though people will often find a way to work around barriers, who would choose that course?

ORGANIZATION DESIGN IS A LEADERSHIP COMPETENCY

One of the most difficult challenges for new general managers who have been promoted after leading great teams in marketing, sales, or operations is to make their leadership impact scalable across an entire organization. Today’s general managers understand the importance of organizational capabilities to compete, but many are less clear about how to create them. This book is about organizational leadership—aligning the components of the organization to execute strategy and removing barriers so

that members of the organization can make the right decisions and do their best work. As strategies and organizations become more complex, it is not enough to be able to inspire individuals and lead teams. A working knowledge of organization design has become an essential personal competency for any successful leader today.

Among the many forces that increase organizational complexity are

- *Changing business models* and the need to manage a portfolio of varied business models
- *Innovation* in process as well as product
- *Global expansion* and the reality of competing with ever more sophisticated local players
- *Efficiency pressures* to increase volume, reach, and capability without adding overhead expense

Organizations will be as complex as the strategies and challenges they are designed to manage. But complexity, in itself, is not a bad thing. The ability to manage a complex organization that is capable of executing a complex strategy actually provides competitive advantage over firms whose management can only do one thing well. Today's IBM is able to keep many balls in the air at once through a complex web of structure, business process, and human relationships. It is a very difficult design to copy.

Heywood, Spungin, and Turnbull (2007) argue that it is important to differentiate complexity that is experienced by individuals inside the organization from the complexity inherent in the numbers of operating units, functions, and geographic units—the nodes in the network—that must be managed. Leaders sometimes make the mistake of trying to reduce the internal “experience of complexity” by reducing the product offering or by consolidating decision making. Although

this may make the organization easier to manage, it can destroy value. Although the leader's goal should be to avoid unnecessary complexity, he or she must also avoid overly simplistic designs that don't reflect the level of complexity in the strategy. The leader should deliberately design the integration mechanisms and build the management team's ability to collaborate where needed. In this way, the organization can have as many nodes and dimensions as needed, while minimizing the experience of complexity for employees and customers.

When the multiple lines of reporting relationships in a company (such as markets, brands, customers, and geography, to name a few examples) are not designed purposefully, are out of alignment, or set up power imbalances, then the organization does create barriers to leadership impact and effectiveness. Establishing purposeful alignment is core work for today's leaders.

WHY ANOTHER BOOK ON ORGANIZATION DESIGN?

This book is written for the business leader who wants to make better organization design decisions in order to execute complex strategies more effectively and to create the conditions for talent to succeed. It is also for human resource and organization development professionals who advise leaders on these decisions and who help guide the implementation process.

The most frequent request we get from business leaders goes something like this: "I know we need to change, and I have a fairly good idea about what I'd like to do. Give me a process that ensures I'm making the best decisions about the organization and that involves the right people. I want to be sure we're challenging ourselves to think creatively, but at the end of the

day, I want the team to come together on a change that we can support and implement.”

From internal HR and OD staff, we hear questions like this: “I’m often brought in late on decisions, or my client doesn’t believe that using a process and involving anyone beyond the current executive team are even worthwhile. How can I add value earlier in the decision-making process and give my business leaders confidence in my ability to manage this work?”

With this book, our goal has been to create a thought guide for a leader and an executive team to use when making organization design decisions. Our framework for the book is what we call the *five milestone process* of organization design.

- Chapter One highlights the components of each milestone.
- Chapters Two through Fourteen present the models, concepts, and tools that we have found most useful at each phase. The chapters are grouped by milestone and are presented in a logical flow that generally mirrors how the topics arise in the design decision process. Each is also written, however, to serve as a stand-alone reference that can be turned to as design dilemmas arise.
- Chapters Fifteen and Sixteen look at organization design through a project management lens. We share a detailed guide to roles, involvement, and planning and executing design sessions, which ensures that the right people are involved in the decision-making process and that management time and other resources are managed efficiently. Chapter Seventeen specifically addresses leaders and makes the case for organization design as an essential personal leadership competency.

With this book, we are not attempting to be comprehensive. We make the assumption that you are familiar with the foundational concepts of organization design and come with some

experience leading or working in organizations as they have gone through change. We imagine you, our reader, as a smart and successful businessperson or consultant looking for a clear and practical guide that will help you turn your accumulated experience into applied wisdom. Our intention is that this book will provide you with new thinking to add to your toolkit, as well as a coherent way to organize your existing knowledge about the field. In addition, we will share insights into how to make the organization design process straightforward and accessible so that it can become an embedded and replicable management capability.

OUR POINT OF VIEW ON ORGANIZATION DESIGN

When we approach an organization design project, our thinking is guided by a number of beliefs that speak to both the content and the process of organization design work:

1. Good design always starts with a clear picture of the problem you want to solve. Structural change is often overly relied on or is misguided because the business problem is not well defined.
2. Organization structure is a powerful but blunt instrument for change. Changes in processes, people, rewards, and measures are nearly always critical complements to realignments in structure.
3. Organization design is both an art and a science. The best designs include smart, practical judgments rooted in a business case, supported by facts, and often developed through a series of hypotheses to be tested.

4. It is impossible to change culture directly. Culture is the result of decisions made regarding structure, processes, metrics, and talent. People are, for the most part, rational. When the environment changes, they will change their behavior.
5. A primary purpose of an organization is to make decisions. Decisions are influenced by power. Understanding power dynamics and how to shape them is essential to organization design.
6. Organizations should be designed with the expectation that great leaders will run them. Talent and organization work together to make a whole. Organization design work is not complete until the new structure has been staffed with the right leaders.
7. Organization design is an opportunity to grow leaders. Usually it is best not to organize around personalities, but often it does make sense to define roles that will stretch and grow great talent.
8. Organization change, like most systemic change, has more impact when leaders engage the right cross section of players in the design and the implementation process.
9. Having said that, design is a leadership responsibility—not a consensus activity. Design decision making should not be delegated.

The book shares our combined forty years of study, work, and learning about the field. It reflects the many sources of knowledge that we have integrated into our work and, of course, the clients we have had the privilege to assist. Four of the thought leaders who have influenced us and shaped our beliefs and approach should be mentioned specifically. Jay Galbraith is one of the founders of the field of organization design. The Star Model (Galbraith, 1995) serves as the foundation of all our work.

Walt Mahler's seminal thinking on leadership development and organization design informs our approach to talent and how to design organizations to develop leaders (Mahler, 1975; Mahler and Drotter, 1986). Bob Simons's levers-of-control model has inspired our thinking on the governance of complex organizations (Simons, 1995, 2005). We thank our friend and colleague Michael Shuster for suggesting the adaptation of the Simons model for this use. Finally, Dick Axelrod has taught us how to enrich the design process with multiple perspectives by engaging whole systems and large groups (Axelrod, 2002). We humbly share in this book what we have learned as we have built on the work of our mentors.

The Five Milestones

ORGANIZATION DESIGN WORK NEEDS A ROAD MAP. Although the process is not strictly linear, we have found it useful to think about five steps that we call the *five milestone process* of organization design. Each design project will have its own unique path, with iterations and digressions from the flow that we present. There is no foolproof recipe that one can follow step-by-step to design the three-dimensional and invisible construct that is an organization. Organization design is both an art and a science.

That said, having worked across a range of industries, countries, and cultures, and for companies, government entities, and nonprofits of all sizes, we know that organizations can learn from each other and can use the same powerful frameworks to develop their own tailored solutions. We have refined a process that works in a variety of settings for units ranging from a few hundred to forty thousand employees and more. The process is quite scalable to be effective at the enterprise level or within business units and major functions.