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The Decision-Driven Organization

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The Decision-Driven Organization

Idea in Brief

Reorganizations are popular with chief executives, who believe that making big structural changes will lead to better performance. But a Bain & Company study of 57 reorganizations found that most reorgs had no effect—and some actually destroyed value.

In reality, a company's structure results in better performance only if it improves the organization's ability to make and execute key decisions better and faster than competitors. If you can sync your organization's structure with its decisions, then the structure will work better and performance will improve.

To reorganize around decisions, focus on six steps. First, be clear about which decisions are most important. Second, figure out where in the organization those decisions need to be made. Third, organize your structure around sources of value. Fourth, figure out the level of authority your decision makers need, and give it to them. Fifth, adjust other parts of your organizational system to support decision making and execution. And sixth, equip your managers to make decisions quickly and well.

Forget the org chart—the secret is to focus on decisions, not structure.

SPOTLIGHT ON STRATEGIES FOR A CHANGING WORLD

The Decision-Driven Organization

by Marcia W. Blenko, Michael C. Mankins,
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Many CEOs assume that organizational structure—the boxes and lines on a company's org chart—is a key determinant of financial performance. Like generals, they see their job as putting the right collection of troops in the right places. If the battle is about innovation, for example, then the CEO's duty is to create the best possible structure for channeling resources towards innovation.

This belief helps explain why reorganizations are so popular with chief executives. In fact, nearly half of all CEOs launch a reorg during their first two years on the job. Some preside over repeated restructurings. The immediate motives vary. Some are about cutting costs; others are about promoting growth. Some are about shaking up a culture; others are about shifting strategic focus. Whatever the specifics, though, reorgs almost always involve making major structural changes in pursuit of better performance.

Despite the fanfare that usually greets them, however, most reorganizations fall flat. A recent Bain & Company study of 57 reorgs be-

tween 2000 and 2006 found that fewer than one-third produced any meaningful improvement in performance. Most had no effect, and some actually destroyed value. Chrysler, for instance, reorganized its operations three times in the three years preceding its bankruptcy and eventual combination with Fiat. Each time, executives proclaimed that the company was on a new path to profitability. Each time, performance didn't improve.

We believe that this failure is rooted in a profound misunderstanding about the link between structure and performance. Contrary to popular belief, performance is not determined solely by the nature, scale, and disposition of resources, important though they may be. An army's success depends at least as much on the quality of the decisions its officers and soldiers make and execute on the ground as it does on actual fighting power. A corporation's structure, similarly, will produce better performance if and only if it improves the organization's ability to make and execute key decisions better and faster than competitors. It may be

that the strategic priority for your company is to become more innovative. In that case, the reorganization challenge is to structure the company so that its leaders can make decisions that produce more and better innovation over time.

For most companies, this requires a fundamental rethinking of their approach to reorganization. Instead of beginning with an analysis of strengths, weaknesses, opportunities, and threats, structural changes need to start with what we call a decision audit. The goals of the audit are to understand the set of decisions that are critical to the success of your company's strategy and to determine the organizational level at which those decisions should be made and executed to create the most value. If you can align your organization's structure with its decisions, then the structure will work better, and your company's performance will improve.

In this article we set out the basic principles for reorganizing around decisions. Let's begin by taking a closer look at the link between decisions and performance.

What Drives Your Performance?

Organizational structure is not the only determinant of performance. In some cases, it is not even particularly important. That's why changing a company's structure to meet a particular strategic goal can actually exacerbate problems rather than help solve them. For example, an organization struggling to innovate may try to gather more and more creative input—and end up getting too many people involved, thereby slowing the pace of decision making and stifling innovation.

Take the case of Yahoo. In December 2006, then-CEO Terry Semel announced a sweeping reorganization of the company, replacing Yahoo's product-aligned structure with one focused on users and advertiser customers. Seven product units were merged into a group called Audience and another seven moved into a group called Advertisers and Publishers. A unit dubbed Technology would provide infrastructure for the two new operating groups. The idea was to accelerate growth by exploiting economies of scope across Yahoo's rich collection of audience and advertiser products. Semel's team had thought they'd carefully defined roles and responsibilities under the new structure, but decision making and execution

quickly became bogged down. Audience demanded tailored solutions that Technology could not provide at a reasonable cost. Advertisers and Publishers needed its own set of unique products and so was constantly competing with Audience for scarce developer time. In response, Yahoo executives created new roles and management levels to coordinate the units. The organization ballooned to 12 layers, product development slowed as decisions stalled, and overhead costs increased.

Yahoo's experience shows how a lack of attention to the decision-making process can thwart the best-intentioned reorganization and undermine performance. Ultimately, a company's value is no more (and no less) than the sum of the decisions it makes and executes. Its assets, capabilities, and structure are useless unless executives and managers throughout the organization make the essential decisions and get those decisions right more often than not.

Our research and experience confirm the tight link between performance and decisions. In 2008, we and our colleagues at Bain & Company surveyed executives worldwide from 760 companies, most with revenues exceeding \$1 billion, to understand how effective those companies were at making and executing their critical decisions. We used the responses to assess decision quality (whether decisions proved to be right more often than not), speed (whether decisions were made faster or slower than competitors), yield (how well decisions were translated into action), and effort (the time, trouble, and expense required for each key decision). Then we calculated a composite score for each company and compared that score with each firm's financial performance. (See the exhibit "Rate Your Decision Effectiveness" to learn how your company compares with our sample.)

We found that decision effectiveness and financial results correlated at a 95% confidence level or higher for every country, industry, and company size in our sample. Indeed, the companies in our sample that were most effective at decision making and execution generated average total shareholder returns nearly six percentage points higher than those of other firms. We also found that many companies have enormous scope to improve their performance. Top-quintile companies score an average of 71 out of 100 in decision effectiveness,

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while companies in the other four quintiles score, on average, 30 and below. This means that the typical organization has the potential to more than double its decision effectiveness.

What's more, the research revealed no strong statistical relationship between structure and performance. Survey respondents' views about the structure of their company

were not an accurate predictor of either decision effectiveness or financial results.

The conclusion we draw is simple: In a reorganization, decisions rather than structure should be the primary focus. Let's see what that involves.

Conducting a Decision Audit

Many reorganizations begin with a SWOT analysis: What are our organization's strengths, weaknesses, opportunities, and threats? What are our resources and capabilities? What risks do we face? The idea is to determine if the company has everything it needs to support its strategy. All this sounds sensible, and in many ways it is. But the risk is that you'll end up with an organization that's misaligned with your strategy, all because you have ignored decisions. The proper place for this type of SWOT analysis is not, in fact, as a prelude to organizational change but earlier, when you are determining your company's strategy.

A better way to begin a reorganization is with a decision audit. The first step in conducting one is to identify the key decisions you need to make and execute, given your strategy to create maximum value for your shareholders. The set of key decisions for a growth strategy, for instance, will be different from the set for a return-focused strategy. Of course, this exercise does not presuppose a change in strategy. It may be that the reorganization is an attempt to improve an existing strategy, in which case you'll end up with a comparison between the decisions you ought to be concentrating on and the ones you are actually making. The bigger the difference—and the greater the obstacle presented by your organizational structure—the more aggressive your reorg will need to be.

The ongoing turnaround at Ford illustrates the power of explicitly delineating a company's critical decisions. When Alan Mulally became CEO at the automaker in 2006, the company was in dire need of change. Ford had been losing a point or more of market share every year since 2000 and was on the verge of collapse. But rather than change the company's structure first and then worry about decisions, Mulally took the opposite approach. He and his team outlined the decisions that were critical to a turnaround. Only then did they begin to build the new organization around those decisions.

Quick Test: Rate Your Decision Effectiveness

How do your organization's decision abilities stack up against the competition? While hardly a full-scale survey, this short test can give you a quick-and-dirty assessment of decision strengths and weaknesses.

Quality

When looking back on critical decisions, we find that we chose the right course of action

- 4 Most of the time
- 3 Some of the time
- 2 Infrequently
- 1 Never

Q Score ____

Speed

We make critical decisions

- 4 Much faster than competitors
- 3 Somewhat faster than competitors
- 2 Somewhat slower than competitors
- 1 Much slower than competitors

S Score ____

Yield

We execute critical decisions as intended

- 4 Most of the time
- 3 Some of the time
- 2 Infrequently
- 1 Never

Y Score ____

Effort

In making and executing critical decisions

- 4 We put in exactly the right amount of effort
- 3 We put in somewhat too much/too little effort
- 2 We put in way too much/nowhere near enough effort
- 1 We're off the charts

E Score ____

To tally your overall score, multiply your scores for quality (Q), speed (S), and yield (Y) to get your QSY. Next, divide your effort (E) score by 4, and multiply the result by the QSY. If you're putting in exactly the right amount of effort, your QSY wouldn't change. But if you scored effort as a 3, then your score would be 3/4, or 75%, of the QSY.

Using our database, you can compare your decision score with the performance ranges for each benchmark quartile. If you score over 25, for example, you are performing at the level of the top-quartile companies in our survey. Relative to our sample, your organization would appear to decide and deliver.

Total Score [Q x S x Y x (E/4)] ____

More than 25 = You're doing great; keep it up.

21–25 = Pretty good, but could be great.

16–20 = Worse than 50% of companies. Time to act.

15 or less = Major decision reboot required.

Ultimately, a company's value is just the sum of the decisions it makes and executes.

Fixing the company's operations and restoring profitability centered on a schematic depicting Ford's critical decisions. It spelled out the key decisions that needed to be made at each stage in Ford's value chain, along with the infrastructure required to execute them effectively. Every week, Mulally and his team tracked their progress in making and executing these decisions. They divested noncore brands such as Aston Martin, Jaguar, Land Rover, and Volvo; reduced the number of production platforms; began consolidating both suppliers and dealers; and so on. They also reorganized the company, moving from a structure based on regional business units to a global matrix of functions and geographies. This new structure enabled Mulally's team to make its most important decisions better and faster—creating global car platforms, for instance, which had been painfully difficult under the old structure. Set in this context, the reorg made perfect sense and helped restore the company to profitability in early 2010.

As you conduct your own decision audit, you need to consider two types of critical decisions:

- Big, one-off decisions that individually have a significant impact. Petrochemical companies, for example, must make periodic multi-billion-dollar investment decisions, such as if, when, or where to build a new ethylene cracker, which is critical to production. If a company builds at the wrong time, in the wrong place, or with the wrong technology, it will have to live with the consequences for many decades.
- Small, routine decisions that cumulatively have a significant impact. Amazon's continuing success can be attributed partly to a host of savvy merchandising decisions, including those related to special prices and shipping discounts, suggestions for complementary purchases, and targeted e-mail notices about new offerings. None of these decisions carries much value in any one instance. Cumulatively, however, they can mean the difference between success and failure.

Once you have identified which decisions are critical and categorized them, you can figure out where in the organization those decisions should be made. This requires an unbiased assessment of the benefits of scale and coordination versus the benefits of tailoring to local needs and staying close to the customer. In which decisions is scale a critical factor?

Which decisions are better made by business units or functions? Which need coordination across many businesses?

Some decisions are fairly easy to place. Big capital-allocation decisions, for instance, are typically best made by the corporate center so that senior leaders can design and execute a coordinated portfolio strategy across the company. IT investments can usually be left to functions or business units. Decision placement is more of a challenge for product, customer, and channel decisions, which typically involve complex trade-offs. Pricing decisions, for example, need to be coordinated across customer segments and channels. Product decisions must be considered from both an internal and an external perspective. In companies with many different products or services, both the critical decisions themselves and where they should be made may vary widely across the organization.

The Xerox turnaround launched in 2001 under Anne Mulcahy offers a powerful contrast to the Yahoo story. Unlike Semel at Yahoo, Mulcahy's leadership team took a decision-driven approach to the company's reorganization. Team members went through every set of critical decisions Xerox needed to make and execute to fend off bankruptcy, and they made explicit choices about where to locate those decisions. Clarity and simplicity were the guiding principles. In the sales organization, for example, Xerox moved from a global customer structure, in which sales and pricing decisions were made by global teams organized around industry verticals, to a simpler country structure, where those decisions rested with local sales teams. The new structure enabled Xerox to eliminate several layers of middle management, increase local accountability, and take nearly \$1 billion out of the company's cost structure in just two years. The simpler structure also concentrated decisions related to the shift from analog to digital technology—critical to Xerox's success in office products at the time—within the senior leadership of the Product organization, which helped accelerate the pace of new-product introductions in this vital segment. The explicit focus on where decisions should be made was critical to the successful turnaround at Xerox.

At the end of your audit, you may find that making and executing decisions better and faster than competitors doesn't require reorga-

nization and that you can avoid the costly business of structural change altogether. If you find that you are already focused on the right set of critical decisions and you find that they are placed where they should be within the organization, then the source of performance prob-

lems is unlikely to be structural. Problems may stem instead from other organizational issues. Perhaps there is an incentive problem with the sales force. Maybe leaders place too much value on building consensus, at the expense of decisive action. Whatever the issues, they can probably be fixed without a wholesale structural redesign, which will take people's minds off the competition and may actually add to your problems. (See the exhibit "Do You Really Need to Reorganize?")

But for now, we'll assume that your audit does reveal that your structure needs to change. Let's look at how to go about doing that.

Building the Decision-Driven Structure

All complex organizations must be broken down into manageable pieces to ensure that roles and responsibilities for making and executing critical decisions are clear. A good way to determine what the important decisions are in your company is to look at the sources of value in your business and then organize the macrostructure around them.

Take the case of British Gas, a division of the multinational energy and utility company Centrica. In 2006, faced with a serious performance crisis, the company's new leadership team started looking at the sources of value in its business. Managers began by examining differences in profitability by service, by geographic area, and by customer segment. They discovered that profitability and growth varied much more by customer segment than by any other variable.

One segment used large amounts of gas or electricity and paid regularly through guaranteed direct debits. Decisions that helped the company retain these customers, such as how to handle home moves and how best to offer additional services, were most important for this segment. A second customer segment used less energy and paid regularly through a system of prepayment cards. Here the key decisions related to controlling costs, particularly those associated with processing additional payments and with meter reading. A third segment wasn't as consistent in keeping up payments. For that group, the critical decisions related to managing receivables.

Recognizing those different sources of value, managing director Phil Bentley decided that

Quick Test: Do You Really Need to Reorganize?

A comprehensive survey of your organization can help you understand what's undermining or supporting effective decisions—and whether structure or something else is likely to be the most important issue. But this quick test can serve as an early warning device.

Structure

Our structure helps—rather than hinders—the decisions most critical to our success.

- 1 Strongly disagree
- 2 Disagree more than agree
- 3 Agree more than disagree
- 4 Strongly agree

Roles

Individuals understand their roles and accountability in our most critical decisions.

- 1
- 2
- 3
- 4

Processes

Our processes are designed to produce effective, timely decisions and action.

- 1
- 2
- 3
- 4

Information

The people in critical decision roles have the information they need when and how they need it. 1 2 3 4

Measures & Incentives

Our measures and incentives focus people on making and executing effective decisions. 1 2 3 4

Priorities

People understand their priorities clearly enough to be able to make and execute the decisions they face. 1 2 3 4

Decision Style

We make decisions in a style that is effective (for example, that appropriately balances inclusiveness with momentum).

- 1
- 2
- 3
- 4

People

We put our best people in the jobs where they can have the biggest decision impact.

- 1
- 2
- 3
- 4

Behaviors

Our leaders at all levels consistently demonstrate effective decision behaviors.

- 1
- 2
- 3
- 4

Culture

Our culture reinforces prompt, effective decisions and action throughout the organization. 1 2 3 4

To get your total score, add up your individual scores.

More than 35 = You're doing great; keep it up.

31–35 = Good, but room for improvement.

26–30 = Org is serious barrier to decisions.

10–25 = Major org transformation required.

Compared with companies in our database, a score above 35 puts you in the top quartile—meaning that your organization is pretty healthy. A score of 31 to 35 indicates room for improvement, but no immediate signs of organizational breakdown. A score of 30 or below indicates that you definitely have some organizational challenges to address. If you perform at 2 or less on any one issue, that particular ailment likely needs attention.

the best way to structure the company was by customer segment. He established three separate businesses: Premier Energy, Energy First, and Pay-As-You-Go Energy. This new structure allowed him to place accountability for decisions that directly affected customers, such as service levels, positioning, and product bundling, in the business units. Corporate headquarters could focus on noncustomer-facing matters such as IT and finance. The alignment of structure and decisions helped British Gas improve its performance significantly. It reduced customer attrition from about 20% to less than 10%. Its bad debt fell, and the business began growing for the first time in years.

If decision-driven reorganization were just about an audit and, if necessary, aligning the macrostructure with the sources of value, it would be relatively easy to get your next reorg right. But the messy reality of business is that big changes need to be followed up with a whole host of smaller changes.

In most reorgs, this stage of the process usually concentrates on assigning turf and setting out a hierarchy with defined reporting lines. Once again, this approach is misguided, because it does not use decisions as the unit of analysis. Indeed, a focus on turf often devolves into horse trading: Powerful managers grab decision rights they shouldn't really own while weak ones surrender rights they really should own. People end up with responsibilities that are defined either too broadly or too narrowly, given the decisions they need to make. Responsibilities that are too broad result in insufficient supervision and limited accountability. Those that are too narrow can create needless hierarchy—too many watchers and too few doers—and can encourage micromanagement. Without a focus on decisions, these power struggles too often lead to creeping complexity in an organization's infrastructure.

The energy giant BP provides an excellent example of the consequences of an overly complex microstructure. Back in 1994, BP had just a handful of geographic and customer units, which were supported by a few central functions. After a period of significant merger and acquisition activity, however, the company added new geographic areas and created new functions. Spans of control narrowed, and the number of management layers increased. All of these changes increased the number of "decision nodes"—the interfaces between regions,

functions, and layers required to make and execute important decisions—from about 500 in 1994 to roughly 10,000 in 2007.

Each decision node at the company introduced a different set of hurdles for new products, business development deals, and even options for reducing costs. The effects were predictable: Decision making and execution slowed, and costs mounted.

In decision-driven reorganization, the challenge is to determine exactly what authority decision makers need, regardless of their organizational status, if they are to make good decisions and execute them effectively. BP saw that the people who were best equipped to make decisions had to get too many approvals from higher-ups or from regional heads, which delayed execution. So its new chief executive, Tony Hayward, launched a comprehensive simplification program designed to return decision rights to the appropriate people. The initiative eliminated layers of middle management, centralized some operations, and reduced overhead expenses by one-third. It moved the number of decision nodes back toward a target of 5,000. Both the company's decision effectiveness and its performance improved. By late 2009, BP had eliminated \$3 billion in costs and was turning in a profit that beat analysts' expectations by 50%.

Any change in structure may necessitate changes in decision roles, incentives, information flow, performance metrics, and processes. At UD Trucks—formerly Nissan Diesel—a new strategy designed to expand UD's penetration of national accounts required a reorganization of the company. Local branch offices were combined into regions, and national account teams were established. To get the most out of the new structure, the team at UD Trucks clarified decision roles between the national account teams and the company's Truck and Service units. Measures and incentives were reset to encourage collaboration across units and focus the sales force on key accounts. The reorganization at UD Trucks was critical, of course—the new strategy could not have been implemented without it. But goals, processes, information, measures, and incentives also needed to be aligned to make the new structure work.

Finally, you need to help managers develop the skills they need to make decisions quickly and translate them into action consistently.

The Six Steps to Decision-Driven Reorganization

1. Identify your organization's key decisions.
2. Determine where in the organization those decisions should happen.
3. Organize the macrostructure around sources of value.
4. Figure out what level of authority decision makers need.
5. Align other elements of the organizational system, such as incentives, information flow, and processes, with those related to decision making.
6. Help managers develop the skills and behaviors necessary to make and execute decisions quickly and well.

When reorganizing a company, decisions rather than structure should be the focus.

Smart companies mesh individuals' capabilities with the organization's decision-making demands. They invest as needed to ensure that people have the skills required to be better decision makers over time.

A good example of this took place at Hospira, the \$3.9 billion pharmaceutical company spun out from Abbott Laboratories in 2004.

In 2008, Hospira embarked on a major change program. The program included an effort to build new decision capabilities across the company. The top 80 executives attended innovative training workshops that showed them how to identify an organization's critical decisions and outlined Hospira's new approach to effective, efficient decision making and execution. Executives learned to use tools that would help them get the who, what, when, where, and how of each decision right. The workshops also helped leaders learn and adopt the specific behaviors that would be required to make the changes stick.

Hospira's senior leaders began to track the company's changes in decision effectiveness at their bimonthly team meetings. They also began to gather survey data that could help them assess progress in building and sustaining decision capabilities. Since 2008, CEO Chris Begley and his team have seen significant improvements in Hospira's financial and stock price performance, which they attribute largely to improved decision making.

Adjusting to New Structures

A new strategy—or new execution of an existing strategy—can require both macrochanges and microchanges to a company's structure. But any new structure will create new boundaries that people may find hard to cope with and that may make effective decision making more difficult. To get around this problem, it may be necessary to overlay your new structure with some connections that help people reach beyond those boundaries.

In 2001, faced with the bursting of the dot-com bubble, Cisco reorganized. It moved away from the structure that had been in place for much of the company's rise to prominence—a line-of-business structure based on customer segments—and put in place a global functional organization. The logic was simple: Reorganizing around central functions would dramatically reduce the company's costs. While the pros of this move outweighed the cons, the

company's leaders acknowledged that organizing around centralized functions could cause Cisco to lose customer focus and intimacy.

To prevent that, the leadership team has created over the past several years a series of corporate councils and boards directly under the company's operating committee, Cisco's most senior decision-making body. These cross-functional groups formulate and evaluate alternatives for each of the company's major strategic initiatives and then make recommendations to senior management. We find that the process accelerates decision making without sacrificing decision quality. The structural overlay of councils and boards also seems to help functional leaders collaborate and make effective decisions about budgets and resources.

Today, those teams are operating at full steam. Five "segment councils," for instance, support decision making and execution for the company's enterprise, commercial, service provider, small business, and consumer segments. Boards organized around specific market opportunities, such as collaboration and virtualization within the enterprise segment, develop tailored strategies and oversee execution. Finally, four cross-segment councils focus on the arcane but critical topics of emerging solutions, connected architecture, emerging countries, and connected business operations. These interlocking councils and boards have enabled Cisco to maintain its leadership position in the complex, fast-moving telecommunications space and build on the strength of its global functional structure.

Creating parallel decision-making authorities may appear to be in conflict with our general principles of simplicity and clear accountability, but we believe this approach leads to a more streamlined process. Organization overlays such as Cisco's councils and boards introduce valuable expertise that formal structures cannot easily accommodate. They allow fewer people to be involved in making and executing critical decisions—in effect, reducing the number of decision nodes.

It's easy to see why so many CEOs are enticed by the temptation of reorganization. Today's corporate structures can be inordinately complex. Some date from a day when the demands of the business world were quite different than they are today. Simplification, alignment, modernization, a new vision of what the orga-

nization should look like—and all of it accomplished with the stroke of a pen. But to focus exclusively on structure is to confuse means with ends and to assume a connection that may not exist. The reorgs that work best, such as those at Ford, Xerox, and Cisco, focus first on the organization's critical decisions. Then they build an organization that can make and

execute those decisions better and faster than the competition. The result is what executives always seek from reorgs yet so seldom accomplish: improved performance.

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