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Hierarchies for Flow and Profit

by Brian Dive

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formance, vehicle design, and price. With this data, auto companies could then deduce whether various consumer segments really want an environmentally responsible car, what features they are looking for, and, most important, how much they would be willing to pay. The efficacy of consumer choice modeling is that it allows manufacturers to isolate and identify customer preferences among an array of realistic product offerings without having to ask the open-ended question, "What do you want?"

We believe that consumer choice modeling is ideally suited for analysis of the most complex consumer decision processes and that it yields valuable insights for demand-driven strategy development by providing customer value segmentation maps, measuring market share impact of new product–service combinations, and assessing overall brand equity. Perhaps most important, choice modeling can reveal salient differences between managers' beliefs about customers' needs and preferences and customers' actual needs and preferences. For managers seeking reliable feedback on how customers view their products and services, consumer choice modeling provides a rigorous way to turn customer-driven feedback into profitable and sustainable tactics for retaining or capturing market share.

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Hierarchies for Flow and Profit

by Brian Dive

In mid-2007 I ran a Webcast for the management research organization The Conference Board on the subject of organizational design and leadership. We polled the executives of about 40 companies, asking about their layers of management. Upward of 72 percent said they felt the business had too many layers. Worse yet, they did not know what the right number should be.

This is typical, in my experience, of businesspeople. They are mostly in the dark about how their organizational design — the "lines and boxes" signifying reporting relationships in a hierarchy — should be arranged. But most businesspeople can tell when it's working and when it's not, because they know when they're in the "flow zone." A number of researchers, most prominently the psychologist Mihaly Csikszentmihalyi, have identified the value of flow, the state in which people feel happy and fulfilled because they are completely absorbed, caught up in the activity at hand. In organizations, flow typically takes place when the challenges of a job fit naturally with the capabilities that people bring to it.

Organizations, like individuals, need to be in flow to operate smoothly. An organization achieves this state of equilibrium through its management layers. In other words, an organization can approach the flow zone when the positions in its hierarchy have clear, accountable tasks that are aligned to its mission and that match the skills and reach of the people at each level. Or as University of Auckland Business School lecturer Judith McMorland puts it, the key diagnostic can be summed up in two simple questions: "Are you big enough for your job?" and "Is your job big enough for you?" If the answer to both is "yes" throughout the organization, then it is in flow.

A critical component of achieving flow is accountability. If a job has its own discrete decision-making responsibilities, different from those in positions above and below, then the individual in that job feels accountable. He or she has a clear understanding of who the boss is, what the boss expects, why the boss needs particular results, when those deliverables are needed, how those deliverables fit with the organization's goals, and how to accomplish them. The individual is then free to "own" the job, to organize it accordingly, to deploy the resources at hand, and to enter the flow zone.

Most of us intuitively understand this, and we gravitate toward positions in which we feel that our accountability is clear and the job fits our talents. But very few organizations consciously seek to organize their hierarchy with this kind of balance in mind. Many organizations base their hierarchies on quotas for job grades and people's salaries at different levels. As a result, to fit these artificial and often capricious categories, organizations frequently end up with too many layers of management, including some hollow (and expensive) positions near the top of the company and overlapping assignments in the middle. Employees in such a situation do not have a clear sense of who is responsible for which tasks; accountability suffers, and the organization loses its groove.

What, then, is the optimal number of layers for accountability and flow? It depends on the size and scope of the organization, and the complexity of its tasks. For example, my colleague Adam Pearce and I undertook a review of a public utility in New York in 2007. It had more layers of management than it needed. The deputy chief executive officer had 13 direct reports, whereas a middle management field role in the same chain of command had only two. A conventional cost-based analysis had concluded that the company should eliminate the role with the smaller number of direct reports because, according to the criteria used by the analysts, it was operating less efficiently. But a closer look at the span of accountability revealed the field manager was adding value (albeit in a poorly designed structure), whereas the deputy CEO position was a non-job with no distinct accountability of its own. This was the role that most needed to be purged.

Indeed, the secret to determining the appropriate number of layers is to plot accountabilities from the front line — in most cases, the customer — back into the organization, to figure out which jobs are essential to providing customers with the best service and the products that they prefer. Unfortunately, most companies are instead organized from the top down. The hierarchy is designed to reduce complexity for the top layers rather than to add value to the work of those in the other layers or to the consumer.

In an accountable organization, a leader makes only those decisions that cannot be made by his or her direct reports — because they do not have the knowledge, skill, or experience to do so. Each layer includes only those who have the extra capability needed to deal with decisions of greater complexity than those at the level below can master. I have learned, over 40 years of organizational fieldwork in about 70 countries across 20 different industries, including the public sector, that each step change in complexity above the front line needs only one layer of hierarchy. And step changes in complexity are relatively few in number; I have yet to find an organization that justifies more than seven layers of management above the front lines. This observation is borne out by the work of many others in the field, including the fundamental research of management theorist Elliott Jaques. (See "Elliott Jaques Levels with You," by Art Kleiner, *s+b,* First Quarter 2001.)

Designing for flow and accountability is counterintuitive for many companies, and it takes a bit of practice to get used to it. The first level of accountability often requires a role of supervisor to support the immediate line leader, the manager in level two. A third-level leader could be a business unit leader, a plant manager, or a regional manager. In most organizations, about 98 percent of employees reside in one of these first three levels, and an individual at any one of the first three levels should be able to effectively manage up to 1,000 employees.

There is a widespread tendency to build unnecessary tiers of supervisors in level one. This is usually due to faulty assumptions about how many people can be managed by one person, further complicated by poorly designed roles in which distinctions between supervisory and management accountabilities are confused. For example, one company that I observed had a hierarchy in its customer call center designed on the premise that any one individual could effectively supervise 10 people at most. This assumption stemmed from a recently introduced appraisal system adapted from the system used for top management, but far too complicated to be appropriate for the front line. The result was a bureaucracy of

"Are you big enough for your job and is it big enough for you?" If the answer is yes, the organization may be in flow.

busy people, snowed under with paperwork, driven by an appraisal system in which supervisors spent hours each month checking with colleagues about whether their frontline staff "lived the corporate values" and a customer complaints process far too cumbersome to influence the company's products or services.

There is no one-size-fits-all solution to organizational design for flow. But rules of thumb are emerging. For example, most organizations should not build operational units such as hypermarkets, factories, or call centers with more than 1,200 employees; these are apt to be unmanageable. On the other hand, a call center or factory with fewer than 200 employees is probably too small; it hardly justifies the layers of management needed to oversee it. Like the physical architecture of buildings, the architecture of organizations has a "golden mean." We may not always find it easy to achieve, but we know it when we feel it. We can recognize it in the sense of fulfillment, collegiality, and harmony that naturally arises from proper flow and accountability when an organization's hierarchy is in balance. +

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