Beyond Command-and-Control: Managing the Diverse Corporation in Today’s Turbulent Times
Executive Summary

In today’s business environment, the traditional command-and-control model of senior management can take a toll on corporate competitiveness. For most organizations this structure is no longer in step with the market dynamics of today’s global economy.

At a minimum, we see four major changes that are causing a fundamental rethinking of how corporations are managed. First, the world of the CEO is becoming exponentially more complex: larger, faster-paced and higher in risk. It is no longer possible for a CEO to provide direct personal control over his or her expansive domain. Second, we have entered an era where intellectual capital, rather than physical capital, dominates value creation. Third, the revolution around complexity theory has demonstrated that large complex organizations can be run without central control, and that these are more robust than ones based on central control. Finally, the source of growth in shareholder value has shifted from cost reduction to top-line growth—which cannot be dictated from the top. It requires the active cooperation of suppliers, customers and at least the unwilling acquiescence of competitors.

What corporations need today are organizations that act like living organisms, able to rapidly adapt to the changing environment and quickly identify opportunities that can be capitalized upon, yet sufficiently aligned to ensure the cohesion of the entity.

Migrating to an empowered business model where people work as teams, networked by the latest information technology, is not new. Leading management thinkers have been promoting these concepts for many years. So why do most companies still have a business structure modeled by Fredrick Winslow Taylor over 100 years ago? We believe that much of it has to do with CEOs recognizing the sizeable change in behavior, processes and information required by the transformation; not seeing a clear path to achieve the transition; and thus fearing failure. Unfortunately, this has lead to underperformance in the near to intermediate term.

In this Viewpoint we provide a roadmap for making the transition from the command-and-control management model to one that provides more opportunity for the business unit to respond to its markets without increasing risk to the corporation.
Over the past 100 years modern corporations have achieved unprecedented productivity gains that have catalyzed the wealth creation of the twentieth century. Much of these gains can be attributed to management scientists such as Fredrick Winslow Taylor whose ideas encouraged us to organize in a hierarchical fashion where workers were not paid to think, but act out orders of their superiors regardless of whether they were right or wrong.

But the effectiveness of this model is being challenged—and rightfully so. The business world that allowed/engendered this type of thinking no longer exists. At a minimum, we see four major changes in the business environment, which are causing a fundamental rethinking of how corporations are managed.
First, the world of the CEO is becoming exponentially more complex: larger, faster-paced and higher in risk. Examples of the immensity of these factors include:

- The median *Fortune* 500 firm is almost three times larger in real revenues than it was in 1980;
- The average time to develop a new car model has fallen from 60 months to 19 months;
- The size of the M&A market in the U.S. alone has grown from $44 billion in 1980 to $1,425 billion in 1999.

It is simply less possible for an industrial titan, no matter how talented, to provide direct personal control over such an expansive domain.

Second, we have entered the era where intellectual capital, rather than physical capital, dominates value creation. Physical capital (a factory) lends itself to corporate ownership and central control. You don’t want each member of an assembly line to autonomously decide the hours of each shift. And someone needs to safeguard expensive investments in brick and mortar. On the other hand, intellectual capital lends itself to networks and distributed control since the capital is generated—and typically owned—at an individual level, not collective level (though in the best companies it may be captured collectively and shared).

Third, the revolution around complexity theory has demonstrated that large complex organizations can be run without central control, and that under the right culture and support systems, adaptive self-organizing systems will emerge and that these are faster and more robust than ones based on central control. The Internet has provided the technical foundations for this revolution in management.

Fourth, the source of growth in shareholder value has shifted from cost reduction to top-line growth, at least in the U.S. and many places in Europe. This has major implications for the role of top management in creating shareholder value. An agenda focused on cost reduction (typical in the U.S. from 1985 to 1995) lends itself to command-and-control management: if you want someone to cut costs, you can command them to do it—just take away the budgets or shut down the factory. However, value creation going forward is all about top-line growth and this can’t be commanded since it is not just internally driven. It requires the active cooperation of suppliers and customers, and at least the unwilling acquiescence of competitors. It is beyond the “control” of management.

Today corporations need organizations that act like living organisms, able to rapidly adapt to the changing environment and quickly identify opportunities that can be capitalized upon, yet sufficiently aligned to ensure the cohesion of the entity.

Yet, despite the massive changes in the world swirling around them, the management model in many companies remains largely unchanged, rooted in its historical legacy. The command-and-control model, with its underlying assumption that just a few highly skilled and intelligent people can add enormous value, is alive (albeit not necessarily thriving) in most industries. That model may have made sense in an era of smaller corporations facing less marketplace fluidity—but not in today’s world. More and more, we see skirmishes breaking out. Divisional presidents are clamoring for more leash to run their unit as they believe best responds to the market forces around them. They’re trying to
ensure they have the flexibility to be adaptable to changing market environments. However, CEOs, and especially CFOs, hesitate, concerned that with more autonomy comes more risk—risk that corporate alignment will be sacrificed and that the company won’t meet investor expectations.

The purpose of this Viewpoint is to provide a roadmap for making the transition from the command-and-control management model to one that provides more opportunity for the business unit to respond to its markets without increasing risk to the corporation.

### Management Models

In our experience there are four basic models through which most corporations are managed (see Exhibit 1). These range from the financial holding company (Model 1) to the operationally involved company (Model 4); the latter is usually referred to as “command-and-control.” These four models derive their name from the nature of the linkage between the Corporate Core (head office) and the operating units (i.e., operationally involved means that the Core gets involved in the operating decisions of its companies).

This difference reflects fundamentally different philosophies on how and where value is created. Interestingly, the two most extreme models are most dependent on the great person theory—the ability of a very limited number of people to create huge amounts of value through their own contributions. The middle two models reflect leaders who create value by leading rather than doing.

It is useful to deliberately start describing these models at the far end of the spectrum away from the command-and-control model to highlight the starkness of some of the differences.

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### Exhibit 1. Alternative Management Models

<table>
<thead>
<tr>
<th><strong>MODEL 1: FINANCIAL HOLDING COMPANY</strong></th>
<th><strong>MODEL 2: STRATEGY &amp; OVERSIGHT</strong></th>
<th><strong>MODEL 3: ACTIVE CORE STAFF INVOLVEMENT</strong></th>
<th><strong>MODEL 4: OPERATIONALLY INVOLVED (Command-and-Control)</strong></th>
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<tbody>
<tr>
<td>PHILOSOPHY</td>
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<td>PHILOSOPHY</td>
<td>PHILOSOPHY</td>
</tr>
<tr>
<td>• Source of Value</td>
<td>• Value is created by identifying undervalued opportunities OR • By SBUs closest to customer</td>
<td>• Value is created by SBUs using corporate expertise to make key decisions</td>
<td>• Value is created by corporate expertise and control</td>
</tr>
<tr>
<td>• Role of the Core</td>
<td>• Create/enforce disciplined management model • Identify acquisition candidates</td>
<td>• Add value in the linkages between SBUs and drive the strategic agenda</td>
<td>• Collectively make key decisions for SBUs</td>
</tr>
<tr>
<td>WHO WE ARE (Corporate Core)</td>
<td>WHO WE ARE (Corporate Core)</td>
<td>WHO WE ARE (Corporate Core)</td>
<td>WHO WE ARE (Corporate Core)</td>
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<tr>
<td>• We’re an investment company</td>
<td>• We’re the strategic leadership of a collection of management entities</td>
<td>• We’re both consultants to and the strategic leadership of a collection of management entities</td>
<td>• We are the key managers of all SBUs</td>
</tr>
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Source: Booz-Allen & Hamilton
Model 1, the Financial Holding Company, is used by firms such as Hanson Trust and by most private equity investment firms. These firms believe that value is created by picking the right companies to invest in, then putting the right people into key management roles and creating and enforcing a rigorous, disciplined accountability model. These firms, resultanty, have very few people in the Corporate Core (.05 - .07% of total employees). They don’t need central HR or most other head office resources because their companies operate almost totally independently of each other. There is no such thing as a management committee consisting of the key operating company heads—they might not even know each other. Rather, Model 1 companies depend on their involvement in operating company boards to pass on key ideas. They see little need to get involved with how those ideas are implemented—the one and only test is whether the financial results are there. This model is not particularly attractive to most corporations, understandably so, for it implies little value to an operating company in being part of a holding company for a sustained period of time.

Model 2, Strategy & Oversight, is used by companies like GE. Their philosophy is that value is created in two places: by the operating companies closest to the customers and by the corporation in the linkages between the operating companies. The Corporate Core is involved only in setting the corporation’s strategy, setting policy, identifying ways to create value above and beyond the operating companies (e.g., sharing best practices, creating new businesses, etc.) and in creating and enforcing a disciplined accountability system. As a result, it too has a very small, highly focused head office (.15 - .20% of total employees). In this model, however, coordination between businesses becomes more important—it’s the value created in the linkages between them that pays for the corporate expenses (and if no value is being created, then why would the head office, the corporation, exist). This model is found in companies that have a lot of diversity—with businesses that are substantially different.

Model 3, Active Core Staff Involvement, is used by companies like NationsBank. In this model, you begin to see a fundamental shift in philosophy of where and how value is added. In these companies, there is a strong belief that the participation by head office staff in the strategic business unit (SBU) decision-making processes will lead to improved performance by the SBUs. Thus, accountability for results begins to be shared between the head office and the SBUs. Because more expertise is required, the Corporate Core in these companies begins to expand (.25 - .30% of total employees) and the delegations of line managers are smaller. In effect, the Core acts as consultant to or overseer of the SBUs. This model is found more frequently in companies where individual risks are large or where the lines between individual businesses become blurred.

Model 4, Operationally Involved (Command-and-Control), is used by companies like Emerson Electric Company. They have a philosophy that the head office contributes significant value by being actively and heavily involved in the decision-making at the operational level. This model is frequently found in simple, single line businesses or ones that have been under regulatory control. The substantive involvement in the activities of the businesses results in a rather large head office (.35 - .40% of total employees) and substantially less autonomy resting with the managers running the SBUs.
Picking the Right Model

So how does an organization pick the model that will best support it? Booz-Allen believes that five different dimensions must be considered (see Exhibit 2). The first two describe what the model should be; the latter three serve to constrain what the model can be (at least in the near term).

The answer is not always straightforward—several of the factors may conflict with one another (see Exhibit 3). In diversified companies, the market factors tend to weight the decision toward the left, while the internal factors often bias toward the right. However, it is important to recognize that these internal dimensions are often historically rooted—they reflect the way the company has been managed, not the way it should be managed. Thus, these factors should be viewed as “correctable”; they are issues of organizational readiness that can be changed. Organizations can be redesigned, MIS can be strengthened and stronger executives can be promoted or brought in.

<table>
<thead>
<tr>
<th>Exhibit 2. Factors Dictating Which Management Model Is Appropriate</th>
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<tbody>
<tr>
<td><strong>What the Model Should Be</strong></td>
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<tr>
<td><strong>What the Model Can Be</strong></td>
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<tr>
<td><strong>SBU Linkages:</strong> Simply put, the less overlap in the customers, resources or risks, the more autonomously the businesses should be run. In other words, diversity requires that businesses have a high degree of freedom. It is almost impossible for the great man theory to work in a highly diverse environment.</td>
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<tr>
<td><strong>Market Dynamics:</strong> Companies operating in stable markets potentially could be run in a command-and-control environment. Fast-changing markets can’t; the businesses need to be free to respond to and drive market developments.</td>
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<tr>
<td><strong>Structure:</strong> There is no sense in trying to manage businesses separately if, in fact, they are so intertwined that decisions in one business will drive performance in another or if the numbers required to manage the businesses independently just aren’t available. Both of these constraints are addressable but they may constrain the choice of options until they can be addressed.</td>
</tr>
<tr>
<td><strong>Style:</strong> Clearly, the CEO’s own style is critical to determining what management model will be used. Perhaps more importantly, though, is the board’s understanding of how well the CEO’s style will work given the market requirements referred to above. In other words, a hands-off leader won’t work well when a command-and-control environment is required. Similarly, a roll your sleeves up, heavily into operational decisions executive may not make a good CEO in a highly diversified company. (Note: We often find an interesting conundrum. The divisional heads who want autonomy often want the CEO to make the decisions he is responsible for in a consensus style. It’s hard to have it both ways.)</td>
</tr>
<tr>
<td><strong>Readiness:</strong> In many cases what the company aspires to and what it is capable of at a given point are not aligned. For example, in a Strategy &amp; Oversight model (Model 2) there must be a strong performance ethic. This usually does not exist in command-and-control organizations (Model 4). This is no excuse for not migrating to a Model 2 but it does require that the components of the performance ethic be built.</td>
</tr>
</tbody>
</table>

Source: Booz-Allen & Hamilton
The Case for Model 2: Strategy & Oversight

Model 4 or command-and-control is not necessarily an outdated model; there are times when it is the right model to use. As a separate Booz-Allen article on strategic rollups argues, the Model 4 approach is appropriate, and, in fact, necessary, when consolidating a variety of companies and trying to compete as a single institution. It also may be appropriate in single line businesses, that is, when the businesses share common customers, common resources and/or common strategic imperatives. And it is often the only model that can be used in a major turnaround effort—especially one whose success is based on cost reduction. Having acknowledged these situations, it is not the right model in the case of most diversified corporations.

Model 1 (the financial holding company), too, is a valid option. In fact, in our experience, many divisional presidents say they would prefer to operate in a Model 1 environment—“just leave me alone, I’ll get you the numbers.” Understandably, most CEOs aren’t comfortable with that direction for it ultimately questions the very purpose of the corporation’s existence. But the use of tracking stocks and carve outs and today’s demergers question that response. Carve outs,

Exhibit 3. Which Model is Appropriate? A Company Example

<table>
<thead>
<tr>
<th>DIMENSION</th>
<th>ALTERNATIVE MANAGEMENT MODELS</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>MODEL 1: FINANCIAL HOLDING COMPANY</td>
</tr>
<tr>
<td>SBU LINKAGES</td>
<td>Customer Base</td>
</tr>
<tr>
<td></td>
<td>Resources</td>
</tr>
<tr>
<td></td>
<td>Risks</td>
</tr>
<tr>
<td>MARKET DYNAMICS</td>
<td>Market Certainty</td>
</tr>
<tr>
<td></td>
<td>Strategic Agenda</td>
</tr>
<tr>
<td>STRUCTURE</td>
<td>SBU Financial Reporting</td>
</tr>
<tr>
<td></td>
<td>Business Unit Structure</td>
</tr>
<tr>
<td>Style</td>
<td>CEO Style Preferences</td>
</tr>
<tr>
<td></td>
<td>Management Model</td>
</tr>
<tr>
<td>READINESS</td>
<td>SBU/Line Readiness</td>
</tr>
<tr>
<td></td>
<td>Corporate Core Readiness</td>
</tr>
</tbody>
</table>

Source: Booz•Allen & Hamilton

1 “Strategic Rollups: Rethinking Multi-merger Mania,” strategy+business, Second Quarter 2000
because they have separate boards, are, in effect, operating in a Model 1 environment—
demonstrating that it is a viable option even within a large corporation. But moving to a Model 1 raises serious questions about the role of the corporation. Until five to ten years ago, it could be argued that the corporation provided value to operating companies, even in a Model 1. The larger entity’s ability to access lower cost capital and attract better management were two of the primary arguments supporting the need to remain aggregated even when operating in a loose fashion. Neither of those situations holds today. The explosion of venture capital and the resultant difficulty in retaining good managers in larger corporations has turned the historic argument on its head. The value of staying combined now rests on the effectiveness of the performance management model and on creating value in the linkages between the SBUs.

In our view, most diversified corporations will need to accept that the Corporate Core is not capable of dealing directly with the rapid pace of change in most of today’s markets. Delegation of decision-making to business unit executives is not only a requirement to stimulate growth but it is essential to meet long-term shareholder value requirements. This increased autonomy will increase speed and effectiveness of decision-making by putting the decisions in the hands of those closest to the markets that are being served. The corporation itself will create value in the linkages between the businesses rather than in the businesses themselves.

Achieving this state will require corporations to adopt a structure similar to that of a Model 2, Strategy & Oversight. It is perhaps the only way that they can manage. It ensures alignment throughout the organization and it facilitates adaptability—the two factors that a joint Booz-Allen and World Economic Forum research program found were key to sustained financial performance success (see Exhibit 4). (Note: This study reviewed 15 businesses and was based on over 5,000 interviews.)

Exhibit 4. Organization Alignment and Adaptability—Two Key Factors to Financial Success

<table>
<thead>
<tr>
<th>ALIGNED ORGANIZATIONS DEMONSTRATE . . .</th>
<th>IN ALIGNED ORGANIZATIONS . . .</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Common, shared objectives</td>
<td>• Objectives are clear</td>
</tr>
<tr>
<td>• Shared understanding, information</td>
<td>• Roles and responsibilities are well-defined and understood</td>
</tr>
<tr>
<td>• Consistent motivation toward the objective</td>
<td>• Decision-making authority is clear</td>
</tr>
<tr>
<td>• Standard processes and procedures that support the objective</td>
<td>• The right things are accurately measured</td>
</tr>
<tr>
<td>• Standard tools</td>
<td>• Accountability for results is real; sanctions as well as rewards are meted out fairly</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>ADAPTABLE ORGANIZATIONS CAN . . .</th>
<th>IN ADAPTABLE ORGANIZATIONS . . .</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Perceive discontinuous threats or opportunities</td>
<td>• Initiative is valued</td>
</tr>
<tr>
<td>• Communicate perception to decision makers</td>
<td>• Inconsistencies, anomalies and discontinuities are evaluated objectively</td>
</tr>
<tr>
<td>• Objectively consider relevant information</td>
<td>• There is a tolerance for experimentation, alternative points of view and failure</td>
</tr>
<tr>
<td>• Experiment, tolerate a degree of failure</td>
<td>• There are processes for modifying the institutional systems in light of significant discontinuities</td>
</tr>
<tr>
<td>• Implement new ideas that survive experimentation</td>
<td>• Learn from failures as well as successes and institutionalize learning</td>
</tr>
<tr>
<td>• Learn from failures as well as successes and institutionalize learning</td>
<td></td>
</tr>
</tbody>
</table>

Source: Booz-Allen & Hamilton

2 “Creating the Organizational Capacity for Renewal,” Project of the World Economic Forum in partnership with Booz-Allen & Hamilton, April 2000
that establishes guiding principles of behavior—in much the same way that a Model 2’s Core establishes policies to guide behavior of its SBUs. The government in a free model then allows the private sector to respond to the economic and market forces—as a corporation does with its operating companies.

Migrating to an empowered business model where people work as teams, networked by the latest information technology, is not new. Leading management thinkers have been promoting these concepts for many years. So why do most companies still have a business structure modeled by Fredrick Winslow Taylor over 100 years ago? We believe that much of it has to do with CEOs not seeing a clearly laid out path to move to a more empowered Model 2 structure. In many instances it requires a massive leap of faith to move from what has been a successful model for many decades to a new model only tried and tested by a few outstanding companies. As a result, a halfway model is often adopted where some characteristics of the empowered organizations are adopted, but control is kept firmly with the trusted few in the corporate center.

Migrating to a Model 2: What it Means

The apparent simplicity of the philosophy underlying Model 2 can mask the huge operational changes that are required to implement it. Model 2 is not just a concept—it is a corporate way of life. It requires major retooling of executives in the Core and in the business units.

The Core will step out of operational issues and focus only on strategy, policy and dialog with the business units around their strategic agenda and commitments. The simple act of creating this focus will trigger major changes. The Core will no longer provide business services—payroll, benefits administration, general accounting and even legal will be moved into a shared service unit, devolved to the businesses or eliminated. For those activities left in the Core, the way they are done will change to reflect a policy orientation. These changes will redefine the roles of the leading Core executives. For
example, the role of the CFO changes dramatically. First, the transactional activities that are usually under the CFO’s direction are no longer under his/her purview. Second, the CFO’s control function changes in style and in substance. Rather than approving expenditures several levels down in the budget, the CFO develops top-level financial policies and rigorous risk management systems. Rather than collecting data on an ad hoc basis to measure the performance of businesses, the CFO focuses on developing a performance management system that ensures the head of each business can not only discuss historic financial performance, but also the operational measures that will predict future financials. The CFO also takes a different but more proactive role in the strategic leadership of the corporation: rather than set top-down arbitrary budgets (after the usual bottoms-up process), the CFO works with the businesses to develop an understanding of the business’s potential and the actions required to capture that potential.

The business units have to change in Model 2 as well. They have to step up to a more autonomous role. Business units need to make decisions where they can and should (instead of passing the decisions up to avoid personal risk taking) and learn how to ask for help when needed. They must develop an understanding of what the potential of their business really is (not just build off the prior year’s budget and actual performance) and demonstrate a sound game plan to close the gap between potential and actual. They must determine what level of “business services” they need to run their business. These services will no longer be provided by the Core. Rather, the Core will set policy and the businesses will have to consider how they will meet policy requirements: a requirement for functional excellence shifts to a requirement for functional adequacy.

The combination of these effects will change:
• How the executive team interacts and what they do day-to-day;
• Decision-making processes and authorities;
• Planning and review cycles and supporting tools;
• How people are held accountable for results;
• The size and structure of the Corporate Core.

How the Executive Team Interacts

This change in philosophy should have a major impact on the nature and focus of interactions amongst the management team. Several types of relationships will be affected: the role of the executive team as a group; the relationship between the CEO and the business unit heads; the relationship between the Core and the business units; and, finally, much of the major change occurs in the relationship between the CFO and the business units (as described above).

• Executive Team: In some cases the Executive Team composition will be dramatically restructured, resulting in less involvement by executives in the Core and more SBU leader involvement. The biggest change, however, is likely to be in the content of the executive team discussions. Management committee meetings will look and feel much different—even if they are held with the same frequency.
(although they need not be, fort-nightly or monthly meetings generally prove adequate, rather than weekly meetings, which are common in many companies today). In Model 3 and 4 organizations, we have found that much of the content of the meetings is operationally focused. In a Model 2 environment, the focus will shift. Corporate strategy, cross-SBU issues and communications (e.g., cascading the CEO’s agenda) become the focus.

- **CEO and SBU heads**: With the SBUs running the businesses more autonomously, these meetings become the focal point. For the SBU head, the objective is to demonstrate an understanding of the drivers of the business and the competitive situation and to articulate a cogent program to create additional value in the business—in other words, to build confidence in the CEO that the SBU is being managed effectively. Detailed quarterly reviews of performance and monthly one-on-ones are usually adequate to accomplish these goals. For the CEO, the meetings present an opportunity to probe for risks (in terms of financial performance or values), to play what-if games, and to calibrate his or her own sense of trust and confidence in the managers responsible for each business.

- **Core and business units**: The Core has two key types of interactions with the business units. First, they support the CEO’s efforts to establish a performance contract with the business units. This requires interaction as the performance framework is developed and an important but diminished role in preparing feedback on performance (as discussed later, the business units should be responsible for reporting performance through the agreed upon performance framework). The second key area of interaction is in identifying and framing opportunities that create value strategically or operationally across SBUs. An example of this direction is the automotive industry’s strategy to share platforms across models and major product lines (e.g., GM and Fiat sharing platforms across model lines). Another example would be Lockheed Martin’s drive to share best practices across all the business areas in diverse functions, such as engineering, program management and operations.

### Decision-making Processes and Authorities

With the shift to Model 2 comes much more autonomy for the individual business. But what does more autonomy mean? It is most clearly reflected in **delegations/authorities**: decisions that can or cannot be made by the heads of the SBUs. In most Model 3 or Model 4 organizations, the delegations are low and usually based on some sort of dollar value. In a Model 2 organization, the nature and magnitude of the delegations change. First, the discussion shifts to one of decision rights: who has the authority to make what decisions. This deliberation is best taken in the context of what it will take to compete most effectively. Decisions such as, can the businesses hire someone and if so, who; can a line of credit be taken and for how much; how should pricing on a contract be structured; and how much audit is required to ensure the accuracy of reported financials all need to be sorted out. Second, those rights will be boundaried by risk. How much of what kind of risk is the CEO and the board willing to delegate? And risk does not necessarily correlate with size—which often defines today’s delegations. For example, in a large industrial company all new contracts above a threshold value have to be approved by the CEO—even if it reflects only a minor modification to an existing product and contract. On the other hand, new contracts, in areas in which the company has no experience, are not subject to review, because they fall below the dollar threshold even though the risk to the P&L is often substantially higher. In a more autonomous model, much clearer distinction of what defines risk is required. A robust risk management system is a prerequisite to a move to a Model 2. Without it, the CEO generally feels too exposed to surprises.
The planning and review process in a Model 2 organization is also significantly different from that in a Model 3 or 4. In many corporations today the strategic planning department operates as a coordination point to integrate business unit plans each year into an overall “strategy” for presentation to the board for approval. Often strategies are not consistent and there is no link with the financial planning process (see Exhibit 5), which is managed separately by the CFO, resulting in the strategic and financial planning targets being totally different. To manage in this relatively unstructured environment, the command-and-control organization manages each business unit closely and intervenes frequently.

In a Model 2 organization, the strategic planning department does not set annual strategy or intervene in the day-to-day execution of the business unit’s strategy. Instead it focuses on the three to five year time horizon to develop the overall strategic framework that the business units use to develop consistent shorter term (one to two year) business strategies.

For example, in a major bank the strategic planning department might undertake a review of the economics of the industry’s value chain to identify which elements would be attractive for the bank to participate in over the longer term. After the strategic direction is approved by the executive team, the business units use it as a guide to develop their own strategies for value chain positioning, which is then incorporated into their business plans.

To ensure that business units are operating within the overall strategic framework under a Model 2, it is very important that the long-term strategic targets are fully integrated with shorter term business unit financial plans. Without this control point the CEO will not have confidence to give up the amount of control required for Model 2. This requires a much more sophisticated approach to target setting than using “last year’s performance plus some.”

Exhibit 5. Today Strategic Targets Are Not Linked to the Financial Plan - A Company Example

Source: Booz-Allen & Hamilton
Delegation and autonomy are based on trust. And, as we all know from our private lives, trust is something that is earned, not assumed. Therefore, the business units must earn their right to autonomy by delivering results, and the CEO must be comfortable that there are sufficient checks and balances to enable timely identification of problem areas requiring appropriate intervention.

Model 2 is about delegation, not abdication. Let us be blunt, Model 2 works only with a strong performance ethic as a core part of a company’s “culture.” The performance ethic consists of both process and content as displayed in Exhibit 6.

All six process elements must exist in strong form—weakness in any one of them can cause the system to unravel: goals without direction may result in short-term results but not the long-term value creation; accountability without consequence management doesn’t really exist. Additionally, the components of the culture are also important. A performance ethic is about more than making money this quarter or even this year. It’s about building a business for the long-term. Thus, the measurement system has to go beyond financials, most of which are relatively straightforward but inadequate to measure the performance of a business. The traditional financial measurements need to be augmented by three additional sets of measures. First are operational metrics which provide insight into what the future economics of the business might be (e.g., a distribution business might measure route density or warehouse efficiency). Second are institution building measures (e.g., new customer acquisitions, employee attrition rates, patents received, etc.). Third are measurements of adherence to the corporation’s values (e.g., ethical violations, harassment incidents, safety record, etc.).

Size and Structure of the Core

With all these changes in roles and responsibilities, what does a Model 2 Core look like? Much smaller and more highly focused. Activities currently in the head office will be divided into two categories. Those adding value in the linkages between the businesses and those adding value to the businesses themselves. The latter category, including things like payroll, benefits administration, audit and legal should be moved to a shared services environment, devolved or eliminated. Those left in the Core will focus...
only on five missions that enable the corporation to generate value over and above the business units (see Exhibit 7).

This changed role requires a much smaller Core than most command-and-control organizations have today. Rather than a 500-1000+ person head office, a Model 2 Core usually contains 100-200 highly skilled people—depending on the size of the company (see Exhibit 8). For example, a major banking client has adopted a Corporate Core structure of around 100 people, significantly fewer than the 500 people it previously had.

Conclusion

Moving to a Model 2 Core model presents the potential for significant performance benefits in today’s uncertain and quickly changing environment. However, making a successful transition requires much more than moving the lines and boxes or expounding a new philosophy.

Adopting a Model 2 organization requires both corporate and SBU management to adopt a completely different management mindset of empowerment and trust. To build this environment without putting overall performance at risk requires a massive upgrade of management processes for setting targets, reviewing performance and managing consequences. Only when these changes are made will the true potential of the organization be realized.

Exhibit 7. The Five Key Missions of the Corporate Core

<table>
<thead>
<tr>
<th>MISSION</th>
<th>OBJECTIVE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Strategic Leadership</td>
<td>• Provide the vision, leadership and purpose for GROWTH. Initiate “outside the box” thinking to generate future growth and a vital organization</td>
</tr>
<tr>
<td>Identity</td>
<td>• Formulate a shared vision and set of values, and create the most favorable corporate IDENTITY possible to motivate each relevant constituency</td>
</tr>
<tr>
<td>Capital</td>
<td>• Minimize cost of CAPITAL</td>
</tr>
<tr>
<td>Capabilities</td>
<td>• Act as a sourcing/disseminating “market maker” to ensure corporate-wide access to world-class, low-cost CAPABILITIES</td>
</tr>
<tr>
<td>Control</td>
<td>• Exercise CONTROL/MONITORING on behalf of the board and the shareholder. Understand and manage the risks of the business</td>
</tr>
</tbody>
</table>

Source: Booz-Allen & Hamilton

Exhibit 8. Staffing of the Core Versus Company Size (For a Model 2 Organization)

Source: Booz-Allen & Hamilton
What Booz-Allen Brings

Booz-Allen & Hamilton is a global management and technology consulting firm. In more than 90 offices, our team of 9,800 professionals serves the world’s leading industrial, service and governmental organizations. Each member of our multinational team has a single common goal: to help every client we serve achieve and maintain success.

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For more information, please contact any member of the Booz-Allen team.

Boston
John Harris
Senior Vice President
617.371.2924
harris_john@bah.com

Buenos Aires
Jorge Forteza
Senior Vice President
54.11.4.326.3261
forteza_jorge@bah.com

Chicago
Gary Neilson
Senior Vice President
312.578.4727
neilson_gary@bah.com
Vinay Couto
Vice President
312.578.4617
couto_vinay@bah.com
Shelley Keller
Vice President
312.578.4537
keller_shelley@bah.com

Munich
Tom Williams
Vice President
49.89.54525.0
williams_tom@bah.com

New York
Paul Kocourek
Senior Vice President
212.551.6627
kocourek_paul@bah.com
JoAnne Bessler
Vice President
212.551.6572
bessler_joni@bah.com
John Jones
Vice President
212.551.6713
jones_john@bah.com

San Francisco
Bruce A. Pasternack
Senior Vice President
415.627.4215
pasternack_bruce@bah.com
John Treat
Vice President
415.627.4213
treat_john@bah.com
Albert J. Viscio
Vice President
415.627.3321
viscio_albert@bah.com

Sydney
Martin Bollinger
Vice President
61.2.9321.1930
bollinger_marty@bah.com
Paul Hyde
Principal
61.2.9321.2880
hyde_paul@bah.com

Tokyo
Eric Spiegel
Senior Vice President
81.3.3436.8601
spiegel_eric@bah.com
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