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Putting Headquarters
In Its Place
*A Lean, Global
Corporate Core*



Contact Information

Chicago

Vinay Couto

Partner

+1-312-578-4617

vinay.couto@booz.com

Gary Neilson

Senior Partner

+1-312-578-4727

gary.neilson@booz.com

Stockholm

Per-Ola Karlsson

Partner

+46-8-50619049

per-ola.karlsson@booz.com

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EXECUTIVE SUMMARY

This Perspective addresses the challenges of organizational design and proposes a new approach to organizing senior management around the Global Core. It presents four models for this new view of senior management, drawn from our own consulting experience and the firm's study of hundreds of other corporations. These models of the Global Core are pertinent to a variety of organizations ranging from highly diversified financial holding companies to more industry-specific companies where operational involvement by senior management does succeed in creating value. They can serve as the basis for evaluating an individual company's needs, and determining the appropriate level of corporate senior management activity.

SYMPTOMS OF AN AILING HEADQUARTERS

Are you finding it difficult to manage the complexity of a large, global operation?

- Has your corporate headquarters staff grown smaller without making business units more market responsive?
- Or has the corporate headquarters staff remained stubbornly high while the rest of the organization downsized?
- Are fast-growing divisions held back because they have to fight with troubled businesses for resources?
- Does your company have trouble sharing information and transferring best practices across organizational lines?
- Do your business units have redundant service units?
- Have your division managers ever run the numbers on taking their businesses public?
- Are corporate cost allocations significantly higher than the value delivered to the business units?

If you answered yes, then chances are your company is ripe for a re-examination of the structure of corporate headquarters itself. Most companies that have restructured themselves to become more market-

responsive have left the essence of their corporate center intact. We propose that a contemporary networked company needs a radically redesigned corporate headquarters structure, which we call the Global Core.

Booz & Company has been working with many organizations to make them more effective at doing their jobs. We have seen in each case that the more the divisions are required to look to headquarters for making decisions, reviewing and avoiding direct responsibility for their actions, the less effective they are in meeting the immediate challenges of doing business.

The test of any complex organization is whether the whole is worth more than the sum of its parts. Somehow the corporate headquarters has generally escaped that test. The value that the corporate center provides has always been assumed, but rarely measured. If it were measured, the corporate center might have a tough time justifying its existence.

It doesn't have to be this way. We believe that by remaking itself as a Global Core, corporate headquarters can ably represent the corporation in the world of the public and investors, perform essential work for the operating divisions, provide leadership and create the context for growth.

CREATING VALUE AT THE CORPORATE LEVEL

Of all the reinvention that the corporation has undergone in the past decade, the most stubbornly resistant to real change is senior management, or the corporate center, itself.

Not that companies haven't tried. They have streamlined, decentralized and otherwise tried to shed their command-and-control mentality, while implementing their strategies.

It is as if senior management can see themselves doing the same work with fewer people. Or they can justify lodging certain costs in other expense lines. Or they can call themselves by other names. The attendant savings

are dramatic and often convey an air of sacrifice and resolve, which have dramatic impact on shareholders and employees alike.

But these measures haven't worked. Some major companies, for example, AT&T, Hewlett-Packard, ITT and Westinghouse, have decided to split up into several companies, citing the difficulty of managing fundamentally different businesses. Yet others, like General Electric and ABB, have found new ways to manage complexity and diversity. For most, however, focusing the corporate center on value creation represents a radical departure from conventional wisdom.

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WEAKNESS AT THE CENTER, STRENGTH AT THE CORE

The traditional corporate center is built around several critical management processes—business planning, capital allocation, and monitoring and control. This makes sense as long as the market can be understood only from the point of view of the chess grand master, who has the necessary information, knowledge and experience to plot strategy and direct the pieces.

The structure for execution is hierarchical, delivered from a large corporate staff to large divisional staffs, to

stand-alone businesses that have little sense of the whys and wherefores of the larger organization. Like a quality bureaucracy, such a corporate center absorbs enormous overhead, which is bearable in good times. But when good times end, the high fixed costs become a drain on the businesses that have to support it.

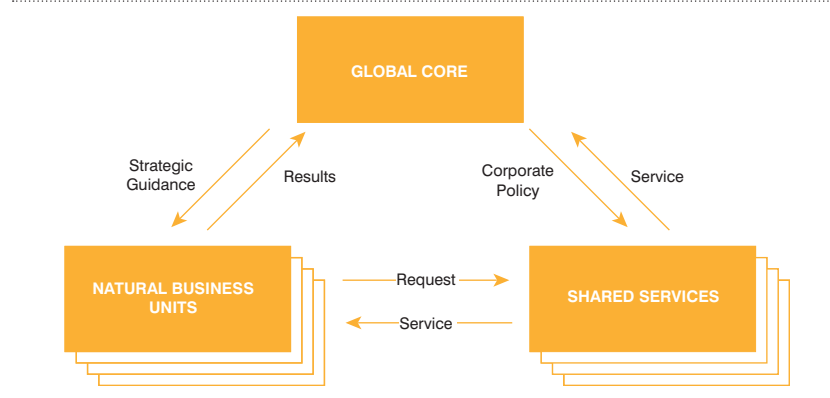
Today, corporate management has no monopoly on wisdom. The marketplace is not a chessboard with known players facing off against one another. Players large and small, familiar and brand-new, are pitted against one another in a game that is constantly changing. In this setting, the corporate center cannot possibly keep up with the speed of focused competitors. The pieces must be self-directed or they will lose a thousand small competitions. To manage the speed of change, organizations need to adopt an alternative organizational

structure. One we call the Centerless Corporation (*see Exhibit 1*). At the heart of the Centerless Corporation is the Global Core, a leaner corporate center.

But in order for the corporate center to be slimmed down, the business units must change as well. It's not as simple as cutting corporate headcount and doing the same job with fewer resources. The actual content of the work must change as well. This implies that the business units must take on more responsibility and accountability for their work (*see "The Natural Business Unit"*).

In the new competitive environment, the key management processes are entrepreneurship, integration of resources to support short-term needs and take advantage of market opportunities, the strengthening of the corporate "network" and a capacity

Exhibit 1
Structure of Centerless Corporation



Source: The Centerless Corporation

for continual renewal, instead of the tendency of any bureaucracy, which is to perpetuate itself.

Senior management becomes flatter. Instead of being the sole connective tissue among the businesses, management facilitates communication among the business units so that they can learn from one another and share opportunities, just as independent corporations do.

Information no longer flows up and down. Instead it seeks the line of greatest opportunity. Staff functions that can't be justified at the business unit level are shared, or outsourced, depending on the characteristics of the business (see "*The Merits of Shared Services*", page 6). The result is greater interdependence between business units based on perceived advantage, rather than mandated connection.

The success of a "centerless" corporation depends on a solid foundation of people, knowledge, and coherence. Well-trained, high motivated people are critical to success in today's fast-changing world. The transfer of knowledge and creating a "learning" company is equally critical. Creating knowledge networks is therefore essential. Finally, coherence is a simple way to describe the management processes and linkages that allow the Centerless Corporation to function, adapt, and prosper by creating value.

The Natural Business Unit

In today's marketplace, the ultimate test for any corporation is the marketplace itself. The way large corporations are organized is ill-suited to a world characterized by globalization, deregulation and technology "where customer solutions" dominate the value proposition. We have developed a new view of the business unit, which we call the Natural Business Unit, or NBU.

The NBU is ideal for working with senior management as described in the Global Core. Each business unit is bounded as if it were a freestanding company, with its own supplier network and its own customers, internal to the corporation or external. It is defined backwards from the point where money changes hands and value is created. And its competitiveness is measured against its best, most focused competitors.

Thus, in an integrated company, each step in the value chain is likely to face competition from focused niche players. An oil company might have its own reserves, drilling capability, refining, shipping and retail operations. Yet, it may be able to buy cheaper crude from other companies, and outsource the extraction to one company, refining to another and shipping to a third, before selling to the consumer at its own outlets. Or it might even sell the finished fuel to its retail competitors and buy its own retail stock from other sources altogether.

Unless each of its own operations is competitive at each step of the way, the company might be better advised to divest some of them. These are judgments that corporate senior management will have to make. Conversely, if senior management places an excessive drag on the NBU compared to senior management of their best competitors, then the NBU might produce more value by being spun off.

The Merits of Shared Services

In the 1980s, the heyday of decentralization, many companies farmed their corporate services out to the business units. Vital services—sales and marketing, human resources, information technology, finance, purchasing and logistics—were paid for by profit centers.

But under the law of unintended consequences, these corporations saved little money. Instead, managers created fiefdoms, and shareholders paid for lost economies of scale from redundant resources, operating facilities, information systems and supplier contracts.

The challenge now is to redress the excesses of decentralization without losing its best qualities—superior service, customization and focus. Our answer to this challenge is Shared Services. Like the Natural Business Unit, a Shared Services organization should test itself against the best of the marketplace. Business units ultimately have the choice of purchasing services internally or on the open market. Of course, the value of Shared Services is more than just financial. To the extent that there is value to be gained from knowledge of the larger corporations, its culture and best practices, a Shared Services unit can provide it.

Like the Global Core itself, Shared Services units will have to create more value than it consumes in overhead.

WHAT IS THE REAL JOB OF CORPORATE MANAGEMENT?

The Global Core is a revolutionary overhaul of the old headquarters. It is global in that it is responsible for key missions across the entire corporation. It is core because it imparts value to all the other elements of the Centerless Model (*see Exhibit 2*), without adding excessive

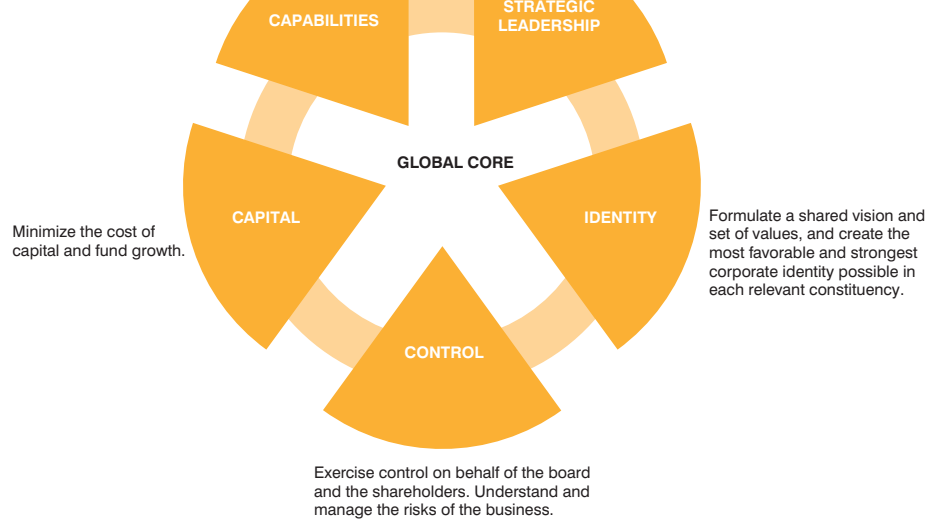
overhead. The core's value must be measured not just in costs, staffing levels, compensation and rents. It must be perceived in terms of the value it creates.

A corporate center destroys value in several ways: by generating overhead,

Exhibit 2
Five Key Missions of the Global Core

Act as a sourcing/disseminating market maker to ensure corporatewide access to world-class, low-cost capabilities. Provide matrix capabilities in nonmatrix organizations.

Provide the vision, leadership and purpose for growth. Initiate outside-the-box thinking to generate future growth.



Source: Booz & Company

paid by the businesses; by slowing the flow of information; by making mistakes in allocating capital among the businesses.

When you strip these destructive elements away, you are left with five missions that create value and that lie at the heart of the Global Core model. They are Strategic Leadership, Identity, Capabilities, Capital and Control. These are not “new” missions. They are inherent in the management of any company. However, as defined in the Centerless Corporate model, they are managed differently, although with varying degrees of involvement.

The Global Core—consisting of the CEO, the senior team and a defined set of support functions necessary for the entire corporation, with minimal overhead charged to the businesses—consigns to the business units themselves maximum responsibility for moneymaking activities. In some cases, the core may be a bare-bones

operation. In others, it may be more actively involved in creating linkages between disparate business units.

Let’s examine these missions one at a time.

Strategic Leadership means providing vision, direction and purpose for helping the corporation grow. It is the creation of a road map to allow the organization to achieve its potential. The road map is not prescriptive. It does not substitute one set of defined tasks for another.

Rather strategic leadership is exerted through the promotion of “out-of-the-box” thinking and behaviors that promote it. Examples include GE’s “boundarylessness” corporation; ABB’s “multidomestic” company; Motorola’s “Six Sigma” quality methodology; Cisco System’s positioning as the Internet company; British Airways’ “world’s favourite airline” strategy, built on customer service; and Banc One’s

“breakthrough planning.” Each of these removes the businesses from a lock-step system of policy and measurement, and encourages people to use their imagination, knowledge and common sense in pursuit of new opportunities.

Identity entails the formulation of a shared vision and values, to be manifest both internally and externally. This does not mean that the identity of the corporation must be the same everywhere, in all divisions and to all customers, in the sense that the face is always the same. Rather, it means that the soul of the corporation is constant. The symbolism utilized for transmitting culture, attitudes, beliefs and standards is coherent and recognizable. By word and by deed, the company conveys its commitment to certain values. These provide the standards for decision making when the company’s reputation is at stake either at the corporate or business unit level—mergers and

acquisitions, lines of business to be entered or exited, advertising and PR campaigns, layoffs and benefit decisions, among others.

To compete at full strength, the corporation needs *capabilities* that can be deployed in a flexible business framework. The marketplace is such that companies have the choice of buying, renting or partnering to capitalize on market opportunities. A big corporation should have the same range of options.

The Global Core is the broker of capabilities in the corporation, coordinating, facilitating and otherwise providing the businesses with what they need to put their plans into effect. Some of these are best developed internally, with a heavily proprietary bent, and can be leveraged throughout the company, but some can be acquired through the same flexible menu of choices enjoyed by niche competitors. Senior management should be comprised not just of those with successful records of business management, but

of functional experts who know the state of the market in technology, skills and communications, which will allow them to facilitate transfer of best practices in these areas, and who know how to leverage strengths. In some cases, access to external world-class capabilities will be important.

There is little question that the Global Core must be responsible for the *capital mission* of the corporation. After all, it is the corporate name that provides leverage for accessing the lowest-cost sources of capital in the global markets. The business units may be the best repositories for information about their customers and markets, but the Global Core alone has the breadth of perspective to work with the business units to secure financing appropriate to their needs.

In addition to market leverage, many financial functions are best lodged in the Global Core, among them investor relations, corporate risk management, and technical financial

advice for cross-border transactions. Each is critical to the business units, though their requirements can best be served in aggregate at the corporate level, leaving the business units to get on with their business.

The *control mission* consists of two basic functions. The first is the legal and fiduciary requirements. These are dictated by laws and regulations—securities market disclosures, tax reporting, environmental compliance and so forth. These are the basics of corporate citizenship and they belong at the corporate level—indeed no business unit would want it.

The second is an enabling role—to ensure that diverse activities are aligned to promote the same strategic vision; to coordinate activities across the firm to fit into a coherent strategy; to set standards for designing work and incentives; and to manage risks that will affect the share price.

The control function translates the vision into “rules of the game” that apply to corporatewide conduct.

WHAT GETS DONE WHERE

Paring the list of missions to five leaves the problem of where to put each element of the corporate center's work. Should they go to the business units, outsourcing, elimination, to a strategic partner, or to a Shared Services group?

The burden of proof for each lies in the nature of its utility to the corporation as a whole, or to the test of the market. While there are

no simple answers, there is, at least, a relatively easy place to start—a sliding scale of six questions (see Exhibit 3).

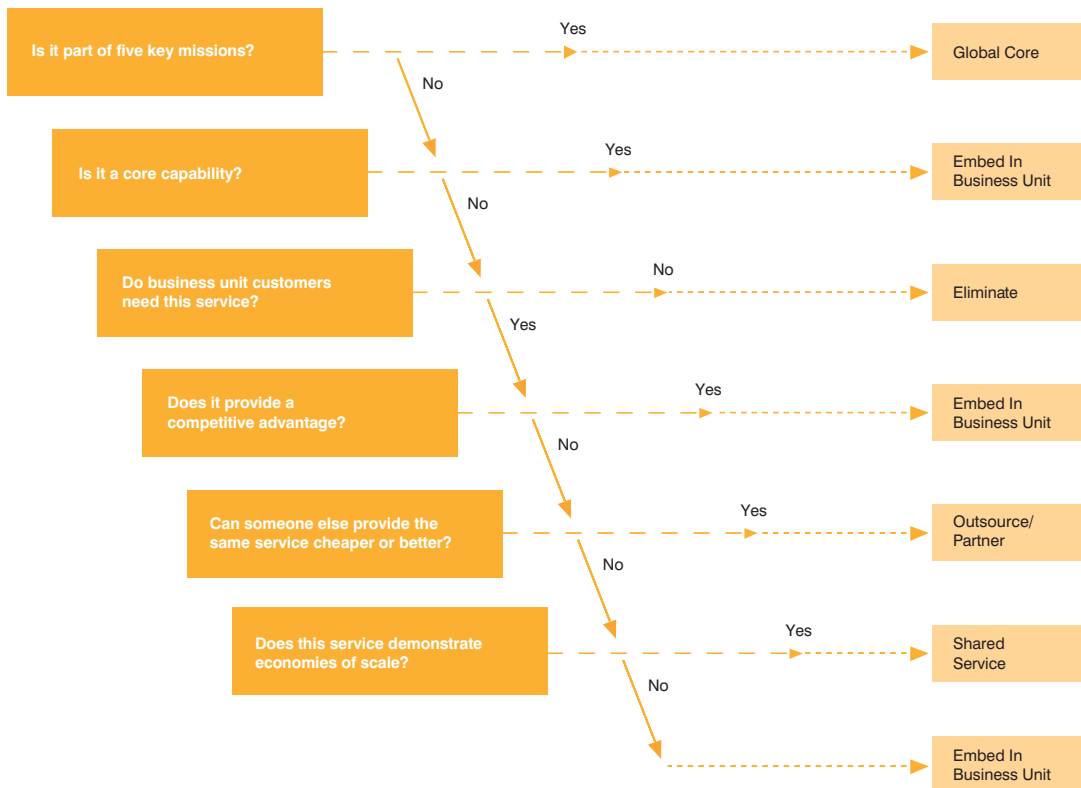
- 1) Is it needed for governance, consistency or fiduciary responsibility? If the answer is yes, then the responsibility clearly lies with the corporation. If not:
- 2) Is it a core capability? If the answer is yes, then it belongs in the business unit. If the answer is no:
- 3) Do business unit customers need the service? If the answer is no, then it can be eliminated. If the answer is yes:

4) Does it provide a competitive advantage? If the answer is yes, it belongs in the business unit. If the answer is no:

5) Can someone else provide the same service cheaper or better? If the answer is yes, then it should be outsourced, or go to a partner. If the answer is no:

6) Are there demonstrable economies of scale? If the answer is yes, it should be turned over to a Shared Services unit. If the answer is no, it should be embedded in the business units that need it.

*Exhibit 3
Decision Tree for Location of Staff Services*



Source: Booz & Company viewpoint; "Shared Services: Management Fad or Real Value?"

FOUR MODELS FOR CORPORATE MANAGEMENT

There is no “one model fits all” Global Core—but rather a range of models with progressive degrees of headquarters’ involvement, depending in large part on the degree of focus in the organization and the competitive realities. Customization of the organizational model is entirely appropriate. The different models require different resource levels—which must be justified through value adding activities.

At one end the approach is minimal. At the other end, there is a considered judgment that the senior management can add value by being much more involved, and the corporation is better served by this hands-on role (see Exhibit 4, page 12).

Model 1: Financial Holding Company
The minimalist approach is embodied in the financial holding company, which is managed as a portfolio, where there is little historical connection between senior management and any of the operating businesses. Given the concentration of financial skills in central management, it should be no surprise that their numbers are the smallest as a percentage of overall employment. As one financial analyst observed of the 50-company Dover Corporation, “They don’t have enough people at the top to interfere even if they want to.”

Proponents of the minimalist approach are at odds with several

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Exhibit 4
Alternative Global Core Models

	1. FINANCIAL HOLDING COMPANY	2. STRATEGY AND OVERSIGHT	3. ACTIVE STAFF INVOLVEMENT	4. OPERATIONALLY INVOLVED
UNDERLYING PHILOSOPHY				
- Where value is created	- Value is created by individual companies, closest to customer	- Value is created by individual companies, closest to customer	- Value is created by individual companies using corporate expertise to help make key decisions	- Value is created by corporate expertise and control
- Role of the corporation	- Create and enforce a disciplined management model	- Add value in the linkages between business units	- Provide guidance to business units via expertise	- Make key decisions for business units
WHO WE ARE (GLOBAL CORE)	- We're an investment company	- We're the strategic leadership of a collection of management entities	- We're both consultants to and the strategic leadership of a collection of management entities	- We are the key managers of all business units
KEY CHARACTERISTICS				
- Performance expectations	- Core sets high financial goals. Business unit are completely accountable for achieving results	- Core sets financial, key operational and value metrics. Business units are accountable for achieving results.	- Core and business units share accountability for broad set of financial and operating metrics	- Core is accountable for financial and operating performance
- Delegations	- Large delegations	- Large delegations with threshold based on risk to corporation	- Moderate delegations based on risk to corporation and to individual business units	- Limited delegations
- Planning philosophy	- Business units commit to multi-year strategic plans – as long as targets are met, no annual review necessary	- Business units commit to multi-year strategic plans – core ensures strategy coherence across elements of linkage and reviews annual budget against plan	- Core proactively and critically reviews business unit strategic plans and annual budgets	- Core dictates business unit strategic plans and budgets
TYPICAL SIZE OF GLOBAL CORE	0.05 - 0.07% of total staff	0.15 - 0.20% of total staff	0.25 - 0.30% of total staff	0.35 - 0.40% of total staff
LARGEST GLOBAL CORE GROUPS	- Finance	- Finance/Planning	- Finance/Planning +	- All functional areas
EXAMPLES	- KKR; Hanson	- GE; Norwest; Lucent; BP (prior to merger with Amoco)	- Amoco (prior to merger with BP); NationsBank	- Emerson Electric Co.

Source: Booz & Company

traditional corporate assumptions. They believe that in their businesses, economies of scale are not particularly important because there is relatively little overlap between businesses, or because the costs of administering scale would overwhelm any savings. When corporate scale is justified, it can be better achieved through networks than through formal hierarchy. The core devotes itself to developing capabilities throughout the corporation that the businesses need, but exercises little control over how they are put to work.

Model 2: Strategy and Oversight
Somewhat more centrally involved, a company like GE, while still extremely diversified, has a heritage of operations in all its subsidiaries. Top management takes a role in strategy and oversight, but leaves most of the capabilities issues of disparate businesses to the business units themselves. The business units work together when the opportunities call for it. When one part of the company wants to sell power-

generating plants to China, it can call on the power-generation financing capabilities of GE Capital Services. But GE Capital also puts its money to work in owning and operating fleets of trucks, sub-prime automobile loans, or even working with very wealthy individuals on managing their fortunes if the margins are higher.

Model 3: Active Staff Involvement
As the corporation becomes more focused, the need is greater for corporate senior managers who understand technological, marketing and other operational issues that are common to the whole business. They can use this understanding to help the business units attain their individual goals, while building networks between them that will help them attain that most elusive of all corporate dreams—synergy. And to the extent that all lines of business have homogeneous technical and cultural requirements, the chance is greater that corporate involvement in HR, operations and other services can add value.

For example, at Amoco, before the merger with BP, the corporate center played a significant role in managing both upstream and downstream operations. In the downstream business, corporate staff was involved in designing the retail format for their gas stations. They felt this level of control was necessary to maintain a consistent brand identity.

Model 4: Operationally Involved
At a company like Emerson Electric Co., senior management has the marketplace perspective of a niche competitor, which itself provides comparative advantage. Therefore, senior management takes part in all company issues, while the business units are responsible for execution.

The percentage of company payroll that resides in senior management rises level by level. But in a well-managed company, those higher levels are amply justified because they are engaged in value creation. Numeric targets are irrelevant, and, based on recent experience of downsizing the corporate office, frequently counterproductive.

At a company like General Electric, top management takes a role in strategy and oversight, but leaves most of the capabilities issues to the business units themselves.

Multinational Example

Booz & Company worked recently with a global oil refining, marketing and distribution company that wanted to restructure its corporate headquarters after several reorganizing and downsizing initiatives had failed to improve performance.

We organized jointly with the client a program team including six full-time professionals (three of which were from Booz & Company) and three partners working closely with senior client executives at the management committee level. The overall process exhibited four major characteristics: 1) Fielding of a small and senior joint team; 2) a very interactive process with all senior client executives; 3) a well-defined approach, but tailored to the client's specific situation and business; and 4) clean timing objectives (15 weeks). The joint client/Booz & Company team performed the following activities:

- Interviewed senior management to understand opinions and issues
- Conducted structured workshops and brainstorming sessions
- Derived a set of organization design principles that guided subsequent activities
- Developed and tested organization design alternatives—what went where
- Mapped out major processes for the core in the new model (e.g., planning, capital allocation, control)
- Developed and tested alternative business unit aggregation models (regional, county, product line, etc.)
- Developed and tested alternative Shared Services model

The results of these short but high-level and intense efforts were quite dramatic: The redesigned Global Core was much leaner and value-added oriented than the previous organization and had fewer than 50 people down from nearly 500. This was made possible by the design of a Shared Services model for major support functions, the distribution of remaining functions to businesses (or outsourcing) and the identification of new process requirements (e.g., information flows) to make the new structure work.

Detailed implementation plans were also laid out as part of the program, and the transition to the new organization was complete within one year.

TESTED AGAINST THE MARKETPLACE

The responsibilities of senior management are critical to corporate well-being. But the ultimate test of corporate well-being is the marketplace. To the extent that corporate responsibilities stand between intentions and actions, opportunities are lost. We have learned from our work that the view from headquarters is often very different from the view in the field.

The senior managers of the best niche companies add more value to the operating businesses than they cost, in terms of overhead and bureaucratic impediments to decision making. That's the test for management of the largest, more diversified companies too.

We believe that by structuring themselves around the five elements of the Global Core model, corporate senior managers can optimize both their own performance and that of the business units. The degree of involvement at the operational level should be determined by senior management's capacity to create value.

The Global Core is a model, not a blueprint. Within that model, there's a great deal of latitude for different companies to create structures that enhance their particular strengths.

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THE NEW DIVISION OF RESPONSIBILITY

Science writer David J. Freedman once wrote, “What most managers think of as scientific management is based on a conception of science that few current scientists would defend. While traditional science focused on analysis, prediction and control, the new science emphasizes chaos and complexity.”

That was in 1992. But old habits die hard—senior management at many companies persist in trying to deal with a chaotic, complex marketplace by weighing in at the operational level, building in layers of expense and crippling delay, and destroying value. By leaving nothing to chance, they incur the biggest risk of all.

In a centerless corporation, senior management creates value by assuming responsibility for the things that can be done best at the corporate level, and giving the business units the tools to respond to marketplace challenges.

Resources

The Centerless Corporation: Transforming Your Organization for Growth and Prosperity, by Booz Allen Hamilton's Albert J. Viscio and Bruce A. Pasternak (Simon & Shuster, 1998)

About the Authors

Vinay Couto is a partner with Booz & Company based in Chicago. He leads the firm's global shared services and outsourcing advisory work.

Per-Ola Karlsson is a Booz & Company partner working in Stockholm. He leads the firm's European Organization and Strategic Leadership Practice.

Gary Neilson is a Booz & Company senior partner working in Chicago. He focuses on organizational transformation to increase effectiveness and efficiency for companies in North America.

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