

# Organizational Structure

A Guide for Sustainable Entrepreneurs

**SUSTAINABLE ENTREPRENEURSHIP PROJECT**

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# **Organizational Structure: A Guide for Sustainable Entrepreneurs**

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The Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)) engages in and promotes research, education and training activities relating to entrepreneurial ventures launched with the aspiration to create sustainable enterprises that achieve significant growth in scale and value creation through the development of innovative products or services which form the basis for a successful international business. In furtherance of its mission the Project is involved in the preparation and distribution of Libraries of Resources for Sustainable Entrepreneurs covering Entrepreneurship, Leadership, Management, Organizational Design, Organizational Culture, Strategic Planning, Governance, Corporate Social Responsibility, Compliance and Risk Management, Finance, Human Resources, Product Development and Commercialization, Technology Management, Globalization, and Managing Growth and Change. Each of the Libraries include various Project publications such as handbooks, guides, briefings, articles, checklists, forms, forms, videos and audio works and other resources; management tools such as checklists and questionnaires, forms and training materials; books; chapters or articles in books; articles in journals, newspapers and magazines; theses and dissertations; papers; government and other public domain publications; online articles and databases; blogs; websites; and webinars and podcasts.

## **About the Author**

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# Organizational Structure

## §1 Introduction

Organizational structure, one of the key issues for the organizational designer<sup>1</sup>, is the way in which the members of the organization and their job responsibilities are arranged. Organizational structure includes several important components including roles, relationships, responsibilities and scope of authority, and communications/reporting channels.<sup>2</sup> Organizational designers must consider what Pugh and Hickson referred to as the regularities for achieving activities such as task allocation, coordination and supervision.<sup>3</sup> Other researchers, such as Mintzberg and Schein, emphasized similar design activities and decisions that must necessarily focus on division and allocation of labor among required tasks, coordination of the activities associated with those tasks and establishment and administration of a hierarchy of authority.<sup>4</sup>

The organizational structure typically consists of various business units formed around functions (e.g., research and development, manufacturing, sales and marketing, finance, human resources, etc.), products, markets or customers that are arranged in a hierarchical fashion. The organizational structure determines how power, authority and accountability are formally distributed throughout the organization and obviously has a strong influence on how members (i.e., executives, managers and employees) and different business units interact with one another and the degree to which they will share information and collaborate to achieve the overall goals and objectives of the organization.

Optimally, the strategy selected for the organization will have the strongest influence on its organizational structure since research indicates that the most effective organizations are those that have been able to tightly align strategy and structure. As with the other elements of organizational design, organizational structure must be aligned with strategy. For example, if the strategy is based on identifying and satisfying the needs of a particular target group of customers the human and other resources of the organization should be grouped in the way that is most effective for creating and delivering the outputs demanded by the customers. In addition, however, factors other than strategy have been found to have a significant influence on organizational structure including the preferred styles of leaders and managers of the organization, the organizational climate and culture, the size and complexity of the organization, the skill capabilities of the members of the organization, the level of uncertainty in the organization's external operating environment, the cultural values and norms of the broader society in which the

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<sup>1</sup> For further discussion of the process of organizational design and the key issues for organizational designers, see "Organizational Design" prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

<sup>2</sup> W. Sexton, "Organization Structure", in W. Sexton (Ed.), *Organization Theories* (Columbus, OH: Charles E. Merrill, 1970).

<sup>3</sup> D. Pugh and D. Hickson, *Writers on Organizations* (4<sup>th</sup> Ed.) (London: Penguin Books, 1989).

<sup>4</sup> H. Mintzberg, *Structure in 5's: Designing Effective Organizations* (Englewood Cliffs, NJ: Prentice Hall, 1983; and E. Schein, *Organizational Culture and Leadership* (4<sup>th</sup> Ed.) (San Francisco, CA: The Jossey-Bass Business and Management Series, 2010).

organization is operating, the technology used in organizational activities, the geographic dispersion of the organization's activities, the origin and history of the organization, the type of ownership and control of the organization, and the degree of interdependence on other organizations.<sup>5</sup>

Every organization develops, or consciously designs, a structure that provides a foundation to allow it to conduct all of the activities necessary to meet its strategic goals and objectives.<sup>6</sup> While there are certain models (e.g., function-based, product-based, market-based or matrix structure) that can be used for reference there is no single structure that works for every organization. Instead, the persons charged with designing the organizational structure will need to start with some assumptions about the basic building blocks and then customize the structure to suit the specific situation of the organization at hand—its functional activities, the number and skills of its employees, the size of its business (i.e., revenues, product lines and markets), the geographic location of its various facilities, its strategic goals and objectives and the challenges and opportunities in its external environment that need to be addressed. Designing an appropriate and effective organizational structure can be extremely challenging, particular for rapidly growing and changing organizations, since all decisions regarding the height and breadth of the structure, and groupings of activities therein, involve difficult tradeoffs that must be carefully considered and frequently reevaluated.

## §2 Organizational studies and structure

Organizational structure has been an important concern for those involved in the formal study of organizations. Organizational studies, and the eventual emergence of modern management theory, began with the Industrial Revolution in the 19<sup>th</sup> Century and the subsequent evolution of business organizations toward mass production that occurred in the early 20<sup>th</sup> Century. The leading early organizational theorists included German engineer and sociologist Max Weber, Frederick Winslow Taylor in the United States and Henri Fayol in France, each of whom studied the way that organizations worked and attempted to identify universal rules and principals to be followed in order for organizations to achieve their highest levels of productivity and efficiency. While they each had different ideas the common thread was that organizations should be thought of as machines and, as a result, the preferred structural approach should be highly mechanistic and based on specialization of tasks, formal procedures and rules, and centralized authority.<sup>7</sup>

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<sup>5</sup> For detailed discussion of these factors, see R. Burton and B. Obel, *Strategic Organizational Analysis and Design: The Dynamics of Fit* (3<sup>rd</sup> Ed) (2004) and D. Pugh, D. Hickson, C. Hinings and C. Turner, *Dimensions of Organization Structure*, 13 *Administrative Science Quarterly* 65 (1968).

<sup>6</sup> While the primary focus of this Guide is on business organizations engaged in for-profit activities, and reference is commonly made to “companies” rather than organizations, this Guide uses the term “organization” throughout since this is the common practice of commentators that have conducted research on firms have organized the activities that need to be completed in order to generate revenues and profits.

<sup>7</sup> For further discussion of organizational studies, see “Organizational Studies” prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

Max Weber developed his theories about the impact of capitalism on society in the 19<sup>th</sup> century by observing industrial conditions in Europe and believed that firms would inevitably settle upon a “bureaucracy”, where control and authority is vested in positions rather than people, as the optimal form of organizational structure. While his theories did not attract wide attention until his writings were translated into English in 1949, they did have an impact on other management theorists who guided early organizational design practices in the United States. Taylor sought to turn industrial management into a serious academic discipline, which he referred to as “scientific management,” and claimed that scientific studies of time and motion could be used identify the “one best way” to complete the various tasks carried out in the workplace. Taylor emphasized the need to proactively select, train and develop employees, using scientific methods, rather than simply allowing employees to try and figure out how to do their jobs on their own. He also advocated a stronger and more formal role for managers in actually planning the work of employees and overseeing their performance using scientific management principles. Fayol’s primary contribution was identifying what he believed to be the key management functions within any organization—planning, organizing, commanding, coordinating and controlling. He also developed 14 principles of management, many of which can be found in what is now referred to as the traditional or classical organizational structure—specialization of labor, discipline, formal chain-of-command, subordination of individual interests, centralization and top-down authority.<sup>8</sup>

When put into practice these early management theories and maxims produced what is now referred to as the traditional or classical model of organizational structure—vertically-structured organizations in which the dominant features are high levels of task specialization, functional departments, hierarchical reporting structures, top-down authority and substantial reliance on formal rules, regulations and standardized operating procedures. The classical model can be seen in most of the large companies that fueled the growth of American industry in the first part of the 20<sup>th</sup> century and survived as the dominant mode of organization in the United States through the Great Depression and during and after World War II. However, as American businesses began to be confronted by the challenges of a more complex global economy, including intense competition from foreign firms following different organizational design principles, it became clear that the classical model was not necessarily the “one best way” to organize and manage work activities and that it may well be particularly ill suited to facilitating creativity and innovation and motivating employees.

A number of recent organizational theorists have suggested alternative models for identifying and selecting the appropriate organizational structure. For example, neoclassical or humanistic theory advocates a less formal organizational structure with lower levels of control and more emphasis on allowing decisions to be made at the point where the issue or problem is located by those persons at that level of the organization who are most familiar with the situation. Systems theory is based on the idea that an organization is really a complex social and technical system that requires human, financial and material resources and that each organization must create a specific

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<sup>8</sup> For further discussion of the theories of Weber, Taylor, Fayol and others, see “Organizational Studies” prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

structure that is particular suited to make it most efficient and productive. Proponents of the so-called “contingency approach” argue that the most important factor in organizational design is the organization’s operating environment and, specifically, the sources of uncertainty within that environment and they insist that organizations must be structured in a way that allows them to best control their external environment and quickly and effectively respond to contingencies that have been identified in advance.

The lesson of contingency theory is that there is no single “best structure” and each organization must determine which structure is best for it to deal with what goes on inside the organization (i.e., its internal environment) and the conditions in its chosen external environment. Factors and issues that contribute to the characteristics of the internal environment of an organization include the technology used in the organization’s business activities; the types of tasks and activities that must be performed by the organization in the course of its operations; the skills, training and attitudes of the managers and employees of the organization; the size of the organization; and the number and diversity of the organization’s products and markets. An organization’s external environment includes not only specific customers, suppliers, regulators and competitors, but also broader external environmental conditions—economic/technological; political/legal and social/cultural—which impose constraints and create opportunities that organizations must recognize and attempt to manage in order to be effective in their activities and achieve their stated goals. External environmental conditions not only influence and dictate organizational strategies they also determine essential and overriding characteristics of the work culture within the organization (i.e., the norms, values and attitudes regarding work and workplace relationships shared by managers and employees of the organization). In turn, the organizational work culture guides behaviors within the organization, both organizational processes such as structure and design and individual processes such as motivation and the ways in which organizational members interact with one another.<sup>9</sup>

### In Practice

#### Understanding the Basic Concepts of Organizational Structure

Leading early organizational theorists such as Max Weber, Frederick Winslow Taylor and Henri Fayol all argued, to some degree, that organizations can and should be structured in accordance with certain universal rules and principals. The result of all this was “bureaucracy” and “scientific management” that treated organizations as machines to be run in a mechanistic fashion relying on specialization of the strategy of the organization. For example, if the strategy is based on identifying and satisfying the needs of a particular target group of customers, the human and other resources of the organization should be grouped in the way that is most effective for creating and delivering the outputs demanded by those customers. In addition to strategy, other factors that are thought to have a significant

<sup>9</sup> R. Kanungo and A. Jaeger, *The Need for Indigenous Management in Developing Countries*, in A. Jaeger and R. Kanungo, *Management in Developing Countries 1* (1990). For further discussion of the influence of societal culture, an important element of an organization’s external environment, on organizational design and structure, see “Organizational Studies” in “Organizational Design: A Library of Resources for Sustainable Entrepreneurs” prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

tasks, formal procedures and rules and centralized authority. As time has gone by, however, the balance has shifted toward the so-called “contingency approach” based on the belief that the most important factor in designing the organizational structure is the organization’s operating environment and, specifically, the sources of uncertainty within that environment. If this is true, senior managers and those working with them on organizational design cannot rely on a single “best structure” for all situations and must instead search for a unique structure that allows them to best control their external environment and quickly and effectively respond to contingencies that have been identified in advance. This process can be difficult and time-consuming and should begin with making sure that the process of designing the organizational structure is understood. The questions below can serve as a means of getting started:

***What does the term “organizational structure” mean?*** Organizational structure is the way in which the members of an organization and their job responsibilities are arranged. The key components of an organizational structure include roles and responsibilities (task allocation), coordination processes and relationships between members and groups of members, hierarchical structure of power and authority (supervision), monitoring and control mechanisms and channels for communications and information flows.

***What are the building blocks of an organizational structure?*** The organizational structure typically consists of various business units (i.e., groups of organizational members supported by appropriate resources) formed around functions (e.g., research and development, manufacturing, sales and marketing, finance, human resources, etc.), products, markets or customers that are arranged in a hierarchical fashion. Eventually, many organizations evolve toward the use of some combination of two or more of these types (i.e., a “matrix” structure) as their activities continue to grow and become more complex.

***What are the most important influences on the design of the organizational structure?*** The most important determinant of organizational structure is

influence on organizational structure include the preferred styles of leaders and managers of the organization, the organizational climate and culture, the size and complexity of the organization, the skill capabilities of the members of the organization, the level of uncertainty in the organization’s external operating environment, the societal culture, the technology used in organizational activities, the geographic dispersion of the organization’s activities, the origin and history of the organization, the type of ownership and control of the organization and the degree of interdependence on other organizations.

***What dimensions are typically used for profiling and comparing organizational structures?***

Researchers generally rely on some or all of the following dimensions of organizational structure for their comparative work: specialization (i.e., division of labor); standardization (i.e., reliance of regularly used and legitimized organizational procedures); standardization of employment practices; formalization (i.e., used of formal rules and instruction to guide organizational members in carrying out their activities); centralization (i.e., location of decision making authority); methods of coordination; and configuration.

***What are the key questions and challenges for organizational designers?***

Organizational designers must wrestle with the appropriate degree of differentiation, both vertical and horizontal; the appropriate balance between differentiation and integration; the appropriate level of decentralization; and the appropriate balance between standardization and mutual adjustment.

***What are the most important goals and objectives when establishing the organizational structure?***

The organizational structure should relate well to the being pursued by the organization and its overall environment including competitors, suppliers, government agencies and the like; facilitate the use and effective exploitation of the core competencies of the organization including its people and technology; motivate the members; and promote the flow of information necessary for all members of the organization to perform their activities and tasks.

### §3 Key issues for designing the organizational structure

When researchers analyze the structure of an organization, or managers take on the challenge of creating the best design and structure for their organization, it is useful to

have a frame of reference for identifying the most salient questions. This frame of reference is based on a handful of dimensions of organizational structure. While, understandably, there is debate as to how many dimensions should be recognized and how they should be defined and measured it would appear to be reasonable to rely on the six dimensions of organizational structures that were identified by the Aston researchers: specialization (i.e., division of labor), standardization (i.e., reliance of regularly used and legitimized organizational procedures), standardization of employment practices, formalization (i.e., used of formal rules and instruction to guide organizational members in carrying out their activities), centralization (i.e., location of decision making authority) and configuration.<sup>10</sup>

This dimensional framework not only facilitates comparisons between different organizations it also suggests a short list of key questions and issues that managers everywhere must consider and answer regarding how the activities of their organization should be carried out.<sup>11</sup> First, the roles and responsibilities of each member of the organization, including executives, managers and employees, must be defined. Second, a hierarchical structure of authority and power must be established in order to identify the locus for decision making within the organization. Third, channels for communication and information flow should be created through the establishment of reporting rules and procedures. Fourth, mechanisms for monitoring and controlling the activities of the members should be established. Fifth, processes for coordinating the work activities of members positioned in different parts of the organizational structure should be developed and implemented. Finally, decisions need to be made about the dimensions that should be used a guide for grouping members of the organization to efficiently collaborate to produce the desired outputs (e.g., functional departments or product-focused business units). Each of these basic questions comes with a myriad of sub-issues. For example, when assessing how control will be exerted decisions must be made about the appropriate degree of centralization, spans of control and complexity of written rules and procedures.

When establishing the organizational structure the primary goal is to find the arrangement that is most effective in allowing the organization to achieve its overall goals and objectives and the organization must create a structure that relates well to the strategy being pursued by the organization and its overall environment including competitors, suppliers, government agencies and the like. In addition, the structure should facilitate the use and effective exploitation of the core competencies of the organization including its people and technology. It is also important to design the roles and responsibilities of each of the positions within the structure in a way that not only achieves the goals of the organization but which also motivates the members. This underscores the need for

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<sup>10</sup> See, e.g., D. Pugh, D. Hickson, C. Hinings and C. Turner, "Dimensions of Organization Structure", 13 *Administrative Science Quarterly* 65 (1968); J. Child and A. Kieser, "Organization and Managerial Roles in British and West German Companies: An Examination of the Culture-Free Thesis", in D. Hickson and C. McMillan (Eds), *Organization and Nations: The Aston Program IV* 51 (1980); and R Payne and D. Pugh, "Organizational Structure and Climate", in M. Dunnette (Ed), *Handbook of Industrial and Organizational Psychology* 1125 (1976).

<sup>11</sup> For detailed discussion of each of these questions, see "Challenges in Designing the Organizational Structure" in "Organizational Design: A Library of Resources for Sustainable Entrepreneurs" prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

structure to be aligned with human resources management policies and practices and the rewards systems used within the organization. Finally the chosen structure must be supported by processes and linking mechanisms that promote the flow of information necessary for all members of the organization to perform their activities and tasks.<sup>12</sup>

#### **§4 Building blocks of organizational structure**

While there are a large and ever increasing number of models of organizational structure there are nonetheless some basic building blocks that remain relatively constant and which should be familiar to those involved in designing the structure for any particular organization. First there is the specification of the roles to be played by each of the members of the organization. Organizational roles are generally assigned to specific positions and should be clearly defined by a set of tasks and activities and specification of authority and reporting responsibilities. The second fundamental building block is the way in which the organization creates formal units for groups of members with interrelated organizational roles. Common examples include functional departments, divisions and strategic business units and organizations may select from several dimensions (e.g., functions, products, geographic markets or customer types) when determining the most efficient structure. The last basic building block is the organizational chart, which depicts the choices made regarding the first two elements—organizational roles and business units.

#### **§5 --Organizational roles**

One of the first challenges confronting any organization as it begins to grow and bring on additional members is how best to allocate human and other resources to specific tasks and activities and how to establish lines of authority within the organization to ensure that these tasks and activities are completed in a manner that conforms to the performance standards necessary for the organization to achieve its strategic goals and objectives. These issues are referred to generally as “differentiation” and can be further broken down on two dimensions—vertical differentiation, which involves decisions about how authority and control should be distributed up and down the organizational structure among the various hierarchical levels; and horizontal differentiation, which involves decisions about how various work-related tasks and activities should be divided and grouped. The challenge for the organizational designer with respect to vertical differentiation is to determine how many levels should be included in the organizational hierarchy and how authority and responsibility should be distributed among them. As to horizontal differentiation, the designer must balance the need to establish and maintain an efficient degree of division of labor while still promoting the development of specialized skills among the organization’s human resources.

The foundation upon which differentiation occurs is the decisions made about the organizational roles that will be assigned to the various positions created within the organization to enable it to perform all the necessary tasks and activities. Each definition

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<sup>12</sup> See M. Jelinek, J. Litterer and R. Miles (Eds.), *Organization by Design: Theory and Practice*, (Business Publications, Inc., Plano, Texas, 1981).

of an organizational role includes all of the task-related behaviors that are expected of, and the responsibilities assigned to, any person asked to perform that role. Once a person is assigned an organizational role he or she can thereafter be held accountable for the resources that are provided by the organization to perform the role and for fulfilling the responsibilities assigned to the role. For example, if a salesperson is given a marketing budget to use for contacting new prospects and soliciting new orders he or she will ultimately be evaluated on the revenues and profits generated by those efforts. Put another way, the salesperson will be held accountable for how the cash resources in the budget were used and for whether or not he or she fulfilled his or her responsibility to build the organization's customer base.

Organizational roles cannot and must not exist in isolation and the structure of the organization is based on the decisions made about how the organizational roles should relate to each other and, in particular, how the persons performing each of the roles are expected to interact with persons performing other roles in the organization. One of the key issues is identifying which organizational roles will have authority over the activities carried out by persons occupying other roles. Authority includes the legitimate right to hold persons in roles subject to such authority accountable for the actions that are taken while carrying out the tasks associated with their roles. Authority also includes the power to control how specified organizational resources are used and the responsibility to coordinate the work of others subject to the authority and make sure that they are motivated to act in the best interests of the organization.

As an organization grows, and differentiation increases, the founders and initial senior managers select certain areas in which they wish or simply need to specialize at that time and define their own organizational roles accordingly. As with any other person assigned an organizational role each founder and senior manager will be assigned a certain amount of authority over persons and other resources and decisions should be made about how all of the members of the senior management group will interact with one another. Other necessary tasks and activities will be assigned to newly-defined organizational roles that hopefully will be filled by persons with the appropriate skills and experience to perform the relevant tasks. This is the process of specialization that allows the members of the organization to develop their individual skills and serve the organization in a way that fits best with their own interests and aptitudes. Done correctly and consistently, specialization will ultimately lead to creation of a core competency that the organization can use as a strategic advantage. However, specialization, or differentiation, must be carefully balanced with integration to ensure that members of the organization continue to collaborate on projects that require the skills of multiple organizational roles.

## **§6 --Organizational units**

As an organization grows, and the level of differentiation increases, the managers of the organization begin to structure the activities of the organization by grouping positions that perform similar or related organizational roles into formal organizational units. The two most common forms of organizational units are functions, sometimes referred to as departments, and divisions. Functional units include positions that require similar skills,

training and experience and which use the same types of knowledge, tools, procedures and techniques in order to perform the tasks associated with each of the positions included within the unit. Katz and Kahn have usefully broken out functional units into several broad categories of functional tasks—support (e.g., purchasing or procurement, sales and marketing, legal and public relations); production (e.g., operations, production control and quality control); maintenance (e.g., personnel or human resources, engineering and maintenance or janitorial services); and adaptive (e.g., research and development, market research and strategic planning). They also recognized a managerial function that focuses on specific aspects of controlling and coordinating the activities of the organization in order for it operate efficiently and achieve its goals and objectives.<sup>13</sup>

Divisional units include two or more functional units which, acting together, are responsible for the production of specific products and services and, in many case, additional tasks and activities associated with creating value for the organization from the marketing and sale of such products and services. The number of functional and divisional units created and operated by a company is a good measure of the level of complexity of, and degree of differentiation within, the organizational structure. For example, during the early stages of a new organization it is likely that the organizational structure will include a modest number of functional units (i.e., only departments that are absolutely necessary to develop and produce the initial product or service) and no divisional units since there is only a single product or service to manage. At the other extreme, however, is the large global organization that will have hundreds of divisional units, generally product- or geographic-focused divisions or subsidiaries, widely disbursed around the world.

## §7 --Organization chart

The most common method for depicting the structure of an organization is the “organization chart”, which shows the division of work activities among various functional and division units, the formal hierarchy of authority and the way in which people and units within the organization are expected to relate to one another. The organization chart provides an overview of who does what within the organization and at whose direction these activities are carried out. The traditional form of organization chart includes boxes for each important organizational role or unit (i.e., function or division). The next level of detail on the chart is a box for each of the key positions in the organization and each box has a line connecting it to the applicable immediate supervisor that defines the primary reporting relationship for the position. By looking at the organization chart one can quickly determine the authority of a position by looking at how high on the chart it is, how many subordinate positions report to it, and how many activities must be integrated through the position. The summary information on the organization chart is typically supported by job descriptions that detail the tasks to be performed; the skills necessary to perform the tasks; and the qualifications, education

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<sup>13</sup> See D. Katz and R.L. Kahn, the Social Psychology of Organizing (New York: Wiley, 1966).

and/or experience considered to be necessary in order to perform the responsibilities of the position.<sup>14</sup>

The organizational chart can provide valuable information about the decisions that have been made with respect to vertical and horizontal differentiation within the structure of the organization. Looking at an organizational chart vertically, from top to bottom, gives the reader an idea of the hierarchical structure of the organization and the way in which the organizational roles relate to one another with respect to authority, rank and accountability. The organizational roles that are located at the top of the organizational chart, including the CEO and the members of the senior executive team, have more authority and responsibility than the organizational roles that are lower on the chart. When the organizational chart is examined horizontally, from side to side, the reader can learn how the organization has decided to divide the labor associated with the activities of the company into specific organizational roles and then, as the organization grows, aggregate related organizational roles into functions or divisions.

As helpful as it can be the organization chart does have significant limitations. For example, the charts does not generally include information on the various policies and practices of the organization with respect to key issues such as planning and control, compensation, promotion and recruitment. In addition, every organization has its own set of informal structures that arise in response to the formal structure and the personalities and attitudes of the specific and unique individuals that make the organization run. As such, in order to understand how the organization really works it is necessary to identify four important facets of organizational structure—the formal set of organizational interrelationships depicted on the organization chart, the job descriptions and responsibilities, organizational policies and practices, and the casual and spontaneous communications that arise outside of the formal direction of management (i.e., the organizational culture). Another complicating factor is that the boundaries of the organization chart are typically limited to the organization's own units and do not take into account resources available from, and relationships with, strategic alliance partners and other key external vendors such as outsourcing services providers.

Organizations should consider how information materials, such as a formal manual, and additional training and communications can be used to describe the organizational structure and provide managers and employees with a guide to how the work of the organization will be divided and coordinated. Without this information, members will encounter problems in completing their tasks and thus may experience high levels of stress and anxiety. This process should begin from the very first day that new members join the organization with an explanation of the organization chart and any additional chart or diagrams that may have been prepared to outline work activities in a particular functional or divisional unit. New members should be provided with a copy of the organization chart and a follow up meeting should be scheduled for soon after the member arrives to spend additional time explaining the structure of the organization and how the member's unit, and specific job duties, fits into the overall work flow.

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<sup>14</sup> S. Power, "Organizational Structure," in Carl Heyel and Belden Menkus, *Handbook of Management for the Growing Business* (New York: Van Nostrand Reinhold Company, 1986), 404.

## §8 Influence of societal culture on organizational structure

Two main hypotheses dominate the discussion of, and research on, the influence of societal culture on organizational structure across nations. The first hypothesis is often referred to as the “culture-free” hypothesis and suggests, in the words of Holt, “that culture has no influence on the way organizations are structured and is supported with significant research showing organizations within many nations around the world reflect the same relationships between size, specialization, formalization, and decentralization”.<sup>15</sup> Holt noted that “[t]he culture-free hypothesis is best represented by the research of Hickson and his associates”, who were among the first to take advantage of a framework developed by researchers originally affiliated with the University of Aston that became widely used as the basis for standardized cross-national analysis of both organizational structure and context.<sup>16</sup> The studies conducted by the Aston researchers led them to conclude that “[s]ize and dependence . . . [are] . . . the bases for an explanation of the broad features of organizations worldwide”.<sup>17</sup> In fact, they argued that the relationships that “the relationships between the structural characteristics (structuring of activities and concentration of authority) and variables of organizational context (size, operation, technology and ownership) will be stable across cultures”.<sup>18</sup>

The culture-free hypothesis described above is part of a larger theory of a “logic of industrialism” that predicts and requires certain universal changes that all firms, regardless of the societal culture in which they operate, must make as they develop and move toward large-scale industrialism.<sup>19</sup> However, while the proponents of the culture-

<sup>15</sup> M. Holt, “Culture-Free or Culture-Bound?: Two Views of Swaying Branches”, 1(3) *International Journal of Business, Humanities and Technology* 80 (2011).

<sup>16</sup> Id. For more information on the Aston Program, see D. Hickson and C. McMillan, *Organizations and Nations: The Aston Program IV* (1981); D. Hickson, C. Hinings, C. McMillan and J. Schwitter, “The Culture-Free Context of Organization Structure: A Tri-National Comparison”, *Sociology* 59 (1974); D. Pugh, D. Hickson and the Open University Course Team, *Organizational Context and Structure in Various Cultures*, in T. Weinsall (Ed), *Societal Culture and Management* (1993), 425.

<sup>17</sup> D. Pugh, D. Hickson and the Open University Course Team, *Organizational Context and Structure in Various Cultures*, in T. Weinsall (Ed), *Societal Culture and Management* (1993), 425, 433. The size of the organization was measured by the number of employees and “dependence” was measured by various factors such as organizational status (i.e., branch, head branch, subsidiary or principal unit), public accountability (i.e., ownership), integration with suppliers and dependence on its largest customer. Id. at 430.

<sup>18</sup> H. Sabri, “Do Power Distance and Uncertainty-avoidance Determine Organizational Structure?: A Culture Bound versus Culture Free Debate”, 11(3) *The International Journal of Knowledge, Culture and Change Management*, 11(3) (2012), 131.

<sup>19</sup> M. Holt, “Culture-Free or Culture-Bound?: Two Views of Swaying Branches”, *International Journal of Business, Humanities and Technology*, 1(3) (2011), 81 (citing F. Harbison and C. Myers, *Management in the Industrial World: An International Analysis* (1959); and C. Kerr, J. Dunlop, F. Harbison and C. Myers, *Industrialism and Industrial Man* (1960)). According to Pugh et al., the “logic of industrialism” has its roots in the arguments first made in the 1960s that industrialism driven by science and technology is a worldwide phenomenon that will advance independent from any specific government or culture and will ultimately lead to global convergence. See D. Pugh, T. Clark and G. Mallory, *Organization Structure and Structural Change in European Manufacturing Organizations*, 168 *Verhandelingen Letterkunde, Nieuwe Reeks* 225-238, 225-226 (1996) (citing C. Kerr, J. Dunlop, F. Harbison and C. Myers, *Industrialism and Industrial Man* (1960)).

free hypothesis were quite active and persuasive, other researchers had significant questions. For example, a study of oil refineries in Britain and France conducted by Gallie in 1978 failed to support the culture-free position and, in fact, Gallie discovered differences in attitudes and relations with managers between the British and French workers that were so substantial that he was led to conclude that such difference could only be understood by taking into account cultural influences.<sup>20</sup> Other studies conducted over a number of decades have also concluded that the culture-free hypothesis was incomplete and that it was necessary to take the cultural context of the organization into account to explain decisions about organizational structure.<sup>21</sup> All this eventually led to the formalization of “culture-bound” hypothesis, a term that was coined by Hofstede in one of his earlier publications and which holds that there are indeed differences among cultures as to many internal organizational features.<sup>22</sup>

Hofstede and others have argued strongly and consistently that “people, in different cultures, react to organizational problems according to their implicit model of how organizations should be structured” and that “[t]his means that, other factors being equal, people from a particular national background will prefer a particular structure because it fits their implicit model of structure, and similar organizations in different countries will resemble different types because of different cultural preferences”.<sup>23</sup> For example, Hofstede argued that his cultural dimensions of power distance and uncertainty avoidance should, along with specific demands of the activities engaged in by the organization and the technology used by the organization in those activities, be strong predictors of the

<sup>20</sup> D. Gallie, *In search of the new working class: Automation and social integration within the capitalist enterprise* (Cambridge, England: Cambridge University Press, 1978).

<sup>21</sup> See, e.g., J. Child and A. Kieser, “Organizational and managerial roles in British and West German Companies: An examination of the culture-free thesis” in T. Weinsall, *Societal culture and management* (New York: Walter de Gruyter, 1993), 455-477; P. Clark, “Cultural context as a determinant of organizational rationality: A comparison of the tobacco industries in Britain and France” in C. Lammers and D. Hickson, *Organizations alike and unlike: International and interinstitutional studies in the sociology of organization* (London: Routledge & Kegan Paul, 1979), 272-286; G. Hofstede, “Hierarchical power distance in forty countries” in C. Lammers and D. Hickson, *Organizations alike and unlike: International and interinstitutional studies in the sociology of organization* (London: Routledge & Kegan Paul, 1979), 97-119; G. Hofstede and G.J. Hofstede, *Cultures and Organizations: Software of the mind* (New York: McGraw-Hill, 2005); M. Tayeb, “Japanese management style” in R. Daily, *Organisational Behaviour* (London: Pitman, 1990), 257-282; and M. Tayeb, “Organizations and national culture: Methodology considered”, *Organization Studies*, 1994, 429-446.

<sup>22</sup> In 1984 Hofstede argued that organizations were “culture bound” and members of a particular national societal culture would prefer a specific organizational structure because it fit well with the “implicit model of design” that they had in their minds and which Hofstede famously referred to as the “software of their minds”. The natural consequence of this argument that organizations in different countries, even though engaged in similar activities, would have different structures due to differences in the cultural preferences. See G. Hofstede, *Culture’s Consequences: International Differences in Work-Related Values* (1984).

<sup>23</sup> H. Sabri, “Do Power Distance and Uncertainty-avoidance Determine Organizational Structure?: A Culture Bound versus Culture Free Debate”, *The International Journal of Knowledge, Culture and Change Management*, 11(3) (2012), 131. Other researchers that have argued that culture influences organizational structure include C. Handy, *Gods of Management* (3<sup>rd</sup> Ed.) (1991); D. Pheysey, *Organizational Culture: Types and Transformation* (1993); J. Mannen and S. Barley, *Cultural Organization: Fragments of a Theory*, in P. Frost, L. Moore, M. Louis, C. Lundberg and J. Martin (Eds), *Organizational Culture* (1985) and M. Al-Tayeb, *Organizations and National Culture: A Comparative Analysis* (1988).

optimal form of organizational structure.<sup>24</sup> While other researchers, such as Sabri, were not able to confirm the predictive value of Hofstede's cultural dimensions with respect to organizational structure in various societies<sup>25</sup> evidence gathered from cross-country studies and comparative analysis of managerial "control practices" in France, Britain and Germany allowed Horowitz to propose a list of several "local factors" that might be relevant in determining which control mechanisms are preferred in a particular country: the impact of educational backgrounds, including training in particular areas relating to establishment and administration of control systems; the desired level of sophistication in planning required for the operations of the particular firm; and, finally, the impact of societal beliefs and attitudes towards authority and centralism (i.e., culture).<sup>26</sup>

After reviewing the research and arguments on both sides of the debate, Holt concluded that "[t]he evidence of cultural differences between nations is overwhelming" and that "one cannot base a prediction on structure or process from a single cultural dimension".<sup>27</sup> Holt argued that "[a]s people share a common culture system they are likely to influence the organizations they enter" and culturally-based assumptions regarding "[t]he patterns of relationships, rules and belief systems, expectations about authority and its legitimate use, an individual's rights and obligations to the collective all influence the structure of organizations".<sup>28</sup> Holt believed that "[i]f two nations have differing cultural orientations there should be tendencies toward differing patterns of organizational structure within those nations".<sup>29</sup> Another strong, and succinct, statement of the culture-bound hypothesis was offered by Axelsson et al., who wrote: ". . . human preferences and decisions which are shaped by the values within society are refracted through individual personalities. Therefore, the organization and the behaviour of those associated with it must reflect the characteristics of the surrounding culture. There may be structural regularities across national cultures, but they are relatively unimportant in the face of the substantial differences in the ways that individuals interact and in the views they hold of the organization's place in its environment."<sup>30</sup>

<sup>24</sup> G. Hofstede, *Culture's Consequences: International Differences in Work-Related Values* (1984). This made sense to Hofstede because these two dimensions certainly influenced organizational structure since they helped to answer two critical questions that must be addressed by the organizational designer: "who has the power to decide what (hierarchy)? And what rules or procedures will be followed to reach the desired organizational goals (formalization)?" G. Hofstede, *Cultures and Organizations, Software of the Mind* 42 (1991). For further discussion, see "Organizational Studies" prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

<sup>25</sup> H. Sabri, "Do Power Distance and Uncertainty-avoidance Determine Organizational Structure?: A Culture Bound versus Culture Free Debate", *The International Journal of Knowledge, Culture and Change Management*, 11(3) (2012), 131.

<sup>26</sup> J. Horowitz, "Management Control in France, Great Britain and Germany", in T. Weinsall, *Societal Culture and Management* 445, 454 (1993).

<sup>27</sup> M. Holt, "Culture-Free or Culture-Bound?: Two Views of Swaying Branches", *International Journal of Business, Humanities and Technology*, 1(3) (2011), 83.

<sup>28</sup> Id.

<sup>29</sup> Id.

<sup>30</sup> R. Axelsson, D. Cray, G. Mallory and D. Wilson, "Decision Style in British and Swedish Organizations: A Comparative Examination of Strategic Decision-Making", *British Journal of Management*, 2 (1991) 67, 68.

There have been a variety of attempts to suggest models of organizational structures that might be used for comparisons across national or cultural borders. For example, the Aston researchers suggested a topology of organizational structure that included the following four forms based on two key dimensions—the degree of concentration of authority and the degree of structuring activities: workflow bureaucracies; personnel bureaucracies; full bureaucracies; and non-bureaucracies/implicitly structured.<sup>31</sup> Later, Hofstede and others appeared with their ideas of an “implicit model” of organizations based on empirical measures of a country’s place on the power distance and uncertainty avoidance dimensions of Hofstede’s broader scheme for describing and contrasting societal cultures. Power distance was assumed to correlate with the degree of organizational hierarchy—the higher the power distance the more hierarchical the organization—and uncertainty avoidance was assumed to correlate with the degree of formalization—a higher desire for avoiding uncertainty led to more formalization within the organizational structure. Their suggested typology also included four types of organizational structure: the “village market”; the “well-oiled machine”; the “family” (or “tribe”); and the “traditional bureaucracy (or “pyramid of people”).<sup>32</sup> Other entrants in the effort to develop a typology of organizational structures have included Mintzberg, the ITIM Culture and Management Consultancy, Laurent, and Rieger and Wong-Rieger.<sup>33</sup>

## §9 Evolution of the organizational structure

When an organization has just been launched and only a small number of persons are involved there is generally ample opportunity for face-to-face communication among the members of the group and the need for a formal organizational structure is generally low provided that sufficient attention is paid to strategic planning and setting mutually agreed goals and objectives. At that point the founders and other members of the organization can generally allocate and organize work activities based on their skills, experience and preferences and the organizational structure, to the extent one exists, will generally be organic with a flat hierarchy and strong reliance on informal norms and values to control the activities and interactions of all of the members of the organization. The founders are generally involved in most of the decisions relating to the activities of the organization

<sup>31</sup> See D. Hickson and D. Pugh, *Management Worldwide: Distinctive Styles Amid Globalization* (2d Ed) (2001). For further discussion, see “Organizational Studies” prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

<sup>32</sup> See G. Hofstede, “Motivation, Leadership and Organization: Do American Theories Apply Abroad?”, *Organization Dynamics*, 9 (1980), 42, 51-54; G. Hofstede, *Cultures and Organizations* (1991), 54; and S. Schneider and J.-L. Barsoux, *Managing Across Cultures* (2<sup>nd</sup> Ed.) (2002). For further discussion, see “Organizational Studies” prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

<sup>33</sup> See H. Mintzberg, *Structures in Fives: Designing Effective Organizations* (1983); H. Wursten, *Culture and Change Management*, ITIM Culture and Management Consultancy, <http://www.itim.org/articleonchangemanagement.pdf>; A. Laurent, *The Cultural Diversity of Western Conceptions of Management*, in *International Studies of Management and Organization* (Vol. XIII, Nos. 1-2, *Cross-Cultural Management II: Empirical Studies* 75 (Spring-Summer 1983); and F. Rieger and D. Wong-Rieger, *Organization and Culture in Developing Countries: A Configurational Model*, in A. Jaeger and R. Kanungo, *Management in Developing Countries* 101 (1990). For further discussion, see “Organizational Studies” prepared and distributed by the Sustainable Entrepreneurship Project ([www.seproject.org](http://www.seproject.org)).

and other members of the organization can usually count on easy access to the founders to discuss ideas and concerns. In fact, the most popular method for passing along role assignments within top performing smaller organizations is informal conversation. Much less popular, although used with some frequency, is written job descriptions and meetings. The founders are also more directly involved in designing and monitoring role assignments in top performing organizations. If input is needed from other members it can be obtained quickly and efficiently and news of significant events, such as the outcome of a meeting with a new vendor or customer, can be conveyed in real time without the trouble and expense of creating and maintaining formal information and communications processes.

As organizations grow from very small (i.e., less than 20 employees) to relatively large (i.e., 80 or more employees), one notes significant changes in the management of workflow and structure becomes an important managerial challenge. At some point the range of activities and tasks that need to be performed within the organization expands to the point where the founders no longer have the time and skill to personally oversee all of them. The founders are forced to delegate responsibilities and decision making authority to new executives who join the founders as the leaders of the organization, generally focusing on specific functional areas (i.e., an increase in specialization). As new employees join the organization more managers must also be brought in to provide the direct supervision that the founders and other senior executives can no longer offer and the result is the creation of a traditional chain in command structure accompanied by an inevitable increase in the number of hierarchical levels within the organization structure.

With regard to assignment of work and coordination of workflow the CEO begins to abandon reliance on informal conversations and turns to alternative methods such as formal meetings, written guidelines and pre-established roles and definitions and descriptions of jobs. Policies must become more formal as the organization grows in order to protect the organization against potential legal and regulatory liabilities. However, organizations must walk a fine line in this area and exercise caution against excessive reliance on written guidelines to coordinate workflow. Care should also be taken when developing and using job descriptions since they may be used as excuses for some employees for not doing necessary work based on the fact that it was not part of their job description. In order to compensate for the inability of the CEO to directly supervise all activities as the organization grows, larger organizations also begin to rely more heavily on formal monitoring of quality, production and costs and regular comparison of performance in those areas against budgeted targets and goals. This is not necessarily a negative development and it is generally recommended that even the smallest organizations establish objective work standards and targets and then invest in monitoring systems to compare actual performance against the goals that have been set. When selecting and implementing monitoring systems, organizations should seek out standardized software programs that are already customized to the specific market or industry.

In order for delegation to be executed effectively the organization must create a formal structure that provides employees with guidance on what they can and cannot do and who

they are responsible to and managers with a definition of the scope of their authority including which employees they are responsible for and will be reporting to them. This means tying responsibilities and authority to positions defined by the designers of the organizational structure that will then need to be filled by current or new employees thought to be best suited to effectively discharge the responsibilities associated with the position. Changes will also be needed with respect to the processes used by the organization for communication and sharing of information and organizations typically adopt and attempt to enforce more rules and standard operating procedures as further support for the efforts of management to control and supervise.<sup>34</sup>

The end result of all of the changes that occur as the organization grows is a slow and often invisible and unintended transformation to a mechanistic organizational structure that can create significant operational issues for the senior executives of the organization including slower decision making processes, poor information flow and problems with coordination. At that point, affirmative steps need to be taken to try and reverse the evolutionary movement of the organizational structure to retain the spirit of innovation that prevailed when the firm was first launched and everyone knew one another and could communicate and collaborate easily and quickly. The first thing to remember is that while the CEO can, and ultimately must, delegate decisions regarding daily operations to subordinates he or she must nonetheless retain authority and responsibility for performance standards and setting the overall direction of the organization. Second, as the size of the organization grows and activities become more complex there should be greater reliance on group problem-solving techniques as opposed to creating stifling and cumbersome bureaucratic structures. The CEO should use meetings and teams while maintaining control over the most important strategic and operational aspects of the organization. Meetings can and should be used to review actual performance against work standards and targets and as group problem-solving sessions to address issues ranging from productivity to morale. The CEO should also use meeting as an opportunity to reinforce work standards and cultural values. Finally, a concerted effort must be made to identify and remove unnecessary levels of management, decentralize authority, standardize routine tasks and activities to free managers and employees to concentrate on more creative projects and improve automated information processing capabilities so that reporting channels can be eliminated or streamlined. Obviously these changes will not be easy to implement and rarely can be done within substantial disruption to day-to-day operations. Personnel changes, including elimination managerial positions and alterations to reporting channels, can cause stress among workers and endanger morale and increased reliance on automated information processing may require large investments in equipment and training. Nonetheless, the organization may have little choice if it wishes to remain competitive in its chosen domain.

Additional changes in the structure will be needed as the organization continues to grow and/or modifications are made to the organizational strategy. Organizational design is a dynamic process and the structure of the organization should continuously evolve over time in order to adapt to changes in the environment in which the organization operates.

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<sup>34</sup> S. Power, "Organizational Structure," in C. Heyel and B. Menkus, *Handbook of Management for the Growing Business* (New York: Van Nostrand Reinhold Company, 1986), 403.

However, changing the structure of an organization can be a difficult task, particularly when the members of the organizations have been operating in a certain way for an extended period of time. Implementing changes in organizational structure requires the investment of substantial human and financial resources and it is often impossible to accurately predict in advance how long it will take for the change to take effect and whether the change will produce the desired results. These challenges explain why organizations change their structures infrequently and also underscore the importance of carefully considering structural issues before the organization embarks on new growth or shifts existing resources toward a different strategic objective.

### References and Resources

The Sustainable Entrepreneurship Project's Library of Resources for Sustainable Entrepreneurs relating to Organizational Design is available at <https://seproject.org/organizational-design/> and includes materials relating to the subject matters of this Guide including various Project publications such as handbooks, guides, briefings, articles, checklists, forms, forms, videos and audio works and other resources; management tools such as checklists and questionnaires, forms and training materials; books; chapters or articles in books; articles in journals, newspapers and magazines; theses and dissertations; papers; government and other public domain publications; online articles and databases; blogs; websites; and webinars and podcasts. Changes to the Library are made on a continuous basis and notifications of changes, as well as new versions of this Guide, will be provided to readers that enter their names on the Project mailing list by following the procedures on the Project's website.

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