

10

Structure

Design, governance, and style

“No matter which structure you land on, it’s always the clarity of definition around roles and responsibilities—and communication, communication, communication—that will determine the success of your matrix model.”

—Phil Rohrbaugh, Vice Chair of the U.S. firm and
Managing Partner of the Chicago office, KPMG

“You need to have a governance system in which the authority and the responsibility to make certain decisions is assigned to a set group of people so the aircraft carrier of a law firm can navigate the seas.”

—Ralph Baxter, Chairman and CEO, Orrick

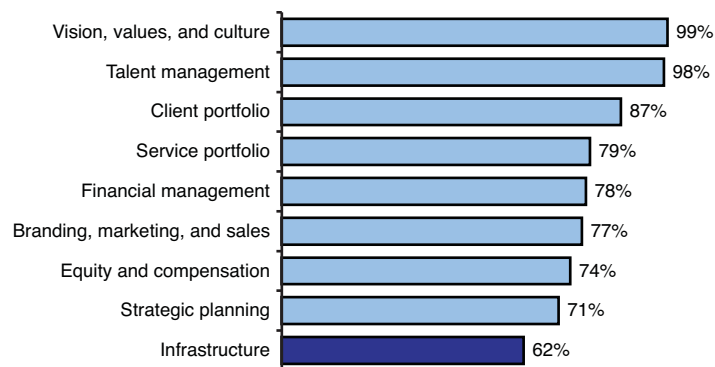
“We really hate bureaucracy. That is why we are pretty flat and there is not a lot of politics happening here.”

—Donna Imperato, President and CEO, Cohn & Wolfe

The choice of organizational structure and governance model has critical implications for professional service firms. Together they form a firm’s internal architecture—the invisible scaffolding that supports everything, from day-to-day operations to strategic planning and effective execution. The structure delineates the organizational layers and management reporting hierarchies within the firm. Governance is the leadership style—collaborative, dictatorial, or corporate—and the policies, systems, and procedures that underpin the enterprise. Organization design choices can reinforce or undermine culture, endanger or enhance performance and service quality, and enable or diminish profitability.

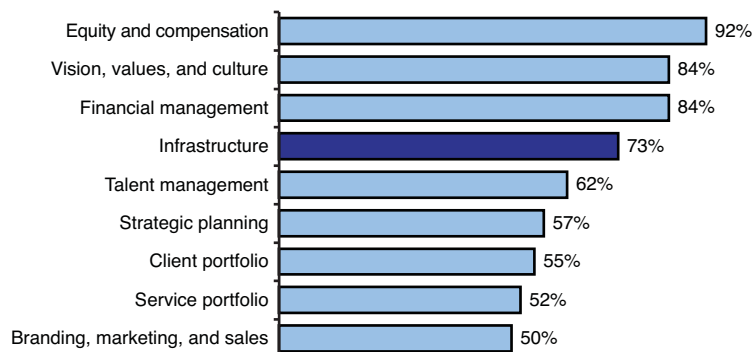
Talking about organizational charts, management layers, policies and procedures—the nuts and bolts of how a firm organizes to conduct business and make decisions—wasn't a particularly passionate topic for our interviewees. Organization structure and governance ranked lowest on the leadership agenda. However, it still was very much on the list of priorities, with 62 percent of the interviewees giving it top marks, as shown in Exhibit 10.1.

EXHIBIT 10.1 Infrastructure and governance ranked last in order of importance



Firm leaders agreed that, although not as sexy as values or culture, decisions related to structure and governance are a vital component to success and long-term viability and an essential piece of the management mosaic. In fact, interviewees rated their performance fairly high in this area, with 73 percent giving themselves good or excellent reviews for having an effective organizational structure and governance model, as shown in Exhibit 10.2.

EXHIBIT 10.2 Three-quarters believe they do a good job managing infrastructure



Why Getting It Right Is So Challenging

“The challenge is how to find the right structure to make sure that you execute effectively on your strategy.”

“I don’t think a year passes that we don’t make some changes to the organizational model to better address the complex needs and dynamic nature of the firm.”

“One of the problems with scale is that unmanaged autonomy can be catastrophic.”

In traditional command-and-control environments, the distinction between leaders and followers is clearly defined, and hierarchical decision making predominates. The opposite is true in a partner/owner enterprise, where the prevailing model is a network of peers, and major decisions must always involve a high degree of consensus. Professionals need and demand generous doses of freedom and flexibility in practicing their skills and serving clients. If they believe their firm’s structure and/or governance approach undermine rather than support their independence, even the most disciplined and loyal of professionals is likely to ignore or bypass them.

Like traditional corporations, professional service firms need an effective structure to support and coordinate the business of serving clients in a profitable manner. For firm leaders, the toughest challenge is crafting an organizational model that gives professionals independence to operate creatively within a stable, efficient infrastructure. Many firms find that there is a fine line between too much freedom and too much bureaucracy.

To further complicate the decision process, there is no one-size-fits-all approach to structuring a professional service business. Just as there is no ideal strategy or execution model, there is no perfect organizational structure. The real key is alignment with a firm’s values, culture, and strategic direction. As one firm leader noted, “I think that the vision, the values, and the culture drive the organization more than its structure. You can succeed with multiple variations of infrastructure and governance.”

Organization design is not a rigid process, but an evolutionary one. Structures must evolve over time to adapt to changes in firm direction and growth. Many of the firms that participated in the study have changed structures several times during the course of their life cycle. Firm leaders agree that structure is a useful lever to employ to keep the business running smoothly and to stimulate growth and change the firm’s direction. However, adeptly managing the structure lever is an art in itself.

Seven Essentials for a Successful Infrastructure and Governance Model

“I really believe if you want to improve an organization, you need to change it. An organization that is going to be sustaining and is going to succeed in the long run is an organization that’s able to adapt to the constant flux and the constant change that the environment creates.”

When it comes to operating efficiently and having a well-oiled governance mechanism in place for top-level decision making, the best-run firms share seven defining characteristics. Specifically, these high-performing enterprises do the following:

1. *Embrace a one-firm concept.* Successful firms strive to cultivate a one-firm mind-set by developing organization structures that foster a collaborative, rather than siloed, operating environment. While aggressively pursuing global expansion via organic growth and/or acquisitions, they work hard to ensure that increased scale does not erode their one-firm spirit of collegiality and service.
2. *Operate transparently.* Closed-door decision making by a single leader or small leadership cadre is not a recipe for success in a consensus-driven culture. For the partner/owner model to work, everyone must feel that they’ve been heard and have participated in debating and resolving key issues. At the very least, they must completely understand and approve of the decision-making process. The most effective leaders are those who provide both access and action. They are adept at walking the line between ensuring that professionals feel they have a participative role in setting a firm’s direction and making the hard choices required to move forward.
3. *Train professionals in business skills.* Star performers rise to the top of their firms based on their professional acumen, not their business skills. As a result, the fundamentals of running a business efficiently and profitably are often well outside their knowledge base. And yet, as firms grow larger and more complex, a blend of professional expertise and business savvy is becoming essential. PSFs operate most effectively when they can tap into a strong team of professionals who are proven client relationship builders with a strong grasp of business practices and bottom-line realities. More and more firms are seeing the benefits of adding executive skills to their professional development mix. Increasingly, firms are providing MBA-type

training to senior professionals to better prepare them for the multifaceted responsibilities they face as they rise to leadership positions.

4. *Use professional nonbillable support teams.* Although they want professionals to be exposed to business basics, successful service firms stick to their knitting. When it comes to managing operations, they hire sophisticated administrative executives and give them wide latitude within their areas of responsibility. Over the years, noncore functions—finance, marketing, information services, and human resources—have grown increasingly professionalized. Across all industry segments, professional service businesses are cautiously adding new slots to their organization charts by bringing onboard COOs, CFOs, CMOs, CIOs, and CHROs. As firms seek to build strong administrative teams, many are acknowledging the importance of these roles by putting the executives who hold these positions on their management committees.
5. *Emphasize process efficiency.* The best-run firms strive to ensure that their revenue-producing professionals focus the lion's share of their time and talent on client work and relationship building. These firms invest substantially in systems and support mechanisms to boost internal efficiency and speed service delivery. To streamline their operations, they take aggressive advantage of technology to build cost-effective back-office operations. To enhance efficiency and reduce costs, leading-edge firms are using global integration tools employed by traditional multinationals, from shared services to outsourcing and offshoring (see “Clifford Chance Offshoring Program”).
6. *Clearly define roles and responsibilities, policies and procedures.* Reporting relationships can be particularly confusing in a multi-service, multiproject professional service firm. At any given point in time, professionals—even senior partners—report to multiple people and have multiple people reporting to them. The lines of who is doing what and for whom are often blurred and change regularly as client projects come and go. The best-run firms map roles with care so that whatever hat or hats a professional is wearing—engagement manager, business unit leader, practice group head, trainer, or mentor—the responsibilities are well defined. Performance against expectations are monitored and measured to determine progression in the firm as well as annual compensation.

In addition to defining roles, the day-to-day business of running the firm is well established and documented. Policies and guidelines from quality assurance to client and engagement management

Clifford Chance Offshoring Program

With 3,600 lawyers in 29 offices across 20 countries, Clifford Chance is one of the world's leading law firms. In 2006, the firm began to explore the pros and cons of centralizing and offshoring some of its business services. According to David Childs, Global Managing Partner, the shared service concept provided an attractive opportunity to reduce costs, improve efficiency, and standardize service quality and consistency.

The firm established its Shared Services Center outside New Delhi in 2007. The Center's 300-plus people manage about 10 percent of the firm's business service functions including human resources, finance, IT, business development, and administration. In addition, the firm established a separate program called Knowledge Center India, which engages in paralegal-level activities such as research, due diligence, and document drafting for Clifford Chance offices. Amanda Burton, Chief Operating Officer, who led the development of the Center and now oversees its operations, offers the following advice to firms considering an offshoring option:

- *Do what's right for your firm.* Given the investment involved, scale is key to making this option work. It's important to weigh offshore pros and cons carefully in light of your firm's size, growth strategy, and centralizing capabilities.
- *Investigate other industries.* Look beyond your own industry to identify innovative approaches and new ideas. When the firm began to explore offshoring, Burton talked to many clients in financial services, who offered valuable do's and don'ts—and also reaffirmed their own decisions to pursue this option.
- *Choose the right location.* Clifford Chance selected New Delhi for several reasons: English language capability, a strong talent base which included several good law schools, 24/7 coverage, and cost.
- *Treat offshoring as a major project.* If you pursue an offshore strategy, have a strong business case, project plan, and launch, timetable to roll out, and the people capable of delivering the desired results: The firm imported a Clifford Chance lawyer to set up the Knowledge Center and sends an attorney every 6 months to train and oversee the paralegal team. "Offshoring is a big commitment," says Burton. "People worry about their jobs and how shifting administrative and/or knowledge-based activities offshore

will affect their ability to function effectively. Don't underestimate the importance of change management."

- *Invest in cultural training.* This is especially critical if you plan to locate your offshore program in a country that you don't currently operate in. It can help you hit the ground running and attract the talent that will best serve your needs.

While the investment in time and energy in setting up its offshore shared services program has been substantial, the savings that Clifford Chance has begun to reap have proven impressive. The firm now has one team performing a range of business functions versus 29 teams in 29 offices, and the project is on track on its business case goal to deliver 8 million pounds in annual savings. As Childs sums up, "By reaching out to clients for advice, building a strong business case, committing to change management, and investing in cultural training, the firm mitigated the risks involved and set the stage for greater operational efficiency."

and collection processes are clearly defined for all levels of professionals.

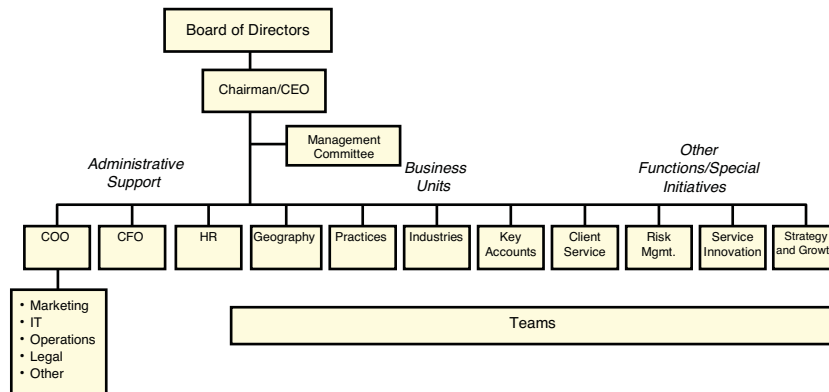
7. *Adapt structure and governance when appropriate.* PSFs are fluid organizations operating in fluid environments. The best firms keep an eye on their structures and governance models and periodically review their effectiveness. Whether it's a tweak or a major change, firms remain agile and adapt as necessary.

Organizational Structure: The Scaffolding That Supports the Firm

"In a professional service firm, a conventional linear diagram doesn't really represent power or the reality of how organizations work. People-based organizations have a delicate balance of responsibility and commitment."

"We value being as flat as possible. The premise is we believe the best decisions can be made as close to the client as possible."

While many variations emerged, the organization charts of the firms surveyed proved to be remarkably similar in their basic configuration, as shown in Exhibit 10.3.

EXHIBIT 10.3 Common elements in a PSF organization chart

At the upper layer of the chart is the firm's top leadership team, often consisting of one or two oversight groups: a board of directors and/or a management committee, and a chairman and/or CEO. Directly below this level is a second layer that includes the leaders of various business units, typically heads of regions, practices or industries depending on how the firm is organized; the heads of key administrative support functions; and senior professionals who manage special functions and high-profile initiatives of importance to the firm. Underpinning the entire organization is a fluid network of cross-functional, often cross-border teams that are attached to clients, services, and geographies, and a host of specialized activities such as intellectual capital development, training, and growth initiatives.

Variations on structure are driven primarily by differences in size, geographic reach, practice diversity, and culture. We found an overwhelming preference among the best-run firms interviewed for lean organizational structures that keep both hierarchical reporting and bureaucracy to a minimum. The following sections describe each organizational layer in a typical PSF structure.

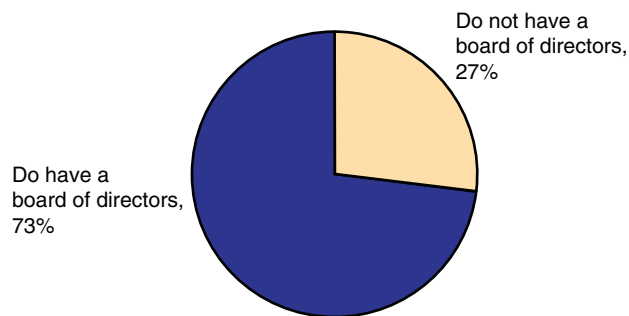
Board of Directors: Composition and Selection

"We've got a number of categories for board members. We're looking for practice mix: gender, age, and, really, any other unique attributes that appropriately represent the full partnership."

"Our board is elected by the firm, and their allegiance is to the firm as a whole, not to their narrow section of interest."

As shown in Exhibit 10.4, nearly three-quarters (73 percent) of the firms studied indicated that they have a board of directors in addition to a management committee.

EXHIBIT 10.4 Most firms have a board of directors



Typically, a board of directors is not involved in day-to-day decision making or firm operations. Instead, most frequently, the board provides corporate governance oversight, monitors shareholder value concerns, and provides impact analysis and final approval of top-level strategic decisions and investments. Some CEOs and management committees use board members as sounding boards. In this consultative capacity, board members help the CEO think through ideas, assess marketplace threats and opportunities, and arrive at decisions concerning long-term vision and strategic direction.

Most boards have standing subcommittees. A nominating committee, for example, may be charged with overseeing succession planning and identifying people for key roles. Other common standing groups include a compensation committee, which monitors partner revenue distribution, and an admissions committee, which oversees the promotion of new partners. Board members may also serve on ad hoc committees created to investigate special projects or urgent issues. Typically such ad hoc groups consist of selected board members and partners at large with expertise in the area being addressed.

In the vast majority of privately held firms, the board of directors is composed of senior partners. Typically, board membership mirrors a firm's broad demographics and includes a mix of professionals representative of the firm's practice areas, geographic footprint, and, in some cases (although not many), age and gender. In some firms, key functional

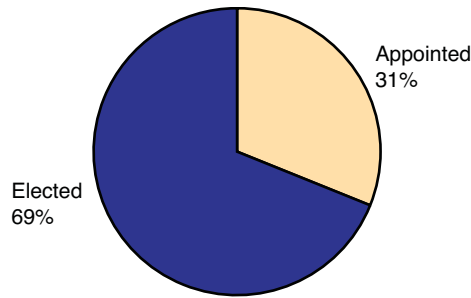
positions may also be represented on the board. For example, to ensure that its board reflects a diversity of backgrounds and viewpoints, Smith-Group has adopted a 9/9 board structure, with nine members who represent practices and disciplines and nine management executives focused on business and operations.

Boards vary dramatically in size, with smaller firms having as few as 5 to 10 members and larger firms typically 15 to 20. McKinsey is run by a board of members who serve 3-year terms and act as the firm's ultimate policy makers. These board members are distributed among four permanent committees that handle all major decisions related to their area of expertise: a client committee, a people committee, a knowledge committee, and a finance committee.

A few privately held firms have appointed outside directors, but this is rare. Dewberry, for instance, is a family business and balances the family members on its board with an equal number of outside directors. Gensler's ten-member board consists of the firm's founder, practicing partners, and an outside board member—a strategist who offers expert counsel on key issues. DLA Piper has a global board consisting of members drawn in equal numbers from its U.S. and non-U.S. operations, along with two independent outside directors.

As required by federal regulatory agencies or dictated by investors, firms that are either public companies or partially owned by third-party investors have boards that include outside members—much like that of a public company. For Booz Allen Hamilton, which is partially owned by the Carlyle Group, Ralph Shrader, the firm's CEO, serves as chairman of a board that consists of two of the firm's senior partners, three senior executives from Carlyle, and two outside directors.

The majority of firms (69 percent) elect their board members, as shown in Exhibit 10.5. Most members serve for a predetermined period, typically 2 to 3 years, and are eligible for election to a second term. Elections typically are staggered so that no more than one-third of board members are replaced in any given year.

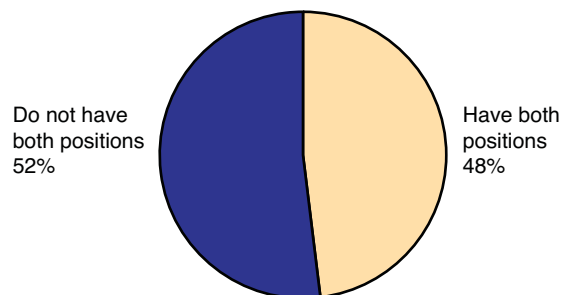


Nominating policies differ widely. In many firms, any full-equity partner can run for the board of directors. In some firms, any partner can simply throw his or her hat in the ring. In still others, a candidate must be nominated by another partner. When it comes to electing members, generally every partner has an equal vote, and the majority rules. In some firms, however, more experienced partners have accumulated more units of partnership and therefore have more votes. In firms where board members are appointed, new members may be chosen by the CEO with input from others on the board, or a slate of potential candidates may be nominated by the board chair and then voted on by the board.

Chairman: Selection and Role

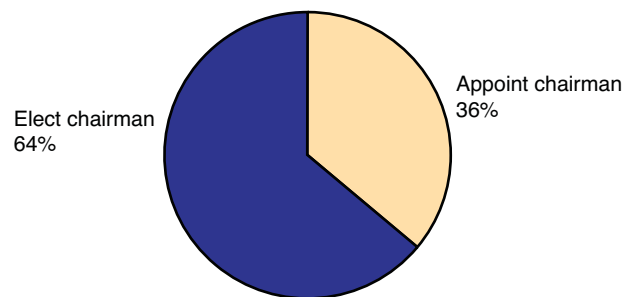
Overall, the position of chairman wins mixed reviews across the industry. Among the firms in our survey, 52 percent indicated that they did not have both a chairman and a CEO, and 48 percent said they did, as shown in Exhibit 10.6.

EXHIBIT 10.6 About half the firms surveyed have both a chairman and CEO role



In firms that have both a chairman and a CEO, 64 percent elect the chairman, as shown in Exhibit 10.7. The scope of the chairman's role varies widely, but typically it does not involve oversight of day-to-day operations. In isolated cases, this position is purely that of a figurehead. More often, however, the chairman primarily performs one of two functions: serving as guardian of the firm's vision and values, or acting as the firm's ambassador—the face of the firm to major clients and the public.

EXHIBIT 10.7 Most firms elect the chairman



In the guardian role, the chairman's chief function is to ensure that a firm is staying on track in its progress toward attaining its long-term strategic goals. Some chairmen see this role in broad brushstrokes: building a great company, maintaining the integrity of the firm's vision, and nurturing its culture. In an ambassadorial role, a chairman generally plays a more active part in helping orchestrate the firm's long-term growth and profitability by offering advisory input on engagements, mobilizing contacts, and identifying promising strategic initiatives. Some chairmen who serve as the public face of their firm may also interact with major clients, represent their firms at high-level industry forums, and be involved in business development.

CEO: Selection, Role, and Succession

In contrast to the big-picture, hands-off role of the chairman, the CEO is charged with the day-to-day, year-to-year responsibilities of running the organization. The flat, lean organization structures of most PSFs mean that the CEO often has an amazing number of direct reports. This pulls the CEO into all areas of the business, from operations, finance, marketing, and human resources to business unit management and

frontline client work. It is, as discussed in Chapter 11, “Style of Leadership,” a very demanding job.

Selection

The process of selecting the firm’s CEO varies dramatically across firms—ranging from informal to elaborate nominating and vetting procedures. Overall, the approaches to candidate identification and selection fall into three broad categories:

- *The current leader selects a successor.* In this selection model, the current leader chooses the new head of the firm. Many of the interviewees said that an important part of their job as the senior leader in the firm is to ensure that their organization has a legitimate candidate or candidates who could potentially succeed them. Most say that their choices are not handpicked exclusively by them, but are individuals who have demonstrated skills, experiences, and the aptitude to continue to learn, grow, and develop. It is the leader’s responsibility to make sure that these individuals get the right kind of experience so they can eventually take the helm. Even in firms where the leader chooses a successor, the partnership always has a say in the decision.
- *A hybrid selection/election process.* In the hybrid model, the outgoing leader and the management team (or board) appoint the new CEO after input from the firm’s partners. This input process can be extensive and time-consuming in a professional service partnership environment where everyone has a voice and collaboration is key. In some firms, partners ultimately vote on a slate of nominees, and in others the board makes the final decision (see “Election Process at Skadden, Arps”).
- *The partners elect.* In some firms, leadership selection resembles a presidential election. The multistep election process starts with a solicitation of nominations from all firm partners. The firm leadership committee selects the top group of candidates—typically around ten—who must present position papers that are distributed to all partners. The partners then cast another vote, and the list is narrowed to the top two candidates. These candidates must publicly debate the issues before the partners. The partnership then casts a final vote, and the candidate with the most votes is elected.

Election Process at Skadden, Arps

In 2009, law firm Skadden, Arps selected its third Executive Partner in the firm's 61-year history. Executive Partner Eric Friedman reports that the firm was proud of the "open and transparent" selection process it completed. Friedman's predecessor, Bob Sheehan, who was finishing a third 5-year term, initiated the selection process 2 years earlier when he told the Policy Committee that it needed to identify a successor.

The Policy Committee appointed a Succession Committee, made up of nine partners from around the firm. Led by Mike Rogan, cohead of the firm's Global Transaction Practice, the Succession Committee included partners from Skadden's major practices and geographic regions. The committee developed a questionnaire that was sent to all partners, asking them to discuss any concerns they had about the firm, their vision for the future, the characteristics they would like to see in a new Executive Partner, and any suggested changes to the management structure, such as whether the firm should have comanaging partners. In an initial "first pass" to gauge sentiment, the partners were asked to submit suggestions on whom they might recommend for the position.

The Succession Committee reviewed the feedback and then fanned out across the firm to meet one on one with each of Skadden's then-450 partners to gather opinions and recommendations. The committee developed an initial list of 19 candidates. It was reduced to five based on a synthesis of the information derived from the meetings with partners and another review of the responses to the questionnaires. The five top candidates were asked to submit in writing their vision and goals for the firm and answer questions such as "Why are you the right person for the position?", "How do you see this role?", and "What major challenges does the firm face?" Each candidate was interviewed by the Succession Committee over a 2-day period.

The committee agreed on one candidate to recommend to the Policy Committee, which unanimously approved his recommendation. Then they submitted the nominee to the partnership for a confidential electronic vote. Under firm governance provisions, the partnership was required to vote by secret ballot to be tabulated by an independent third party. The candidate, Eric Friedman, was elected as the firm's next Executive Partner in May 2008 and formally assumed the role in April 2009. The entire process took less than four months.

Friedman says, “In retrospect, the selection process was especially useful to me because it provided the opportunity to think about how the firm needed to position itself in a more competitive legal environment. My partners have been extremely supportive as we work to reinforce our position as the premier law firm providing services to major corporations and financial institutions on their most difficult financial and governance issues. Also, the transition itself was very smooth. We gradually morphed over a 12-month period from Bob, to Bob and Eric, to Eric.”

Friedman notes that the move from leading day-to-day client engagements to a more strategic client advisory role required a significant adjustment in how he ran his practice. “Bottom line, the transition afforded everyone—myself, my clients, and my partners—an opportunity to recalibrate how it might work going forward.”

Term Limits for the CEO

“I think that changing the leadership is just a way of sort of shaking the carpet out in the wind and getting it nice and fresh as you bring it back in.”

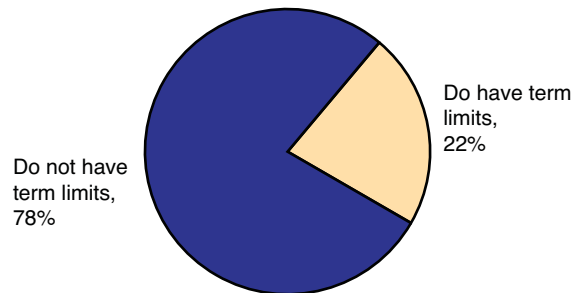
Term limits for the CEO/managing partner position proved to be a lightning-rod issue that provoked lively discussion. As with the to-bill-or-not-to-bill question discussed in Chapter 11, most leaders fell firmly into one of two camps. Either they felt strongly that changing leaders on a regular basis helps keep a firm fresh and attuned to markets needs, or they believed that frequent leadership changes disrupt operations and can endanger a firm’s brand or credibility in the marketplace.

One of the main arguments in favor of term limits is that operating within an established time frame pushes a CEO to aspire to a higher level of performance. “I actually think the 4-year term is a good thing,” observed Jerry Leamon, Global Managing Partner, Services, Deloitte Touche Tohmatsu Limited. “You get people coming in who have huge ambitions about what they want to accomplish, and they do extraordinary things to get it all done during their tenure.”

Despite the intensity of views pro and con on this issue, the majority of firms have chosen to give their leaders open-ended mandates. In fact, four

out of five of the firms surveyed do not impose term limits on their CEO/managing partner, as shown in Exhibit 10.8.

EXHIBIT 10.8 Most place no term limits on CEOs



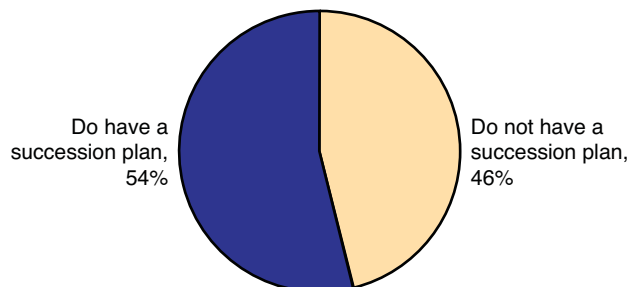
Succession Planning

"I think organizations are making a big mistake if they rely on just, 'Oh, the next leader will come.'"

"There's no succession planning because anybody can be nominated. We have a very open and free process for leadership. It should be a distributed leadership model, not a tight sort of hierarchical management model."

Given the rich crop of potential leaders, how do professional service firms choose one for the top slot? Our interviews revealed the surprising finding that many firms have no succession plan or process in place. Of the firms that said they do have a plan, a significant number outlined what could more accurately be called an approach. Overall, only 54 percent of our interviewees say their firms have a program in place to identify future leaders, as shown in Exhibit 10.9.

EXHIBIT 10.9 Slightly more than half have a succession plan



Among the 46 percent who said they have no succession plan, the reasons given varied. Some interviewees say that succession planning is culturally inappropriate for their organization. As one former CEO said, “We have an abundance of very smart people who are capable of running this organization. Leaders rise to the top on their own.” For this firm and for several others in our study, firm leaders emerge naturally and are chosen through a general election process when needed. Others noted that they are still too new or too small to require a formal plan. Quite a few others expressed concern about their lack of a planning process and are debating how to develop a program.

For the firms that do have some form of plan, the degree of structure and formality varied widely. Several firms have nominating committees in place that are responsible for formal succession planning for all key roles—looking at the next generation of leaders and maintaining a short list of potential candidates.

Some firms have a leadership development group that identifies and grooms professionals for all the firm’s top leadership positions across regions, practices, and industries. Each firm leader is required to look several layers down into the organization to identify candidates for his or her role and for the subroles in his or her area of responsibility. As one partner explained, “Every year I am required to identify or reconfirm my successor and answer a few basic questions: Are they ready now? If not, when, and what skills do they need to get there?”

For other firms, thoughts about the successor to the firm leader are just that—thoughts with little solid action. Plans for replacing the leader are ignited only when the current leader announces his or her plan to retire or step down.

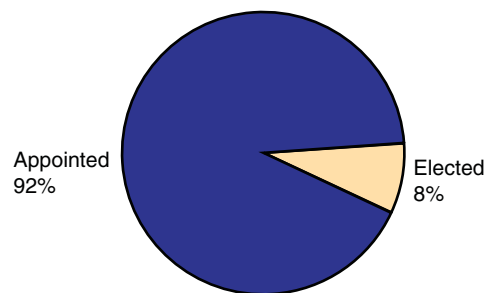
Management Committee: Composition and Selection

In most professional service firms, the management committee—also called the operations, executive, or policy committee—is responsible for overseeing day-to-day operations and working with the CEO to manage the business and monitor financial performance.

Executives who report directly to the CEO usually comprise the management committee. Depending on how a firm configures its management committee, members may include the leaders of business units, the

heads of key administrative functions, and senior professionals overseeing special projects or initiatives. Many firms have designated committee slots for these positions in the organization structure, and professionals automatically become committee members when they are appointed to those roles. Depending on firm size, these committees typically have from 5 to 12 members, with some committees having as many as 20 to 30, although this is unusual. Most committee members do not have term limits; they continue to serve as members of the committee as long as they retain their role in the firm's leadership structure. Overwhelmingly, these committee members are appointed rather than elected, as shown in Exhibit 10.10.

EXHIBIT 10.10 Most firms appoint rather than elect management committees



Business Units: Structure and Seat of Power

“The optimal organization has a balance between geographies, functions or practices, and industries.”

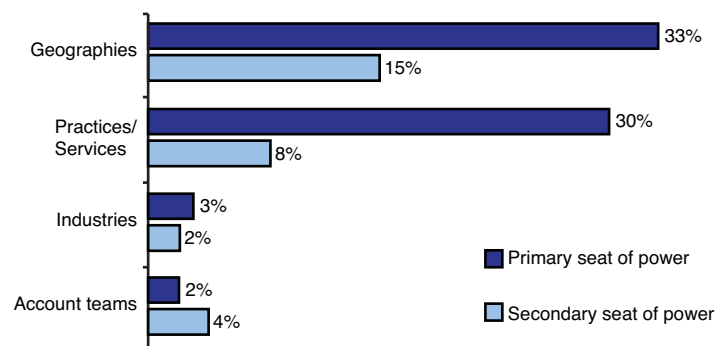
“I think what you need is a tension in the matrix. If you drive it down one dimension in the matrix at the expense of all the others, you suboptimize somewhere else.”

Business units in professional service firms are organized across two, three, and sometimes four dimensions—regions/offices, practices/service lines, industries, and, in the case of advertising and public relations firms, key accounts. This complex matrix organizational model with its multiple cross-organizational reporting requirements is routinely panned by most business gurus and has been proven to be notoriously difficult to manage. Why, then, do PSFs tenaciously embrace this model, and why does it seem to work so well in the professional service industry? There are several reasons why a matrix structure is well suited for PSFs:

- *It supports a consensus culture.* As a network of peers, a professional service firm can thrive only if it fosters a consensus-driven environment. The matrix model provides multiple leadership opportunities for senior professionals to play an active participatory role in firm management.
- *It provides maximum flexibility.* PSFs are fluid organizations. In serving clients, professionals operate in multiple teams, practices, and geographies. A matrix structure offers the flexibility needed to run a multiclient, multiproject-driven business. It also enables firms to optimize and share talent and resources across geographies, functions, and clients.
- *It accommodates growth.* Even the smallest PSFs offer multiple skills and service capabilities. As firms grow, they tend to bring in more specialized professionals to expand service offerings and move into new geographic regions. Eventually, they channel their growth by breaking their organization into more manageable units. Well suited to facilitating expansion, the matrix model allows firms to retain the lean, flat operating structure that best supports a consensus culture.

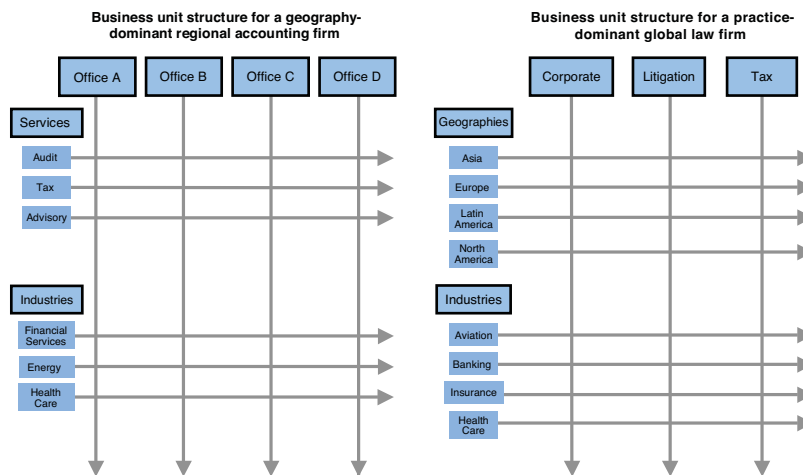
Inevitably, as a firm grows, one dimension of the matrix model predominates. It becomes the seat of power that controls the business unit P&L and drives planning, performance, reviews, and compensation decisions. Which dimension of the business units becomes the dominant driver in a firm depends on a complex interplay of factors: culture, markets, client needs, and geographic reach. Structuring internally by either practice area or geographic region are the two approaches that most firms opt for as their enterprises expand. For the firms studied, geography was the dominant driver, followed by practice/service lines, as shown in Exhibit 10.11.

EXHIBIT 10.11 Geographies and services are primary seats of power in most firms



The business unit organizational map in a firm where geography dominates looks different from that of a practice-driven firm, as shown in Exhibit 10.12. But the same matrix principle of multiple reporting relationship and cross-functional teaming applies.

EXHIBIT 10.12 Business unit structures



Distinct advantages and disadvantages are inherent in each organizational choice. Organizing by geography tends to result in a stronger, tighter operating model, whereas organizing by industry tends to result in more robust go-to-market capabilities. In general, using practice/service lines as a firm's dominant organizing vehicle leads to more consistent execution.

Historically, geographies have tended to be the dominant seat of power for many firms. However, as many people have experienced, this model can all too easily promote competition rather than collaboration, which can result in damaging bottlenecks and fiefdoms to the detriment of the organization as a whole. One firm's performance, for example, was dangerously compromised, according to a senior executive, because its regions were "absolutely Napoleonic" in their single-minded focus on serving only their own geographies.

As firms grow more global, the practice/service model is likely to become more dominant. Increasingly, firms are gravitating toward this approach because they find that practices are the most efficient organizing vehicle for building an operating system that can deliver client value on an integrated global basis. A practice-driven infrastructure

facilitates cross-border team building, knowledge management, and resource deployment. It also enables firms of varying sizes to fully leverage the matrix model and its network of professionals so that they can deliver just-in-time expertise anywhere in the world. Many firm leaders contend that having practice groups predominate is essential for successful global integration.

When it comes to creating a high-performance operating model, whether it is driven primarily by industry, service line, or geography, the secret to success is striking the right balance among dimensions so that while one predominates, the others remain robust and well tended. If a firm pushes too hard in one direction at the expense of the others, it risks suboptimal performance. Creating tension in the matrix—just the right amount of push and pull among the units—is critical to keeping the model dynamic and effective.

Other Functions/Special Initiatives

Many firms identify areas of focus that they believe are important enough to warrant an elevated spot on their organization chart and a seat at the management committee table. These can be areas that a leadership team views as vital to preserving firm culture or critical to the management of their business. Client service, quality control, innovation, thought leadership, talent development, and risk management are all examples of issues that have a huge impact on growth and profitability and that may be accorded special attention. Several of the largest firms included in our study have added a new global integration role to their leadership ranks with the mandate to consolidate multiple geographies into fewer, more unified units.

Administrative Support

“You simply can’t do this job well without a good COO.”

“You can mitigate a lot of headaches by having strong leadership on the administrative side.”

For many professional service firms, the administrative side of their organization chart continues to evolve. Many firm leaders expressed an interest in upgrading the sophistication and performance levels of their support

infrastructures. At the same time, there is a persistent reluctance to invest substantially in upgrading the nonrevenue-producing side of the house.

This hesitancy is rooted in several concerns. First, star performers tend to believe that they can do it all—including mastering and running the business aspect of their firms. Second, many enterprises are justifiably concerned about the cost of bringing onboard high-level executives who are not revenue producers. Small and midsize firms are especially sensitive to the revenue impact of nonbillable support positions. Finally, there is a well-founded fear that business management executives recruited from the corporate world may be unable to function optimally in a nontraditional matrix environment. War stories abound of senior people recruited from outside the industry who quickly became frustrated with the consensus culture and bolted.

Despite these caveats, nonbillable executives are on the rise. Although administrative responsibilities vary from segment to segment and firm to firm, this side of the organization chart has some consistency. In general, the top spots—those who have a seat at the management committee table—tend to include the COO (if the firm has one), the CFO, and the CHRO. Nearly half of our respondents have a COO role, and virtually all have a CFO, although this position varies dramatically from a pure financial controller to a respected partner-level executive.

The COO role is evolving across the professional service industry. Many firms are finding that a strong COO can have a transformative effect on operations, improving efficiency by effectively deploying and managing resources and technology. Having a trusted executive manage the administrative functions and operating issues reduces the CEO's number of direct reports and allows him or her to pay more attention to strategy and market-facing issues. In fact, some CEOs today insist on having a strong COO onboard as a precondition of their service.

Changing the Structure

At critical junctures in their growth, firms find themselves facing internal and/or external pressures to change the organizational structure or governance policies and procedures. In some cases, rapid expansion forces them to break into smaller units; in others, evolving client needs drive a shift in focus and operating structure. Whatever the trigger, at some point

in time, firms find that their organization structure is becoming an impediment rather than an asset to the organization. When this occurs, successful enterprises regroup, take stock, and reconfigure.

Several common signs indicate that it may be time to reevaluate the structure and governance model:

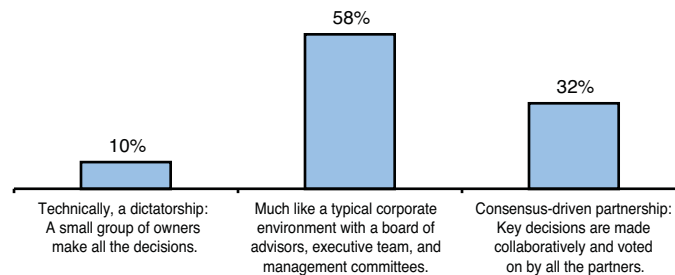
- *Clients start complaining.* When clients become concerned about the quality and consistency of the work across geographies, or are frustrated with the complexity of the firm's hierarchy and siloed practice areas, it's time to change.
- *Partners don't know each other anymore.* Size is the major factor that drives change to structure and governance. Up to a certain size, the firm can rely on the fact that everyone knows each other and works well together. At some point the firm becomes too large to work effectively as a single unit.
- *It takes too long to make important decisions.* This is a sign that either the wrong leaders are in place or the structure or operating procedures are getting in the way.
- *Communication among the partners seems to go awry too frequently.* A sense that communication isn't working well often happens as organizations grow geographically. Old ways of communicating don't work in an increasingly dispersed environment.
- *Professionals regularly don't follow the rules.* Professionals like to do things their own way. However, when both the professional and the support team consistently refuse to conform to the operating policies and procedures, it is time to regroup. Instead of trying to force everyone to take certain paths, as set forth in the "rule book," maybe the rules need to change to conform to how people work, communicate, and get things done.
- *Some start to feel like second-class citizens.* A them-versus-us scenario can develop as a firm adds new geographic locations, often called satellite offices. It becomes harder to retain talent as professionals become disenfranchised and feel like they are on the outskirts.

Governance Style

"Our partners generally accept that management must be allowed to manage—as long as they have a fair opportunity to have their voices heard."

In the professional service industry, governance style ranges from monarch-like dictatorial decision making to a totally inclusive emphasis on consensus building and partner involvement (see Exhibit 10.13).

EXHIBIT 10.13 Governance style ranges from dictatorship to total consensus



As partnerships by their very nature, PSFs require some degree of consensus on key governance issues. Nearly a third (32 percent) of the firms surveyed placed themselves in the high range of our scale in terms of their consensus-driven governance style. Another 58 percent claim they are somewhere in the middle, and a minority (10 percent), typically smaller firms with the original founders in place, keep the decision-making reins tightly controlled by a small leadership team. One firm leader in this category saw himself as a “benevolent dictator.”

Although they are committed to navigating between consensus and decision, a number of leaders interviewed stressed that a collaborative firm isn’t the same as a democratic one. The governance style that most firms embrace involves a leadership team that operates fairly autonomously in a number of key areas while remaining participative and transparent enough to keep partners engaged and supportive. Clearly, operating with a relatively pure consensus model is easier in a smaller firm. As firms scale up, gaining agreement around key decisions becomes far more challenging. In the largest high-performance firms, the partnership as a whole rarely or only selectively votes on issues. Partner vote-worthy matters generally include electing a new partner slate, partner expulsion, and/or opening new offices. In larger firms, maintaining a governance style firmly rooted in consensus decision making requires constant work and an enormous amount of communication with partners (see “A.T. Kearney Revamps Structure and Governance”).

A.T. Kearney Revamps Structure and Governance

In 1996, the partners of management consulting firm A.T. Kearney voted to sell their firm to global business and technology services company, EDS, and become an operating division of the publically traded organization. Ten years later, the partners negotiated a management buyout to repurchase the firm and, in 2006, A.T. Kearney became what Managing Officer and Chairman of the Board Paul Laudicina calls “an 80-year-old start-up.” The 170 partners that participated in the MBO essentially had the opportunity to recreate the firm. “We had a young group of aggressive, ambitious partners all anxious to roll up their sleeves and make a success of this new firm that they owned,” says Laudicina.

A team of partners was selected to negotiate the terms of the buyback and prepare for a “constitutional convention” held in Atlanta, Georgia, to align the partnership around key governance, ownership, and structural issues that would become part of the new shareholders’ agreement and Articles of Association. “It was all about entrepreneurship, accountability, and responsibility,” says Laudicina. “Ten years of public company corporate mentality had created an employee–employer mentality, and we needed to return to an owner–partner psychology and ethos.” Specific decisions included:

- **Ownership and equity**—The firm became a privately held corporation. Each new officer is required to make an investment to become a shareholding partner. Shares are bought based on the book value determined annually by the board, and shares must be sold when partners leave the firm. Partner compensation is performance-driven and based on quantitative and qualitative metrics.
- **Governance**—There was a strong bias post-MBO that the firm have a very open and free process for leadership. “There was a sense that the leadership of the organization should be a broad, diverse group of partners,” notes Laudicina. “We wanted a transparent, distributed leadership model, not a tight hierarchical management model. The partners agreed to a one-partner, one-vote system, with a partnership elected Board of Directors and Managing Officer who serve a maximum of two consecutive 3-year terms if reelected. The board and managing officer positions are elected though an open nominating process, and every voting

eligible nominee. Nominees are required to post position papers on their platform that are reviewed by the partners; whoever receives the highest number of votes is elected to the position.

- **Structure**—Laudicina formed a senior leadership team consisting of himself, the Chief Operating Officer, the regional leaders and administrative heads—CFO, CHRO, General Counsel, and the Chief Communications Director—all of whom had to be newly hired and their departments reestablished post the separation. Like most PSFs, the firm operates in a matrix structure with geographic units, ten industries, and eleven service practices. Unit leaders report to the COO and are appointed by the Managing Officer after input from partners. Immediately post-MBO, most of the leadership authority within the firm, along with P&L responsibility, were endowed in the geographies. “We needed to jumpstart the new organization quickly and establish cohesiveness with clear lines of authority without ambiguity among the local partners,” says Laudicina. “However, the firm is determined to create a more balanced distribution of power and is moving in that direction.”

The firm has tried to incorporate lessons learned from the EDS corporate experience, particularly the value of clearly established processes. “A very rigorous and strong central series of process capabilities supports and ensures key initiatives such as the integrity of the code of conduct, the uniformity of training and human resource policies, consistency around brand development and projection, and financial stability,” says Laudicina. “The challenge is maintaining disciplined processes within an entrepreneurial partnership structure—if you can balance the two, you’ve got the best of both worlds.”

CHAPTER SUMMARY

Structure

- There is widespread agreement that a firm's infrastructure and governance model has a major impact on its overall performance, service delivery, and strategic execution. The key is to align structure with strategy and culture.
 - Choosing the right operating structure for the firm presents three major challenges:
 1. Finding the right balance between freedom and bureaucracy is difficult.
 2. There is no ideal "one-size-fits-all" model.
 3. Structures must continually evolve to adapt to changes in firm growth and direction.
 - The best-run firms share seven defining characteristics. These enterprises do the following:
 1. Embrace a one firm mind-set.
 2. Operate transparently.
 3. Train professionals in business skills.
 4. Use professional nonbillable support teams.
 5. Emphasize process efficiency.
 6. Clearly define roles and responsibilities, policies and procedures.
 7. Adapt structure and governance when appropriate.
 - Governance styles range from dictatorial to consensus-driven, with most well-run firms committed to striking a healthy balance between participatory decision making and efficient execution.
 - PSF organizations are flat and lean, keeping bureaucracy to a minimum. Although variations emerged, PSF organizational models have many similarities (see Exhibit 10.3).
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