

Understanding Your Company's Performance Architecture

Fred Nickols

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www.nickols.us
nickols@att.net

Responsible Practice

Responsible practice requires being able to say that a given intervention will produce a given result or, conversely, that a certain result requires a certain intervention. This means that responsible practice depends on being able to identify and exploit the linkages and causal connections between the results we seek and the means at our disposal. These linkages and connections exist in what can be called a company's "performance architecture." The purpose of this article is to define and briefly explain the structures that make up a company's performance architecture.

Performance Architecture

"Performance Architecture" refers to three related domains of organizational performance: financial, operational and behavioral. These domains are depicted in the Performance Pyramid in **Figure 1**. The numbered tabs represent *linkages* between the domains. Mapping an organization's performance architecture creates a roadmap for realizing results.

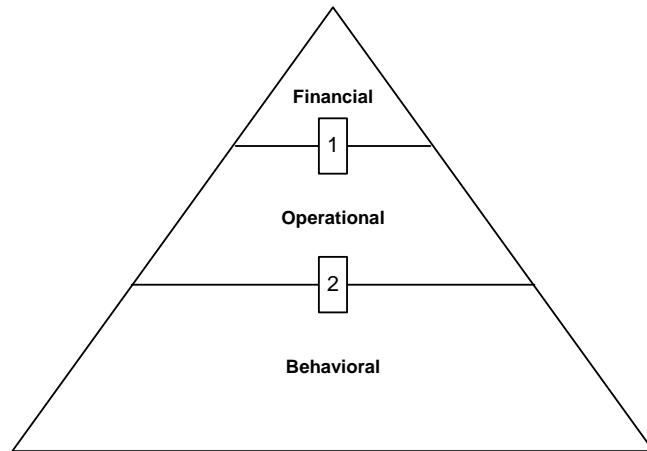


Figure 1 - The Performance Pyramid

Each domain of performance has a different structure. The structure of the *financial domain is mathematical in nature*; it is concerned with counted and calculated values (e.g., profit). The structure of the *operational domain is physical in nature*; it is concerned with stocks and flows, with systems of production, distribution and the like. The operational domain manifests itself in the organization's processes. The structure of the *behavioral domain is psychological in nature*; it is concerned with human behavior and performance, with people. A brief discussion of these three domains follows.

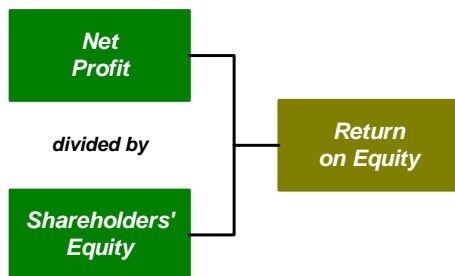


Figure 2 - High-Level Structure of ROE

Financial Domain

The financial domain is defined by the organization's chart of accounts, its accounting systems and the measures of financial performance used. The high-level structure of one measure of for-profit business performance – ROE or return on equity – is shown in **Figure 2**.

The financial measures used vary from organization to organization. In one company, Profit as a percent of Sales might be an important measure; in another, that measure doesn't get much attention but Return on Assets Managed does. Publicly traded stock companies might pay attention to earnings per share but that measure is meaningless with re-

spect to a nonprofit. In nonprofits, retained earnings takes the place of profit and contributes to the nonprofit's invested reserves. All organizations use financial measures as gauges of their financial performance.

Tab 1 in the Performance Pyramid (Figure 1) refers to the linkages between the organization's financial performance and its operational performance. The organization's chart of accounts, revenue booking, cost allocation mechanisms and financial reports are the best starting points for identifying the linkages between financial and operational performance. The task is a matter of identifying the measure and then analyzing its mathematical structure. Carry this analysis deep enough and, sooner or later, financial measures tie to operational variables. Figure 3 shows several levels of detail in the structure of Return on Equity.

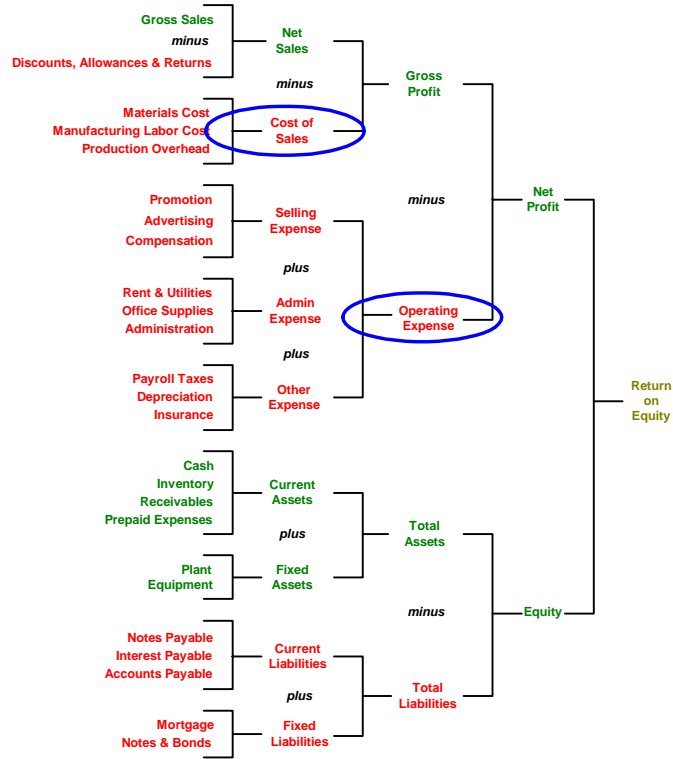


Figure 3 - Detailed View of Return on Equity

The circled items in Figure 3 illustrate that the linkages between financial and operational performance are found in the low-level details of the structure of key financial measures. For example, further decomposition of the Cost of Sales and Operating Expense variables would lead through the organization's chart of accounts and cost accounting system into its operational structures and processes.

Operational Domain

The operational domain is defined mainly by two kinds of processes: *transformation* and *transaction* processes. Transformation processes convert organizational inputs into outputs (e.g., raw materials into finished products). Transaction processes focus on exchanging organizational outputs for new inputs (e.g., finished products or services for money). Both categories can be viewed as systems by which the output production and the input acquisition work of the organization are accomplished. The basic structure of a work system is depicted in Figure 4. It shows that inputs are transformed

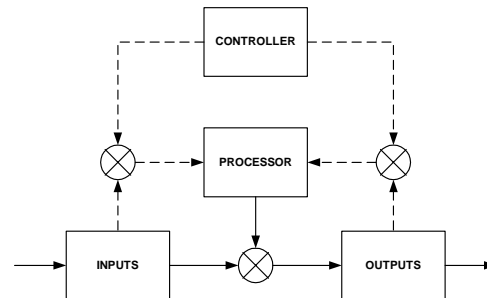


Figure 4 - Work System Structure

into outputs as a consequence of interactions between those inputs and the system's processor (which might be a machine or a human being).

Behavioral Domain

This is the domain of human performance. Because people in organizations are there to accomplish the work of the organization, be it output production or input acquisition, two models are of use here. First, the work system model (Figure 4) can be used to examine work processes in which the "processor" is a person. Second, a model that depicts people as purposeful, goal-oriented actors also proves useful where the behavior of people is of central interest. The model in Figure 5 is a closed-loop, feedback-controlled model.¹

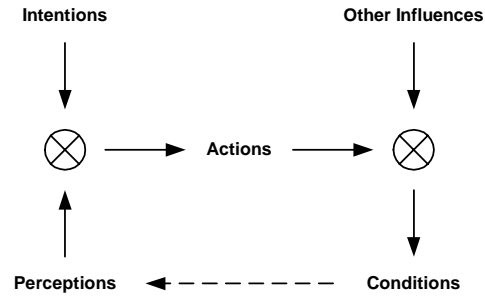


Figure 5 - The Structure of Human Performance

Tab 2 in the Performance Pyramid (Figure 1) refers to the links between the operational and behavioral domains. People in organizations are process participants; they do work and thus their work products and actions feed directly into the organization's processes. In many cases, people are the processors.

Conclusion

The ends we seek and the means at our disposal are linked through at least three different yet related domains of performance: financial, operational and behavioral. For any given result, there are one or more paths through, between and across all or some of these three domains that defines the "performance architecture" for a particular result. Being able to map and trace our way through the various structures comprising this architecture makes the probability of identifying suitable changes and interventions much higher than would otherwise be the case. It allows us to say, for a given result, the actions that will lead to it; and, for a given action, the result that is likely to be produced.

Contact the Author

Fred Nickols can be reached by e-mail at nickols@att.net. Other articles of his can be found on his web site at: <http://home.att.net/~nickols/articles.htm>.

¹ This model is based on the work of William T. Powers, particularly his Perceptual Control Theory (PCT). Interested readers should refer to two of his books for more detail. *Behavior: The Control of Perception* (1973) and *Making Sense of Behavior* (1998).