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TOWARDS THE BUSINESS FEDERATION
IN MANAGEMENT CONSULTING FIRMS:
A PRELIMINARY STUDY IN NORWAY AND SPAIN

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Abstract

This research presents the Business Federation as a new organizational form. It builds on core concepts of competence-based management to illustrate how this new form deviates from other organizational archetypes (for the basis on which autonomy and authority in decision making are based, and new roles ascribed to top management, support services and business units). We argue that specific design choices associated with the Business Federation form provide an organizational framework to solve major management challenges posed by current competitive environment.

The research elaborates on the previous work on the Federal Form of organizing advanced by authors such as Charles Handy and Esteban Masifern, and tries to apply the strengths and requirements of this new form to Professional Service Firms, clearly representative of knowledge-based companies. Empirically, it presents the results of an initial test on the extent to which management consulting firms in Norway and Spain are implementing key features of this federation form. And finally, we test whether this has any effect on growth, as a key indicator of performance in consulting companies.

TOWARDS THE BUSINESS FEDERATION IN MANAGEMENT CONSULTING FIRMS: A PRELIMINARY STUDY IN NORWAY AND SPAIN

1. The context for the emergence of business federation

Nowadays companies are facing an acceleration in the rate of competitive changes. The competitive landscape is reshaped by forces such as globalization, deregulation, technological advances and social changes. As a result of these shifts, newly created organizational forms are subjected to test as managers experiment with sometimes radical, ill-understood new organizational arrangements (Ilinitich, D'Aveni and Lewin, 1996; Galbraith and Lawler, 1993; Snow, Miles and Coleman, 1992; Bowman and Carter, 1997).

Competitive and social forces are placing heavy demands on companies. Managers try to couple the advantages associated with former competitive regimes, such as scale economies resulting from resource accumulation and control, with the demands of the new reality. Specifically, Snow, Miles and Coleman (1992) caution that managers, who want their companies to be strong competitors in the 21st century, will need to search globally for opportunities and resources, to maximize returns on all the assets dedicated to a business, to perform only those functions for which the company can develop expert skill and to outsource the rest of activities in which the company does not have a competitive advantage. These authors claim that the new competitive reality demands to be simultaneously efficient and adaptive.

In similar terms, Bander-Fuller and Volberda (1997) suggests that a major challenge to renew large complex companies is to cope with the flexibility paradox of managing both change and preservation. Tushman and O'Reilly (1997) add that companies will have to learn to be ambidextrous organizations, that is, to manage internally inconsistent competencies, structures and cultures yet with a single vision, which will enable the companies of tomorrow to lead evolutionary and revolutionary change.

Ilinitich, D'Aveni and Lewin (1996) warn that dominant paradigms in organizational theory based on uncertainty avoidance and stability seeking are inadequate for the new competitive context. Several alternative approaches have been introduced for coping with new paradoxes such as the one on efficiency versus adaptiveness, such as the network organization (Miles and Snow, 1986), the virtual corporation (Davidow and Malone, 1992; Asava and Engwall, 1994) and the horizontal organization (Ostroff and Smith, 1992). A deeper understanding on how to deal with the tension of competence-leveraging and competence-building both within firms (Løwendahl and Haanes, 1997) and among partners (Stein, 1997) is a necessary step towards solving these management challenges.

Even though structural flexibility is major management concern, Handy (1994) extends the nature of contradictions that managers face today to issues associated with power and control. Handy (1992, 1994) identifies as the major paradoxes of modern business: 1. the need to attain the advantages of large companies as well as the small ones ; 2. the recognition that open and free markets are the best guarantee of efficiency, yet personal preferences often lead managers to organize operations for centralized control; 3. Managers' desire to run businesses as if they were wholly-owned yet, increasingly, due to external collaborations and outsourcing, they will not have full command, and will have to put up with managing them on the basis of shared interest and mutual respect. O'Toole and Bennis (1992) discuss some of these dilemmas and emphasize the distinguished role of leadership within the federation.

Handy advances that the concept of federalism applied to the business context is particularly appropriate to deal with these contradictions. Moreover, the author adds an additional paradox of particular interest in the context of knowledge-based companies. The pull of professionals, high achievers who see themselves as having careers beyond the organization, constitute the fourth paradox pushing companies towards federalism. Highly qualified professional expect the company to recognize their individual talent and demand space and autonomy to provide their contributions. Professionals feel proud of their advanced knowledge and resentful to giving up too much independency to management. They make undoubtedly true the claim that people are the firm's truly chief assets.

As companies increasingly face this new management reality, Handy professes "the move to federalism is inevitable". To help to understand how it is supposed to work, Handy (1992, 1994) puts forward five principles of federalism:

- Subsidiarity. It means that power belongs to the lowest possible point in the organization. Handy points out that subsidiarity is the reverse of empowerment. Only with the agreement of the lower units can upper levels exercise authority. It is, in effect, a form of inverted delegation.
- Interdependence. It implies that power and expertise are spread around to avoid the risk and pitfalls associated with placing them in a single center.
- A set of basic and common rules of conduct. With subsidiarity and interdependence, companies will need mechanisms of cohesion, i.e. holding the pieces together. That could be accomplished through a common way of communication, shared strategic thinking, measurement schemes, value and mission statements, a single vision, etc.).
- Separation of powers as to keep management, monitoring and governance in segregated units. Governance will ultimately be democratic, accountable to all the stakeholder groups in which the firm depends.
- Twin citizenship. Any organizational member feels like citizen of both a local unit and the federated union. The whole draws its strength from strong leadership of its local units, which enables strong local identity as well as a feeling of membership to the larger entity.

The former is very much in line with the claim that the key drivers of market evolution and dynamism are increasingly related to intra- and interfirm processes of knowledge creation rather than mechanisms of control over production and distribution assets, which have been the main focus of attention in industrial organization theory in the

past (Sanchez, 1996). It becomes necessary to investigate the processes by which firms identify, build, acquire, deploy, protect and retire resources (Heene and Sanchez, 1997). A deeper understanding of new organizational forms which address current management challenges is a step towards opening the “black box” of the firm in the search for true sources of competitive advantage.

2. The business federation

The Business Federation is defined, in Masifern and Masifern (1997), as a new organizational form characterized by several features: 1) its organizational design explicitly recognizes two or more dimensions (product functions, customer groups, geographical markets, technologies, steps in the value chain, support services, functional specialists, or others), 2) the firm is governed by the rules associated with the regenerated company (i.e., it is oriented to objectives, oriented to people, and managed under an open systems approach). 3) the three distinctive organizational units (corporate level, business unit level and support units) receive roles which significantly differ from those prevailing in traditional bureaucratic organizations.

First, in the similar terms as in the matrix or the network organization, the multifaced nature of activities is directly addressed in the organizational design of the business federation. Second, the rules of regeneration are new rules of internal design, initially suggested as alternative organizing principles by Masifern (1964), to signal the departure from the rules of more traditional, bureaucratic forms. For example, some of the implications of the regeneration rules are: a manager’s authority is positional and not subject to personal ownership, therefore the same manager has different authority depending on the task under consideration; there are several types of authority, not just line and staff (competence overrules hierarchy to define authority for some management positions); personnel involvement, participation, competence building are non-ceiling processes; management by objectives displaces management by command and control; firms operate with business units and profit units, while cost centers are disappear; transfer prices are market driven, not cost driven; organizing principles are guided by subsystems and processes, not by functions, tasks and specialities. etc.

Third, the business federation ascribes new roles to the corporate level, business unit level and support units in strategy setting and control as well as in integration and coordinational of activities. The implications are several. For instance, the glue that holds together the corporation comes from several aspects: a new role of senior management, that integrates and coordinates on the basis of a institutional (1) and corporate strategy; a set of the boosting units (support services) shared by business units, and through the specific organizational design of the federation, described below. Masifern (1993) adds that this new organizational form places a strong emphasis on creativity, internal as well as external collaboration and resource sharing, and puts the contact with the user/consumer as a definitional parameter.

(1) Institutional Strategy is a declaration, with the will to last, of the company's beliefs and values, a few basic companywide guidelines and the expression of the obligations and accountability of company shareholders. It basically collects the commitments that shareholders voluntarily assume in front of stakeholders, and we defend that they should be included in the company legal statutes (Masifern, 1994).

The Business Federation explicitly recognizes three structural units widely used in the literature, corporate, business and support units. Yet, it ascribes to them distinct roles than those that receive in traditional forms. These are:

a) The **corporate level**. Management theory has traditionally assigned to the corporate office of any multibusiness company four roles: to articulate and adhere to the corporate strategy, to act as the guardian of resources of the corporation, to fulfil the general overhead functions of the corporation, and finally, to set the administrative context for the firm by choosing the structure, systems and processes to control the various units and achieve coherence across them (Collis and Montgomery, 1997).

In the federation, corporate management significantly influences its units' integration and coordination, yet, the nature of the relationship and mechanisms to perform this role significantly differ from those in hierarchical forms. Corporate management shapes the overall strategic logic of the corporation (Sanchez and Heene, 1996), while general managers at the business level have ample discretion in business resource allocation. Business units are responsible for their own management and monitoring. Corporate influence in business strategic planning and control is infrequent and exceptional. Another critical role of the center is to see in which aspects the different business units should cooperate and how resources should be shared. The aim in the federation is that business units be emancipated in most functions and activities, and cooperate and share in a few vital lines of interdependence.

A key responsibility of the corporate level in the federation is to continuously look for new services, to add value to the business units (Masifern and Masifern, 1997). Top management identifies the competencies that will be critical in sustaining competition and supporting corporate and business development (Heene and Sanchez, 1997). In defining the strategic logic and principles of corporate resource allocation, top management plays a critical role in balancing the need for competence building within boosting units and competence leveraging at the business level.

b) **Business level**. This is the front line, the level in contact with the customer or user/consumer. It may be constituted by a single business type or a business grouping. Unlike the support units, businesses sell to external customers. The business units (referred here as *federated units*) enjoy almost total operational independence and considerable freedom in its strategic orientation, within a few constraints set by the corporate level.

The role of the business manager in the business federation is similar to that of an entrepreneur, in the sense that he decides his own strategy, holds control, governs his unit's organization, however he will request new offerings within his business domain and choose among the products and services offered by the support units, rather than developing the products within his business unit. The entrepreneurial character of business managers is a key aspect of strategic flexibility, given the need to be quick in making and implementing decisions, in response to the demands of complex and dynamic environments (Sanchez, 1995).

Business assets are used in repeatable patterns of action, allowing coordinated deployments of specific sets of knowledge (Sanchez, Heene, and Thomas, 1996). Businesses are not distracted by decisions about how to develop technological and organizational skills, which is a concern of corporate and boosting units. Businesses focus on performing front-line activities better than competitors.

Business cohesion has been traditionally sought through top-level direct involvement both in integration and coordination responsibilities as well as through strong influence on strategy-setting and also through strategic and operational control. The federation pursues cohesion through different means (Masifern, 1993): a common understanding of the institutional strategy, a shared understanding of internal rules of organizing (spawned from a regenerative conception), common services and products or a peculiar democratic style of leadership, to which adds a shared strategic logic (Sanchez and Heene, 1996).

c) ***Service support level.*** This level is made up of units whose responsibility is to develop products/services to strengthen the competitive position of businesses. Therefore, this level is referred as *boosting units*.. Even though they are concerned with competence leveraging, the main purpose of boosting units is competence building to support business units. They act as facilitators, supporting the direct value creation of the business core. These facilitating or boosting units focus on continually changing and adapting the products offered by federated units. Its role is to stimulate the constant transformation of activities in the operating core. In this sense, this unit is similar to the “university” in the machine adhocracy identified by Bowman and Carter (1997). For example, their activities will be directed to new products and services, skill-development groups, personnel systems, common purchasing, insurance, marketing, logistics, data processing, maintenance of physical resources, etc.

Each boosting unit is a profit center, not a cost center. Its services/products are offered to the federated units, who have the choice to buy internally, externally or disregard the offering. The relationship between the two is governed by market rules. The corporate level can make some of the products/services developed by boosting units compulsory for the entire federation, normally just only a few essential, for example, a logo identifying corporate image (Masifern, Fraguas and Vilà, 1997).

Boosting units can eventually “sell” outside of the federal company. In this case, they would be treated as businesses. Then, it is questionable whether the two selling activities, inside and outside oriented, should be kept together (Masifern and Masifern, 1997).

The roles of three structural units have only been succinctly described here. Masifern and Masifern (1997) summarize them as illustrated in chart 1.

Chart 1
Roles in the Federation

Corporate level

- To look for new products, services, resources, facilities and activities to be added to the assortment to boost the entrepreneurs' performance.
- To determine which of services/products (only a few) are to be compulsory for the businesses/entrepreneurs.
- To develop and instil the federation's institutional strategy (how the company thinks) and the limitations (the least possible) in the activities for both the business/entrepreneurial units and the facilitating/boosting units.
- To set corporate strategic priorities.
- To allocate strategic funds.
- To get the business units and people to adopt the maxim "what is good for the institution, is good for me".
- To facilitate cohesion through a shared strategic thought.

Business level (Federated Units or Entrepreneurial Units)

- To manage (strategy, organization, operation and control) the unit's activities (as in an independent enterprise).
- To create and pursue market opportunities.
- To ensure its people's commitment.
- The full responsibility for the unit's results and value increases.

Boosting level (Facilitating units)

- To develop and improve the competitive assortment (products and services) offered at the entrepreneurial level to increase its value.
- To "sell" its offerings to the entrepreneurs (who may buy it or not, except for a few exceptions that may be mandatory).
- Responsible for the results of its profit centre.
- To harmonize the different needs, skills, knowledge and resources.
- To detect or receive initiatives both from entrepreneurs and outside parties. To develop them, with the aim to sell to the entrepreneurs.
- They are providers of innovative solutions.
- Their business is to help other people's business (the entrepreneurs).

(Source: Masifern and Masifern, 1997).

The business federation is very much in line with current times. Nowadays diversity is considered a plus, we all want to be part of a strong entity but at the same time enjoy autonomy in accomplishing our tasks, firms seek to maintain flexibility as well as get focused in our accomplishments. This new form has a nice fit with the emerging management paradigm (competence-based management, organizational renewal, empowerment, coexistence of entrepreneurs, leaders and coaches, among others). Pre-eminent companies (Asea Brown Boveri, Banc One, IBM, GE, PepsiCo, to mention a few) are exploring with new organizational solutions in their attempt to provide quicker responses to business opportunities, to become more versatile in front of market changes and be more

fine-tuned to customer needs. Due to competitive pressures, at the same time, smaller companies are struggling to get the advantages of larger ones. The federation provides a framework which gives responses to both types of companies.

3. Building blocks of the federation in knowledge-based companies

Managers feel frustrated when they try to apply classical organizational archetypes to the purpose of developing competences in dynamic environments. Traditional models were built on assumptions that do not hold in the turbulent environments of the 1990's (Quinn, 1992). Past economic regimes rewarded firms for maintaining strong organizational hierarchies and strict work rules. As the new business regime emerges, competitive progress and corporate development are becoming increasingly dependent upon organizational capabilities to continuously adjust to the demands of dynamic environments.

Higher order capabilities, such as organizational capabilities associated with new organizational forms which allow to address current management challenges (Masifern and Masifern, 1997), become critical to building, leveraging, and maintaining competence (Sanchez and Heene, 1997). The business federation puts a strong emphasis on creativity, internal and external collaboration, resource sharing, and responsiveness to consumers. This new organizational form purpues to create "a state of perpetual corporate entrepreneurial in which continuous learning about how to build and leverage new competences more effectively becomes a central activity of strategic management" (Sanchez and Heene, 1997). In addition, the philosophy and rules of the business federation nicely fit with the principles of organizing knowledge and talent-based professionals.

Even though operating as a business federation is a complex task (Masifern and Masifern, 1997), it is possible to identify some design parameters which we believe are more relevant to ascertain the progress towards this organizational form. Here, we focus on autonomy as a proxy of subsidiary, the use of support services as a proxy of boosting units, lack of control, and ownership of resources generated at the business level as a proxy of ownership/power relationships. These four dimensions may provide a reasonable map of federalist behavior of knowledge-based companies.

Autonomy. Managerial autonomy in strategy formulation and implementation has received growing importance in the field of business administration (Jemison, 1980). Granting business unit managers autonomy puts decision making rights in the hands of those who are closest to markets and thus are best able to recognize and adapt to changing market conditions (Goldmann et al., 1995; Frost, 1987). Increased management autonomy to operating units is generally seen as a desirable feature (Kennerley, 1993), especially under increasingly harsh and turbulent environments, requiring flexibility in acting upon new business opportunities. To others, autonomy is not a design choice but a necessary conditions for building an agile enterprise (Asava et al, 1994). Only companies that have placed significant authority close to the professionals will be able to respond rapidly to changes in customers demands. It is also suggested that customization of services at the local level can provide better market access and higher client satisfaction (Campell et al, 1995; Gage, 1992).

In the federation, it is not the center that gives away power by delegation. The corporate level does not provide autonomy to local units. Instead, corporate decision rights are the result of some pieces of power coalescing up in the organization. They are handed

over by lower units to the corporate level, since local managers understand that it is in the best interest of the corporation to centralize those decisions and activities. Beyond that, only under severe cases, when local decisions would violate the common guiding principles or damage the overall organization, the upper level is entitled to intervene.

The business federation operates with discrete local units that have substantial authority when it comes to taking local decisions. Business managers have ample degrees of freedom to adapt organizational standards and rules to the mandates of local circumstances, since it is assumed that the growing complexity and variety of local customer demands put customer-face personnel in better position than corporate officers and staff to address the management issues. Autonomy can provide the basic conditions for fast responses only if managers possess the relevant knowledge and best competence for better decision making. The business federation explicitly recognizes that nowadays competences will be spread across the corporation. It creates the necessary arrangements so that knowledge from individuals, even though widely dispersed across the organization, can be easily accessible to local units. The federation brings into play dispersed knowledge by designing for interdependence and resource sharing, both recognized as central aspects of the business federation (Masifern and Masifern, 1997).

The necessary fit of all organizational parameters suggests that autonomy has to be related to other design dimensions. Galbraith and Kazanjian (1986) claimed that autonomy requires greater coordination by corporate management, while Barnevik (1991) argued that only top management possesses the broad vision to translate a perception of relationships along a series of businesses into reality.

The business federation makes explicit use of other design parameters to complement autonomy in order to build organizational competences to respond to the new competitive landscape. Companies moving toward the federalist structure will need to find means to achieve cohesion among autonomous units, i.e. to get a sense of belonging to a single identity and gain the advantages of a larger size of a the corporation. Autonomous units will benefit from being part of a federated union if this can fulfil some basic tasks which otherwise should be performed by businesses, or can provide resources which enhance the position of its business, or other source of leverage stemming from a larger entity. The existence of support services which boost the competitive position of businesses in the marketplace serves a number of purposes in the business federation, as we see next.

Boosting units (and coordination within the federation). Although addressed in the literature (e.g., Lawrence and Lorsch, 1967; Mintzberg, 1979), organisational theory lacks a rigorous, integrated theory of coordinating mechanisms. The stream of research on competence-based strategic management represents a significant step towards fulfilling this need in the area of knowledge creation and leverage.

Central staff groups represent a significant piece of headquarters cost, and therefore they need to contribute to value creation (Goold, Campbell, and Alexander, 1994). Increasingly, corporate support services are not treated as cost centers but as profit centers. Support services then serve their internal customers (business units), who in turn serve external customers. For example, Barnevik (1991) illustrates examples of market orientation in services drawn from IBM, 3M, ABB, Kodak, Honda, and Xerox. This is line with the rules of the regenerated company, where relationships among organizational units are governed basically by market rules.

The basic rationale for headquarters to supply support services is to achieve economies of scale (e.g. Galunic and Eisenhardt, 1996). Centralizing services at the corporate level can facilitate reaching a critical mass which otherwise would not be possible by duplicated services located at the business level. Centralization entails to develop scale skills, allowing services to be provided more cost-effectively, or functional skills to be better utilized (Goold et al, 1987).

Since the earlier work of Chandler (1962), it is recognized that services and resources from corporate level enhance the action at the business level. For PSFs, receiving support services from the firm enhances the position of a local office in the struggle for prominence in the market place. This is the main reason why support services are referred in the federation as *boosting units*. Yet, the principles of regeneration demand freedom in deciding if each business unit is to use the services, how to use them, and reaching an agreement for valuing internally these services.

The federation provides a context for specialisation of knowledge acquisition, accumulation and deployment, with different roles for different organizational units. Specifically, it sheds new light on the role of corporate services. Boosting units are devoted to internal processes of competence building. Their role is to internally develop new products and services to be offered to business units in order to enhance the competitive action at the business level. Boosting units also serve as coordinating mechanisms of pooled interdependence among business units, due to shared services offered by business units. They address the suggestion of providing means to enhance consistency among different and separate activities (Sanchez, Heene, and Thomas, 1996). Sharing services also contributes with another aspect of relevance given the risks of dispersion in highly autonomous forms. Boosting units constitute a key element of cohesion within the firm. The glue that holds the federation together will come from a number of organizational parameters (e.g., an institutional and corporate strategy, as suggested by Masifern and Masifern, 1997), but similar service offerings in PSFs is a key ingredient.

Lack of control. The need for control has been a pervasive core principle in all the literature drawn from hierarchical organizations. Among managers it has been argued that businesses pursue fundamentally different strategies of control, with some firms relying on bureaucratic, explicit control and others relying on the development of shared culture through processes of socialization. While the bureaucratic control focus on inventions such as job ladders and administrative routines, the socialization processes rely less on formal exchange systems as the practices and decision-making styles will have to become internalized in the way that they become a part of the individuals' value systems.

In our study of PSFs we are particularly interested in socialization as a control aspect because many of these companies have a distinct, unique culture for example in the way recruitment is taking place. When people enter an organization and begin to learn the ropes, they learn how to perceive things, how to make sense out of things, and even what their preferences should be from those in their environment.

In our study of the federation we believe what both bureaucratic and more social control can be used in combination. However, what we believe that managers first of all needs is less emphasis on follow detailed bureaucratic control systems; more on building a rich, engaging purpose behind the company, where control is one of many ingredients. Next, corporate success stories seem to focus less on formal structural design and more on informal channels of power.

Ownership/power relationships. There is increasingly managerial and research interest on less formal ways of getting things done, these less formal methods rely more on power, leverage individuals' positions in social networks, and entail ongoing negotiations among organisational participants. In the ownership of resources, informal, non hierarchical influence have become more important. Organizations have flattened their hierarchies, taking out levels of management as well as leagues of middle management. There is simply less hierarchy left. The increasing emphasis on high-commitment or high-involvement work practices and the concomitant emphasis on self-managed teams (e.g. Gupta et al, 1991), means that the exercise of formal, hierarchical control is less consistent with organisational values and ways of organising.

Masifern and Masifern (1997) point out that the federated units cannot depend economically on the center if they are to fully exploit their potential. Masifern suggests that identifying who enjoys the ownership of resources generated by the federated units (such as cash flow, knowledge assets, or even clients) could illustrate the nature of the relationship.

Ownership is also a reflection of power relationships in the federation. Research has identified numerous sources of power for both individuals and organizational submits (Perrow, 1986). In the federation, structural power, deriving from position in a network of relationships, may not be as important as competence-based authority, derived from expertise in areas used by other units. The federation needs to develop the rules which govern the use of resources spread in the organization when serving local markets in a way that the overall company benefits.

4. Professional service firms (PSFs)

4.1. PSF and competence-based strategic management

Over the last five decades, or so, a pronounced structural change has taken place in industrialized countries. The service sector has shown a remarkable growth measured among dimensions such as share of GNP, employment, and international trade.

In this paper we limit our analysis to a subgroup within the service sector called professional service firms (PSFs). These companies must be successful in the talent market and the client market.

In the talent market the critical aspect is to handle competence as a resource. In PSFs competence must continually be built in order to stay competitive (Heene and Sanchez, 1997). The emphasis on competence in the talent market can have positive effects on how the PSF handles the client market. For example, by building competence within the organization the relationship with knowledgeable buyers can become smoother.

However, there are no clear rules for client handling for PSFs because in the nature of interaction with the client may vary. Maister (1993) classifies projects under three categories. A client's problem may be ill-structured and request a customised service. The customer would then choose a PSF with an outstanding ability to develop a solution on the basis of state of the art expertise. Maister refers to this first type as "brain projects", involving a highly skilled and highly paid professionals. A second case takes place when a client faces a problem that is familiar to the PSF, in the case that similar knowledge that is needed for the focal project has been applied on other cases. Clients with these kinds of problems seek firms

with experience in solving similar problem; what Maister (1993) calls “grey hair” tasks. Thirdly, a client might face a well-recognised and familiar type of problem. The operational steps can be rather programmatic. Maister calls this type of professional job a “procedure project”. All these kinds of tasks demand local adaptiveness to customise the service of the PSF, yet we would expect that the advantage of the federalism would be more apparent in the first and second categories.

The information asymmetry or knowledge gap between the service provider and the client also creates challenges for both the PSF and the clients. PSFs are typically hired because they have some expertise that the client does not have available. When there is a significant information asymmetry between the client and the PSF in the sense that, even ex post, the client is unable to determine unambiguously the value received (Friedson, 1960; Karpik, 1989), signals of value and quality are demonstrated through successes such as winning an architectural competition or obtaining a Nobel price. The more specialised the expertise is, the more difficult it is for the client firm to evaluate the quality of what is, or is to be, delivered, in accordance with the moral hazard problem in managerial economics, where market signalling is a means for potential employees to reveal information on their performance potential (Spence, 1973). While the information asymmetry in second-hand product markets leads to the poorest quality cars (“lemons”) offered for sale (Akerlof, 1970), the same information asymmetry in professional services appears to lead to a premium price and high demand for highest quality services.

4.2. The PSFs and the federation

As mentioned, the success of PSFs is either won or lost in the market for clients, and the market for talent. Professional service firms then can be characterised by a successful blend of projects won, projects completed, and people recruited. When slack professional time available is adequate to accommodate work on new proposals or potential clients, the firm may be able to develop and maintain positive spirals of value creation (Normann, 1991), whereby excellent professionals are able to perform outstanding on profitability, professional development, and improved procedures. On the other hand, professionals without interesting work quickly search elsewhere for new challenges. If this should happen, the probability of winning new projects is reduced.

The extent to which the PSF is able to move closer to the federation is dependent on the ability to build and sustain competence. The value of competence as a human assets to the firm will depend on its ability to attract, retain and develop highly qualified professionals. PSFs rely on several organizational processes to accomplish this goal. It is critical for the PSF that the professionals pull together and develop a strong and competitive culture to retain the best experts. Project teams and network designs are used to develop share values as well as to bring together a diverse set of professionals. Organizational solutions, based on extensive autonomy and empowerment, shared understanding and trust, mutually reinforced interdependence, arm’s length supervision, as the business federation provides, will contribute to retain qualified professionals.

PSFs seem to represent a kind of “inverted organizations” capturing managers’ and academics’ interest. With their flat structures, service-oriented workforce, and consensus-oriented decision making processes, these firms are becoming benchmarks used by other types of companies in order to organize knowledge as a critical resource (Quinn, 1992). Therefore, we use PSFs as the empirical setting for this study because we believe the federation addresses some management challenges for this type of companies. In addition,

insights from studying PSFs may be useful to companies in other industries, to the extent that they are looking at them as a reference on how they may want to move in the future.

5. Methodology

Given the nature of the consulting business, a priori we expect that consulting services provide a very adequate setting for the adoption of changes in design parameters which represent moves towards the business federation form. Theoretical developments of the federation suggest that this form provides a way to balance the need for both coordination and local autonomy, gaining the benefits of both efficiency and flexibility. Therefore, insights derived from the business federation should have power in explaining the phenomenon of specific configurational choices in strategy consulting companies. So, an implicit general hypothesis of this study is that sampled companies will provide general support for the adoption of the design parameters as representative of closeness to the business federation. To the extent, that consulting companies share some characteristic of the federation form, we try to relate specific design choices with growth, as a measure of company performance.

Theoretical developments of the federation suggest a way to balance the need for both coordination and local autonomy, gaining the benefits of both efficiency and flexibility. Therefore, insights derived from the business federation should have power in explaining the phenomenon of specific configurational choices in strategy consulting companies. An implicit general hypothesis of this study is that sampled companies will provide general support for the adoption of the design parameters as representative of closeness to the business federation. To the extent that consulting companies share some characteristic of the federation form, we try to relate specific design choices with growth, as a measure of company performance.

Given the scarcity of accumulated knowledge on both the business federation as theoretical ground to explain organizational choices, and strategy consulting as empirical setting, we selected theory-building goals, research design and data-collection methods accordingly in an exploratory manner.

Sample

Companies providing top management services in Norway and Spain are the initial population of interest. Top management services here are conceived to include strategy, both formulation and implementation, as well as related areas such as restructuring, mergers and acquisitions, etc. Given that this research is restricted to the internal configuration of firms and the relationship between the periphery and the centre (1), consulting companies needed to have several offices.

The unit of analysis was the top-management consulting service referred as within the local office of management consulting companies. As suggested by Glaser and Strauss (1967), focusing on a relatively homogeneous group will enhance the likelihood of correct interpretation of common categories. The same authors suggested that the differences

(1) The federation can serve as a mechanism governing inter-firm cooperative activities (Provan, 1983; Masifern and Masifern, 1997), yet this is not the research subject here.

between observations should be maximized. We chose to minimize differences in terms of the nature of activity being conducted by sampled firms (a focus on strategy practice and two possible geographical markets), while allowing differences in other office and company attributes (such as the core service which originated each firm, year that the company was founded, geographical origin, company and office size). In addition, we included both fast growing and stagnant companies. Initial interviews, prior to the survey used here, suggested a variety of organizational design practices, some closer to the main characteristics of the federation and others removed from it. Interviews and a simple demographic survey contributed with basic information about the sampled companies. Table 1 outlines the demographic features of companies that comprise this study.

Sixteen consulting companies agreed to participate. Three companies contributed with responses from both their local offices in Spain and Norway, allowing a greater depth of understanding of the firms design decisions (identified hereon with sub indexes a and b). A total of 19 local enterprises were studied. Ten offices were located in Norway, eight in Spain and one company reported on its office in Portugal. All companies were international in their scope of activities, yet with varying degrees of international exposure. Four were in their initial stage of internationalization, two of them with more than half of operations based in their home country. Nine companies had been initially incorporated in the United States and seven in Europe. All companies offered other management consulting services (information technology, operations, finance, privatization, human resources, business process re-engineering and other) in addition to top-management consulting. Six were highly diversified firms covering most of the spectrum of these consulting services. Five companies were consulting branches of firms initially created with a primary involvement in auditing, corporate finance and related areas. Eight companies had top-management services as their primary area of concern. Finally, three companies were created after 1990, raising some concern on the inclusion of these firms on the test of the relationship between closeness to the federation and office growth, the latter being selected as the performance indicator for this study.

Table 1
Description of companies

Comp.	Geographic Focus	Firm Created	Office Opened	Number Services	Company Size	Office Size	Num.Off. Europe
	[1]	[2]	[3]	[4]	[5]	[6]	[7]
1	Local	a1981	1980-89	F	S	S	S
2	Local	a1981	a1990	F	S	S	S
3	Intern.	b1930	1980-89	M	M	M	M
4	Intern.	1961-80	1980-89	M	M	M	S
5	Intern.	1930-60	1970-79	D	M	M	M
6	Intern.	1961-80	a1990	M	S	S	S
7a	Intern.	1961-80	a1990	F	M	S	S
7b	Intern.	1961-80	1970-79	F	M	S	S
8a	Intern.	b1930	b1970	M	L	L	L
8b	Intern.	b1930	b1970	M	L	L	L
9a	Intern.	b1930	b1970	D	L	L	L
9b	Intern.	b1930	b1970	D	L	L	L
10	Intern.	b1930	b1970	D	L	L	L
11	Intern.	b1930	b1970	M	M	M	L
12	Intern.	b1930	b1970	F	L	M	L
13	Intern.	1930-60	1980-89	M	M	M	M
14	Intern.	b1930	1980-89	F	M	S	M
15	Intern.	b1930	1970-79	D	M	M	S
16	Intern.	b1930	1980-89	D	M	S	S

Notes:

Specific numbers are not provided for confidentiality reasons, due to an agreement not to provide any piece of data which could lead to disclosure of participating companies.

[1] Local means more than 50% of operations were based on the home country; international otherwise.

[2] Year that the company was created (not referred to the last transformation such as merge, or split, but the original founding): “b” means before; “a” means after.

[3] Year that the surveyed office was opened: “b” means before; “a” means after.

[4] Number of consulting services offered by the office (among the following: strategy, IT, BPR, operations, finance, audit, HHRR, marketing, privatization/ government, change management; others additional would count as one). F: Focused, M: Medium number, D: Diversified.

[5] Number of consultants that the company has in Europe. L: More than 2000, M: Between 400 and 2000, S: Less than 400.

[6] Number of consultants of the office. L: More than 200, M: Between 50 and 200, S: Less than 50.

[7] Number of offices in Europe. L: More than 50, M: Between 25 and 50, S: Less than 25.

Data collection and measurement schemes

The study collected quantitative data, through a survey, which was complemented with on-site personal interviews for some of the companies. After initial interviews and data collection from archival sources, and a pre-test of the instrument with two consulting companies, we sent out the questionnaire in October of 1997. The interviews were carried out between July and November of 1997. Some companies accepted to be interviewed several occasions.

A questionnaire was used as the primary data collection instrument (see Appendix 1). Interviews helped us to sharpen our ability to measure and understand the phenomenon under investigation. Our insights and interpretations from quantitative analysis were contrasted, when possible, with the use of qualitative data, collected prior and after the distribution of the survey. Even though this research follows exploratory techniques of data analysis, it tries to complement some features of multiple case-study designs with the strengths of quantitative analysis. Jointly, they both allow the collection of a broad range of data from a variety of sources, as new items are gathered in an iterative fashion, based on insights gained during the course of the study.

The main research issue is to identify the extent of closeness to the federation form, and subsequently to study whether this has any relationship with growth. We use here four dimensions which would be included in the identification of this new form; yet, we agree that these do not suffice to conclude that a company is operating under a federation form, on the basis of these limited attributes. This is a major reason because we present this research as progress towards the business federation, and not as adoption of the new form.

Analysis

In accordance with the exploratory purpose of this research, the data analysis used a number of simple techniques with an approach to maximize what could be learned from the data collected rather than theory validation. The first step was to create indexes of “closeness to the federation” for each of the four design dimensions. For each item in the questionnaire, we computed the proximity to the “ideal response” of a company operating under the federation form. This represents transformation of data with the use of a similar Likert scale, from 1 to 5, as included in the original survey. It was directly related to the number of services for which the office had to pay, since we imply that paying for a service would entail freedom to use it or not.

The second step was to compute the composite measures described in the preceding section. The focus on design parameters, as well as their relationship with growth, the latter just in terms of profits and revenues. We will not specifically deal with the construct of strategy, and will not include growth in other than the two aforementioned financial aspects.

Some basic descriptive statistics for the variables of interest are as follow:

	Mean	Mode	Median	St. deviation	Range
Autonomy	4.13	4.15	4.15	0.62	2.82-5.00
Boosting Units	3.74	3.33/3.67	3.67	0.63	2.67-5.00
Lack of Control	3.09	2.00	3.00	1.01	2.00-5.00
Resource Ownership	4.25	5.00	4.25	0.79	3.00-5.00
Growth	4.36	5.00	5.00	0.94	2.00-5.00

A basic obstacle in our analysis is that we face an important problem of right censoring for the growth variable. A significant number of companies reported the top level of growth on revenues and profits. Further studies will use a broader scale of growth as well as alternative indicators of office performance.

Given the initial distribution of single variables and the small sample in this first study, a correct use of traditional multivariate analysis could not be guaranteed. Therefore, just as preliminary test of the relationships, we computed correlation analyses between variables, both the complete set of data as well as using a number of partitions of the sample, which could be illustrative of the underlying relationships for specific types of companies. We mainly used the demographic characteristics discussed above, which included the attributes of table 1.

6. Findings

The first insight derived from the analysis is that, overall, the companies included in the sample provided high degree of autonomy to their local offices. Our ex ante predictions that management consulting firm can be described with federalist elements was expected due to the nature of the consulting industry.

Reasonably high levels of autonomy at the country level could be expected given the need for local adaptiveness of most of consulting services and the fact that competitive advantage in this industry is more easily associated with the ability of the company to tailor made its services to clients' needs. (It is worth mentioning that only four items out of 14 that composed the autonomy composite got averages below 4.00. Remember that a 5 would imply the local offices had full authority to decide on a specific issue, given that we are always measuring closeness to the federation. Mean values for those items where authority was less decentralized were: promotion to a partner position (3.20), changing the business strategy of the local office (3.36), the decision to merge with another national company (3.58) or entering into an alliance at a national level (4.00). In similar vein, mean values for another design dimension, the retention of ownership by the local office over the resources generated at the local level, turned out to be also high. Local ownership of professional skills was rated 4.66, ownership of clients 4.55, while cash flow generated and cash available both were rated 3.88. Less strong, but still significantly high was the availability and use of boosting units to strengthen the competitive capability of local offices. On average, the availability of services was rated 4.73, the freedom in the way to use these services 3.84, and having to pay for the services that local offices receive was rated 2.63, the latter meaning that, in about half of the cases, offices have to pay for the support received, and therefore we can imply that the use of the corporate services reported here was not mandatory for local offices.

The results for the construct of lack of control of local offices are somehow disappointing. The overall evaluation of closeness to the federation is not that high (a mean value of 3.09, which would translate into an approximate quarterly reporting practice overall), significantly more distant than the other three design dimensions. It may be that, in effect, the performance of local offices is closely monitored, implying a deviation from the basic principle of strong leadership of the local units within the federation or, as mentioned before, that frequent reporting serves purposes other than control, as it would be the case for information sharing and benchmarking for self-management purposes, which would not contradict the federation logic.

Out of the insights made from different partitions of the company set, one worth mentioning is the distinct result of closeness to the federation of seven offices which belonged to companies originally based on audit and finance services as compared with the remaining companies. The average rates of the set of five companies (seven offices) were higher than that of the rest of companies for all concepts. The actual mean values were as

follow: autonomy (4.57 vs. 3.88), boosting units (3.90 vs. 3.64), lack of control (3.23 vs. 3.00), resource ownership (4.79 vs. 3.94) and growth (4.50 vs. 4.29).

We explored the relationship between design dimensions and growth with two different approaches, one based on rank order of the values in the distribution of the four design parameters and growth, and the other with the use of correlation coefficients.

The logic of the theoretical framework suggests that the closer a company is to the federation the higher its growth should be, while low values of closeness to the federation would be associated with lower growth rates. Ranking the offices in ascending order on the basis of each design dimension and growth provided us with interesting insights. In line with the logic, higher ranks meant closer to the federation and higher growth, and lower ranks would imply a distant position from federation and lower growth. Ten offices provided very good fit with this logic: six offices got very high ranks for both the design dimensions and growth, three offices got intermediate ranks for both, and one obtained low ranks for the design dimensions and growth. Out of the remaining set of companies, seven offices provided reasonable fit and two could be assessed as unfitted. One of the problematic responses come from an office with low values for the federation dimensions, yet very high growth; this was mainly due to the fact that the office had been very recently opened, so relative growth was explosive, even though absolute growth was not. The other divergent response has been associated to misinterpretation of the specific item within the survey, as additional data suggested that the firm responded with average annual growth for the five year period rather than total growth rate for the same period. In some of the subsequent analyses, we dropped these two observations, since its characterization as outliers could be justified.

The analysis of the sorted data provide interesting insights. Out of the ten offices with good fit with the logic, all the six offices closer to the federation come from companies created before 1930. Also, the offices had be opened before 1970 in all cases but one, which opened in the 1980-89 period. The company size, in terms of number of consultants in Europe, was large; the office size was also large, and the companies closer to the federation had an extensive number of offices in Europe. On the other hand, none of the four companies more removed from the federation was created before 1930 and only one in the 1930-60. None of the latter companies had been classified as large, the office was always characterized as small or medium sized, and the number of European offices of the firm was small in all but one case, that had a moderate number. However, no conclusion could be drawn on the relationship to the number of services provided, since there were representatives of diversified, mid range and focused firms in both categories.

The relationship between the four design dimensions and growth was also investigated with the use of correlation coefficients (r) with the original composite indexes (not the ranked variables). Putting all firms together, all correlations (r), generated from the test of the relationship of each dimension with growth, were low. The correlation with autonomy increased when the two problematic responses mentioned before were dropped, leading to $r_1=0.23$, which got up to $r_1=0.40$ when a third questionable company was removed and topped its highest value $r_1=0.91$ for a test within a set of five companies which could be characterized as “strategy boutiques”, meaning that strategy practice was a dominant activity within the set of services provided by the company.

The correlation between boosting units and growth was moderate in most of the partitions tested, reaching its highest value when applied to the subset of ten offices mentioned in the last two paragraphs on rank order analysis. Within the ten offices with good fit with the logic, $r_2=0.52$. For the subset of “strategy boutiques”, r_2 was 0.42. The

computation of r for the relationship of lack of office control and office growth was negative in most of the cases. It was surprising the high values it received in some cases ($r_3=-0.95$ for “strategy boutiques”, or $r_3=-0.58$ for diversified companies).

The test of the relationship between ownership of resources generated by the local office and office growth (r_4) also got diverse results. The highest value come again from the subset of the ten offices fitted to the logic, $r_4=0.94$, yet with varying indexes in other cases. For instances, looking at the diversity of services offered by the companies, r_4 was 0.53 for focused companies, while it was -0.54 for mid range diversified firms, and -0.31 for highly diversified companies.

Other partitions, such as by geographical market, by number of offices in Europe, by office size, for the subset of firms originally created on the basis on audit and finance, etc. are not reported here for the sake of brevity.

7. Discussion and implications

Our results suggest that the management consulting firms move close to the federation form. However, closeness to the federation of a company cannot be assessed on the basis of a single design dimension. Neither do we believe that the four dimensions used here are enough to characterize the actual organizational design of a firm as an illustration of a Business Federation form. Yet, our results suggest that firms included in our sample follow organizational practices that fall close to the federalist behaviour, along the aspects covered by this study. This similarity seems stronger for older and larger companies, which is in line with the argument that the federation may be an organizational solution reached by firm unsatisfied with more traditional organizational forms.

The business federation form is not theoretically derived, but an attempt to develop a robust solution to novel practical problems. Yet, the framework of competence-based theory helped us to develop the logic of organizational role of its internal units and their interaction. By paying attention to the logic of organizational and cognitive processes and opening up the firm’s “black box”(Heene and Sanchez, 1997), we will progressively understand the rationale of moves towards the federation by management consulting firms.

This research does not support the claim that companies become more bureaucratic as the get older. Rather, the federation may be a stage of evolution for some companies to respond to current competitive demands. Yet, as Masifern mentioned, a company reaches this new form in a process of organizational evolution. We believe that PSFs will move forward to the federalist design in their attempt to build, leverage, and maintain competence (Sanchez, 1993, 1995). The federation provides a framework on how to build and exploit competencies in a coordinated way. We see this as the heart of the entrepreneurship in all organizational units within the federation, with different implication for how this entrepreneurial character will manifest.

The high levels of the design dimensions may be a growing competitive necessity in the consulting industry rather just a source of competitive advantage. In spite of this, the overall high values, as compared with some initial findings from other industries, do suggest that the federation will be easily accepted in customer face industries with high degree of turbulence and dynamism.

The finding of a reasonable fit between closeness to the federation and growth with we use of exploratory data analysis is encouraging. The initial expectation that operating under a federation form may constitute an organizational capability of firms is still valid. The use here of a composite measure of growth made up of both profits and revenues implies that the two objectives are served jointly, rather than having to compromise. With a larger sample and a more spread measure of performance it would be possible to run multivariate analyses to evaluate the direct effect on each of these design dimensions as well as control for the effect of variables which probably moderate the effect. The conclusions provided here can only be partial and preliminary, as a result of the limited insights obtained from partitioning the data. The finding of support for the logic of the federation within specific subsets of companies contributes to suggest that a more complete study should be very illustrative of the underlying relationships present in the data, but which we are not capable to fully identify.

8. Conclusions

The competence-based stream of research seems to suit nicely the logic on the federation form. Both play high importance to organizational processes to address the demands of the dynamic and uncertain environments. Yet given the preliminary nature of developments on both areas, and the complexity of the Business Federation form, we believe that company moves will be adopted in a progressive way.

Complex companies, such as consulting firms, need to get both the benefits of adaptability and efficiency, to come closer to the customer and benefit from being part of a large system which provides support services. Furthermore, the management consulting industry, because of its activity, seems to go further along the road to decentralization, and some companies are likely to become federated. Large and older companies operating in multiple geographical locations or multiple businesses seem to be ahead in this emerging evolution.

The federation is not the only path. Some companies are retaining high degrees of centralization as they expand globally, but we do think that the trend is going in the direction identified here.

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Appendix 1

Questionnaire

We are interested in the Top Management or Strategy Consulting practice, even though your company may offer other services. By “head office” we mean regional office at European level, central corporate office, or the set of core partners usually referred as the firm. The relevant situation is the one prevailing in September 1997.

Note: A similar instrument was used for companies in Spain with logical adjustments in the country reference.

QUESTION ONE

To what extent does the Norwegian part of the consulting firm have flexibility in customizing a service to a specific client?

(put a circle around one of the numbers)

1	2	3	4	5
Total flexibility in customizing services	Relatively high flexibility in customizing	Moderate flexibility in customizing	Low degree of flexibility in customizing	No flexibility in customizing services

QUESTION TWO

What is the nature of authority that the Norwegian office has on the following issues?

(put a circle around a number on each dimension)

	Full authority to decide	We decide, but head office can approve or refuse	We decide jointly with head office	We suggest, but head office decides	Our local office has no say on the issue
Standard client fees	1	2	3	4	5
Discount rates on basic fees	1	2	3	4	5
Schools you recruit consultants from	1	2	3	4	5
Promotion to a partner position	1	2	3	4	5
Hiring a new manager	1	2	3	4	5
Distribution of consultants working time	1	2	3	4	5
Composition of a local project team	1	2	3	4	5
Use of local skills demanded by a foreign office	1	2	3	4	5
Changing the business strategy of the office	1	2	3	4	5

Appendix (continued)

QUESTION FIVE

How often do you have to send reports on the following matters to the foreign office you report to? (put a circle around a number on each of the dimensions)

	Once a month	Quarterly	Annually	Never
Revenue figures	1	2	3	4
Profit figures	1	2	3	4
Other performance indicators (specify)	1	2	3	4
Other performance indicators (specify)	1	2	3	4

QUESTION SIX

Who is the “owner” the following resources generated by the Norwegian office?

	Norwegian Office	Regional Office	Head office	Not relevant to our situation
Cash flow generated	1	2	3	0
Cash available	1	2	3	0
Professional skills (people)	1	2	3	0
Clients	1	2	3	0

QUESTION SEVEN

If you have to weight the source on value you add to your clients, how would you divide 100% points?

Designing specific solutions for clients’ problems (product leadership)	___ %
Strong relationships with traditional clients (customer intimacy)	___ %
Better delivery of services available in the industry (operational excellence)	___ %

Appendix (continued)

QUESTION EIGHT

We would appreciate to have an indication of the growth rate in recent years for the Norwegian unit (only for the top management consulting practice). We kindly ask you, for those items you feel comfortable with, to provide the total increase from 1991 until 1996 (not average annual, but total).

Increases on:	Less than 10%	Between 10 and 25 %	Between 25 and 50 %	Between 50 and 100%	More than 100 %
Number of management consultants	1	2	3	4	5
Total compensation to personnel	1	2	3	4	5
Revenues	1	2	3	4	5
Profits	1	2	3	4	5
Return on revenues	1	2	3	4	5
Fees, Prices	1	2	3	4	5