



## ***Organization Structures in the Distressed Company***

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Why is an organization structured as it is and when are changes to this structure appropriate? When we think about the term organization structure, we think of the formal structure of the organization chart of the company. That is, the CEO is at the top with various officers reporting to him or her and each successive level reporting to the next. The purpose of the organization structure is to allow an organization to harness its human resources in a way to achieve a desired outcome. In other words, not everyone can report to the top boss and therefore we have to develop a way to best organize to have the greatest impact.

In most businesses the classic organizational structures include:

- **Functional Structure** – In which each function within a company stovepipes up to the executive management, thus, accounting is a function, sales is a function, engineering is a function and so on. These functions support the operating entities in the organization.
- **Divisional Structure** – In the divisional structure, the company's staff is organized by division and each division will have all, or most, of its own functions, including support functions. Therefore a division that sells to the military will be a relatively autonomous group having its own marketing and accounting functions. Likewise, a division that sells to another industry will have its own marketing and accounting functions.
- **Matrix Structure** - The matrix structure essentially combines elements of the functional structure and the divisional structure. As example, in a matrix structure, each division may have an accounting person assigned to it, but each of these accounting people will report up to the chief accounting officer.
- **Flat Structure** - In a flat structure, all employees tend to report to one, or a very few, executives. This is seen typically in founder operated business with a strong founder who likes to have influence on every decision. This is not a very scalable model.

However, in the past decade or two, there has been an increased emphasis on more non-traditional models including:

- **Team Model** – Within this model, resources are grouped in teams. The teams may be permanent or a fluid grouping of personnel that is brought together for a specific time or task.
- **Virtual/Informal Model** - In these models, small teams run an organization and use external resources to complete most tasks. We see the more informal models heavily used in the technology industries and start-up organizations.

This article addresses how organizations tend to change during times of disruption and turnaround. The experience of most professional turnaround practitioners is that a structure that was put in place to support long-term growth tends to need alteration to support the transition back to profitability.

### **Five Stages in a Successful Turnaround**

Turnarounds by definition are times of great change. We know that one of the most significant predictors of success in a turnaround is the organization's willingness to embrace change. Underperforming companies must almost always initiate change to have a chance of turning around. While change is not the only driver of a turnaround, very few turnarounds will have any chance of success if there is a resistance to change.

The Turnaround Management Association (TMA), the largest association of professional turnaround practitioners in the world, has identified the following as the five classic stages of a successful turnaround:

- Changing Management
- Analyze the Situation
- Implement an Emergency Action Plan
- Restructuring Business
- Return to Normal

Turnaround leaders are always biased towards action. Change is the one constant element of turnarounds. In the five classic stages of a turnaround, we see the overriding theme of change; change management, analyze, change through emergency action plan, change through restructure. Every stage of the process generally involves change to the organization, manpower and resource allocation. While there is no one model that fits all turnarounds, there are some common elements that are relevant to the discussion of organizational structures during turnarounds:

### **Flattening of the Organization Structure**

Turnaround leaders often tend to flatten the organization structure. The height or flatness of an organization relates to the number of layers within an organization. A tall organization is one with many layers; while a flat organization is one consisting of fewer layers with more employees at each layer. The flattening of an organization during a turnaround allows the leader, or leaders, to have better clarity of changing situations and more impact on both the speed and direction of decisions. Flattening an organization structure allows for change to occur quickly and for these refinements to changes to be implemented rapidly.

Because of the uncertainty and dynamic nature of turnarounds, very rarely does every change work as planned. The turnaround leader must be able to analyze the impact of each planned change and be prepared to make adjustments to reflect any unintended results. Since taller

organization structures have more layers it tends to inhibit this required speed while flat organizations tend to support it.

### **Organizational Informality**

In companies undergoing a turnaround the organization structure tends to be less formal. In this regard, the term informality is used to indicate that the organization does not follow strict chain of command. Employees are expected to do what needs to be done in order to achieve a goal without regard to strict organization structure issues or allocation of resources.

In healthy companies operating under normal conditions, formal organization structures are generally more attractive as they tend to allow for more long-term planning and better allocation of resources for long-term initiatives. However, in turnarounds, this formality tends to slow decision making and plan implementation. Turnaround leaders will often spend time with employees at various levels within the organization and will often bypass the formal chain of command structure. This informal structure allows the leader to gain a better level of understanding of how the turnaround plan is being implemented at the staff level. It also circumvents selective and biased, information flow as information moves up an organization. In turnarounds, chains of commands will often have a feeling of the childhood game 'whisper down the lane' where each successive person who touches information may unintentionally, or intentionally, alter the information until it becomes unrecognizable. This phenomenon can render dead even the best turnaround plan.

The informality of the structure has the consequence of allowing individuals at all levels of an organization to contribute without regard to their formal title or the resources allocated to them. Generally, the only barrier is their ability to contribute to the success of the turnaround.

### **Fluid Organization Structure**

Organizational structures in companies undergoing a turnaround tend to be very fluid. In high performing organizations, the organization structure tends to be fairly rigid. The rigidity of a healthy organization allows it to have predictable structure and allocation of resources. This in turn, supports longer term planning and initiatives. On the contrary, in turnarounds, this same rigidity paralyzes quick decision making and fast implementation.

In healthy organizations, changes are usually only made after substantial analysis and research; again, this supports longer term planning. In contrast, during a turnaround, the organization structure tends to change more often. As changes are made to the turnaround plan, or as the company begins to achieve early goals, the organization may require changes to continue to progress along the turnaround path. In a turnaround, the organization structure must be the servant of the plan. As the plan changes or progresses, often the organization structure must change as well.

### **Allocation of Resources During the Turnaround**

Oftentimes, during a turnaround, the resources of the company are very constrained. Most companies undergoing a turnaround also have some level of liquidity constraint, or other

significant resource constraint. These constraints necessarily have a limiting impact on resource allocation. During a turnaround the resources of a company; human, financial and otherwise, flow to the areas of the business that can achieve the goals of the turnaround. The areas of the organization with lower profit potential, or whose profits may be more speculative, tend to receive lower resource allocation. In contrast to a more stable organization, resource allocation tends to move towards near term goals at the expense of longer-term plans.

When a company is healthy the resources tend to be allocated through a formal process. During a formal budget process, often both the financial and human resources of an organization are evaluated on an annual basis. Once this process is complete, the organization has a pretty formal road map for staffing levels and budget levels for some period of time, usually one year, but perhaps longer.

During turnarounds, resources are generally allocated less formally and more frequently. Approvals for expenditures, other than minor ones, or changes to staffing levels (both increases and decreases) tend to be made continually as change occurs and progress is made in achieving the turnaround plan. Allocation of the resources of the organization literally can be made on a weekly, or even daily, basis as circumstances change. Often, the senior leaders of the organization will meet weekly to discuss how to best allocate the resources to meet the changes and challenges confronting the organization.

### **Individual Performance Matters**

In turnarounds, each individual who can contribute is given tasks that fit well into their skill set. Turnarounds are generally not times with large investments in employee development. Generally, turnarounds are not times with large investments in employee development and the organization must deal with what skill sets employees currently have and not focus on developing new skills. The function of employee development, while critical to long-term success, must often wait until the turnaround is complete. Therefore, often structures have unusual components to deal with the particular strengths and weaknesses of the current employee base.

In many healthy organizations, high performing employees are rewarded for their results by being assigned additional responsibilities that often include management of other employees. This is often done without regard to whether the employee has actual management skills and often without any real training on management techniques. During turnarounds, it is important to ensure that functions that require significant management responsibilities are staffed with professionals that have proven management skills. Finding employees who have been promoted solely based on having achieved well in a tactical position and been given management responsibilities without the requisite skills is an important task in the turnaround plan. To ensure more success in the turnaround plan, these employees are refocused back to the tasks that made them successful and management responsibilities are either supplemented with assistance from stronger managers or are completely eliminated.

During a turnaround, often an employee will have responsibilities changed so that their best attributes can be accessed while weaknesses can be limited. Combined with the fluid and informal organization structure, these responsibility changes can be a formal official change; an unofficial change with no change to title but only to responsibility; the change can be permanent in nature or just for a specific period until skills can be developed or the organization can be reorganized again.

At times, outside hires are supplemented to eliminate organizational weaknesses. While outside hires can have a positive impact on the turnaround plan there are several issues that must be confronted:

1. Attracting qualified employees during a turnaround can be difficult; often turnaround managers will seek professionals that have familiarity and confidence with the executive's success. This improves recruiting success.
2. Finding employees that can quickly come into an organization and add value, while the organization is experiencing significant change, is difficult and the pool of potential applicants is necessarily limited.
3. Time required to recruit and hire, takes time away from turnaround plan.
4. Due to perceived risk in distress organizations, qualified prospective employees will often require a compensation premium to accept a job.

To the degree that there is a significant skill gap, the turnaround leader will often look for one or two key hires that can have a great impact on the turnaround plan. These hires are often known professionals who have been through turnarounds. This improves the probability that the on boarding employee will have the ability to add value immediately. Addressing any remaining holes in the organization requires altering the organization structure to maximize the strengths of current staff.

### **Use of Managers and Leaders**

Turnaround leaders generally have very specific uses of managers and leaders. Understanding how to use natural leaders and how to use skilled managers can have a very big impact on the success of the turnaround.

Turnarounds are usually ran by one strong leader who has a very defined vision of the future and how to get the organization to the future. However, these strong leaders are generally supported by other employees in the organization who possess leadership skills. Lower level leaders are critical to keeping the workforce motivated, selling the vision of the company to vendors and customers and otherwise carrying the turnaround flag throughout the organization. These specific individuals allow the turnaround effort to be scaled and eliminates the requirement of one executive leader to do everything. While the single executive leader may choose those in the organization who he believes possess leadership skills, during turnarounds many of these lower level leaders find a way to be self-selected. They find ways to add value and bring forth new ideas. They tend to get the notice of the senior leader and find a way to have their voice heard and their actions to have impact. These lower level leaders often

have little, or no, formal authority and may have little, or no, resources directly reporting to them. These leaders can have a significant impact on the strategic direction of the turnaround and its ultimate success.

Those with management skills are also important to the turnaround effort. Managers with strong process and organizational skills are used to tactically achieve the plan laid out by the leader(s). They are used to corral the mass of resources of the organization to perform the task required to achieve the turnaround plan. These managers tend to have strong tactical skills but may lack true leadership skills.

True management skills are critically important in the turnaround effort. While the leaders set the tone and develop the map, it is the managers who can organize the efforts of the staff. Placing employees in significant management roles that do not have strong management skills or who do not fully believe in the turnaround plan can cause a critical error in the turnaround process.

In summary, healthy organizations tend to have formal organizations that change infrequently. They have very formal processes for decision making and the allocation of resources is generally performed in a formal process. Further, healthy organizations tend to provide an opportunity for employee development and staffing decisions may be made with the aspirational idea that the employee will develop the skills required through on the job training.

During turnarounds, organization structure tends to be very different than healthy organizations. Organizations are much less formal. The actual structure for operating the business and making decisions may be very different than the formal structure on paper. Employees, and especially leaders, are expected to contribute beyond their given title or position on the organization chart. Changes to the formal reporting structure and organization structure tend to happen frequently and informal changes may be constant.

In turnarounds, the contribution of employees tends to be significantly a function of their ability and desire to contribute, much more so than a function of the formal structure. Because of the pace of work required to achieve a turnaround plan and the continual changes, the strengths and weaknesses of employees are more evident.

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