

# Organizational Structure

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## 1. Control in the market and in organizations

Market	Allocation of property rights	Automatic evaluation of consequences	Automatic compensation
Organization	Allocation of decision rights	Artificial evaluation of consequences	Artificial compensation

*Example: trucking in Europe and the USA*

### Comparison

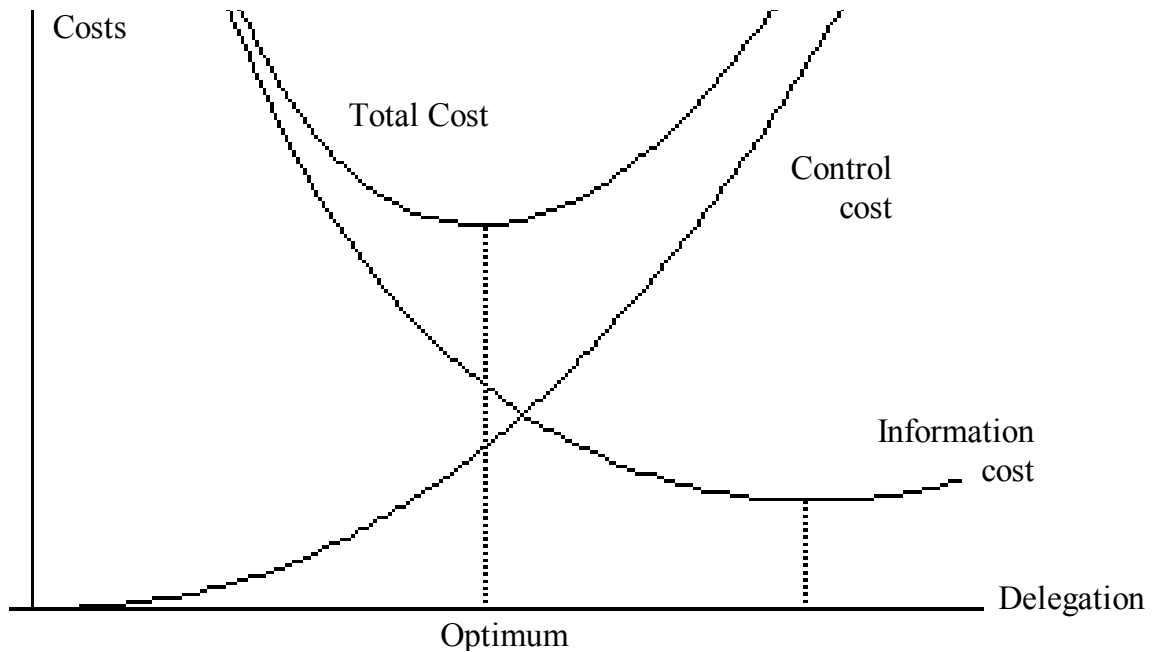
	Market	Organization
Control mechanism	prices system	allocation of rights, measurement and compensation systems
Rights	alienable property rights	non-alienable decision rights
Characteristics of control	natural, automatic, explicit	artificial, planned, diffused
Development of control	Complete	Variable

### Examples

- a) Property and information: trucks, tips
- c) Telephone use

## 2. Information and decentralization

- a) A fundamental economic problem: produce and use information
- b) In organizations: put together information and decision rights
- c) Information costs and inconsistency of incentives when increasing decentralization:

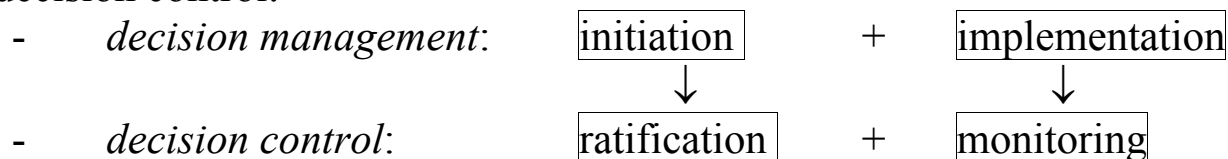


- d) Knowledge management: *Chief Knowledge Officer*
- e) Two types of information. If information is used:
  - to decide: + qualitative and particular ?
  - to control: + quantitative and aggregate ?Consequence: *computers ¿generate centralization?*

### 3. The structure of the decision process

#### Basic control mechanism (Fama & Jensen '83):

- Divide decision process, delegating decision management, but retaining decision control:



#### Efficient patterns of rights distribution:

- 1) If those who manage decisions do not bear residual risk (are not owners), do not control such decisions.  
Ex.: Open corporations and mutual firms:  
Separation of management decision rights from residual risk bearing ⇒  
⇒ Separation of decision from control rights: decision rights are exerted by managers—control rights are exerted by the general meeting of shareholders and the board of directors
- 2) If the same persons manage and control decisions, they also bear residual risk: Proprietorships, closed corporations and partnerships
- 3) Hierarchies: each level manages some decisions and controls other, *different*, decisions.

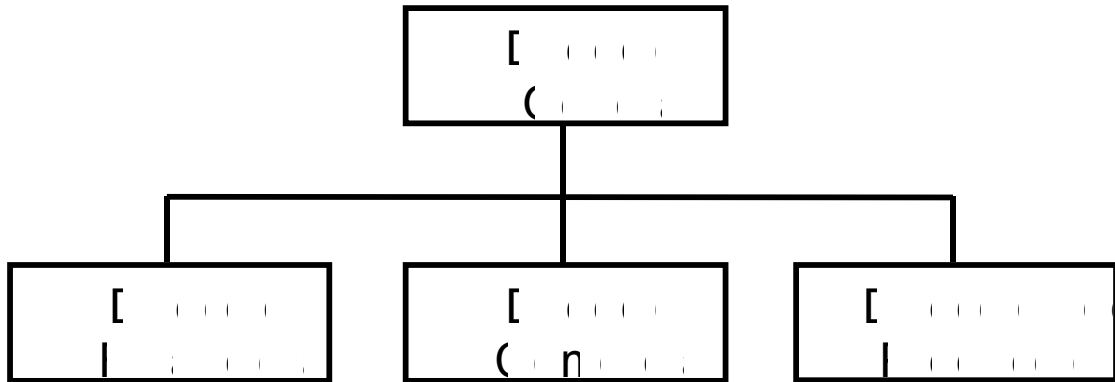
## 4. Formal organizational structures

### 1. Precedents: armies, Catholic church, ... not artisan firms. What about:

families, rural villages, feudal, monasteries?

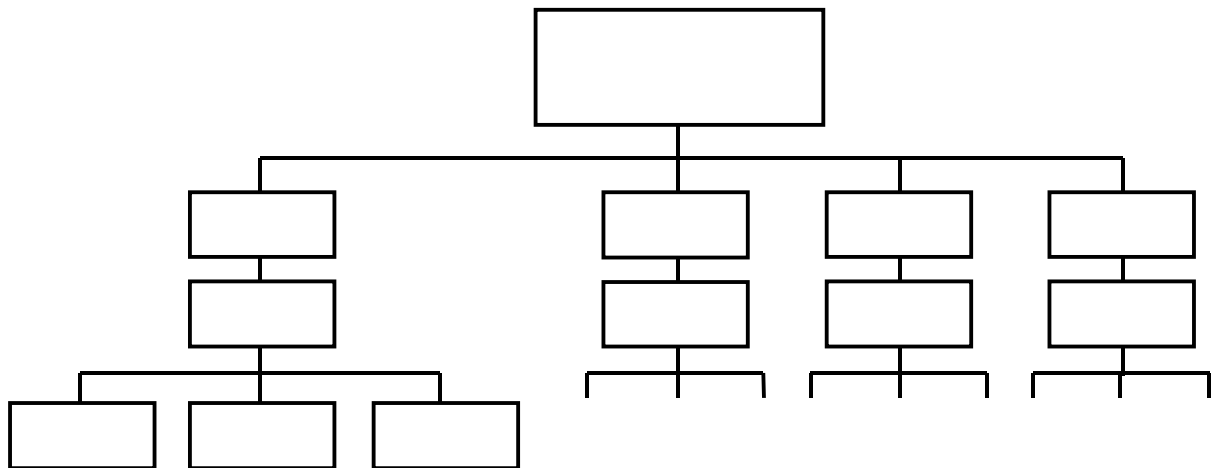
### 2. Functional structure

Each department contains a specialized function:

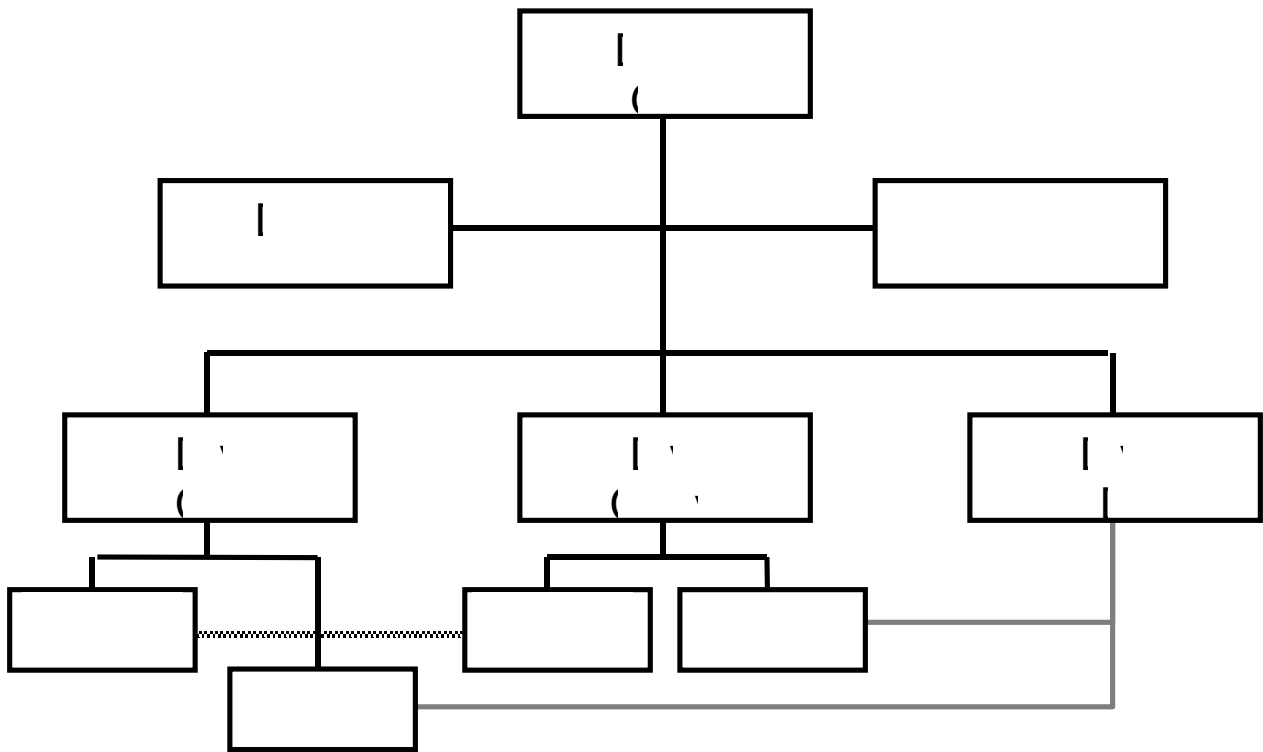


- good / poor coordination within / between depts.
- good functional knowledge (b/c specialization) but “tunnel vision”
- OK if small size and market variety or stable technology allow easy or routinized coordination

### 3. Holding structure

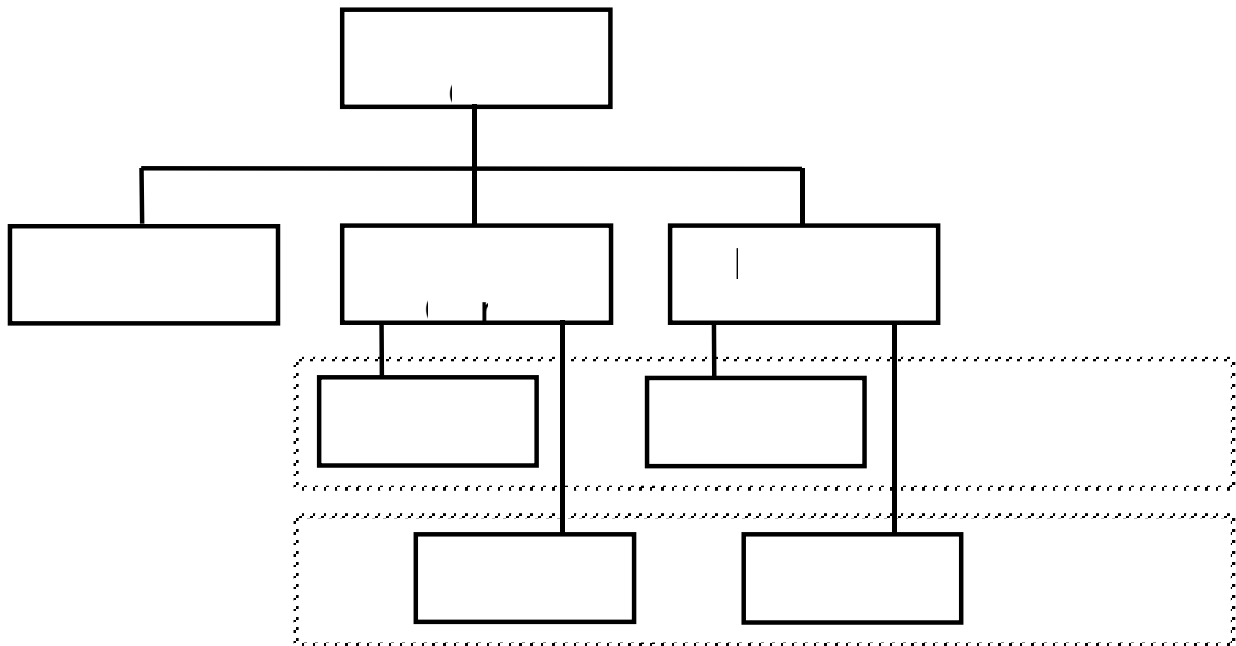


### 4. Multidivisional structure: An equilibrium solution



## 5. Matrix structure

- formalized coordination of functional structures:



- Who is really in charge?
- Example: Universities

## 6. Conglomerates

- ◆ multidivisional with different markets
- ◆ *holding* with headquarters involved in divisional strategy
- ◆ Do they create value? Empirical issue, but consider:
  - a) Diversification?
  - b) Internal *capital* markets?
  - c) Internal *takeover* markets?