

# Oversight of Organizational Performance Management



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## Introduction

This paper discusses the need for improved oversight of organizational performance management by boards of directors. It identifies shortcomings in current oversight practice and suggests several ways that the systems approach to performance management presented in the *Baldrige Excellence Framework* can be used to overcome those shortcomings. More generally, the paper calls for boards to increase their use of systems thinking in fulfilling their oversight responsibilities.

## The Baldrige Excellence Framework

The *Baldrige Excellence Framework* is a product of the Baldrige Performance Excellence Program which resides inside the National Institute for Standards and Technology (NIST), which is part of the U.S. Department of Commerce. The *Framework* was designed in the late 1980's to improve the quality, productivity, and competitiveness of U.S. manufacturing and service companies and small businesses. It is revised every two years. Its scope was expanded in the late 1990's and early 2000's to include education, healthcare, and nonprofit organizations. Thus, today the *Framework* supports performance management in organizations that range from manufacturing plants, to credit unions, to hospitals, to schools and universities, to government agencies, military units, cities, towns, and car dealerships.

The *Baldrige Excellence Framework* includes the Criteria for Performance Excellence; Core Values and Concepts; and a Scoring System with Process Scoring Guidelines and Results Scoring Guidelines. Over the last three decades the *Framework* has been successfully used by thousands of organizations across the U.S. and around the world to improve their performance management.

The term "performance excellence" is commonly used to describe the focus of the Baldrige Performance Excellence Program, its *Baldrige Excellence Framework*, and its Malcolm Baldrige National Quality Award. But people who are unfamiliar with these Baldrige initiatives often don't understand or even misinterpret the term "performance excellence". As a result, many don't grasp the purpose or the value of the initiatives and thus may not be drawn to them. And that's understandable. The term "performance excellence" is quite generic and far from being self-explanatory or even interesting.

In the context of the *Baldrige Excellence Framework*, performance excellence refers to excellence in the use of a systems approach in the management of organizational performance. It is through the use of the *Baldrige Excellence Framework* that an organizational performance management system can be designed, understood, evaluated, and improved. Thus, in this paper, the expression "organizational performance management" (OPM) is used when referring to the focus of Baldrige initiatives.

Of course, organizational performance management is a concept with many different operational approaches including Management By Objectives, Functional Management, and the systems approach advocated by the Baldrige Performance Excellence Program.

## Improving Organizational Performance Management (OPM)

In general, there are three different levels or types of activity that are required to achieve and sustain excellence in the management of organizational performance: (1) Oversight, (2) Leadership, and (3) Execution. Oversight of OPM is the responsibility of the organization's board of directors; Leadership of OPM is the responsibility of the organization's senior executives; and day-to-day Execution of OPM is carried out by mid-level and below managers and the workforces they lead.

In practice, the *Baldrige Excellence Framework* is primarily used by those charged with level (3) responsibilities--the Execution of OPM. Their work includes the regular assessment and improvement of the day-to-day performance of the organizational system and its many subsystems and processes and their linkages.

Senior executives and especially boards of directors tend to be discouraged from using the *Baldrige Excellence Framework* due to its level of detail. The 2017-2018 *Framework* is 58 pages long and its Criteria for Performance Excellence includes about 370 questions.

In 2015, in response to the concerns of users and potential users of the *Framework*, The Baldrige Performance Excellence Program introduced a shorter, less complex version of the *Baldrige Excellence Framework* called the *Baldrige Excellence Builder*. It's been well received by college students and by organizations considering or just beginning to address OPM from a systems perspective. But it still does not fully meet the needs or expectations of many senior executives, nor has it yet encouraged boards of directors to embrace Baldrige's approach to OPM.

In a very recent step toward simplification and clarity, the Baldrige Performance Excellence Program reduced the 2019-2020 Criteria for Performance Excellence by 2 pages and has begun using the tag line, "Proven Leadership and Management Practices for High Performance."

## Amplifying the Baldrige Excellence Framework

Over the years materials have been developed outside the Baldrige Performance Excellence Program to amplify and explain the Baldrige approach to OPM. Examples include Blazey and Grizzell (2017), Brown (2017), and Kendall and Bodinson (2016). And many consultants make a living doing the same thing. But very little of the writing and consulting has been aimed squarely at top executives or boards of directors.

One recent exception is John Vinyard's *Baldrige for Leaders* (2017). Vinyard steps through the Organizational Profile and the Seven Categories for the Criteria for Performance Excellence explaining why particular concepts and elements should be important and useful to executives. He explains the Criteria in the language of executives and in the context of

functions and issues they deal with regularly. In so doing, he gives executives reasons to use the *Baldrige Excellence Framework* and ways to use it without needing to grasp all its details.

Another example, produced inside the Baldrige Program, is the book entitled *Baldrige 20/20: An Executive's Guide to the Criteria for Performance Excellence* (2011). It explains why executives should adopt the Baldrige approach to OPM. It does so by describing the stories, strategies, and results of Baldrige Award winners. It also introduces the Criteria for Performance Excellence and how it should be used.

But, with so little effort focused on convincing top executives of Baldrige's value, it's not surprising that their boards of directors lack familiarity with Baldrige and how it can be used to facilitate the board's oversight responsibilities.

The closest some boards get to Baldrige is when a senior executive tells the board that there are different possible "tools" that can be used to improve OPM. The executive then flashes a list on the boardroom screen that might include Lean, Six Sigma, Agile, TQM, ISO, Kaizen, and Baldrige. What such a list reveals is that the senior executive doesn't understand that Baldrige is a framework within which the other approaches or tools can be successfully applied. The other approaches generally focus on specific variables like waste or quality and are often applied on subsystems, not the entire organization. But it's the entire organization for which the board of directors has oversight responsibility, not particular subsystems.

By the way, even organizations that successfully employ the *Baldrige Framework* don't necessarily encourage their boards to use it. If they did, you would likely see more boards developing CEO Succession Plans that target executives with Baldrige backgrounds. Why? In order to improve the continuity of management practices across administrations.

So what materials or processes are available to help boards understand the value of using the *Baldrige Excellence Framework* and to facilitate their use of the *Framework*? Not much. I'm only aware of one two-page flyer that former Baldrige Excellence Program Director Harry Hertz and I developed about 13 years ago (National Institute of Standards and Technology, circa 2006). In my experience, most Baldrige-related materials, courses, and consultants focus on the Execution of OPM; a few focus on the Leadership of OPM; and hardly anyone focuses on or even thinks about the board's Oversight of OPM.

## **Board Oversight**

Boards of directors of publicly traded companies in the U.S. don't run their companies or make day-to-day decisions. Management does that. But the board has overall responsibility for the actions management takes and the resulting performance of the company. In short, management executes; the board oversees. That oversight function includes both monitoring and advising functions and is frequently described as "noses in, fingers out" (Browning and Sparks, 2015).

The board acts for and on behalf of the company's shareholders and other stakeholders that are impacted by the decisions made by the executive team and the board. The board's primary duties are: (1) hiring and evaluating the CEO; (2) maintaining a succession process for developing or finding the next CEO; (3) ensuring an appropriate strategic plan is in place that includes the company's purpose, values, envisioned future, strategies to achieve the vision, and metrics to monitor the company's progress; (4) monitoring the execution of the strategic plan and keeping management focused on the long-term performance of the company; (5) monitoring the company's risk management process and (6) overseeing the company's performance in a wide variety of areas such as financial, marketplace, customer satisfaction, product and service quality, corporate culture, talent management, cybersecurity, etc. (Tricker, 2015; Browning and Sparks, 2015; and Monks and Minow, 2011).

All six primary responsibilities either contribute directly to the company's management of organizational performance or support the board's oversight of performance management. And together those responsibilities illustrate the level of complexity the board must deal with in fulfilling its fiduciary duty to shareholders and other stakeholders.

## **Dealing with Complexity in OPM**

Organizations are complex human activity systems and their oversight requires both "reductionist thinking" (also called analytical or scientific thinking) and "systems thinking" (Chapman, 2015; Checkland, 1981). The former reduces or simplifies complexity; the latter takes the complexity into consideration and keeps the big picture in focus. Because it's natural for humans to simplify complex situations and because analytical thinking is a powerful approach to problem-solving that we've all been taught in school, people readily apply analytical thinking even to the point of overuse and to the exclusion of systems thinking, which most people have not been taught to use.

Reductionist thinking presumes that an organization can be understood and improved by analyzing the components of the organization. It simplifies organizational complexity by breaking down the problem of interest into progressively smaller parts that can be more easily evaluated and understood.

But this approach tends to ignore the linkages and relationships between components. It also focuses attention away from the system as a whole and the behaviors and problems that only emerge at the system level, not at lower levels of the system. A system is more than a collection of its parts.

Systems thinking--also called holistic thinking--retains and exploits the complexity of the system in seeking answers to questions. It recognizes that different behaviors and issues emerge at different levels of a system. And it encourages movement between system levels in looking for solutions, particularly upward movement. Upward movement both changes the perspective and the nature of the existing complexity in ways that reductionist thinking avoids (Jackson, 2003).

For example, if your task is to evaluate the performance of a department, you generally focus on the performance of a group of people, and the relationships between and among them. But if you move upward in the system to the division level, you introduce a different view of the problem. The focus shifts to the evaluation of the department as one of many departments and to the relationships between and among those departments. Upward movement introduces new relationships; downward movement tends to dismiss relationships. And, more generally, systems thinking can help provide an understanding of the complex content in which reductionist thinking takes place.

The language of systems is particularly well suited for dealing with the complexity of overseeing, leading, and executing organizational performance management.

Over reliance on purely reductionist approaches in the oversight of an organization's performance is clearly a mistake. It's well known that if you focus on the optimization of the performance of each subsystem in isolation, you won't optimize the performance of the overall system.

Systems thinking and reductionist thinking are complementary. One is not better than the other. Each can provide insights that don't follow from the other (Chapman, 2005).

For several reasons, it is a constant challenge for boards of directors to regularly apply both reductionist and systems thinking:

- (1) Much of the board's work is required to be done in committees which are focused on particular subsystems (Audit Committee, Compensation Committee, Governance Committee, etc.)
- (2) The length and the complexity of the materials that management provides for directors to use in preparing for each board meeting, the "Board Book," often runs well into the hundreds of pages. Including committee materials, a length of 400 to 500 pages is not unusual. Thus, in preparing for meetings, directors are effectively encouraged to simplify and reduce the content and complexity of the materials.
- (3) The Board Books are generally organized by division or subunit and, thus, directors are encouraged to focus on the material subunit by subunit rather than on the system. Further, the linkages between subunits often are not featured.
- (4) Oral presentations by senior executives during board meetings are generally presented by division or subunit with the financial impact on the entire corporation featured, but probably not its effects on other corporate-wide results such as workforce culture or customer satisfaction. Nor is there likely to be a routine description of the subunit's impacts on other subunits, such as the sharing of best practices.

All four points tend to encourage reductionist thinking on the part of the board. And points (2), (3), and (4) suggest that management can have a significant impact on whether the board routinely does or does not apply systems thinking.

Of course, the information lacking in points (3) and (4) may well be presented at subsequent board meetings. In fact, it probably will be. But by presenting the information sequentially over time, the board's ability to assess the performance of the entire system and the firm's OPM at any one point in time is difficult or even impossible. In general, the routine sequential presentation of partial performance management issues and results--unless carefully coordinated over time, kept available to the board over time, and reviewed as needed--can make systems thinking quite challenging.

## **The Increasing Complexity of Board Oversight**

In recent years, because of the organic evolution of corporate governance and outside pressures from investors, proxy advisory firms, and government agencies, boards have begun to adopt governance guidelines and policies that encourage different styles of thinking. For example, guidelines targeted at improving the diversity of boards with respect to gender, race, experience, age, and ethnicity are designed to bring a wider set of opinions and backgrounds to the table.

But recent calls for cognitive diversity--are particularly interesting in the context of the board's oversight of OPM. Cognitive diversity refers to differences in perspectives and information processing styles (Reynolds and Lewis, 2017). Cognitive diversity prevents boards from being composed of like-minded directors, who, when dealing with complex situations and problems, may all go down the same rat hole. Interestingly, Reynolds and Lewis demonstrate that cognitive diversity cannot be predicted by factors such as gender, age, or ethnicity. This means that having a diverse board -- in the usual sense--does not guarantee that the board will be cognitively diverse. Thus, for the benefit of the board's oversight function -- which requires both reductionist and systems thinking--cognitive diversity should be openly and vigorously pursued.

Boards are also being pressured by socially conscious investors to think more broadly about the effects of corporate decisions. Such investors are said to emphasize Environmental, Social, and Governance (ESG) issues in making their investment decisions. Is the firm a steward of nature? How does the firm treat its employees, customers, suppliers, shareholders, and the communities where it operates? What are the governance policies of the executive team and the board of directors? Is diversity a priority? Is the level of executive compensation appropriate?

The materiality of ESG issues will differ from company to company. For example, climate change may be relevant to a manufacturer, but not to a financial services company. But for most companies and their boards the oversight of ESG issues adds new breadth and depth to the management of organizational performance. Think of this as another step in the evolution of OPM. And with each new step a boards' oversight responsibilities become more significant, more complex, and more holistic. This again emphasizes the need for cognitively



diverse boards and oversight systems that routinely and formally require both reductionist and systems thinking.

## Using the *Baldrige Excellence Framework* to Improve Oversight

Despite the length and level of detail of the *Baldrige Excellence Framework*, it can be easily used to improve any board's oversight functions. It's not necessary to understand the overall implementation of the *Framework*. Instead, use your reductionist thinking instincts and just look at individual pieces of the Criteria for Performance Excellence and consider how they might be used to assist the board. Here are a few examples:

(1) The 2017-2018 Criteria for Performance Excellence lays out roughly 370 questions across the Organizational Profile and Seven Categories: 1. Leadership; 2. Strategy; 3. Customers; 4. Measurement, Analysis, and Knowledge Management; 5. Workforce; 6. Operations; and 7. Results. Pick a category that you'd like to know more about in the organization that you oversee and scan the questions posed in that Category. You'll either find questions that you can ask management directly, or the existing questions can be used to trigger your own personalized question.

For example, here is a question you will find in the Leadership Category: "How do you address and anticipate legal, regulatory, and community concerns with your products and operations?"

In the Customer Category: "How do you obtain information on customers' satisfaction with your organization relative to your competitors?"

In the Operations Category: "How do you deal with poorly performing suppliers?"

(2) Use the list of questions in each Category to help you identify gaps in the management of organizational performance or in the board's oversight of OPM.

(3) Excellence in oversight of OPM requires a relatively deep knowledge of the organization that may take a new director a year or more to acquire. To this end the *Baldrige Excellence Framework's* Organization Profile can be very helpful in the process of onboarding new directors. Have management complete the Organization Profile and use it in the orientation process for new directors. It will help them understand the organization's purpose, vision, workforce, customers, suppliers, regulatory environment, competitive position, organizational performance management systems, etc. Be sure to put the Organizational Profile on the board's portal for future reference.

(4) The organization's overall performance is a function of the activities in the first six Categories of the Criteria. Thus, many of the questions in the Seventh Category-- Results--redirect your attention back to the first six categories and their impact on the overall results. So, if you are looking for explanations for reported organizational

performance or ways to improve performance, scan the questions in the Results Category and the Notes below the questions.

(5) Use the chains of related questions that flow from the Organizational Profile to the six Categories and on to the Results Category to develop systems-level questions for management.

(6) For reasons previously noted, other than through financial and market results, most boards spend relatively little time discussing and learning about the systems-level view of their company and the impacts of the company's subsystems on each other and on the overall performance of the corporate system. Similarly, little time is spent thinking about and discussing the board's overall system of oversight and how it should evolve and improve. One simple approach to encourage and stimulate the board's attention to both of those systems is to develop and use systems charts. That is, charts that provide a systems view of the organization. One such chart appears in the *Baldrige Excellence Framework* and is shown in Figure 1. It summarizes the Criteria for Performance Excellence and can serve as a generic representation of a corporation's performance management system.

The board should encourage management to use system charts in board books and in their board meeting presentations. Systems charts establish context; help directors better understand and visualize system complexity; and prompt relevant system-oriented questions that rarely arise during reductionist presentations. Boards should also regularly use system charts in their committee meetings and executive sessions. And the most useful charts should be organized and maintained in the Resource Section of the board's portal for future reference. Individual directors should consult them when preparing for board meetings.

Figure 1:



# Criteria for Performance Excellence Overview and Structure

## Criteria for Performance Excellence Overview: A Systems Perspective

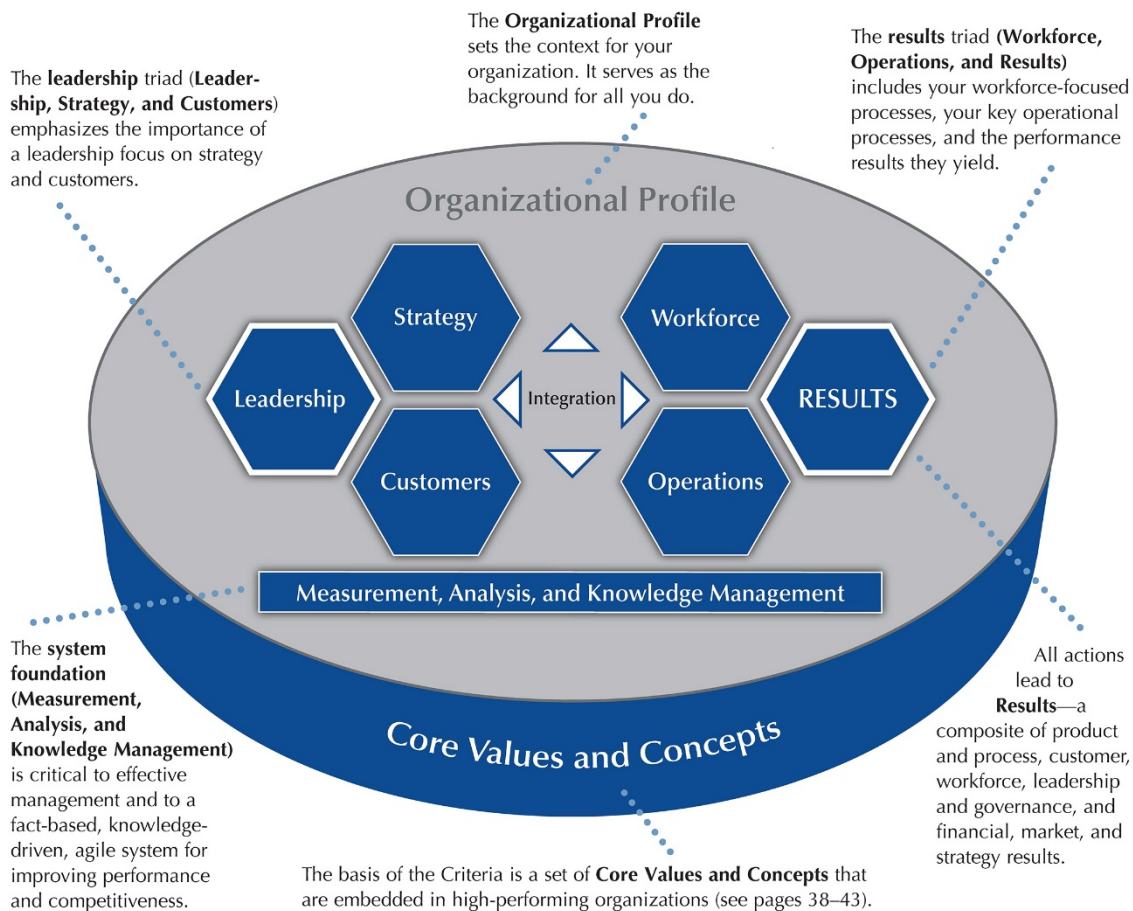
The **performance system** consists of the six categories in the center of the figure. These categories define your processes and the results you achieve.

Performance excellence requires strong **Leadership** and is demonstrated through outstanding **Results**.

The word “**integration**” at the center of the figure shows that all the elements of the system are interrelated.

The **center horizontal arrowheads** show the critical linkage between the leadership triad (on the left) and the results triad (on the right) and the central relationship between the Leadership and Results categories.

The **center vertical arrowheads** point to the Organizational Profile and the system foundation, which provide information on and feedback to key processes and the organizational environment.



From Baldrige Performance Excellence Program. 2019. 2019–2020 Baldrige Excellence Framework: Leadership and Management Practices for High Performance. Gaithersburg, MD: U.S. Department of Commerce, National Institute of Standards and Technology. <https://www.nist.gov/baldrige>.

While these six ad hoc approaches to using the *Baldrige Excellence Framework* will certainly help to improve a board's oversight of OPM, a more systemic approach to OPM oversight is needed. One could be developed using the *Baldrige Excellence Framework* as a starting point, but it must be developed specifically for boards of directors. That is, it must be expressed in the language of boards and corporate governance. It must take into consideration the legal and fiduciary responsibilities of the board, the diversity of the board, the severe time constraints that boards work under, the sequential nature of the board's annual agenda, etc. Don't be concerned that it doesn't reflect the language, interests, or needs of Leadership-level executives or Execution-level managers. Only the board of directors performs the Oversight function.

## Conclusion

Over the last three decades, corporations have been strongly influenced by a number of different forces including institutional investors, federal and state governments, proxy advisor firms, and shareholder activists. And as companies have been pressured to evolve, so have their boards. The scope, complexity, and importance of the board's oversight role have dramatically increased since the 1990's driven by the force's noted above and events such as the Enron debacle in 2001 (Tricker, 2015) and the Great Recession. Charan (2005) describes the board's oversight role as evolving from ceremonial to liberated to progressive.

By the way, this evolution has benefited significantly from the guidance of professional organizations such as the National Association of Corporate Directors and Executive Education Programs for Directors at several of the countries' top business schools.

The primary message of this paper is that boards need more support in the recognition, characterization, and exploitation of organizational complexity. Boards need to be able to reduce the complexity they face and to exploit that complexity. They do well with the former, the latter is problematic. The *Baldrige Excellence Framework* is helpful in this regard. It provides a systems approach for understanding and exploiting the complexity of organizations. In organizations in more than 120 countries worldwide, it is used by management to facilitate systems thinking. But for this framework to be widely used by boards, a version of it needs to be produced specifically for boards. Or, a vehicle needs to be developed that interprets the *Baldrige Excellence Framework* for boards and explains how it and systems thinking can be used in the board's oversight of organizational performance management.

Since the quality revolution that swept the Western World in the 1980's and 1990's, executives have been encouraged to use systems theory and systems thinking in managing organizational performance. It's time for boards to rethink their duties and responsibilities in light of the increasing complexity they face and to formally increase their reliance on systems approaches to corporate oversight.

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## About The Foundation for the Malcolm Baldrige National Quality Award Institute for Performance Excellence

The Baldrige Foundation is the private-sector partner of the Baldrige Performance Excellence Program (BPEP), a federal program in the National Institute of Standards and Technology within the Department of Commerce. The Mission of the Baldrige Foundation is to ensure the long-term financial growth and viability of BPEP, and to support organizational performance excellence. The Institute for Performance Excellence is a thought leader on performance excellence, leadership and management. Our team carries out this mission in a number of ways: undertaking research projects, hosting conferences and activities, conducting executive-level training, and publishing and distributing a wide variety of educational materials. Its mission is to improve the practice of leadership and management in pursuit of performance excellence and its impact in an ever-changing world.

To learn more about the Baldrige Foundation or Institute for Performance Excellence, please contact Al Faber, President and CEO at (202) 870-3136 or [afaber@baldrigefoundation.org](mailto:afaber@baldrigefoundation.org). The Baldrige Foundation is recognized by the Internal Revenue Service as a 501(c)(3) tax exempt organization. Your donations and contributions are tax deductible. To learn more visit [www.baldrigefoundation.org](http://www.baldrigefoundation.org). To learn more about BPEP visit [www.nist.gov/baldrige](http://www.nist.gov/baldrige).