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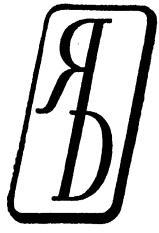
BUSINESS ORGANIZATION AND MANAGEMENT

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REVISED EDITION



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PREFACE

SINCE the original edition of this book was published in 1941, its wide use has suggested important revisions to the authors. This revised edition, therefore, is offered in the belief that its subject matter is presented more logically and clearly than was done in the first publication. To that end, the book has been completely reorganized and rewritten, and much new material has been added to its text.

According to the new arrangement, the first chapter is a condensed historical sketch emphasizing the major landmarks in business history which form the background against which organization and management may be studied in proper perspective. Since management is essentially a task of leadership, the next two chapters deal with the human element in organization and management and with the principles of authority, responsibility, and accountability to which it is subject.

The principles of authority, responsibility, and accountability are the basis of a hierarchy which characterizes a business organization. Such a hierarchy suggests stratification. In logical sequence, therefore, the next four chapters constitute an exposition of the levels theory of organization, including the functions and procedures of the board of directors, the executive, and the supervisory levels of management.

There follows in Chapters VIII–X an analysis of the departmental structure of a business organization. The next four chapters are devoted to an exhaustive treatment of the management process under such headings as "Centralization and Decentralization of Management," "The Formulation of Policy," "Efficiency in Management," and "The Principles of Incentive."

Chapters XV and XVI deal with types of management related to business management, but not business management as it is ordinarily conceived. For example, "business association" management is an important phase of modern business relationships. Likewise, every student and executive of business should understand the difference between the problems which arise in the management of private businesses and those involved in government-owned businesses.

The final chapter (Chap. XVII) is devoted to a discussion of management as a career. It is hoped that this section will be found both useful and stimulating as an aid to vocational guidance.

The questions that appear at the end of the chapters are an important feature of this book. Great care and attention have gone into their

preparation. They cannot be answered properly by simple quotations from the book, but rather they are designed to stimulate independent, logical thinking and to point the way to the practical application of the principles and procedures that have been explained in the text. Instructors are encouraged to use these questions freely both for class discussion and for occasional and final examinations. Following these questions there appear a limited number of selected references to titles of books suitable for supplemental reading.

The present book is neither an imitation nor a duplication of textbooks on industrial organization, introductory surveys of business enterprises, or of surveys of the financial and legal aspects of business organization. It is rather a definitive treatment of the principles of organization and management that are the energizing elements of all types of business, large or small, and wherever managerial leadership is required. It can be an introductory textbook, or it can be used near the end of a degree curriculum to emphasize the interrelationships of executive specializations.

The book is so arranged that it is suitable for courses of varying lengths. That is to say, in some institutions it may be desirable that the subject be covered in a quarter or a semester; in others it may run throughout the year. For the short course, an intensive study of the first ten chapters will suffice to give a thorough understanding of the theory and application of the fundamental principles of organization and management. For a longer course, ample material has been included in the book for extended presentation and illustration of the basic concepts of the subject.

The text includes more than fifty diagrams, charts, and other illustrations, most of which are original with the authors. The work naturally reflects the executive experience of the writers themselves, as well as the experiences of a great many other executives with whom they have had close association. The authors are indebted to many colleagues, friends, and associates for their encouragement and criticisms during the years in which the original book and this revised edition were in preparation.

ELMORE PETERSEN
E. GROSVENOR PLOWMAN

MARCH, 1948

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CHAPTER I

THE BACKGROUND OF ORGANIZATION AND MANAGEMENT

INTRODUCTION

IT IS indisputable that any consideration of present-day business problems involves an examination of business from the standpoint of organization and management. The field of business organization and management deals with both internal and external relationships. There are internal organic arrangements upon which are established the relationships between persons, functions, and the physical resources of a going concern. There are also external relationships upon which business, in final effect, is dependent for its successful operation.

Essentially, business is an activity in which two or more persons engage in an exchange of values, whether goods or services, for mutual gain or profit. To the extent that such exchanges produce utilities, business is an economic activity; but "business" and "economic activity" are not synonymous. Production in its simplest connotation is an economic activity, but an economic activity does not become business until goods or services produced are exchanged for other goods or services, or their money equivalent. The importance of this distinction is that it permits study of the influence of economic environment upon business, even though business itself is a *part* of such environment. For example, dealers in goods are not able to set selling prices at any level desired; nor can they dictate their own terms for the supplies they need. They must yield to the pressure of economic forces not of their own making or choosing—forces which spring from such facts as natural resources, climate, racial characteristics of populations, standards of living, and many others.

BUSINESS IN ANCIENT TIMES

The history of civilization is a record of people seeking to better themselves, both materially and spiritually, by means of exchanges one with another—in short, by means of business. Business has always been limited in its significance by its environment and by its objectives.

As far as can be determined, only a relatively small proportion of the total population of the ancient world was engaged in activities which could be called "business." The reasons for this condition are clear. In ancient times people were by force of circumstances economically self-

sufficient. Because of the difficulties in transportation and the rudimentary methods of communication then prevailing, one social group knew little about the life and affairs of another group, even though the distance separating them was small. Moreover, the development of a medium of exchange, beyond that of simple barter, was elementary, if not entirely absent. Governments and laws were unstable, the utilization of the forces of nature in the development of power was lacking, and the processes of production were limited to the skills of handicraft.

Business units in ancient times consisted mainly of individual proprietors operating in the role of tradesmen. They were adventurers who dared to take risks—not only of investment in wares, in the hope of future exchange, but also of life itself. There were the risks of the sea, the main highway of ancient commerce; and where the routes of trade lay overland, there were the risks of robber bands and bandits, a prevailing hazard where the protection afforded by organized society through government was unknown.

It is not to be wondered at, therefore, that the gains sought by these early businessmen were somewhat commensurate with the risks they took, or that their practices in seeking such gains approached the level of their hazardous occupation. To be able to outwit their ancient gods in a storm at sea and to fight off the bandits in port and on the trail were qualities required of the merchant. Life itself was near the biological level of the survival of the fittest. In this contest of wits and of courage it was quite natural to find a carry-over into trade practices themselves. Thus we find that "piracy was the initiator of maritime trade among the Greeks of the Homeric era, as among the Norse Vikings; for a long time the two vocations developed in concert."[1]

Disparaging Opinions

Early merchants thus earned for themselves an unenviable reputation while they sought material profits in the barter of goods. From ancient times a reflection of opprobrium has been cast upon business. For example, Aristotle in his essay on *Politics and Ethics* wrote: "Of the two sorts of money-making, one is a part of household management, the other is retail trade: the former necessary and honorable, the latter a kind of exchange which is justly censured; for it is unnatural, and a mode by which men gain from one another." A Hebrew at the time of the prophets wrote: "As a nail sticketh fast between the joinings of the stones, so doth sin stick close between buying and selling."[2] It is said that Cicero in Rome observed that one could not be proficient as a merchant without lying. In

[1] Henri Pirenne, *Medieval Cities: Their Origins and the Revival of Trade* (Princeton, N.J.: Princeton University Press, 1925), p. 109.

[2] *Ecclesiasticus*, chap. 27.

the Middle Ages the attitude of the clergy continued to be unfavorable. In the eyes of the church, one could hardly be a Christian and a businessman at the same time. "The merchant," says a text attributed to St. Jerome, "can please God only with difficulty."

History and literature are replete with references to the degrading occupation of business. Nobility, by whatever standard, from classical Greece to the French Revolution, never had anything but disdain for the merchant, whom the English of the twelfth century picturesquely called *piepowdrous* ("dusty-foot").[3] Even Adam Smith, in his famous *Wealth of Nations*, could not refrain from remarking in reference to businessmen that "they are an order of persons who have for their purpose the deception and oppression of the public; and upon most occasions have both deceived and oppressed it."

Napoleon could think of no more scornful characterization of England than to call her a "nation of shopkeepers." Perhaps in Napoleon's mind, "shopkeepers" was a generic term used to include all businessmen. It may be that it is from the ancient merchants, whose origin is lost in the obscure past, that most forms of business stem. Certainly, many "firsts" can be traced to them. A contemporary of Napoleon, Thomas Jefferson, president of the United States, likewise arraigned business: "The operation of buying in the cheapest and selling in the dearest market inevitably led to chicanery and accumulation of great wealth, of speculation, intrigue, and exploitation." And no less bitter in recent days is the assertion by James Harvey Robinson that "there is no more flagrant example of a systematic endeavor to get something for nothing than the present business system based on profits and absentee ownership of stocks."[4]

Commendatory Contributions

These criticisms emphasize the unscrupulous and seamy side of early business institutions. But the ancient businessmen also had their virtues. It has been said, for example, that "civilization has always ridden the wings of trade." This fine phrase of Wissler's simply signifies that in the ancient world the farthest reaches of the traders' ships marked the boundaries of culture. Or again, "Long before the State arose from its couch, in the morning twilight of history, trade had already completed a good part of its day's work. While the States were fighting one another, trade found out and leveled the roads that lead from one people to another, and established between them a relation of exchange of goods and ideas; a pathfinder in the wilderness; a herald of peace; a torchbearer of culture."[5]

[3] Pirenne, *op. cit.*, p. 127.

[4] Willis Wissler, *Business Administration* (New York: McGraw-Hill Book Co., 1931), p. 74.

[5] J. H. S. Bossard and J. F. Dewhurst, *University Education for Business* (Philadelphia: University of Pennsylvania Press, 1931), p. 3.

This conflict of opinion as to the nature and end of business offers no solution in itself. It does, however, present a problem of relationships and objectives which did not emerge until modern times. It is a problem of ethics and ideals, of standards of business conduct which must be met by management if both public and private interests with a vital stake in business, are to be satisfactorily served. When the merchant of olden times had no protection for his life and property save his own wits and strength, the business he prosecuted could hardly have been motivated by high ideals. But today the conditions under which business exists are vastly different. In return for the right of private property and for the protection called "government of an organized society," the public expects honesty and "square dealing" in its relations with business.

The foregoing brief survey of personal attitudes and opinions regarding business and businessmen is not intended to be an adequate historical appraisal of business. Rather, by giving fleeting glimpses of the past, it is intended to suggest the origin and nature of a type of environment in which business management finds itself at the present time. It is a psychological environment created out of the mental attitudes of many people, largely intangible and nebulous, but nevertheless real. It is an environment which must be reckoned with as an obstacle to progress in business, and, to that extent, an obstacle not only to be overcome but also to be dissipated by management.

BUSINESS IN THE MIDDLE AGES

The development of associations of individuals into organizations for purposes of management began with the Roman *collegium.* The *collegium* corresponds to our modern corporation in that under the Roman law it consisted of at least three persons and there was complete separation between the rights of the *collegium* as a body and those of its individual members. An organization of this kind could own property, sue, and be sued, as well as carry on trade and other activities in its own name. The *collegium* remained in existence even though its original members were changed. It was governed by its own bylaws, which established rights and relationships with respect to the authority and responsibilities of those who managed its affairs.

After the dissolution of the Roman Empire the Roman form of corporation persisted in religious and public governing bodies. Business organizations shaded off into *societates,* which were not incorporated but which resembled partnerships, yet maintaining the elements of group action through certain of its members designated to represent it.

The Institution of Insurance

By the time of the Middle Ages the institution of insurance had appeared. It had its inception in Lombardy not later than the twelfth

century. In form, purpose, and objective, this early type of business organization has a genetic bearing on business practices and environment in modern times. To be sure, writers have sometimes called the marine loans of the ancient Greeks the origin of insurance. By means of these loans, money was advanced on a vessel or a cargo. If the voyage was successful, the sum advanced would be repaid with high interest—in fact, so high as to cover not only the use of the money but the risk of losing it. If the ship were lost, no repayment of the loan was required.

This system of protection obviously differed from the Lombard method of covering risks for a premium paid under contract and independent of any loan. The nature of the Lombardy-type contract was a written agreement signed by each individual underwriter for the part of the risk he assumed. It was a mutual arrangement, first between shipowners and later between men who had capital to employ for the purpose. It was only natural that the energetic traders of the Italian city-states of Venice, Genoa, and Florence should evolve this method of mutual financial protection in their expanding business. "In fact," says Vance, "the word *policy* is a monument to the Italian origin of insurance, it being derived from the Italian word *polizia*."[6] The term "policy" as here used in connection with insurance should, of course, not be confused with "business policy," which is the sense in which the term will be used throughout the remainder of this book.

From Italy the custom of making mutual contracts of insurance spread to other parts of Europe. Lombard Street in London, still the insurance center of the English metropolis, marks the locality in which the early Italian traders with Britain had their headquarters. Likewise, Lloyds takes its name from Lloyd's coffeehouse, where in the seventeenth century it was the custom of men interested in the insurance business to gather and to make their agreements. The method employed is further interestingly described by Vance:

> The method employed in making such insurance contracts was for the person desiring the insurance to pass around among the company assembled a slip upon which was written a description of the vessel and its cargo, with the name of the master and the character of his crew, and the voyage contemplated. Those desiring to become insurers of the ventures so described would write beneath the description on this slip their names or initials, and opposite thereto the amount which each was willing to be liable for as insurer. When the total amount of insurance desired by the owner of the vessel was thus underwritten, the contract was complete. From this practice, among those congregating at Lloyd's is derived the term *underwriters,* as now applied to insurers.[7]

The point to be made from the foregoing example is that in the late Middle Ages businessmen began to form organizations for their common

[6] W. R. Vance, *Law of Insurance* (St. Paul: West Publishing Co., 1904), p. 4.
[7] *Ibid.*, p. 10.

benefit. These insurance groups were much more highly organized than the merchant guilds with which they were contemporary. Moreover, they have been a permanent feature of economics and business from their inception to the present time. In them is manifest the confidence and trust so essential to permanence and progress in business. Their basis was the pooling and sharing of capital, judgment, and risk—all essential characteristics of modern business management.

Furthermore, these insurance groups did much more to develop the foundations of business management than their contemporaries, the goldsmiths or moneylenders. A loan need bear little relation to the business venture. It is itself a contract, enforceable in its own terms. On the other hand, insurance against loss in the course of trade required estimates of the degree of risk as well as the ability on the part of the insurers to settle partial losses or to take over damaged ships or cargoes for possible salvage. These elements not only called for business knowledge to be possessed by insurers but also made necessary accurate record-keeping and careful appraisal of the value of goods and services. Thus insurance encouraged development of record-keeping and accounting procedures. As late as the seventeenth century, Samuel Pepys regarded the decimal or Arabic system of arithmetic as a novel idea, but still chiefly experimental rather than practical. To him notched tally sticks were the most important record-keeping devices for the British Royal Navy, which he served as "clerk" or chief administrative officer for many years.

The Guilds

There were other general features of trade and industry in the Middle Ages which had a bearing upon the development of organization and management. Among these were the medieval guilds, two of which deserve special notice—the merchant guilds and the craft guilds. The merchant guilds were the first to appear. Traces of them are to be found in the tenth century in Italy. In an English town charter granted in 1087, a merchant guild is mentioned. By the twelfth century, guilds of this kind flourished in France and Germany as well.

If a counterpart of the guild is sought in modern times, perhaps the trade association offers the closest resemblance. The merchant guild was an organization of merchants which had for its fundamental purpose the welfare of its members. Included in this objective were considerations of the security of the life and property of members traveling and trading at a distance; the discouragement of unfair competition; aid to members in time of want; and the maintenance of the monopoly of retail trade in cities where the guilds were located. The guilds were not corporations in the modern sense. They were primarily associations of persons, regulating the business of their members.

Craft guilds appeared later than the merchant guilds, and with their development the latter gradually dwindled in importance and finally went out of existence. The craft guild was an organization of artisans in a town or district who were engaged in the same occupation. Such associations were monopolistic, and no one might engage in trade unless he was a member of an appropriate guild. Unsuccessful attempts have been made to trace the modern trade union to an origin in the craft guild. There is some resemblance in their purposes, but they differ widely in their membership. The craft guild of the Middle Ages consisted of persons who were both employers and employees, whereas modern union membership is confined to employees.

At the height of its strength the craft guild was dominant as a regulator of industry in the pre-factory era. It maintained standards of manufacturing and, like the merchant guilds, attempted to establish monopoly. It regulated the sale of the products of its members and laid down rules governing wages and hours. In fact, there was hardly a phase of the worker's occupation and product which did not come under the surveillance of his guild. So powerful did these organizations become that it was not uncommon for them to assume or to be given semigovernmental functions by the towns of their locations.

The Domestic System

Like other phenomena in the course of human events, the old guild system broke down under the impact of new economic forces. One of these was the development and extension of the domestic system of manufacture. This transition was so gradual that any attempt to affix a date to the change is impossible. But the domestic system was commonly known in England by the late 1400's, though it appeared earlier in the textile industries of Flanders and Italy.

Unlike the guild system in which the master-craftsman bought his raw material and transformed it into finished products in his own shop and sold these products to customers usually on the spot, the domestic system introduced a new factor into the stream of production and trade. This factor was the *entrepreneur* or manager. He also bought raw materials for the purpose of manufacture; but instead of performing the processing in his own shop, the work was given out to employees who carried on the labor in their own homes. These laborers had no investment in either the materials or the tools, since these were supplied by the enterpriser. He took the risks of production and sale and out of the proceeds of his undertaking paid the domestic laborers on a piece-wage basis.

It is not difficult to discern the beginnings of modern business management in this system. Its new type of employer was not a craftsman—he was a promoter. He gave his attention to the sources and purchase of

raw materials, to the employment of labor, and to markets and the sale of goods. By its establishment the domestic system stimulated the increased use of capital; it expanded markets and contributed to the growth of population. In the latter case, the laborers who carried on the manufacturing processes were concentrated in villages and the suburbs of larger towns and cities. Furthermore, in the sixteenth and seventeenth centuries, what might then properly be called English "industrial" centers attracted to them skilled Flemish, Walloon, and Huguenot artisans who fled from persecution in their own countries.

It should be observed that, while the domestic system introduced a new technique into trade and industry and developed a new type of businessman with a broader outlook than had ever been known before, still the free flow of the stream of trade was dammed in midstream by the lack of machinery. Raw materials at one end were sufficient in character and quantity. Markets, and the means of transportation to them, were also available. In between, the productive processes were still in the handicraft stage, carried on under the roofs of humble cottagers. Again the stage was set for the next act in the great moving drama of business, namely, the Industrial Revolution.

THE INDUSTRIAL REVOLUTION

Definition

The term "Industrial Revolution" is significant chiefly because it marks a great transition in the methods of production and distribution of the material means of life, and consequently a radical change in the organization and management of business enterprises. By definition the Industrial Revolution may be described as the transformation which has been brought about since the latter part of the eighteenth century by reason of technical discoveries and inventions and their application to all the economic functions of society.

This transformation has been gradual rather than abrupt and catastrophic. It has been evolutionary in its development. The constant tide of change and progress which has taken place has been almost an imperceptible blending of the old with the new as time has passed. It has been taking place for two hundred years, and it cannot be said to be complete today even in the most industrially advanced countries. Nor have its initial stages been passed in all parts of the world. There are places and peoples in Asia, Africa, and elsewhere for whom the Industrial Revolution has just begun.

As a matter of convenience, historians have commonly agreed upon 1760 as the date which most nearly identifies the dividing line between the handicraft or tool-using stage and the machine age in industrial develop-

ment. Prior to this time, very little progress had been made in the application of mechanical power to take the place of hand labor. What had been accomplished was chiefly to strengthen and to supplement the physical energy of the human body.

But the Industrial Revolution had been in preparation for two centuries or more. For example, before the end of the fifteenth century Leonardo da Vinci in Italy, whose name is immortal because of his great works of art, had designed, and in some instances invented, many mechanical devices, which in principle were to become basic to modern industry and commerce centuries after his time. Among them may be mentioned machines for spinning, weaving, cloth-warping, rope-making, grinding, and needle-sharpening; also, rolling mills, roller bearings, draw benches, boring machines, automobiles, and flying machines. The course of invention has three stages. First, there is the analysis of various unrelated facts or problems. Second, there follows the synthesis of these facts into a strategic or basic invention. The third and final stage is the adaptation of the particular process or device to practical use and the exploration of its further possibilities. Leonardo had arrived at the stage of synthesis or basic invention; but because of the age and environment in which he lived, the useful application of his ingenuity, and its great possibilities, was denied him. With this last stage lacking, the impact of his inventions (and others like them by other men) upon the industrial life of mankind was not felt for more than a century after Leonardo's lifetime.

The Industrial Revolution did not depend upon machine invention alone. It also required an available supply of raw materials, metals, and fuel. It depended upon power transmission, markets, engineering skill, machine design, and even chemical discoveries. Furthermore, it required financial resources and the development of organized enterprise on a scale different in tempo and temper from that which had prevailed in the epoch of the self-sufficing village and household economy. Such conditions most nearly prevailed in England in the middle 1700's. Hence, the great transition in economic life is most clearly discerned in that country.

Industrial Revolution in England

During the Middle Ages manufacturing in England was essentially in the hands of small independent operators who combined industry and agriculture. Along with farming, they were master artisans who occasionally employed journeymen and trained apprentices on a limited scale. The farmer's family made its own clothing from wool of its own flock or flax from its own fields. When apprentices and journeymen who were not members of the family were engaged, there was a close attachment between them and their master, and they were recognized as family

dependents. The characteristic industrial organization was the agricultural village, where nearly all the goods produced were also consumed. Any surplus was used for local barter between villages.

With the growth of the domestic system, trade increased and villages became towns with markets and middlemen. This development came into competition with the old guilds of craftsmen, who, through organization, regulations, restrictions, and monopoly, sought to preserve their traditional system from change. Owing to their restrictive policies, the guildsmen failed to take advantage of expanding trade, and thereby afforded a rich opportunity for the new class of merchants to flourish.

These men, while primarily merchants, were at the same time pioneer capitalists and industrialists. They promoted manufacturing by dispersing it beyond the confines of the towns dominated by the guilds. They furnished the capital for the purchase and distribution of raw materials. They paid wages to the cottagers who made the finished products, and they took the risks of marketing the goods that were ready for sale. Craftsmen's shops continued for a time, but the guild system had lost its importance in England before the eighteenth century. The transition from the domestic to the factory system was imminent, and this meant the submergence of the guilds. The struggle between the craft guild system and the factory system has always been a characteristic of the Industrial Revolution.

There is considerable evidence to indicate why these industrial changes occurred in England near the middle of the eighteenth century and since then have developed in other countries. The merchants who had bought raw materials to be "put out" and processed by cottagers found that there was economy and profit in buying raw materials in bulk and in giving closer supervision to workers. Workers soon came to be supplied with patterns, specifications, tools, and equipment. The next step was for the merchants to set up their own workshops where goods could be assembled and finished for market. Dependents then increased to hundreds—and even thousands—for individual operators, until there developed in some industries a full factory system with all the workers assembled under one roof. Thus industries needing large sums of capital passed into the hands of industrialists who had it or knew where to get it. Many of these, who had started from small beginnings, gradually established control over the production of the wares they sold in the markets which they had previously discovered and developed.

Market development coincided with the expansion of trade and commerce. The period of discovery and exploration of the Western Hemisphere in the sixteenth century had resulted in colonization and settlement in the next century. Not only did British trade extend itself to the colonies of England, but as new trade routes were established, it reached out to the West Indies, Africa, and the Orient as well. At the same time, new

markets were coming into being on the continent of Europe because of a similar expansion of the trade and commercial activities of France, Spain, Holland, and the Scandinavian countries. As a consequence, British trade doubled from 1720 to 1760.[8] Increased trade provided a greater fund of capital to merchants and a greater spending power for consumers. It exerted a pressure on increased production to which the resourcefulness of industry was forced to respond.

This response had many aspects. Improved exchange and banking institutions were developed to facilitate the financial and credit requirements of an expanded commerce. Joint-stock companies were established which changed the form of ownership of business concerns from the traditional sole proprietorship operating on a small scale to companies which had the characteristics of large-scale enterprises. And, most important, the long inventive effort culminated in the application of power to machines, thus replacing the work of animals and men. These mechanical devices were spearheaded by such inventions as Watt's steam engine in 1769, Arkwright's roller frame in the same year, Hargreaves' spinning jenny in 1770, Crompton's spinning mule in 1779, and Cartwright's power loom in 1785.

These advances in mechanical equipment and other scientific discoveries capable of industrial application were powerful motives that stimulated technological progress in England at the close of the eighteenth century. In coal mines steam-driven pumps lifted water from flooded pits. In the iron industry grooved rolling mills supplanted hammering in 1783 and steam power was applied to blast furnaces in 1790, thereby making it practical and economical to use coal in place of charcoal in the reduction of iron ore. Because of improved machinery, cotton from the colonies soon outstripped wool as the basic raw material in the textile industry. Likewise in the manufacture of pottery, new methods and devices displaced old ones which had remained practically unchanged from antiquity. Moreover, there were waiting markets—new and old, foreign and domestic—for the products of the factories of England.

All of these advances, being "modern" at the time, were free from old traditions, restrictions, and vested interests. This economic freedom, coupled with the hope and promise of profits, projected the economy of England out of its medieval state into the modern industrial age.

Industrial Revolution in the United States

When it is remembered that the colonization of what was later to become the United States of America began early in the seventeenth century, it is obvious that colonial industry was also confined to the handicraft stage as it was in England at that time. For example, when in 1610

[8] Arnold Toynbee, *The Industrial Revolution of the Eighteenth Century in England* (London: Longmans & Co., 1913), p. 33.

Captain John Smith called upon the mother country to help establish "manufacturing" in his Virginia colony, he emphasized craftsmen such as "iron men, hammer men, blacksmiths, coopers, carpenters, shipwrights, turners, bakers, weavers, shoemakers, sawyers, tile-makers, salt-makers, rope-makers, sope-ash men, minerall men, silke-dressers, and those who spin wool."[9]

What was true in Virginia was true in all of the other colonies. Goods were produced primarily for local and home use; and since the frontiersman was essentially a farmer, he concentrated on his main task and relied on others only for such necessities as he could not make or produce himself. Outside the home, there was little development in the manufacture of goods for sale in the market. What the nature of such goods should be was determined by the natural resources readily at hand and the opportunities available for exchange by barter. Furthermore, the development of pure manufactures was handicapped by the lack of capital (there were no banks in the colonies) and skilled labor, the insufficiency of money, poor transportation facilities, and the sparseness of the population.

Industrial development in the colonies was also hampered by restrictions of the British Parliament. The growth of colonial manufactures depended in large part upon trade with England. But English manufacturers were opposed to the growth of any industry in the colonies which would be in competition with themselves. Accordingly, Parliament passed stringent laws suppressing colonial manufactures. The first of these laws was an act in 1699 which forbade either the trading in wool, yarn, and woolen cloth between the colonies or the exporting of these products to England or any other country. In 1732 the exportation of hats was forbidden; and in 1750 a law was passed prohibiting the erection of any slitting or rolling mills, or any plate, forge, or steel furnaces located in the colonies. After new industrial machines came into use in England, Parliament likewise jealously guarded the exportation of such machines, plans, or models, and even forbade the emigration of skilled workmen who knew how to run them.

Up to the time of the American Revolution, it may be said that industrial development in the colonies had barely reached the transitional stage between the domestic and factory systems. Therefore the prevailing type of business organization was the owner-manager form, which was suited to household industries, small plants like gristmills and forges, merchant employers, shipowners, and storekeepers. Clark states that the largest individual enterprise in colonial America represented an investment of only $250,000.[10]

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[9] E. L. Bogart, *Economic History of the American People* (New York: Longmans, Green & Co., 1930), p. 101.

[10] Victor S. Clark, *History of Manufactures in the United States* (New York: McGraw-Hill Book Co., 1929), p. 174.

The Revolutionary War itself had a stimulating effect upon American industry. Born of necessity owing to the urgent demand for war supplies and munitions of all kinds, domestic producers sought to meet these requirements. The factory had not yet developed and foreign commerce had been interrupted and retarded. In the period immediately prior to the outbreak of the war the colonists, in defiance of British legal restrictions, had made some progress in the iron and steel business. Firearms had been manufactured, powder mills had been established, and cut nails and other metal articles had been produced in increasing quantities. The effect upon the textile industry was to increase the products of wool and cotton and "to hasten the transition of homespun manufactures into household industries, organized by merchant employers and small manufacturers who supplied a commercial market."[11]

During the Revolutionary War and immediately following it, certain important events took place in industry which hastened the beginning of the factory system in the United States. In 1775 a spinning jenny was put into operation in Philadelphia; in 1786 machines for the carding, roping, and spinning of cotton and wool were constructed in Massachusetts; in 1787 the first cotton factory in the United States was erected at Beverly, Massachusetts; in 1789, Samuel Slater, sometimes referred to as the "father of American manufactures," set up a spinning plant in Pawtucket, Rhode Island; and in 1793 Eli Whitney, a Connecticut schoolteacher, invented the cotton gin to separate the seed from the cotton fibers. This machine was considered the most important invention of its time, for it completely revolutionized the textile industry and hence the early economy of the United States.

In spite of these technical improvements in manufacturing, colonial habits and occupations predominated in the first quarter-century following the Revolutionary War. Further hindrances to industrial development were provided by the Embargo Act of 1807, by the Non-Intercourse Act of 1809, and, finally, by the outbreak of the War of 1812. As a result, the country was thrown back upon its own resources because it could no longer remain dependent upon European countries for its manufactured goods. It has been pointed out that the year 1808 may be recognized as the date in American history which marks the transition of the United States from industrial dependence upon other nations to industrial self-sufficiency and diversified internal development.[12]

After the conclusion of peace in 1814, American ports were again open to the importation of foreign goods. To protect the new and struggling manufacturing enterprises which had sprung up during the war against such foreign competition, Congress enacted tariff measures carrying higher duties on imports than had prevailed previously. These tariffs

[11] *Ibid.*, p. 224.

[12] Bogart, *op. cit.*, p. 392.

helped iron and textile industries particularly and made it possible for the factory system to become established in the United States. That system, with its concentration of workers, equipment, and all the processes involved in factory manufacturing, called for new methods of business organization and management, previously untried and unknown because they had been unnecessary in small owner-operator establishments.

Public interest was centered not only in the protection and growth of manufactures but also in other internal improvements which favorably influenced industrial development. Improved roads were built and canals were opened; and finally the railroad, which was first successfully operated in 1828, brought wider areas within the reach of the farms, forests, and factories. Large-scale operations of business establishments still lagged behind such expansion. There was a wide scattering of small manufacturing plants and other types of business in every settled part of the country. However, as transportation facilities and industrial techniques improved, this diffusion of establishments was counteracted by a movement toward concentration. By 1850 concentration and combination were beginning to affect the character of American business.

Industrialization Since 1850

In the decade 1850–60 the United States made remarkable industrial progress. The Civil War, itself, tended to stimulate and extend that progress and to intensify trends and tendencies that were already apparent. When that war ended, the stage was set for the transition from small-scale to large-scale business operations. The factors which made this transition possible, if not inevitable, were the so-called "Yankee ingenuity" and the prevailing economic conditions.

From 1860 on, the rapidly growing population increased the domestic demand for the products of extractive as well as manufacturing industries. Likewise, concurrent industrial development and higher standards of living in foreign countries created an expanding demand for American goods abroad. Improved transportation facilities made distribution of these products to both foreign and domestic markets relatively easy. On the supply side, there was an abundance of rich and varied natural resources. The increased need of capital was supplied from the savings of Americans themselves and from investments on the part of the people in foreign countries, especially Great Britain, France, Germany, and Belgium. Of course, the repayment of such loans and the interest on them automatically stimulated the export demand for American goods. The labor supply was another important factor which presented no problem. It was met by the natural increase in the population plus the immigration of millions of people in the productive age group between fifteen and forty-five years.

An abundance of power was also available—first, water power and then steam power derived from the enormous resources of coal. Developments of power from both water and steam led to generation and distribution of electricity on a large scale. A more recent application of electrical power to industry has been by means of the internal combustion engine, which is capable of serving efficiently as a central power plant for a small factory.

Joined with all of these resources has been the inventive urge and skill of American engineers and technicians. "The American inventor did not merely modify the methods of making old things; in many instances he produced absolutely new commodities and devised original ways of manufacturing them. So important has invention become in modern industry that progress along these lines is no longer left to the unaided efforts of some talented individual. Practically every great manufacturing plant today has its research department in which experiments are being carried on at an expense far beyond the means of an individual inventor."[18]

The increase in number, size, and kind of enterprises and the concentration of business establishments into large units are forces which have had their effect upon the character of business organization and management. From the legal and financial standpoint, the evolution of integration began with simple loose agreements between competitors, usually with respect to prices and output. This was the typical form from 1865 to 1875. It was followed by a more formal arrangement called the "pool," whereby independent businesses sought to improve their competitive position by limiting production, sharing markets, and pooling profits. The pool was common between 1875 and 1895; but before it had become obsolete, a new and stronger type of organization appeared, known as the "trust." It provided for a board of trustees to whom the stockholders of competing corporations surrendered their shares of stock and in return received trust certificates. The trustees were thereby empowered to manage all the companies involved in the trust and to divide the profits of the venture among the holders of the trust certificates.

Trusts led to monopolies, which precipitated antitrust legislation in the early 1890's. After the trusts were dissolved, large-scale combinations continued as holding companies. This form of organization is a corporation, which, through the ownership of stock of subsidiary corporations, can gain control of formerly independent units, although not necessarily engaging in any business itself. Holding companies became the dominant method of merger, or combination of corporations, in the period of the late nineties and the early part of the twentieth century. Such corporate integration has continued through amalgamations and mergers, not only of former competing units, but often of enterprises engaged in widely

[18] *Ibid.*, p. 573.

divergent business and industrial activities. The merger, characteristic of modern business in the United States, is an attempt to attain efficient organization and management—conditions necessary for the successful operation of large-scale production of goods and services.

It must not be assumed, however, that all business is big in the United States. Testimony before the Temporary National Economic Committee of the Seventy-fifth Congress revealed that, of 1,730,000 employers who filed social security returns with the Treasury Department in 1937, 25 per cent had only 1 employee, 50 per cent had 3 employees or less, and 76 per cent had 9 employees or less. On the other hand, 195 employers, or one ten-thousandth of the total number, reported 12.3 per cent of the workers.[14]

This varied situation is portrayed also in the analysis of the size of business corporations in terms of assets (see Table 1). Corporations with

TABLE 1

SIZE OF CORPORATIONS BY ASSETS, 1935*

Asset Classes in Thousands of Dollars	Per Cent of Total Corporations	Per Cent of Total Assets Owned	Asset Classes in Thousands of Dollars	Per Cent of Total Corporations	Per Cent of Total Assets Owned
Under 50	54.7	1.4	1,000–5,000	4.4	12.6
50–100	14.1	1.4	5,000–10,000	0.7	6.4
100–250	14.0	3.0	10,000–50,000	0.6	16.2
250–500	6.9	3.3	50,000 and		
500–1,000	4.4	4.2	over	0.2	51.5

* "Investigation of Concentration of Economic Power," *Hearings before the Temporary National Economic Committee, U.S. Senate (75th Cong., 3d sess.)*, Part I, p. 229.

assets of $50,000 or less accounted for 54.7 per cent of the total number of companies who submitted balance sheets to the United States Bureau of Internal Revenue in 1935. At the other extreme, only two-tenths of 1 per cent of all corporations had assets of $50,000,000 or more. Only 1.4 per cent of the total assets were owned by the group of small concerns, while 51.6 per cent of the assets were owned by the large enterprises.[15]

In manufacturing, the United States Census of Manufactures of 1937 reported 166,794 manufacturing establishments with an over-all average of 59 wage earners each. In highly industrialized New England, there were 15,568 companies, with an average of 74 wage earners each. Although in the United States there are manufacturing concerns employing over 100,000 persons each, the averages indicated are reduced because of

[14] "Investigation of Concentrations of Economic Power," *Hearings before the Temporary National Economic Committee, U.S. Senate (75th Cong., 3d sess.)*, Part I, pp. 97–99.

[15] *Ibid.*, p. 229.

the large number of enterprises, such as candy and bakery shops, which produce for immediate retail consumption and hence have only a few employees, but which are, nevertheless, included in the census as manufacturing establishments. Regardless of size, however, fundamentally every business is confronted with the basic problems of organization and management. For the purposes of the discussions which follow, a typical business enterprise has been assumed to be one having at least 100 employees of whom approximately 10 per cent would be included in the management group.

THE BUSINESS CORPORATION

Prevalence of the Corporate Form

According to the most recent available statistics, summarized in Table 2, sole proprietorships are still the most numerous business firms in

TABLE 2

TYPES OF BUSINESS ORGANIZATIONS IN THE UNITED STATES ACCORDING TO LEGAL FORM*

Type	Number	Per Cent
Individual proprietorships	1,333,854	63.5
Corporations	530,779	25.2
Partnerships	237,367	11.3
Totals	2,102,000	100.0

* "Investigation of Concentration of Economic Power," *Hearings before the Temporary National Economic Committee, U.S. Senate (75th Cong., 3d sess.)*, Part I, pp. 84 and 228.

the United States. Yet, because of its dominance in economic activity, illustrated in Table 3, the corporation is the most important form of business organization in this country. As was shown in Table 1, there are a great many small corporations which, from the standpoint of management, are but legally modified sole proprietorships. Practically all moderately large concerns are incorporated, and, without exception, all of the largest privately owned business enterprises in the United States are corporations. Our government also frequently uses devices closely allied to the corporate form when it engages, as an owner or proprietor, in the operation of a business enterprise.

Because of its conspicuous position, therefore, the corporate form of business will be the basis upon which the discussion of the principles of organization and management in the succeeding chapters will be developed. It may be reiterated, however, that these principles are equally

TABLE 3

IMPORTANCE OF CORPORATE ACTIVITY BY BRANCHES OF INDUSTRY, 1937*

Industry	Per Cent of National Income	Per Cent of Business Done by Corporations in Each Industry
Agriculture	8.9	7
Mining	2.1	96
Electric light, power, and manufactured gas	1.6	100
Manufacturing	24.0	92
Contract construction	2.1	36
Transportation	7.3	89
Communication	1.3	100
Trade	12.5	58
Finance	9.3	84
Government	13.5	58
Service	11.9	30
Miscellaneous	4.2	33

* "Investigation of Concentration of Economic Power," *Hearings before the Temporary National Economic Committee, U.S. Senate (75th Cong., 3d sess.)*, Part I, p. 96.

applicable to all forms of business establishments wherein leader-follower and superior-subordinate relationships prevail.

Definition, Characteristics, and Development of the Corporate Form

The classical definition of a corporation is that given by Chief Justice Marshall in his opinion in the famous Dartmouth College case handed down in 1819:

> A corporation is an artificial being, invisible, intangible, and existing only in contemplation of the law. Being a mere creation of the law, it possesses only those properties which the charter of its creation confers upon it, either expressly or as incidental to its very existence. . . . Among the most important are immortality and, if the expression may be allowed, individuality, properties by which a perpetual succession of many persons are considered as the same, and may act as a single individual. They enable a corporation to manage its own affairs, and to hold property without the perplexing intricacies, the hazardous and endless necessity of perpetual conveyances for the purpose of transmitting it from hand to hand.[16]

Thus a corporation is a legal, artificial owner of business. It may own only a part of a single business enterprise, or it may own several separate business enterprises. To understand how its affairs are managed as a going concern, it is necessary to recognize its important characteristics.

A corporation is created by the voluntary association of a group of natural persons through a lawful grant of powers and privileges by the state. It is given life by a legal charter in conformity with established

[16] 4 Wheaton 636.

statutes called "corporation laws." By this charter its powers and privileges are defined in general terms, and its license to engage upon business activity is authorized. The original voluntary association thereby becomes identified as a legal being or artificial person, capable of carrying on business transactions as does a natural person.

While a corporation is a voluntary association on the part of its members, its existence is compulsory from the side of the state. It is self-renewing; and it is, therefore, sometimes characterized as having immortality. Its life cannot be terminated except by consent of the state, which is to say, according to law. In the management of its affairs a corporation is subject to majority rule. Its members are not each the agent for another, as is the case in a partnership. Having secured its authority through its charter, the incorporated group called "shareholders," by majority vote of shares of stock, delegates its management authority to its directors and officers. As a legal unit, a corporation is autonomous. It is self-governing within the limitations of its charter and such statutory restrictions as may be provided by corporation and regulatory laws. Thus the artificial personality of a corporation is derived from a combination of voluntary association and majority rule in conformity with public authority established by law.

Since a corporation is a creature of the state from which it receives its authority, it cannot escape public responsibility. A business corporation may be brought into being by motives of private gain on the part of the individuals concerned; yet the only ultimate justification for its being given important rights and privileges through a charter granted by the state is the public welfare. Incorporation of a business under public law is a modern device presumed to utilize private interest more effectively in the public benefit.

The development of the corporate form of business can be traced back to Roman law. While the Roman *collegium* corresponded to the modern corporation in certain aspects, the business corporation of today did not spring directly from it. Nevertheless, the civil law of Rome undoubtedly had a direct affect upon the corporation laws of later times.

Neither were the medieval guilds of England true corporations. They were rather loose federations of traders and craftsmen chartered by the sovereign. The first charters issued for trading purposes in England were not to English companies, which were then nonexistent, but to branches of the Hanseatic League. In 1266 and 1267 the merchants of Hamburg and Lübeck received from Henry III the right to establish their own "hansas," or trading associations, in London. It was not until the sixteenth century that English corporations became important business organizations.

The original English incorporated business concerns were the Mer-

chants of Staple, who were, as their title implies, wool buyers. Other early chartered companies were the Merchant Adventurers, who were shipowners as well as traders and who were a major influence in the growth of British foreign trade in the sixteenth century. It was during the seventeenth century that chartered joint-stock associations came into existence. Of the old regulated concerns, these companies most nearly resemble the modern corporation. Many of them were organized for colonization as well as for trade. "Adventurers" or merchants furnished the money required in their enterprises, and "planters," other members of the firms, became colonists. They were not only successful from a business standpoint, but they came to exert a far-reaching influence in history as well. One of the most extraordinary of them was the East India Company, which played a major role in establishing England's position in the Orient. Another was the Hudson's Bay Company, which still exists as a commercial concern but which was chartered in 1670 to secure control of the land, trade, commerce, and natural resources of the entire area tributary to Hudson Bay.[17]

Most of the British North American colonies were, in their inception, similarly chartered companies. Examples of these are as follows: the London Company, chartered in 1606, which founded the Jamestown Colony in Virginia in 1607; the Plymouth Company, chartered in 1620, which founded Plymouth Colony the same year; the Massachusetts Bay Company, chartered in 1629, which founded the Boston Colony in 1630; and the Georgia Company, chartered in 1732, which established a colony at Savannah in 1733. Similar companies of other countries which established colonies in the New World were the Dutch East India Company at New Netherlands (New York), chartered in 1624, and the South Company of Sweden at New Sweden (Delaware), chartered in 1638.

In the colonies, themselves, the British government erected corporations by charter during the eighteenth century. Two of these were the Ohio Company, organized in 1749 to deal in land "beyond the mountains," meaning the Appalachians, and Dartmouth College, in New Hampshire, chartered in 1769. The first clear case of the creation of a business corporation for profit under a legislative charter granted by a colonial government was the New London Society United for Trade and Commerce in Connecticut chartered by the Connecticut General Assembly in 1732.[18] It was not until after the Revolutionary War that business corporations began to appear in appreciable numbers. It is said that during the colonial period only seven such organizations were chartered.[19]

[17] For further details about the Hudson's Bay Company, see Chap. III, pp. 62–63.

[18] Lewis H. Haney, *Business Organization and Combination* (New York: Macmillan Co., 1913), p. 102.

[19] Corporation Survey Committee of the Twentieth Century Fund, *Big Business: Its Growth and Its Place* (New York: Twentieth Century Fund, Inc., 1937), p. 12.

After the turn of the nineteenth century the use of the corporate form of organization increased. This impetus was due to two principal factors. The first of these factors was the general expansion of the national economy. At first, such corporations were mostly small manufacturing concerns, and stagecoach and turnpike companies. Following the War of 1812, the period between 1815 and 1835 was an era marked by the rapid growth of banking and insurance companies and by the construction of canals and railroads. All of these enterprises opened new fields and gave new importance to the corporation. It was at the time a method by means of which the permanent investments required in such business undertakings could be realized to the fullest extent.

The second factor contributing to the expansion of corporations was the enactment of general incorporation laws by the various states. The early manner of creating corporations in the United States was by special statute. For example, when the Bank of North America was chartered in 1781, it required an act of the Continental Congress under the implied powers of the Confederation. There never has been a national general incorporation law on our federal statutes. Until Massachusetts passed the first of such acts in 1829, a business could be legally incorporated only by a special enactment of a legislative body. The pattern set by Massachusetts was followed by Ohio in 1846, New York in 1849, and, subsequently, by all the other states in the Union. Such laws have contributed as much, if not more, to the tremendous expansion of the corporate form of business organization than any other single factor.

It is not difficult to see why this is so. When incorporation procedure had to rely upon special legislative enactment, opportunities for discrimination were all too prevalent. Because of "pull," special favors to legislators, and even bribery, the incorporation of sound business enterprises often failed when unsound undertakings succeeded. Furthermore, such special acts were time-consuming and slow. Recesses, adjournments, and the general lack of continuity of legislative assemblies made incorporations impossible except when lawmakers were in formal session. General incorporation laws eliminated such delaying obstacles. These statutes also established uniformity in the provisions of corporation charters and in the conditions that must be met by the applicants for such charters. Finally, free enterprise in the development of natural resources and the business expansion of the country required laws under which individuals could freely incorporate and which would facilitate, rather than impede, such progress.

Importance of Large Corporations

Since the beginning of the twentieth century, there has been a continuous growth in the influence of corporations in American business. In

the period from 1910 to 1938, corporations increased in number by 90 per cent while the total number of business firms increased 45 per cent. In other words, the number of corporations increased about twice as fast as all firms put together.[20] Nevertheless, as was shown in Table 2, corporations account for only slightly more than 25 per cent of the total number of business concerns.

In considering the influence and importance of corporations in the business structure, the number of companies is not alone important; the dominant position occupied by corporations in the business activity of the country is equally significant. For example, it has been established that, in 1937, corporations accounted for 60–65 per cent of the total volume of business of all industrial groups in the United States, and for 92 per cent of the country's manufactures.[21]

Size is another important factor in considering the influence of corporations in the business structure. In many areas of our economy, it is the large corporation that is significant. By "large" is meant companies with assets of $100,000,000 or more. According to the *Statistics of Income* of the United States Bureau of Internal Revenue for 1941, there were, then, 426 of these giant concerns. While they constituted only one-tenth of 1 per cent of the total number of all corporations, they owned 48 per cent of all corporate assets and accounted for 22 per cent of the total gross receipts of all corporate enterprises. Of these 426 large companies, 199 were financial institutions and 227 were nonfinancial. Of the latter, 109 were transportation and other public utilities and 95 were manufacturing concerns.[22]

The magnitude of this concentration of business activity in a relatively small fraction of the total number of active corporations suggests the complex problems of organization and management involved in their operations. Such problems are, by no means, limited to large-scale businesses; but as corporations have grown in size and scope in this country, the burdens and responsibilities of management have increased correspondingly.

Influence of Corporations on Management

The development of the corporate form of business in the United States has created the modern setting for management. It is a setting in which there is a diffusion of ownership coupled with the consequent

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[20] "Investigation of Concentration of Economic Power," *loc. cit.*, p. 94.

[21] *Ibid.*, p. 97.

[22] U.S. Bureau of Internal Revenue, *Statistics of Income, 1941* (Washington, D.C.: U.S. Government Printing Office), Part 2, pp. 142–227.

separation of that ownership from active business leadership, which is the essence of management itself.

The owners of a corporation are its stockholders. In large corporations, especially, stockholders are commonly distributed widely among the public. The managers of such concerns are, therefore, not its owners, except to a very limited extent. Theoretically, the direction and control of the affairs of a corporation are vested in its stockholders by virtue of their share-voting power. Because they are spread so widely throughout the population, they are not able to exercise the power which they legally possess. Hence, the management of a corporation comes about through the delegation of authority to directors, officers, and other members of a selected management group.

The relatively small extent to which ownership and management are combined in our largest business corporations is pointed out by Gordon in an analysis of 176 companies. He shows that in 63 of these concerns management owned less than 1 per cent of the voting common stock. Holdings were less than 5 per cent in 120 of them, and the median holding of voting stock by management in the entire group of 176 corporations was 2.11 per cent.[23]

This separation of ownership and management is more marked in larger corporations than it is in smaller ones. In the very smallest type of incorporated firm, the principal owner may likely be its manager. As owner-manager, his decisions—actually as well as theoretically—determine the course of the business. He must assume the risks of profits and loss, and the stability and permanence of the investment represented by shares of stock, the majority of which he holds. Thus, in him the two basic elements of the entrepreneur—leadership and risk—are combined.

As a corporation increases in size, these two elements are separated. The functions of leadership are not performed by persons who risk property, secure profits, or sustain loss. They are performed by an elected representative group of directors and by hired executives, who may have few or no direct ownership interests in the business.

Against this background of growth and development of business enterprise in our country, there emerge the problems of organization and management which must be met. Thus modern business environment has three essential aspects. Owing to the dominant position of the corporate form of business, ownership and management have become increasingly separated; consequently, the concept of trusteeship has emerged as a major responsibility of the management group; and finally, the social significance of business has come to be recognized in its true perspective. As

[23] R. A. Gordon, *Business Leadership in the Large Corporation* (Washington, D.C.: Brookings Institution, 1945), p. 26.

Drucker puts it so aptly: "The central problem of all modern society is not whether we want Big Business but what we want of it, and what organization of Big Business and of the society it serves is best equipped to realize our wishes and demands."[24]

SUMMARY

In laying the background for an understanding of modern business organization and management, the evolution of business enterprise from ancient times to the present has been briefly sketched. From the rudimentary forms of trade in antiquity—wholly individualistic in nature—evolved the necessity for cooperation and association of businessmen in the Middle Ages. Out of these spontaneous and loose organizations came a division of labor, a separation of management from production, and the emergence of the entrepreneur in the domestic system.

As a result of the widening markets developed by the merchant promoters, the demand for goods outran the supply, and factories were established to take the place of household industries. Meantime, experiments had been going on which led to the invention of machines to supplement and supplant human labor in the factories. This transition from the handicraft stage of industry to factories equipped with power-driven machines marked the beginning of the Industrial Revolution in England in the eighteenth century.

The Industrial Revolution resulted in improved methods of production and in an increase in the amount and kind of goods available to consumers. At the same time, it stimulated the demand for raw materials in greater quantity and variety. New markets for the products of industry and new sources of supply of raw materials depended upon better transportation facilities. As railroads supplanted horse-drawn vehicles on land, and steamships outmoded sailing vessels in seagoing traffic, the influence of expanding markets transformed small-scale industries into large-scale undertakings.

In the United States the requirements of an economy geared to the full utilization of its abundant natural resources, its growing population, and its philosophy of private enterprise called for a type of business that was compatible with a complex and an expanding capitalistic system. The corporate form of business enterprise has been the answer to that call. It has become a dominant factor in our business structure. As such, it has produced new and complicated problems of organization and management. The need for ingenuity, vision, daring, and skill is as great in the field of business management as invention has been in industrial processes. The existence of the corporation signifies another era of evolu-

[24] Peter F. Drucker, *Concept of the Corporation* (New York: John Day Co., 1946), pp. 3–10.

tion—the age of "scientific management," a contemporary part of an ever moving industrial revolution.

QUESTIONS

1. The term "Industrial Revolution" has been criticized extensively by persons who regard human history as a manifestation of constant evolution. Nevertheless, the term has merit and value, in the sense that it describes the sudden effect of great inventions together with the release of individual initiative of many businessmen in England as that country broke away from the rigid legal controls and patterns of the Middle Ages.

   Discuss the era of industrial progress, which is commonly called the Industrial Revolution, from the following standpoints:

   a) Was the Industrial Revolution primarily an era of rapid and extensive changes in business and industry rather than the creation of something new, hitherto unknown and untried?

   b) Did the public generally in England believe that rapid industrial progress was a good thing, or did they resist the Industrial Revolution that was taking place?

   c) To what extent were the following factors present in the era of the Industrial Revolution: (1) the opportunity to exploit new inventions for profit; (2) the legal right to employ masses of workers; (3) the availability of the facilities of transportation and communication that would permit extensive world trade and other forms of marketing on a large scale?

2. Point out similarities and differences between the meanings of the following titles:

   a) Merchant adventurer

   b) Entrepreneur

   c) Organizer of an enterprise

   d) Manager of an enterprise

3. To fully comprehend the significant historical background of business, it is among other things necessary to have an understanding of both movements and concepts. Accordingly, distinguish between the expressions "laissez faire" and "industrial revolution," and show the implications of each to the other.

   (To answer this question properly, it will be necessary to consult references other than the textbook. Standard books on economics and encyclopedia articles will be found useful.)

4. We know from the writings of Marco Polo that in the thirteenth century, China was advanced at least as far as was Europe with respect to guild systems, inventions, and trading methods. Then, why didn't the Industrial Revolution take place in China instead of in England and western Europe? Also, why didn't it happen in Venice, where shipbuilding, in relation to the

times, was on a scale of mass production, and from whose highly developed commercial organization nearly all of the commerce of the world was controlled for a thousand years?

(For additional reading references bearing on this topic see Waldo Ricci, *The Travels of Marco Polo* (translation from L. F. Benedetto, New York: Viking Press, 1931); Henri Pirenne, *Medieval Cities: Their Origins and Revival of Trade* (Princeton, N.J.: Princeton University Press, 1925); and references in standard encyclopedias).

5. It is certain that the Industrial Revolution would not have been so intensive or so significant if the government of England had not abandoned its medieval efforts to direct the methods and the objects of industry and trade. With this transition in mind, discuss the following topics with respect to their effect upon industrial and commercial change:
   a) Piracy and privateering were commonplace on the high seas of the world. Define each of these activities, and show how their elimination fostered rather than retarded the development of trade and industry.
   b) Explain how minimum wage regulations and safety measures with respect to working conditions may form socially desirable bases for all business enterprises without reducing requisite incentive for the enterpriser.

6. Define and distinguish between the following terms:
   a) The Roman *collegium* and "an American college."
   b) The Roman *societas* and "an American fraternal society."
   c) A "business partnership" and a "business corporation."
   d) The original "Lloyds of London insurance underwriters," and "an American fire or marine insurance company."
   e) "A medieval merchants guild" and "an American association of businessmen," such as a chamber of commerce.

7. Prior to the year 1700, little attention was paid by the public to the problem of obtaining adequate supplies of pure water for human consumption and use. Accordingly, with the invention of cast-iron pipe, steam pumping engines, and other devices, domestic water supply became a fertile field for private business enterprise. More recently, the supply of water for domestic use, other than bottled water, has tended to become a governmental activity. In fact, in the United States most municipalities now own and operate their water supply systems and finance part or all of the cost of operating them by charging rates for water consumed by the people at their premises.
   a) Trace the similar rise and decline of private enterprise in the construction, maintenance, and operation of highways, bridges, and ferries.
   b) Without attempting to discuss the broader issue of socialism versus private enterprise, justify the above governmental activities in terms of the opportunities thereby created for private business enterprisers, such

as contractors, manufacturers, and highway motor transportation operators.

8. Grinding flour by hand is a tedious process, and the product that results from it is of uncertain and variable quality. Hence, flour milling by mechanical devices, driven chiefly by water power, in towns and on the domains of the nobility preceded the Industrial Revolution by a thousand years. But breadmaking has only recently emerged from the home and small craft shop to become a factory process.
   a) What reasons can you give for the reluctance or inability on the part of private enterprise to establish breadbaking on a factory basis until comparatively recent years?
   b) Flour milling has tended to be concentrated in certain localities and in large factory enterprises. Breadbaking continues to be relatively dispersed in many comparatively small factories. Why does this dispersion persist in this important food industry?

9. Aluminum has come to be recognized as a major metal since the Industrial Revolution took place. The extensive usefulness of this metal has been made possible by scientific research and the development of mass production methods which require large amounts of electrical energy. Even the generation of electricity for industrial purposes is a product of modern times.
   a) What would happen to the production of aluminum in its primary forms if it became necessary to manufacture it in small laboratories instead of in large factories? What are the implications involved in this illustration with respect to the social significance of large-scale industry?
   b) There are thousands of small business enterprises throughout the world that utilize aluminum in the manufacture of many common articles, such as cooking utensils. What are the implications involved in this illustration with respect to the effect of mass production upon the development of small factories and other business concerns?

10. The factory technique known as the "assembly line" has been the most significant single factor in the manufacture of automobiles that has brought motor car transportation within the reach of more people in this country than ever were able to enjoy riding or driving horses. The mass production of automobiles has provided many new opportunities for small factories, shops, sales offices, and other businesses related to the motor industry. When a local dealer sells an automobile, he transfers all financial risk to a bank or finance company; similarly, the manager of a local unit of a chain of gasoline filling stations bears no personal financial risk.
   a) Explain how it is that the advances in the mass production of motor cars has made possible the wide acceptance and use of the automobile in the everyday lives of people.
   b) Explain and give examples of the interrelation of large-scale enterprises and small businesses as exemplified by the automobile industry.

c) Explain and give examples of the tendency to separate managerial responsibility from financial risk in modern business.

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Chapter II

THE HUMAN ELEMENT IN ORGANIZATION AND MANAGEMENT

FUNDAMENTALS OF ORGANIZATION AND MANAGEMENT

THE fundamental principles of organization and management are universal. They are equally applicable to a partnership, a corporation, or a sole proprietorship. They are relevant regardless of the legal structure of a business, because the essential differences between legal types of business organization are centered in ownership and formal external relationships, not in operating techniques. The problems of organization and management are essentially the same for all types and sizes of business. Nevertheless, because of the characteristic part it plays today, it is almost instinctive to think of modern business solely in terms of the corporation. While this attitude is not correct, it does suggest the importance of the corporate form as an example with which to make clear the interplay of principles in the modern world of work.

In their external characteristics, it may be said that business units differ according to the kind of work that they perform. That is to say, the specific operations of a department store differ from those of a bank, and those of a factory vary from those of a transportation system. They are all engaged in business, however, and to the extent that they produce goods or services and seek to profit by a system of exchange, they are confronted with fundamentally identical considerations of organization and management. Furthermore, they all must combine the economic factors of land, labor, capital, and enterprise, but in varying degrees of importance. The processes of combination may differ, but there will be certain factors which are common to all business.

Ownership, management, and operation, when joined, describe a business unit in its broadest outline. In a small proprietorship or partnership enterprise, the relationship usually is simple and clear. Those who are the owners may also be the managers, and not infrequently they perform a considerable amount of routine work of the concern as well. The typical corporation is an enterprise of some size and is more highly differentiated in its organization. Therefore it is helpful to use this form for purposes of analysis in distinguishing one factor from another. These distinguishing characteristics are illustrated in Figure 1. In its present economic and political environment, ownership and administrative manage-

ment of business fill the top cup of the hyperboloid or hourglass, and operative management and labor fill the lower half.

Another approach to the differentiation of interests in the corporate organization of business in its relation to management has been made by Henry P. Dutton.[1] He calls attention to the fact that every act, whether simple or complex, has three component parts or stages. They are desire or will, perception or thought, and action or performance. If this formula

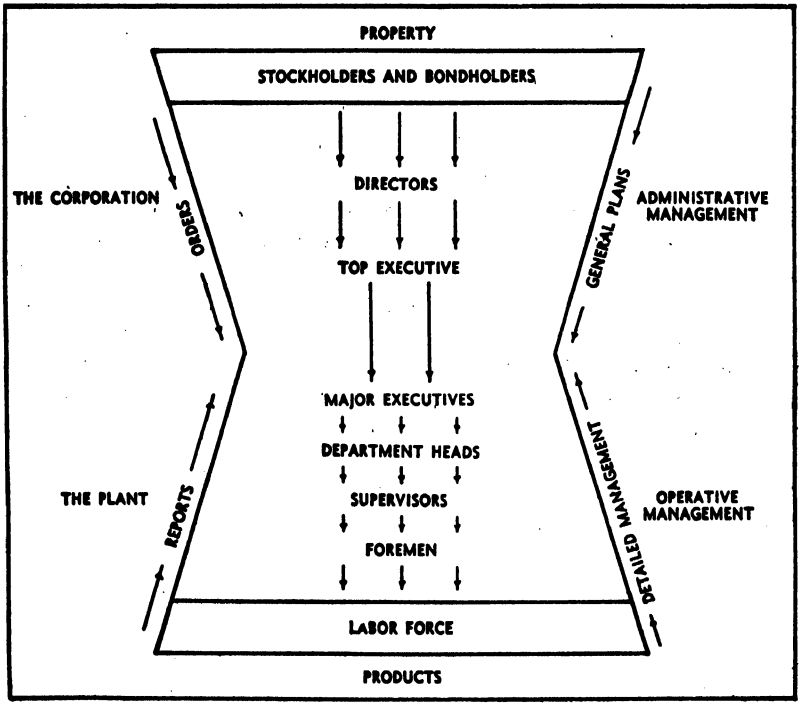


FIG. 1.—Organized relationship between ownership and management in a corporate form of business enterprise.

is applied to a business corporation, the parts thus represented are found to be distributed quantitatively in varying degrees among the groups which make up the organization, as shown in Figure 2.

This diagram shows clearly that there is seldom a complete separation between authority to act, the plan of action, and performance. Its purpose is to indicate that in these realms of activity there is a division of labor, so to speak, but that in this division there is also interdependence. For example, the most menial laborer exercises some discretion in his

[1] Henry P. Dutton, *Principles of Organization* (New York: McGraw-Hill Book Co., 1931), pp. 4–7.

daily work, even though most of his time may be taken up by routine tasks under definite orders. At the top level the stockholders represent ownership, which in a corporation is often absentee ownership. Ownership represents authority which has its source in the right of private property. By virtue of this right, ownership is vested with the ultimate power to act within the limitations of its charter granted by the state. Quantitatively, therefore, the bar representing the stockholders shows a proportionately larger space devoted to will than to performance.

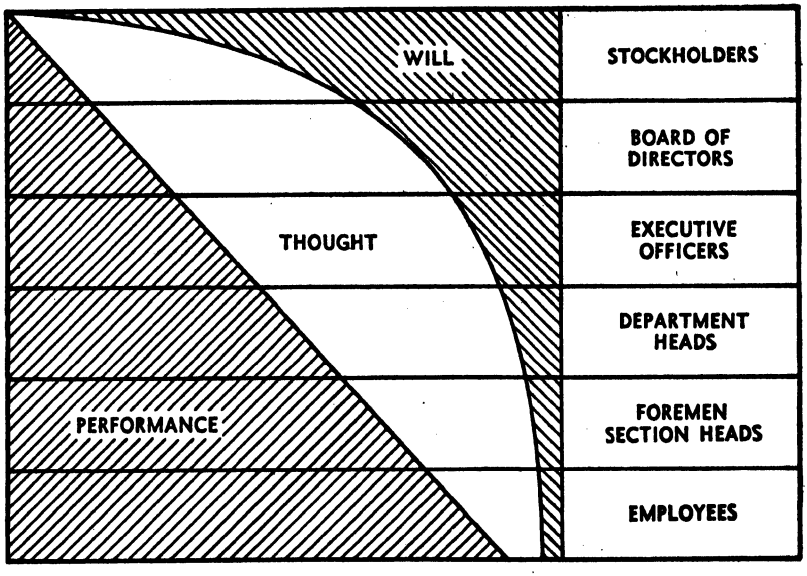


FIG. 2.—Distribution of the functions of will, thought, and performance in the relationship between ownership and management in a corporate form of business enterprise. Adapted from Henry P. Dutton, *Principles of Organization* (New York: McGraw-Hill Book Co., 1931).

The purpose of these illustrations has been to emphasize the various relationships which exist in business organization in its legal and managerial aspects. It is impossible, however, to pursue satisfactorily the implications of these relationships without an understanding of the terms used to describe them.

Management Defined

Frequent references have been made to "organization for management" and the "management group." These expressions obviously imply that there exist in business enterprise both an activity and a company of persons to which these terms may properly be applied. "What is management?" is a question which immediately arises.

Management may be defined in several different ways depending on the assumptions upon which the definition is postulated. From the broad social point of view, management is a technique or method developed as a result of the human tendency to form groups. Examples of such groups are governments, clubs of various sorts, and business enterprises. Whatever the group may be, it must have its own management. In this comprehensive sense, "management" may be defined as "a technique by means of which the purposes and objectives of a particular human group are determined, clarified, and effectuated." These ends are achieved by furnishing the group with leadership, that is, a differentiated segment of its membership which organizes the entire group and proceeds to accomplish the desired goal. Notice here the dual concept of process and structure: management *does* and management *is*. This dual relationship between functions and functioners must be clearly recognized, for it exists in both management and organization.

If, now, the general concept of management is considered in its specific aspects, other definitions must follow. In the different types of human groups which require management, the concept itself varies in details of application but not in fundamental meaning. By way of illustration, the following types may be given:

1. *Government* means the protection, regulation, and motivation of its citizens by any political unit. Government in this sense is rarely thought of as management, though it conforms in every respect to the comprehensive definition stated above.

2. *Public management* is the organization of any unit of government, and the exercise of authority and responsibility over the employees of such a unit.

3. *Military management* is a special type of public management. It involves the recruiting, training, organization, discipline, equipping, and command of military units such as air forces, land armies, and naval fleets.

4. *Association or club management* is a composite of government and public management, but varying in proportions according to its objective and methods. A chamber of commerce, for example, may motivate its members to work for a civic enterprise such as an airport, or it may attempt to prevent or stamp out some unfair trade practice. These voluntary actions are government management in character. In contrast, the typical club or society resembles public management in that it has its group of employees which must be organized and supervised much as a government unit.

5. *Business management* is a specialized and distinct type, differing materially from government and public management. In view of the fact that further amplification will follow, here it may be briefly said that business management includes the organization, direction, control, and supervision of the operations of a business unit.

6. *Government proprietary management* is a special type of business management. When a business enterprise is taken over by government by

reason of ownership or control, the authority of proprietorship is vested in some unit of government. As a result, not only must such unit engage in the normal functions of business management, but it is also involved in government and public management problems and considerations.

Although these six types of management differ in many outward respects, each of them rests on the same fundamental considerations of human characteristics and behavior. There can be no question as to the validity of certain basic principles of management which govern the association of human beings for any purpose, and groups of any size.

Attempts are sometimes made to differentiate between "administrative management" and "operating management." Where this division is made, the board of directors and top executives are placed in the first classification, and the major executives, department heads, and the supervisors in the second, as in Figure 1, above. The theory of this segregation is based on duties performed. It is assumed that the activities of the directors and the top executive have chiefly to do with policy-forming, and those of the officers lower in rank with execution. A major difficulty with such an analysis is that in reality no clear-cut line of demarcation can be drawn between those who make policies and those who execute them. To the extent that any member of the management group contributes to the plans and purpose of a business enterprise, he is engaged more or less in policy-forming. Even employees or groups of the employees, though no part of the "management," at times have great influence in policy formulation, as well as in operating management.

In summary, "management" may be defined as "a psychological process of exerting leadership upon followers which satisfies a fundamental human craving." It provides a logical basis for individual division of labor and specialization within a particular group. Management exerts leadership by assuming authority, imposing responsibility, and exacting accountability for all actions of individuals coming within the scope of the organization. This leadership is also manifested by resisting attack upon and fostering the progress of the central purpose and objective of the group. In this way coordination among all the members of a unit is effected.

Organization Defined

This psychological process of exerting leadership reflects only the dynamic or more active half of the concept of management. In addition to the motivating force of leadership, management also consists of organization. Organization results from leadership. To its psychological aspects, therefore, must be added the definition of "organization" as "a phase of management."

Here again the dual concept of process and structure appears. It is impossible to obtain a clear concept of organization except in this twofold sense. In the first place, organization may be conceived as consisting of a framework by means of which the work of a business, managerial and otherwise, is performed. Such an arrangement or structure suggests order, articulation, system, and harmonious action. It, too, is dynamic in that its elements are live, pulsating human beings. It consists of a hierarchy of grades or ranks of executives and employees held together by a fabric of interrelated policies, orders, and instructions. It provides the necessary channels, reservoirs, and points of origin and termination for the flow of all types of management directions and controls.

In the second place, organization denotes a process. A business organization does not come into existence spontaneously. It is the result of the creative effort of management. While yet the creator of an organization, management is also a part of its own creation. Perhaps it is simpler to say that one task of management is that of building and maintaining the organization structure. This task involves determining the extent of specialization that is to be present in the work of a business unit; it undertakes the allocation of authority, responsibility, and accountability for the performance of such specialized work; and it strives for coordination in the work to be done by the utilization of the human and material resources available to it. Thus, organization is the process of specializing the work of management so that harmonious and efficient business activity may result; and it may also be thought of as the product of this process, that is, the structure of the personnel relationships of a business enterprise.

The dual relationship between organization and management is illustrated by the pyramid in Figure 3. In this figure, organization, that is, the human structure of a business unit, is seen to consist of a unity composed of the directors, top executive, major executives, department heads, supervisors, and employees. Management, however, includes only the first five of these groups. They are the ones who are charged with the authority and responsibility of building the organization structure and of determining the policies of the business; and they are held accountable for accomplishing its work, in accordance with such policies.

It is not incorrect to omit the stockholders from such a diagram. In a business corporation, as in representative government, the group which holds final authority lies outside of the organized unit itself. While the citizens of a country, vested with the right of suffrage, constitute the ultimate authority in government, still, in the usual connotation of the term, they are not the government. They could be, as they were in the old town meetings. But, taken as a whole, the citizenry is too cumbersome to work out proposals and to put them into operation. Therefore, it delegates this authority to legislatures, reserving the right of approval or

disapproval by its votes for the members of these lawmaking bodies. Similarly, in a corporation the stockholders are the ultimate authority. As in government, they are often numerous and scattered, and by their votes they delegate their authority to a representative group called a "board of directors" which becomes a part of a business organization precisely as a legislature becomes a part of government.

Organization and Management

The foregoing concepts supplement each other in forming a comprehensive statement of the fundamental characteristics of organization and

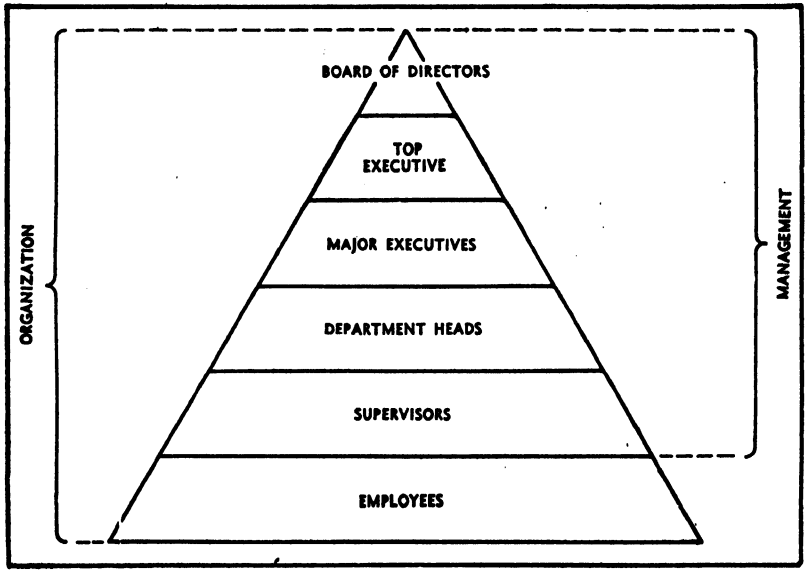


FIG. 3.—Dual relationship of organization and management.

management. They are presented together in Figure 4. *This chart is so arranged that it may be read from left to right and from top to bottom.* The first column contains three subtitles which refer to the definitions in the second column. These definitions are arranged vertically in the same order as they appeared previously in this chapter. The first one states what management is and does; the second defines the leadership aspect of management; and the third one, organization. Reading from top to bottom, the definitions are divided into three groupings, which may be designated as (1) the general statement, (2) the statement of method, and (3) the statement of result. Reading from left to right, the arrangement suggests the nature of management by indicating interrelationships.

From the foregoing analysis of Figure 4, the following definitions may be constructed by reading vertically, each of the three columns:

1. *Management in General Terms.*—Management is a technique by means of which the purposes and objectives of some particular human group are determined, clarified, and effectuated. This technique consists of a psychological process of exerting leadership upon followers and the creation of an organization, logically and systematically devised to allocate authority, responsibility, and accountability within the group.

Definition Subtitle	General Statement	Statement of Method	Statement of Result
What management is and does:	Management is a technique for determining, clarifying, and effectuating the purposes and objectives of some particular human group	By furnishing group leadership	Organizes the entire group and proceeds toward accomplishment of the desired objective
What leadership is and does:	Leadership is a psychological process for providing guidance for followers which satisfies a fundamental human craving	By assuming authority over and responsibility for individual actions within the scope of the organization and by resisting attack upon and fostering progress toward the purposes and objectives of the group	Effects coordination among all members of the group
What organization is and does:	Organization is a structural pattern for allocating authority, responsibility, and accountability within the group	By providing the necessary channels, reservoirs, points of origin and termination for the flow of all types of management directions and accountability controls to and from each member of the group	Facilitates the motivation of each member of the group, thus creating individual morale

Fig. 4.—Organization and management defined.

2. *Management in Terms of Method, i.e., Leadership.*—Management is a method of providing leadership in group action. This is accomplished (*a*) by assuming authority over and responsibility for actions of individuals which come within the scope of the group; (*b*) by molding the actions of individual members of the group in order to resist attack upon, and to foster the progress of, the purposes and objectives of the group; and (*c*) by providing channels for the flow of all types of managerial directions and accountability controls to and from the individual members of the group.

3. *Management in Terms of Result, i.e., Organization.*—Management creates organization. The process of organizing consists of the task of specializ-

ing the work of management so that harmonious and efficient activity may result. The product of organizing is a structure of human beings held together by a fabric of coordinated relationships by means of which the individual members of the group are motivated toward the realization of the common objective.

THE FUNCTION OF LEADERSHIP IN ORGANIZATION AND MANAGEMENT

It is clear, from the foregoing analysis, that both the motivation and the technique of organization and management depend upon the leadership of one or more persons. The distinctive task of leadership is to direct and to unify the efforts and inclinations of the individuals of a group. Leadership implies followership; the one is as important as the other, even though conventions of etiquette erroneously direct attention to the former and forbid emphasis upon the latter. Necessarily, there are few leaders and many followers; but to be effective, leadership must be a cooperative enterprise.

Management itself is a cooperative undertaking. It comes about through the organized effort of people—that is to say, through their consciously coordinated activities designed to accomplish some desired end. It goes without saying that modern society could not function without organization. It is the difference between order and chaos in all human affairs. The process of providing leadership for followers to satisfy a fundamental craving for guidance to action is a characteristic of all biological life from insects to human beings. Therefore, people instinctively "organize" for a great variety of purposes. Yet, as has been pointed out by Barnard,[2] successful cooperation in or by formal organization is an abnormal, not a normal condition in modern civilization. True, organizations of all sorts are omnipresent, but what is observed are the survivors of innumerable failures. They are the exceptions rather than the rule. Among human institutions, permanency of organization is a rare quality, to be found in only a few instances. History is strewn with the residue of organizations that were in existence for a time, only to disintegrate and disappear. This record of failure has been true of nations and governments—organizations on a grand scale—as well as business and other enterprises which on their lesser scale, were similarly the product of cooperative effort.

This lack of stability and permanence in organization has been as prevalent among business institutions as elsewhere. The high mortality of business firms and the causes of failure have been the concern of investors, credit agencies, lawmakers, and other members of the public.

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[2] Chester I. Barnard, *The Functions of the Executive* (Cambridge, Mass.: Harvard University Press, 1938), p. 5.

By "failure" used in this sense is meant discontinuance, with or without losses, voluntary or involuntary, and does not necessarily refer to insolvency or bankruptcy alone.

It is reported by a leading mercantile agency[3] that the active life of the average business enterprise is five and one-half years. This is but a fraction of the average length of life of American citizens, who now have an over-all life expectancy at birth of 62.81 years for males and 67.29 for females.[4] Some business enterprises do exist materially longer than human beings, but they are exceptions which prove the rule. For example, among the millions of business concerns in existence in the United States in 1926, there were only twelve companies which had been in continuous operation under the management of the families that had originally established them before 1776. Similarly, only eighty-seven companies, in the entire United States, had remained unchanged in basic form and identity during the period from 1826 to 1926—in spite of the fact that, by 1826, the corporate form of business with its provisions for continuous life had become fairly typical.[5]

Business failures and liquidations are attributable to a variety of causes. Among them are business incompetence, lack of capital, poor credit risks, competition, speculation, and personal extravagance. Added to these managerial causes are the external hazards of fires, floods, unseasonable weather, and bad business conditions. Credit-rating agencies are inclined to combine all of these causes as evidences of poor management. Even the impersonal and external risks to which business is undoubtedly subject could be avoided, mitigated, or overcome to a considerable extent by more capable management.[6]

Whether it be a business enterprise or any other type of formal organization, its stability and permanency depends upon its adjustment to its external environment composed of many complex elements—social, biological, and physical—and upon its internal conditions of management. Its survival in the interaction of the forces of these external and internal factors devolves upon the decisions and actions of its leadership.

Leadership Defined

In considering the definition of leadership, it is important to recognize that the verb "to lead" has two commonly accepted meanings, and to distinguish between them. Used one way, it denotes pre-eminence or superiority in excellence; used in the other way, it means guidance or direction. It is in the latter sense that it applies to the leadership function in management. A leader may properly guide others and, to a degree,

[3] Roy A. Foulke, *Behind the Scenes of Business* (New York: Dun & Bradstreet, Inc., 1937), p. 147.

[4] Source: U.S. Bureau of the Census.

[5] Foulke, *op. cit.*, p. 148.

[6] *Ibid.*, pp. 67–68.

govern their activities without himself excelling in the work of his subordinates.

In Figure 4, above, "leadership" has been defined as "a psychological process for providing guidance for followers, which satisfies a fundamental human craving." This definition has several implications. Psychologically, it implies that a leader possesses certain traits, qualities, and skills which enable him to get something done by others; and because of his influence, members of a group become willing to act under his guidance. As a prominent business executive has said, "leadership is the art or technique of persuading men."[7]

The group instinct is a natural social phenomenon. From its beginning, society (man's collective life) has been an expression of association. Without association it could not have existed. Consequently, a degree of human cooperation and mutual association has prevailed from the very start of civilized experience, and it is without doubt through this cooperation under leadership that man has become dominant upon the earth. It has always been the groups that were best organized and that had the most competent leadership that stood the best chance of surviving.

There exists, therefore, the fundamental craving for guidance in the cooperative effort of people toward a goal which they deem to be desirable. Without that guidance, a group lacks motivation, direction, and decision. Leadership in a group is a unifying influence whereby efforts of its members are changed from the heterogeneous purposes of individuals to a common course of action toward a common goal. Translated into terms of management, leadership, in this sense, has been described by Gordon as "the function of organizing and directing business enterprise, of making the decisions which determine the course of a firm's activities."[8] We recognize in this definition that leadership in a business enterprise resolves itself into *executive activity*, for it is in the executive of a concern—of whatever title and status—that the tasks of managerial leadership are concentrated. The discussion of the principles of business organization and management which follows is, therefore, confined to a consideration of the principles which govern the activities of that group of persons, who, by reason of rank or position, issues orders and is thereby distinguished from another group who puts them into effect.

The Objectives of Executive Leadership

By "objective" is meant "the goal or intended purpose which defines the scope and direction of managerial effort." It implies the cooperative

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[7] Henry S. Dennison, quoted by J. H. S. Bossard and J. F. Dewhurst, *University Education for Business* (Philadelphia: University of Pennsylvania Press, 1931), p. 103.

[8] Robert A. Gordon, *Business Leadership in the Large Corporation* (Washington, D.C.: Brookings Institution, 1945), p. 5.

teamwork of a group or association of persons under the guidance of a leader.

Since business transactions are measured in terms of money, and since work and goods are bought and paid for with money or its equivalent, it follows that the primary objective of every business is expressed in pecuniary values. Income and outgo are instinctively translated into dollars and cents, and in the process, management deliberately strives to so conduct its affairs that the amount taken in will exceed the amount paid out. For private business enterprises, this basic objective or purpose is called the "profit motive," or the "profit objective."

Enterprises organized as cooperative societies, eleemosynary institutions, or government-owned concerns are confronted with precisely the same objective. By them, however, the objective is commonly designated as the "service motive." To understand the distinction between the profit motive and the service motive, it is necessary only to notice that the real difference lies in the distribution of profits and not in realizing them. Private businesses divide profits on the basis of ownership represented by investment. Cooperatives and noncommercial enterprises distribute them in some other way, each peculiar to its particular type. It may be on the basis of patronage, as with cooperatives; or increased services, as with charitable institutions; or even reduced taxes, as with some government-owned establishments.

To maintain that the profit motive, and private business which this motive represents, is the antithesis of the service motive, is obviously fatuous. The indispensable element of all business is service of some sort. Without service being rendered, society does not long tolerate any business enterprise, private or public, and since society stands in the place of final authority, it can and it does eventually erase from its scroll all those that will not or cannot serve.

It should be pointed out, however, that in the matter of service rendered, private business must render the service required of it and earn a profit as well. Socialized, governmental, and noncommercial enterprises, on the other hand, render service to be sure; but in the absence of profit, they may fall back upon such resources as donations, subscriptions, and revenue from public taxation for resources with which to cover deficits. But even in such instances, except in purely charitable and philanthropic institutions, society often eventually tires of deficit financing, and when social support ceases, so does the enterprise. As a sound principle, it may be asserted that no business enterprise, whatever its legal status may be, can long render service unless it makes a profit. In other words, private, cooperative, and public businesses can give services efficiently and permanently only so long as each obtains income in excess of its expenditures. It follows, therefore, that the purposes of executive activity are twofold: to render service and to do so profitably.

But profitableness is neither a temporary nor a self-exclusive condition. It cannot come into being, or exist, without taking into account other concomitant objectives. Permanency and stability of the interests of ownership, satisfactory labor relations, and the favorable acceptance of the enterprise by the public are examples of such aims. Toward them, business leadership must also strive if a profitable business is to be achieved and maintained.

In the internal affairs of management, there are subsidiary goals which contribute to the central objective of the enterprise. A business organization is usually a collection of divisions or departments, each of which requires leadership in order to perform its particular functions. The heads of such divisions must determine departmental objectives, and they must secure the cooperation of their subordinates to achieve such ends.

A particular end or goal may or may not be the prerogative of a designated department head. It may have been decided for him by someone else, depending upon the nature and the extent of his authority. Within the limits of that authority and in conformity to it, the leader must necessarily determine the course of action required of him. But in pursuing the realization of objectives, leadership will always be subject to conditions which are both internal and external in character.

The Conditions of Executive Leadership

The business executive is not independent of his environment, but he must adapt himself to it. He occupies a central position in the productive process, and as such many forces converge upon him. There are the requirements of ownership having to do with capital, how it shall be invested, used, and preserved; what profits ought to be made; and how these profits are to be distributed. There are the demands of customers with respect to goods and services—their quantity, quality, and availability, and the price to be charged for them—all of which he must translate into production. His are also the problems arising out of government regulations, competition, and the vagaries of public opinion.

In a sense, he performs a dual function—that of adjustment to the business environment and that of innovation—which in itself serves to change that environment. By virtue of new processes, new products, and new markets, changes in national economic conditions may be effected even to the extent of raising the standards of living of the people. Executive business leadership is not a passive agent that merely responds to events as they occur. Rather, it is creative in the sense that it translates situations into action, a function fundamental to economic and business development.

Adjustment and innovation are likewise conditions that exist in the internal affairs of business and to which the executive must adapt him-

self. As has already been stated, in some degree or another he must share in the determination of the objectives or goals of the enterprise, not only in the light of its external environment, but also in relation to the resources and limitations of the firm itself. Its resources are both human and physical, and its limitations may be defined by the scope of its occupational objective, its competitive and geographical situation, and its financial strength. From the internal standpoint, therefore, the executive is in the midst of the conditions which require that he make decisions affecting policy.

To accomplish its occupational objective, namely, the kind of goods or services it purposes to produce, an enterprise has its own environment of technological procedures and operations. They are instruments for the accomplishment of objectives already determined, but they are conditions to which the executive must adapt himself and which offer to him opportunities for innovation. It does not necessarily follow that a leader, to effect changes and improvements in productive processes, whether of goods or services, must have high technical competence himself. He may be called upon to guide such operations even though he has no particular skill in them. It is not unusual that highly skilled technicians are incompetent as executive leaders. The important thing is for the executive to recognize the technological conditions that surround him, and to have a considerable knowledge and understanding of the special technical aspects of the work that he is called upon to direct.

The principal instrumentality of internal management is personnel. Personnel relations create conditions of executive leadership which have to do with the selection of major and minor officials at one level, and with the selection, assignment, training, compensation, and promotion of workers at another level. Into an organization there continually come numbers of individuals with little or no prior knowledge of its aims and purposes. These workers are assigned to special tasks in accordance with a scheme or pattern of special functions to be performed. As a business expands, there is a tendency toward a more and more complete functionalization of individual duties.

In this way an organization grows by division. Its work is divided into departments in order to secure the effective participation of its personnel. Each department or division of the business, in turn, must have its own directive head or leader. The successful operation of a business depends upon this managerial and operational division of labor, but involved in it is the risk of divided interests. It is natural for both workers and departmental heads to see the problems of an organization primarily in terms of their particular jobs. Therefore, since functions and departments increase in number and specialization as a business grows and

expands, there is danger that a corresponding condition of specialized interests will develop.

It is at this point that executive leadership is confronted with another internal situation. It may be described as "coordination management." Only the top leader can, at this evolutionary stage, correct the undesirable tendencies which functionalization and division of labor in modern business tend to create. Unifying the work and interests of the individuals who constitute an organization is distinctly the task of the highest executive leader.

Involved in this task are the methods used to secure unified action. It is true that executives may be distinguished from workers because executives give the orders that workers put into effect. But executive leadership to be most effective consists of something more than merely giving commands. By command is implied *power over* people, a purpose on the part of the one who issues commands to secure the results in which he is particularly interested. For the business executive, command is not enough. It leaves out the quality of leadership or *power with* people. As Ordway Tead has pointed out, command is interested solely in results, while leadership is equally concerned about the process by which the result is obtained.[9]

Associated with coordination activities involving employer-employee relationships is a condition of executive leadership created by expanding labor organizations and the enactment of protective legislation for labor. This development in the business economy of the country has resulted in an increasingly complex situation that cannot be avoided or evaded by business management. As a consequence, the business executive finds himself concerned with negotiations and other relations with organized labor groups. In dealing with them, he is called upon to effect understandings and agreements with respect to wages, hours, and other conditions of employment.

Finally, realizing the conditions of his work, an executive leader must be a realist in that he must be able to recognize problems that require action and must be able to take action when action is needed. It may not be that the outcome of the undertaking can always be foreseen. Nevertheless, like the "adventurers" who have always spearheaded economic progress, he must be willing to take chances based on reason and such facts as may be available to him. At the same time, he must also be an idealist in that he will seek goals which neither he nor his generation may reach. That is the nature of an ideal: it is a standard of perfection or excellence sought after but never fully realized. Once a goal has been reached, it is no longer an ideal. Its achievement presents new possibilities

[9] Ordway Tead, *The Art of Leadership* (New York: McGraw-Hill Book Co., 1935), p. 12.

and opportunities, thereby projecting ever forward the ideal of business leadership.

THE QUALITIES OF EXECUTIVE LEADERSHIP

Of course, executive activity is something more than giving orders. The power to command rests upon the principle of authority. Since authority involves its concomitant, responsibility, it follows that executive activity also includes accountability or the necessity to answer for intrusted powers and obligations. A moment's reflection on this truth is sufficient to reveal the further fact that executive proficiency has its roots in the personal qualities of the individuals who are charged with the duties of management.

When organization for management is considered in this light, its structure is presented in its true perspective. The executive group of a business has often been compared to a machine. The fallacy of this comparison is emphasized by Fayol, a famous French industrialist, who shares with the American, Frederick W. Taylor, the distinction of having pioneered in the thinking and writing about scientific management. Pointing out that a machine cannot transmit power without some loss, Fayol says, ". . . in the mechanism of administration, . . . every intermediate link in the chain can and must be a source of energy and ideas; there is in each of these links, or men, a power of initiative which, if properly used, can considerably extend a manager's range of activity." Then, using a biological comparison, he remarks that "the part played by man in an organization is analogous to that of a cell in the animal."[10]

It might be added in pursuing this comparison a bit farther that, when an organ fails, the whole animal suffers and even dies; or that, when cells are diseased or atrophied by reason of improper or inadequate nourishment and exercise, not only does their usefulness cease, but they interfere with or obstruct the normal processes of living, drain other tissues and cells of vitality, and the only remedy, if life is to be sustained and health restored, is removal.

If, then, the executive must of necessity be a "source of energy and ideas," his strength will be measured in terms of the qualities which go to make up such energy and ideas. Popular success literature has been filled with accounts of "natural born" executives and "self-made captains of industry." Such writings leave the impression that executive skill is a God-given attribute reserved for the few. This attitude, if carried to its logical conclusion, would remove executive activity from the realm of scientific analysis and action to one of luck or chance.

On the contrary, management is largely a matter of reason, of per-

[10] Henri Fayol, "Administration Industrielle Génèrale." Translated excerpts by L. Urwick in "The Functions of Administration," *Papers on the Science of Administration* (New York: Columbia University Press, 1937), pp. 121–22.

sonality, and of strength of character. But executives are made quite as much by conditions of environment, by the nature of the organizations of which they are a part, and by the influence of their subordinates as by their own personal qualities. Nevertheless, personal traits and characteristics are important and may not be disregarded.

The Quality of Intellect

A business executive is an official vested with the authority and responsibility for the achievement of the purposes and objectives of management. He is the one to whom the ownership, the workers, and the public look for accomplishment. In an age in which business must operate in an environment of complex social, political, and economic conditions and elaborate technological development, the intellectual capacity of an executive is an important quality. As Professor Schell has pointed out in his stimulating little book, *The Technique of Executive Control:*

> The executive is constantly facing problems which yield most readily to the analytical approach of the scientifically-minded thinker. The technical problems involved in coordinating the work of a group of men, materials, and equipment in such a way that maximum quality and quantity with minimum waste is obtained are often exceedingly complex. They require solution well in advance of their actual doing. The successful executive wins his victories through preventive rather than curative action. Thus to plan and schedule the future calls for a process of thought which is distinctly scientific in nature.[11]

Scientific Management

The intellectual character of executive activity suggests the scientific nature of management. Scientific management, as a movement, was founded by Frederick W. Taylor. As a machinist, he first began his work and observations in the Midvale Steel Works, near Philadelphia, in 1885. Later he became a factory manager and then a consulting management engineer. Throughout his life, which came to an end in 1915, he sought to prove the truth of his own proposition that management consists of 75 per cent analysis and 25 per cent common sense. He meant that management is, in fact, more of a science than an art. In the biography of Taylor by Frank B. Copley, the philosophy and underlying principles of scientific management as Taylor developed them are summarized as follows:

> Scientific management, in its essence, consists of a certain philosophy, which results, as before stated, in a combination of four great underlying principles of management. . . . The first of these four groups of duties taken over by the management is the deliberate . . . gathering in of all the great masses of

[11] E. H. Schell, *The Technique of Executive Control* (New York: McGraw-Hill Book Co., 1934), pp. 11–12.

traditional knowledge and then recording it, tabulating it, and, in many cases, finally reducing it to laws, rules and even to mathematical formulae. . . . And later, when these laws, rules and formulae are applied to the everyday work of all the workmen . . . they invariably result, first, in producing a very much larger output per man, as well as an output of a better and higher quality; and second, in enabling the company to pay much higher wages to their workmen; and third, in giving to the company a larger profit. The first of these principles, then, may be called the development of a science to replace the old rule of thumb knowledge of the workmen. . . . The second is the scientific selection and then the progressive development of the workmen. It becomes the duty of those on the management's side to deliberately study the character, the nature, and the performance of each workman with a view to finding out his limitations on the one hand, but even more important, his possibilities for development on the other hand; and then, as deliberately and as systematically to train and help and teach this workman, giving him, wherever it is possible, those opportunities for advancement which will finally enable him to do the highest and most interesting and most profitable class of work for which his natural abilities fit him, and which are open to him in the particular company. . . . The third of the principles of scientific management is bringing of the science and the scientifically selected and trained workman together. . . . Invariably we find very great opposition on the part of those on the management's side to do their new duties. . . . The fourth of the principles of scientific management is perhaps the most difficult . . . to understand. It consists of almost equal division of the actual work of the establishment between the workmen, on the one hand, and the management on the other. . . . All day long every workman's acts are dovetailed in between corresponding acts of management. First the workman does something, and then a man on the management's side does something . . . the management take over all work for which they are better fitted than the workmen. . . .[12]

Since Taylor's time, the term "scientific management" has tended to fall into unfavorable repute in many quarters, chiefly because it became associated in the public mind with worker speed-up systems installed by unscrupulous, self-styled industrial engineers. It also failed to survive in its original form because of its cumbersome method of functionalization. Taylor's emphasis was upon executive-worker relationships, and the output of productive effort as a result of such relationships. Many details of his method may now hold nothing more than historical interest, but his central philosophy of the importance of the scientific approach to management problems lives on.

Psychological Qualities

In addition to these intellectual aspects of executive activity, there are also those of a psychological nature. It is possible that the whole field of

[12] Frank B. Copley, *Biography of Frederick W. Taylor* (New York: Harper & Bros., 1923), Vol. I, pp. 13–17.

adult human pyschology may be considered part of the technique of the executive. Situations involving emotions and attitudes constantly arise between superiors and subordinates. To ignore them, resist them, or even fail to recognize them, will lead to mistakes and sometimes disaster. The major psychological situations may be listed as follows, in the order of their complexity:

1. The simplest relationship is the interplay of attitudes between the executive, personally, who issues or transmits an order, and the employee, personally, who receives and performs it.
2. More involved is the interplay of attitudes between a series of executives who transmit an order from executives in the higher ranks of management through successive levels down to the employee who is to perform it.
3. Most complex of all is the interplay of attitudes between two parallel lines of executives, each of which transmits orders down to the same employee. Such a situation raises the problem of dual subordination or "multiple bosses," generally undesirable but sometimes necessary. In its complexity it may lead to conflict between executives within an organization, as well as to orders to the worker that are conflicting, or otherwise impossible to perform.

These psychological situations offer opportunities for the clash of personalities and emotional reactions. They are so commonplace in the everyday work of the world as to be regarded as trivial by many people who should know better. Issues which arise to rock business and disturb industrial peace frequently have their inception in incidents which are nothing more than personal irritations. All too often industrial strife is due to disagreements which cannot be compromised because of the attitudes of those involved.

What, then, are the attributes of a successful executive? Many attempts have been made to dissect personality in order to weigh the importance and significance of each of its elements. Like a mysterious alloy, it has so far resisted complete analysis. Nevertheless, certain traits can be isolated and weighed. Those which are of value are called "virtues," and their opposites "vices." Obviously, a study of the attributes of a successful executive is concerned with the presence of virtues and the absence, as nearly as possible, of vices.

To list all the virtues which are desirable in an executive would require a catalogue of all worth-while human qualities—mental, moral, and physical. Even then, to make specific application of these elements would be hopeless because different human relationships and different experiences require the calling into play of different characteristics, or the same ones in varying degrees. In other words, no two human beings are precisely alike, nor can all dealings between individuals be based upon the same pattern.

Attributes of Personality

Despite this apparent resistance to analysis and classification there are certain traits which stand out in greater prominence in executive success than others. To be successful, an executive must be both independent and cooperative. He must be independent in the sense that he must think through and solve the separate problems involved in the operation of his portion of the business. He must be cooperative in the sense that the work under his control must form a correlated segment of the larger unit—the business as a whole. On the one hand, he advances by means of independent strategy and diplomacy; and on the other, he subordinates himself and merges his own policies into those of the institution of which he is a part.

The importance of the qualities of personality is emphasized by the attention that has been given to the analysis and evaluation of them by both scholars and executives. For example, Chester I. Barnard, a major executive of the Bell telephone system, lists five characteristics he believes to be fundamental qualities of "those who are leaders." According to his opinion, in the order of importance indicated, they are as follows:

1. *Vitality and Endurance.* These qualities are not to be confused with good health. There are people of good health who have little or moderate vitality. Conversely, there are some who have poor health who have great endurance. Notwithstanding these exceptions, these qualities are important for the following reasons. First, both promote and permit the unremitting acquirement of experience and knowledge. Second, vitality is an element in personal attractiveness or force which is sometimes a compelling aid to persuasiveness. And third, vitality and endurance are important because leadership often involves prolonged periods of work and extreme tension without relief. Failure to endure, may mean permanent inability to lead.

2. *Decisiveness.* Decisiveness needs to be considered in both its positive and negative aspects. Positively, decision is necessary to prevent erroneous action. Negatively, failure to decide creates a destructive condition in organized effort. To delay direction, approval or disapproval introduces indecisiveness throughout the whole process of cooperation and thus restricts experience, experiment, and adaptation to changing conditions.

3. *Persuasiveness.* This is the ability of an individual to induce another to believe or do something. It involves a sense or understanding of the point of view, the interests, and the conditions of those to be persuaded.

4. *Responsibility.* It is an emotional condition that gives an individual a sense of acute dissatisfaction because of failure to do what he feels he is morally bound to do, or because of doing what he thinks he is morally bound not to do, in particular concrete situations.

5. *Intellectual capacity.* This is the quality commonly designated as the posession of "brains." It has been put in fifth place because it is subsidiary to

the other qualities of leadership listed in this analysis. That part of behavior of which people are most conscious is largely intellectual, whereas much of the most effective behavior is unconscious and responsive.[13]

In *The Technique of Executive Control,* to which reference has already been made, three qualities are mentioned of which "the executive requires an unusual allotment." These traits, with brief comments quoted from the author, are as follows:

1. *An innate interest in, and affection for, people.* Executives are moulders of human stuff. Success in handling men requires an abiding interest and continuous thought. To one without this inborn interest, the problem ceases to be appealing after the first flush; the mind closes to progressive thinking, and the ability of the executive to guide and direct is enormously weakened. . . . The executive who has a sincere affection for his men will find his greatest happiness in hastening their self-improvement and progress. His pleasure lies in the making of man. Hence such a leader obtains an unusual degree of loyalty and cooperation. The man-maker believes in people "by and large," searches out the strong points in every individual, and provides incentives for their translation into economic value.

2. *Strength or power of personality.* The executive group represents the nervous system in the organization. Through them the impulses of action are transmitted and finally impressed upon the wills of the employees. The larger and more powerful the impulses, the more pronounced will be the reaction of the employee mind. An effective organization requires executives who have more than average power of personality. It is undoubtedly true that this characteristic is one of the basic elements justifying a natural right to authority.

3. *A scientific trend of mind.* The successful executive wins his victories through preventive rather than curative action. Thus to plan and schedule the future calls for a process of thought which is distinctly scientific in nature. This quality also brings a humility before truth, a sense of discrimination between fact and opinion which are invaluable. The executive can contrast his ideals with an accurate knowledge of existing conditions, and thus find a proper approach to constructive improvement.[14]

Professor Schell makes the further point that as a basis for the foregoing personal analysis, the qualities of moral stamina, physical vigor, and the necessary high level of intelligence have been taken for granted. That is to say, these latter qualities do not, or should not, distinguish business executives from other men who occupy positions of respect and trust. The traits enumerated are those of greatest importance.

Another list of attributes of a successful executive, though perhaps

[13] Chester I. Barnard, "The Nature of Leadership," in S. D. Hoslett (ed.), *Human Factors in Management* (Parkville, Mo.: Park College Press, 1946), pp. 23–26.

[14] Schell, *op. cit.,* pp. 8–13.

not so incisive, has been made by Samuel W. Reyburn.[15] Out of his long experience as a business executive he has summarized what he calls "necessary qualities," under eleven heads. They are:

1. Personal health
2. Integrity
3. Intelligence
4. Industry
5. Classification
6. Analysis
7. Judgment
8. Ability to teach others
9. Enthusiasm
10. Capacity for following through
11. Self-control

Some of these traits need amplification in order to convey Mr. Reyburn's meaning. The qualities of intelligence and industry are supplemented by the statement that they should be coupled with worth-while experience which has been so used as to enrich the individual through concentrated attention. The expressions "classification" and "analysis" obviously are intended to stand for the "scientific mind," spoken of by Professor Schell and the "intellectual capacity" referred to by Mr. Barnard. Self-control is explained as being the ability to marshal and coordinate all one's knowledge and talents and to have the courage to put one's decisions into action.

INFLUENCE OF SIZE ON BUSINESS LEADERSHIP

An organization comes into being when two or more persons join their talents and resources in order to achieve a common end. Most, if not all, business concerns started with small beginnings. Their growth in size has been due to a process of combining units already in existence or by adding new units to an organization previously formed. As enterprises have grown in size, they have increased in scope and complexity, with the consequence that the tasks of management have varied in extent and magnitude directly with the growth that has taken place.

Leadership in Small Business

Fundamentally, the objectives of small business and large business are identical. They vary only in magnitude and complexity. For example, the small business has the same central objective of profit-making as the large one. Stability and permanence of investment are common to both of them. The small concern, like the large one, must secure public approval and acceptance of its products and services as well as its standards of business conduct. It is principally in the realm of internal management that the impact of leadership differs, and then not so much in the ends sought as in the methods of achieving those ends.

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[15] Samuel W. Reyburn, *The Development of a Business Executive* (New York: Associated Dry Goods Corp., 1938), pp. 10–24.

In a small business it is commonly possible for its management to be dominated by the forceful personality of its principal owner or owners. In other words, the owner-manager characteristic prevails—a condition not found in a large corporation. In the small corporation the theoretical power of stockholders over the policies and operations of the business is a fact as well as a legal right. Its stockholders very often are also its directors and executives. In a local enterprise, even its stockholders, inactive as directors or executives, may have a hand in the direct control of its policies. Thus, in a small corporation, the combination of ownership and leadership usually exists. The owner or owners, at least as far as the majority shareholding interests are concerned, exercise the responsibility for and the jurisdiction over all of its operations. These persons may also perform some of its detailed activities.

The conditions of leadership vary widely in small-scale and large-scale business. In each case, of course, leadership must adjust itself to existing and changing political, social, and economic conditions; but the impact of these conditions varies in degree and influence with the size of the enterprise. It is in the internal conditions of management that differences are most marked.

In the small concern there is often no clear-cut division of its activities into departments. The activities of each function of management are not of sufficient volume or importance to warrant specialized executives. In many instances, one executive is responsible for two or more groups of activities. Thus the smaller the unit, or the number of persons constituting it, the less need there is for an elaborate and complicated organization. Specialized services are not necessary, fewer workers have to be trained and supervised, and the relations between employer and employees have little or no formality. Hence, the conditions of control and coordination are simplified, often to the point of becoming spontaneous and automatic.

Basically, the qualities of executive leadership are the same whatever the size of an enterprise may be. The leader in a small company, like the one in a large concern, must have the intellectual capacity to make decisions regarding investment, allocation of resources, product, market, prices, and the employment of workers. His knowledge of all of these factors may not need to be so broad or so technical; nevertheless, the lack of an understanding of them commensurate with the extent of his responsibilities may mean the difference between success and failure. Scientific management may not be highly developed in a small business; yet the necessity for executive leadership on a basis of facts and reason is as important in businesses of small and moderate proportions as in the large ones.

With respect to the attributes of personality elaborated upon at length previously in this chapter, they are as important for an executive of a

small business as for any other leader. It is obvious that successful leadership, to any degree and in whatever circumstances, depends upon such qualities as vitality, endurance, honesty, industry, cooperation, and self-control.

Leadership in a small business is not of a variety different from leadership in a big business. Its roots are in the same soil of physique, intellect, character, and personality. Whether such leadership can measure up to the requirements of executive authority and responsibility demanded of it on the lowest, highest, or intermediary level on the scale of effectiveness of business enterprise depends upon the nurture and development these personal qualities have received.

Leadership in the Large Corporation

A large corporation is distinguished by the fact that, with few exceptions, its ownership and leadership are widely separated. While the ownership of a corporation is vested in its stockholders, and by virtue of the shares of stock they own, the election of directors is their prerogative; yet, in the selection of this board that right is often purely nominal. In practice, the majority of individual stockholders wield practically no influence. With the exception of those persons who hold large blocks of shares, stockholders vote largely by prepared proxies or they default in voting entirely. Hence, stockholders generally, especially when their numbers run into the thousands, make few, if any, decisions or exercise any significant influence in the management of the corporation they own.

Legally, the members of a board of directors can be selected only by the voting of shares of stock, each common share usually carrying one vote. Since the individual stockholders, as a whole, are largely a passive agency in the process of electing directors, how the votes are cast and for whom becomes, then, a matter of the power and influence of a relatively small group of persons. As has been said, some of these groups are often owners of large numbers of shares. Other groups may have no ownership connection with the corporation; but because of their position as creditors, bankers, or customers or because of public prominence, their influence is felt when directors are elected. Also, it is not unusual for the major executive of a corporation to carry considerable weight when members of the board of directors are chosen, although the executives themselves may be minor stockholders or own no shares at all.

The board of directors may also be passive in sharing in the tasks of management. Most commonly, however, it plays an active role. It may limit its sphere of action to the selection of the principal officers of the corporation, the determination of major policies, and the exercise of veto power in the approval or disapproval of proposals brought to its attention by the executives of the firm. There are certain other functions which the

board cannot legally avoid. (A fuller discussion of the powers and functions of a board of directors will be taken up in Chapter V.) Beyond these activities, the real leadership in a large corporation is in the hands of its executives.

This leadership is complicated because decisions are made at various levels of authority. Leadership thereby becomes divided by a process of delegation. First, there is a division in the vertical plane ranging from the chief executive at the top to minor executives at the bottom. And, second, there is a horizontal division based on the specialization of executive functions. Furthermore, leadership may not be confined to a single person but may result from unified action of a group as, for example, an executive, finance, or some other type of committee. Whatever the scheme of organization for management may be, business leadership in a large corporation includes in its responsibilities the initiation and approval of decisions which are determinants in the firm's management. It also includes the creation and maintenance of the organization and the coordination of its various elements.

The successful prosecution of all of these functions depends on the qualities and capabilities of the executives who furnish the leadership. Leadership cannot be impersonal, even in a large enterprise. Leadership is subject to pressures and forces that result from conditions of external environment, organization, and large-scale operations. To them it must respond in the best interests of the company. In a large corporation these interests are more definitely separated than they are in a small business. Ownership and leadership are generally clearly divided. The former must rely completely on the latter for profits and dividends. The relations with employees are often also entirely formal, manifested principally by negotiations with labor organizations. And, finally, the large corporation occupies a more prominent position in public consciousness, politically, socially, and economically. Such prominence often attracts critical attention which smaller concerns can avoid.

All of these conditions surrounding and affecting a large corporation have resulted in a special type of business leadership. It may be called "professional" in the sense that it requires a particular competence and is not a field for amateurs.

PROFESSIONAL BUSINESS LEADERSHIP

Throughout this chapter the discussion of the human element in organization and management has attempted to make it clear that the strategic factor is executive leadership. It is the dynamic constituent part of our economy by which human and physical resources are combined, directed, and made useful to society. As such, executive leadership has sometimes been called "management engineering" in the sense that an

engineer is one who has been trained in, and who follows, a particular calling which conforms to certain standards of procedure and product.

Executive leadership of necessity exists in some degree in every business organization. It has been estimated that in the United States not less than 5,000,000 persons are engaged in executive work, of whom 100,000 occupy major executive positions.[16] Whether these figures are exactly correct is not so important. The significant thing is that they indicate that leadership has become a calling which engages the time and talents of a large fraction of the population engaged in gainful occupations. When leadership attains the status of a career and requires relatively high technological, intellectual, and personal qualities, it becomes professional in character.

The Need for Professional Business Leadership

The need for management engineering at the professional level is most apparent in large-scale business. As a corporation increases in size with respect to its numbers of shareholders, ownership becomes diffused and scattered. Since shares of stock are property, they are bought and sold in the market, and otherwise acquired and transferred by individuals. Thus the legal evidence of ownership comes into the hands of many persons who have no competence to exercise control over the affairs of the firm, some of whose stock they hold. Other stockholders may be entirely disinterested in matters of management. Stocks may be acquired by them for speculative purposes, thereby having a value placed upon them independent of their importance as evidence of ownership. Even persons who purchase corporation stocks for investment purposes may limit their interest to the dividends received. If such returns are not satisfactory, investors know they can dispose of the stock at any time they choose. This dispersion of ownership in a large corporation, therefore, makes it imperative that leadership, theoretically represented by shares of stock, be transferred or delegated to a salaried executive personnel whose job it is to manage the affairs of the business largely independently, but to the interest of its owners.

If the ownership of a large corporation happens to be concentrated in just a few persons, there is still a definite need for the services of professional leadership. The tasks of management of a large enterprise are so numerous and diverse that they cannot be grasped by most individuals who might be its owners. The executive leadership required exceeds the knowledge, time, and the physical resources possessed by the owners. When the stock is closely held, its owners may exercise substantial or complete control over the selection of directors and even the appointment of major officers. Still, the need for a staff of salaried executives, experts

[16] Barnard, *The Functions of the Executive*, p. 289.

in the various and complex ramifications of the management of a large enterprise, to whom actual leadership in the business is delegated, is none the less diminished.

Qualities and Interests of Professional Leadership

Although professional executives are only "hired help," they are salaried persons who attain positions of rank and authority without reference to their share in the ownership of the enterprise they represent. At the same time, they are the ones who are called upon to make decisions which vitally affect all of those who own it. By the process of delegation, they are vested with authority for its efficient and profitable management. From this authority spring such responsibilities as production schedules, price-making, conditions of employment, wage agreements, costs, operating margins, financing, accounting, and marketing. The decisions they make and the courses along which they direct business enterprise affect not only their own firms but sometimes the entire economy of the country as well.

It follows that the qualities which successful professional executives must possess are necessarily more highly developed than those required of owner-managers or salaried employees of small concerns. Generally, professional executives are better educated in order that they may have greater facility in the comprehension of their responsibilities. The qualities of keen judgment and analytical thinking are resources which are indispensable for them. Theirs is the scientific approach to business problems. Decisions based on rule-of-thumb methods, custom, or mere expediency have to be minimized or avoided altogether. Furthermore, long experience is as important as formal education in the acquisition and development of the mental equipment which is required of professional leadership; and the lack of either qualification handicaps the useful application of the other.

As an enterprise grows in size, it is obvious that, in relation to all of its operations, the technical knowledge or skill of its major executives become proportionately less important. Hence, the professional leader must be so constituted that, while he may once have been a technician himself, he has reached the point where he is both willing and able to delegate authority to others who are subordinate in rank but expert in specialized functions. The professional executive consequently must surround himself with a staff that is capable of solving problems, of making recommendations and sometimes decisions in the fields of research, planning, budgets, personnel, and other techniques. "Not to make decisions that others should make is to preserve morale, to develop competence, to fix responsibility, and to preserve authority."[17]

[17] *Ibid.*, p. 194.

Since the pecuniary gains of the professional executive are not the profits of the business but the salary, bonuses, and other personal benefits he may receive, he is confronted with the danger of allowing personal ambitions to predominate over the welfare of the owners, workers and the community to which the enterprise is contributory. Since there is a minimizing of the personal-profit urge—a factor which is probably the strongest motive in owner-manager leadership—other interests must take its place. Stability in professional leadership is, therefore, motivated by such impulses as prestige of position, the challenges that come with authority, and the urge for creation and innovation. There is also the consciousness of trusteeship, which is a recognition of moral responsibility, or the right use of power.

Responsibilities of Professional Leadership

Professional business leadership in any concern, large or small, is subjected to many pressures. On the one hand, it represents that ownership to the personnel within the organization; and on the other, it represents the enterprise to the public. Even when top leadership has delegated all other managerial functions to subordinates in rank, there remains the residual function of coordination. The responsibility to personnel, therefore, comes down to the establishment of unified and harmonious activity. Involved in achieving such a condition are decisions affecting the choice of employees, both salaried persons and wage earners. Within the limitations of externally imposed policies, executive leadership is responsible for wage and salary rates and for other conditions of employment. Leadership must also assume the responsibility for the technological aspects of operational and productive methods and processes. For example, it must simplify the work of direction, supervision, and control through specialization and departmentation without causing the organization to degenerate into a "bureaucratic stiffening of the joints."[18]

In its external relationships, there converge upon the professional leadership of a large enterprise the varied influences and pressures of stockholders' interests, government regulations, labor unions, financial interests, lawsuits, court decisions, and public opinion. In its responsibilities to stockholders, management is obligated to operate the business profitably, but at the same time to maintain its economic and legal stability without retarding its progress. Progress requires initiative, innovation, and response to change. Leadership in such circumstances must achieve a nice balance between taking chances and playing safe. Undue caution in the interest of profit-making may lead to stagnation, atrophy, and deterioration for lack of vitality; but extravagant experimentation and untested ventures may also lead to loss and failure.

[18] Gordon, *op. cit.*, p. 322.

The responsibilities of managing a business within the law are continually becoming more and more complex. While executive leadership in a firm of any considerable size is never without its expert legal counsel, there are still decisions to make on the basis of the recommendations of such counsel and the outcome of public hearings and lawsuits. There is also the requirement of an understanding and implementation of government regulations as they affect the policies and operations of a business institution. Closely related to such problems are the relations with labor unions and their leaders. Since so large a proportion of all wage earners are employed by firms whose managements are in the hands of professional executives, the responsibility for the welfare of the workers and the equitable distribution of a major portion of the national income rests with such leadership.

The responsibility to the public is of several sorts. There is the responsibility for the wise use and conservation of the natural resources which find their way into industry as raw materials. There is a similar responsibility with respect to the contribution of the entire capitalistic system to the standard of living and general welfare of the people. In a more limited sense, there is also the responsibility for financial stability because the savings of millions of individuals, both large and small investors, in large measure account for the money and credit available to management in enterprises of all kinds.

Most important, perhaps, is the broad responsibility of professional business leadership to the public, summed up by Eric Johnston as follows:[19]

> Above all, no business exists in the abstract. It flourishes or withers in a particular social, political, and economic climate. Consciously or not, the business man and those associated with him contribute to their community and their country, for good or ill. In detail the American system is intensely competitive; but in its entirety it is interdependent. Its growth has been and must remain organic. No part of it—whether the workers, the farmers, management, or some particular region—can long be permitted to decline or to suffer without dragging down the rest. They must flourish together. That's the over-all design of our dynamic America, and the heart of the American credo.

QUESTIONS

1. Following the pattern of Figure 1, make a diagram showing the proper relationships of the following groups of persons as they are representative in American army organization:

   a) The President and the Congress of the United States.

[19] Eric Johnston, *America Unlimited* (New York: Doubleday, Doran & Co., 1944), p. 11.

b) Army enlisted personnel, including noncommissioned officers.

c) Chief of Staff of the army headquarters organization.

d) The public, i.e., the civilian citizens of the United States.

e) Army field commanders, such as captains, colonels, and generals.

2. It has often been said that the high mortality, or failure, rate among small and beginning business enterprises is due to the "small" individuals who are the owner-executives. In this statement the word "small" has two different denotations.

   a) Distinguish between these different meanings of the word "small," and defend the accuracy of the statement as written.

   b) Illustrate your answer by imagining yourself to be a young owner of a recently launched small business. Indicate the difficulties you would encounter in the undertaking, and explain how you would set about to avoid the untimely failure, or bankruptcy, of your enterprise.

3. Make up your own list of the desirable personality attributes of an executive by combining the three lists given in the text of this chapter and by adding any other attributes of your own selection, for example, those listed in Question 9, below. Explain fully the reasoning you have followed in preparing your list.

4. In your own language, define the word "profession." Then distinguish clearly between the following occupations and show how each of them conforms or fails to conform to your definition:

   a) Corporation lawyer.

   b) Factory production engineer.

   c) Research chemist in charge of factory product control.

   d) Business executive such as a sales manager.

   e) Certified public accountant employed to make an annual audit of a company.

5. Give illustrations, not necessarily chosen from business experiences, of each of three types of psychological relationships that may exist between executives and subordinates. In presenting these illustrations, let the text material in this chapter be your guide, but do not hesitate to amplify or to criticize it in order that you may state your own views as to the value of the psychological approach to the problems and duties of leadership.

6. In your own words, elaborate upon the following statements so that their meanings are made perfectly clear:

   a) The verb "to lead" has two definite meanings.

   b) There is a difference between having "power over" people and having "power with" people.

   c) The fourth principle of scientific management, as developed by Frederick W. Taylor, is the most difficult principle to understand and to apply.

7. Select some one great American leader, such as Washington or Lincoln, or any other person of your own choice, from recent history. Write a brief

essay setting forth all the reasons for his eminence. You may use the text of this chapter as a guide to your analysis, but draw heavily upon your own study of the person you have chosen. Consult references, such as histories, biographies, and encyclopedias freely, and quote these references in your discussion of the qualities of leadership which are exemplified in the life and character of the individual you have selected for this study.

8. By following the terminology and divisions of Figure 4, contrast the fundamental principles of organization and management that are, in your belief, equally important to:
   a) The operation of a hotel, contrasted with the operation of a naval vessel on a long cruise in foreign waters.
   b) The operation of a radio station as a private enterprise, contrasted with the management of a symphony orchestra by a municipality or by an association on a nonprofit basis.

9. A great military leader has been praised for the following personal characteristics: his habit of seeking out, whether in conferences or in private study, the fundamental principle basic to the subject under consideration; his orderly mind, capable of a comprehensive grasp of problems and situtions; and his ability to present orally and in writing the core of any problem, together with its solution, so clearly that all can follow and understand his reasoning.
   a) Evaluate and expand upon these characteristics of leadership, especially in their relation to other leadership qualities.
   b) Explain fully whether you think that these characteristics of leadership are indispensable to the success of a business executive.

10. Not all corporations organized in the United States represent private enterprise alone. For example, farm cooperatives, mutual savings banks, mutual insurance companies, and associations of various kinds are also incorporated.
   a) If you think there is any, point out the differences that prevail with respect to the "profit motive" in a private business corporation and in such corporations as cooperative business enterprises, mutual insurance companies, and eleemosynary institutions.
   b) If some corporations do not seek to make a profit, explain why they do not, and show who makes up deficits in such instances.
   c) Explain what is meant by the "service motive" as it prevails in different types of corporations.

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CHAPTER III

THE PRINCIPLES OF AUTHORITY, RESPONSIBILITY, AND ACCOUNTABILITY

PRINCIPLE DEFINED

MANY thoughtful persons, contemplating the human relationships that are the essence of management, conclude that the manifestations observed are essentially the interplay of "psychic forces." There is much ground for concurrence in this concept because the distinctions between superiors and subordinates are psychological in nature rather than physical. Moreover, the relationships between superiors and subordinates have been stated in terms of leadership and followership, and the idea embodied in the term "leadership" is the fundamental one of authority and its corollaries—responsibility and accountability.

If, then, this embodiment is fundamental, it is logical to inquire if the concepts of authority, responsibility, and accountability are not principles underlying the whole philosophy of organization and management. It is recognized that a "principle" is a comprehensive law or doctrine from which others are derived or upon which others are based. It emphasizes the idea of a basal truth, unvarying and general in its application to the subject under consideration. It is recognized further that principles are often confused with techniques, criteria, and rules in an attempt to reduce human associations to formulas in order that such phenomena may be dignified as a science. The difference between principles and rules is the difference between the permanent and the transient, between sources and derivatives, or between motives and performance. Being general in their application, principles are the foundation upon which rules—specific in their direction and purpose—are established.

These observations have a logical bearing upon organization and management. It has already been shown that management is essentially the psychological process which provides leadership in group action. Organization, furthermore, is a major aspect of that process, in that, through leadership, it specializes the tasks of management and brings about a structural unity, the parts of which are individual persons held together by a fabric of coordinated relationships. In authority lies the origin of leadership and the *right* by which it is exercised. In all business enterprises the presence and effect of authority are identical in kind, though variable

in scope and degree. By reason of its pervasiveness as well as its indispensability, authority can properly be recognized as a principle.

THE PRINCIPLE OF AUTHORITY

Authority is inherent in leadership. If by nature, accident, indolence, or force of circumstances, one lacks the qualities of leadership, authority will not be his to exercise; or if, perchance, it is assigned to him, it will soon be taken away. But, on the other hand, if he does have ability, he will demonstrate the truth of the assertion that "authority gravitates to him who can." This is simply one way of describing scalar promotion in the executive ranks of management. The dictionary definition of "authority" is "rightful power in virtue of office or trust."

The Source of Authority

The concepts of "right" and "power" lie at the roots of the meaning of authority. But power issues from right through the process of delegation. Therefore, an analysis of authority is concerned first with its source, and second with its nature. Under our democratic form of government the right upon which managerial authority is based has its source in the Constitution of the United States through the guaranty of private property. Since the Constitution is the creature of the people, subject to amendment and modification by the will of the people, it follows that society, through government, is the source from which authority flows to ownership and thence to management.

Society thus releases authority to business enterprise, but never entirely relinquishes its ultimate right and power of control over it. The residuum retained finds expression in regulatory measures embodied in statutory law that must be obeyed. In this way, management is subject to two aspects of the same final authority, namely, (1) that which is delegated constitutionally to ownership through the right of private property, and (2) that which is retained by government and exercised through regulation or limitation. Should this right of private property be taken away, as in the case of a completely totalitarian state, no authority representing private ownership would remain for the discretion of management. Government would become the owner and would therefore control all managerial activities. In other words, objectives, policies, direction, supervision, organization, and all other phases of management would become the subjects of law enactment and enforcement, either by statute, edict, or administrative procedure.

Release of Authority by Charter

The extent to which government may go in releasing its authority to a business enterprise is indicated in the charter of the Hudson's Bay Com-

pany, issued in 1670 by Charles II of England. This charter was granted to Prince Rupert and seventeen "other noblemen and gentlemen," incorporating them as the "Governor and Company of Adventurers of England trading into Hudson's Bay." By its terms, the corporation had secured to it "the sole trade and commerce of all those seas, straits, bays, rivers, lakes, creeks and sounds" tributary to Hudson Bay, together with the possession of "all the lands and territories upon the countries, coasts, and confines of the seas, bays, etc., aforesaid, that are not already actually possessed by or granted to any of our subjects, or possessed by the subjects of any other Christian prince or state." Further, the charter granted complete lordship and entire legislative, judicial, and executive power within these territorial limits over the inhabitants therein situated or to be situated in the future. These latter rights were not surrendered by the Company until 1869, about two hundred years later.[1]

Two hundred and thirty years after the founding of the Hudson's Bay Company by Charles II of England, the American people embarked upon the corporate form of business on a large scale. It is true that many business corporations had been formed in this country before the turn of the twentieth century; but the chartering of the United States Steel Corporation on April 1, 1901, marked a new epoch in the development of industrial combinations in this country. An aid to the creation of so large an enterprise (original capitalization, $1,100,000,000) was the liberality of the corporation law of the state of New Jersey, which granted its charter. The objects of the Corporation as set forth in that charter are, in part, as follows:

> To manufacture iron, steel, manganese, coke, copper, lumber and other materials, and all or any articles consisting, or partly consisting, of iron, steel, copper, wood or other materials, and all or any products thereof.
>
> To acquire, own, lease, occupy, use or develop any lands containing coal or iron, manganese, stone or other ores, or oil, and any wood lands, or other lands for any purpose of the company.
>
> To mine or otherwise to extract or remove, coal, ores, stone and other minerals and timber from any lands owned, acquired, leased or occupied by the Company, or from any other lands.
>
> To buy and sell, or otherwise to deal or to traffic in iron, steel, manganese, copper, stone, ores, coal, coke, wood, lumber and other materials, and any of the products thereof, and any articles consisting or partly consisting thereof.
>
> To construct bridges, buildings, machinery, ships, boats, engines, cars and other equipment, railroads, docks, ships, elevators, water works, gas works, and electric works, viaducts, aqueducts, canals and other waterways, and any other means of transportation, and to sell the same, or otherwise to dispose thereof,

[1] See *The Encyclopædia Britannica* (11 ed.), Vol. XIII, pp. 852–53; also G. Bryce, *Remarkable History of the Hudson's Bay Company* (London, 1900).

or to maintain and operate the same, except that the Company shall not maintain or operate any railroad or canal in the State of New Jersey.

To apply for, obtain, register, purchase, lease or otherwise acquire, and to hold, use, own, operate and introduce, and to sell, assign or otherwise to dispose of, trade-marks, trade-names, patents, inventions, improvements and processes used in connection with or secured under letters patent of the United States, or elsewhere or otherwise, and to use, exercise, develop, grant licenses in respect of, or otherwise to turn to account any such trade-marks, patents, licenses, processes and the like, or any such property or rights.

To engage in any other manufacturing, mining, construction or transportation business of any kind or character whatsoever, and to that end to acquire, hold, own and dispose of any and all property, assets, stocks, bonds and rights of any and every kind, but not to engage in any business hereunder which shall require the exercise of the right of eminent domain within the State of New Jersey.

To acquire by purchase, subscription or otherwise and to hold or to dispose of stocks, bonds or any other obligations of any corporation formed for, or then or theretofore engaged in or pursuing, any one or more of the kinds of business, purposes, objects or operations above indicated, or owning or holding any property of any kind herein mentioned, or of any corporation owning or holding the stocks or the obligations of any such corporation.

To hold for investment, or otherwise, to use, sell or dispose of, any stock, bonds or other obligations of any such other corporation; to aid in any manner any corporation whose stock, bonds or other obligations are held or in any manner guaranteed by the Company, and to do any other acts or things for the preservation, protection, improvement or enhancement of the value of any such stock, bonds or other obligations, or to do any acts or things designed for any such purpose; and, while owner of any such stock, bonds or other obligations, to exercise all the rights, powers and privileges of ownership thereof, and to exercise any and all voting power thereon.

The business or purpose of the Company is from time to time to do any one or more of the acts and things herein set forth; and it may conduct its business in other States, and in the Territories, and in foreign countries, and may have one office, or more than one office, and keep the books of the Company outside of the State of New Jersey, except as otherwise may be provided by law; and may hold, purchase, mortgage and convey real and personal property, either in or out of the State of New Jersey.

Without in any particular limiting any of the objects and powers of the corporation, it is hereby expressly declared and provided that the corporation shall have power to issue bonds and other obligations in payment for property purchased or acquired by it, or for any other object in or about its business; to mortgage or pledge any stocks, bonds or other obligations, or any property which may be acquired by it, to secure any bonds or other obligations by it issued or incurred; to guarantee any dividends, or bonds, or contracts, or other obligations; to make and perform contracts of any kind and description; and in carrying on its business, or for the purpose of attaining or furthering any of its objects, to do any and all other acts and things, and to exercise any and all

other powers which a copartnership or natural person could do and exercise, and which now or hereafter may be authorized by law.[2]

Except for the outright grant of lands and the rights of civil authority, there is little difference in principle between the charter of the Hudson's Bay Company and that of the United States Steel Corporation. After enumerating nearly every conceivable activity in which a steel business could engage, the final clause authorized the Corporation "to do any and all other acts and things, and to exercise any and all other powers which a copartnership or natural person could do and exercise, and which now or hereafter may be authorized by law."

There is little or no evidence to indicate a tendency toward greater restrictions or limitations in the charters of corporations granted by states under the present statutes governing such acts. On the contrary, there has been a competitive struggle among the various states to attract the business of charter-granting to their various jurisdictions. Such liberality, however, has been counteracted by an enormous increase in federal regulatory laws directly affecting all business corporations engaged in interstate commerce.

Restrictions upon Released Authority

While a charter granted by an individual state may give broad powers to a corporation, the freedom of its actual management has not gone unchallenged by the public. Restrictions and limitations upon corporate business—by statute and consequent executive agencies—have taken many new forms in recent years. Some of these, which may be mentioned, are the Securities and Exchange Commission, the increased powers of the Federal Trade Commission, the National Labor Relations Board, the wages and hours law, taxation measures of various kinds and effect, and many others. All of these agencies and laws are, in essence, a manifestation of the fact that the public, through its legislative representation, is becoming niggardly in the scope of authority it is willing to release to management for the operation of American business institutions.

The release of authority plays an important role in determining the character and scope of the social control of business. The doctrine of nationalization, or totalitarianism, stands at one extreme and the doctrine of complete laissez faire at the other. The American, or capitalistic, system occupies the middle ground where the source of authority is effectively guarded in the fundamental law of the land, and where, at the same time, the flow of authority is released in such measure as the people decide that business should be controlled. The right of private ownership prevails; bu

[2] Article III, Amended Certificate of Incorporation of the United States Steel Corporation.

how that right may be exercised is determined by governmental regulation, the development of such regulation being of ever increasing concern to business owners and executives.

The Nature of Authority

Having reviewed the source of authority, we come to a consideration of its nature. Managerial functions and rank depend upon authority received from higher sources, and hence conform to the concept that authority is rightful power in virtue of office or trust. That is to say, executive authority in a business organization is the right to perform certain organic functions of management. When these organic functions are reduced to their essential qualities, the right of executive authority divides itself into six categories or elements. They are the rights to plan, decide, organize, command, enforce, and coordinate.

With each such right there are derived certain concomitant powers. These powers are the manifestations of authority in action and result from delegation. Delegation of authority, as stated previously, means to invest one person with the power to act for another. Thus the source of authority is implied, as well as the manner of releasing it. The corollary is obvious, that in business management as in government, explained above, the control of performance rests largely on the flow or release of authority to act on the part of a superior officer to another officer subordinate in rank.

Theoretically and ultimately, all rights and powers of management rest with ownership. But ownership, for reasons already fully explained, must necessarily delegate its authority to its representative officers. It is in so doing that the divisions illustrated in Figure 5 take place. It would be impossible to successfully attempt to allocate each of the rights shown in this figure to specific executives either by rank or function to the exclusion of others. Rather, these rights and powers cut across the entire organization structure, varying in their incidence at certain points and levels.

Authority: Subtitles	Concomitant Powers
Right to plan:	Power to investigate, to formulate policies, and to interpret objectives
Right to decide:	Power to make decisions, regulations, and adjustments
Right to organize:	Power to select, train, assign, transfer, and promote the personnel
Right to command:	Power to develop strategy, plan tactics, and issue commands
Right to enforce:	Power to require and to secure compliance
Right to coordinate:	Power to determine the general organization architecture and to secure concurrence in action and purpose

Fig. 5.—Rights of executive authority with their concomitant powers.

The Right to Plan

For example, the right to plan carries with it the power to investigate, which includes the use of compulsory measures if necessary. It also includes the power to formulate policies and to interpret basic objectives. We have already observed that to the extent which any executive is called upon to set goals and plan procedures to attain them he is engaged in policy-forming. Some executives have more to do in this regard than others; likewise, certain types of policies are more vital and far-reaching than others. The authority to formulate basic policies, for instance, is reserved by the board of directors and not released to lower levels in the management pyramid.

The Right to Decide

The right to decide involves the power to answer the questions raised by the famous "good marshals"—why, what, when, where, and how. Decisions must be made by all executives, but they differ in kind and degree according to the assignments of executive tasks. It is at this point, however, that the problem of equating authority and responsibility arises. Decision-making is often a process of adjustment and regulation to meet conditions and circumstances as they arise. To be charged with the responsibility for results without having had any power to control the factors which produce them is generally intolerable and an evidence of bad management. Yet it must be recognized that room must be left for the appeal of exceptions.

The Right to Organize

Next is the right to organize. Its concomitant is the power to select, train, assign, transfer, and promote the executives and the employees. The organization process is essentially the task of specializing the work of management in order to secure efficient and harmonious performance. This process results in a structure or framework of human beings held together by the cement of coordinated relationships. These relationships must be both purposeful and dynamic because by them the entire group is motivated toward common ends in conformity with the major policies and the basic objectives of the enterprise.

It may be defensible to assert that the real crux of management inheres in the right and power of organization because within the sphere of this activity there arise the problems of direction, supervision, discipline, and morale. The act of organizing deals closely and intimately with the individuals who are the breath and life of management itself. To select them properly, train and fit them to their jobs, promote them as new needs for

their services appear or as rewards of merit, and to sustain their morale and loyalty are responsibilities which cannot be separated from the assumption of the power to organize. By its nature, this function permeates all levels of management, and all executive heads must deal with it in some proportion.

The Right to Command

Closely related to the right of organization is the right to command. To command is to manage persons by means of orders. This implies the right of authoritative direction in the development of strategy and tactics. Such directives obviously depend, in part at least, upon prior organization. Unless one has had some part in the selection and formation of the group under his jurisdiction, the power to control such subordinates may be difficult.

The Right to Enforce

Orders are ineffectual without *the right and power to enforce* them. There must be compliance with commands, else orderly performance will fail. This does not mean that the power to secure compliance and the right to issue the orders in response to which compliance is expected must come within the authority of the same executive. Sometimes they do, but frequently they do not. Command in the army has heretofore been mentioned. In military management it is the rule, rather than the exception, for orders to flow down from superior officers, who devise and issue them, to other officers lower in rank, whose function it is to see that such commands are carried out. A captain, for example, may have all the necessary authority for enforcement without any authority in the formulation of the orders he seeks to execute. He may be granted interpretative powers, to be sure—but always within the limits and in conformity with the main purposes of the orders as they come down to him. Analogous situations also arise in business management. Hence the power to enforce is not always equated with the power to command.

The Right to Coordinate

The positions of the chief and other executives are strengthened by the delegation of authority to subordinates. The activity which remains when the delegation of rights and their concomitant powers has reached its farthest practical point is "coordination." Since coordinative considerations pervade the whole organization, this right to coordinate must necessarily be delegated in some measure to all executives. But the power to determine the general organization architecture and to assure concurrence and harmony in performance and purpose is usually the reserved—if not the imposed—right of the top executive, who is unwilling or unable to

release it. The authority to plan, make decisions, organize, and prepare orders and execute them, are all rights and powers amenable to delegation. Final coordination is more difficult to delegate because, for the enterprise as a whole, it is a matter of focus rather than dispersion. Each animal in a four-horse team, if properly broken to harness, will coordinate his strength and movements with his teammates; but it is upon the driver who holds the lines that final coordination, that is, pulling together, depends.

THE PRINCIPLE OF RESPONSIBILITY

In civilized society it is recognized that every right carries with it an associated obligation or duty. What is true in the larger sphere of human relationships is equally true in the more limited realm of business management. We have seen that the elements of authority are rights and powers. It follows, then, that the delegation of authority to managerial executives imposes obligations as well. Such obligations are called "responsibilities." Since responsibility is coextensive with authority, it, too, may be recognized as a principle.

Responsibility Defined

"Responsibility" may be defined as "the obligation and the duty of compliance and obedience." Embodied in this definition there are logically two main considerations: (1) the demands to which compliance is required, and (2) the persons to whom obedience is due. These considerations, in turn, are the bases of two of the most important, and often the most troublesome, problems of the leader-follower or superior-subordinate relationship in business organization. Briefly and concisely, but subjects of further elaboration below, the problems may be stated as follows:

1. *With Reference to Compliance.*—Every executive in an organization, regardless of rank, must clearly understand the nature and scope of the functions and duties which he assumes by virtue of his position.

2. *With Reference to Obedience.*—Every executive in an organization, regardless of rank, must clearly understand to whom he is responsible. That is, by virtue of his position and the obligations which it involves, an executive must know from whom he is expected to take authoritative commands, orders, and instructions.

Responsibility for Performance

When we examine the first of these problems, we see at once that responsibility, viewed in the light of the nature and scope of the functions and duties of an executive, includes both performance and personnel. "Performance" relates itself to tasks or units of work to be done. The smallest unit of performance is any given operation which can be per-

formed directly by an individual person. Such a task is easily defined and understood; hence the functional responsibility incidental to it is simplified. Examples of such individualized work are common in modern, highly specialized industry. A mechanic stationed on the assembly line in an automobile plant may have the responsibility for only one task, such as that of fitting and attaching a part securely into its proper place in the motor car as it moves along to completion. He is concerned with nothing else; his function is clear-cut; his responsibility specific.

The task of a foreman, however, who must supervise several such individualized operations, increases in complexity. His job is to oversee the performance of several workmen, no two of which may be precisely the same. Yet he must take the responsibility for their operations. When we consider the level of direction, which is the function of a shop superintendent, a "grouping of groups" is involved which further complicates the situation. Shop operations are combined into a department under the supervision of a manager who is responsible for all the mechanical productive operations of the business. At each successive stage upward in scalar position, definitive separations of responsibility with respect to performance become more difficult without lessening in importance. But it is the process of specialization, with its concomitant distribution of responsibility, which forms the true basis of efficient organization. Responsibility is thus both divided and combined: divided into its elements at the points of actual performance, and combined at each successive stage of supervision and direction. No matter what the scalar stage may be, responsibility must be so clearly understood and recognized as to leave no doubt as to where the obligation and duty of efficient performance lies. In fact, responsibility is inherent, and the problem is not to assume it but rather to understand it.

Responsibility for Persons

What is true of responsibility for performance is equally true with respect to responsibility for persons. There should be no question on the part of any executive as to who are his subordinates, nor should subordinates be left in doubt as to the identity of their superiors. These requisites of responsibility may seem to be self-evident, and yet too often they are not understood; or they may even be deliberately disregarded, to the detriment of the organization.

The division and distribution of responsibility to members of the management group is undertaken to relieve the tension upon the span of control to which an executive may be subjected. There is probably no precise formula for determining the maximum number of subordinates who should report directly to a given superior officer. Whatever such a

number may be, the division effected should provide recognized channels for the flow of authority in which responsibility is inherent. The whole realization of discipline and morale in organized effort rests upon this principle.

Discipline and Morale

"Discipline" can be defined as "obedience and order through conscious compliance with rules and regulations, orders and instructions." By experience and tradition such compliance often becomes automatic and is manifested in the true spirit of cooperation. Individuals who are ignorant of their relationships with respect to managerial status cannot work together effectively. If one does not know where his responsibility begins or where it ends, conditions are ripe for internal dissensions, jealousies, and enmities. Thus morale is also dependent upon responsibility which is clearly defined and properly understood.

"Morale" denotes confidence in and loyalty to superiors. Obviously, a subordinate cannot be loyal to a superior in office when he feels uncertain about the latter's authority. Conversely an executive finds himself in a difficult, if not an inimical position, when he seeks to stimulate confidence and develop loyalty in persons when he is not sure they are responsible to him. Confidence is based on trust and reliance, and also upon assurance of "square dealing" and assistance in routine operations as well as in emergencies. Divided allegiance or hesitation caused by mistaken or uncertain appeals creates an atmosphere in which confidence does not thrive. Likewise, loyalty has two sides: it will not be realized, nor can it be expected, unless it is deserved. Loyalty, by its very nature, is not an obligation which can be imposed by the exercise of authority, nor can one consistently be loyal unless the object of his loyalty merits it.

Since the management process consists of executive directives and controls, it is dependent for its success upon the relationships which spring from personal responsibility. The limitations of the human span of control impose restrictions which make specialization in management imperative. Each resultant cleavage, whether in the horizontal or the vertical plane, carries with it a division of responsibility; but the benefits of such division, whether specialization takes place in executive or operative tasks, may be nullified by the failure to clarify responsibilities or to adhere to them when once they are understood. In other words, there is no room in good organization for misunderstanding on the part of superiors as to whom orders may properly be given or from whom compliance may be expected. Neither should subordinates be left in doubt regarding those from whom instructions may be taken or to whom they should report. The scalar structure of organization implies a relationship of mutual re-

liance and loyalty between those who command and those who obey. When such mutuality is lacking, or if it is destroyed, both discipline and morale disintegrate and disappear.

THE PRINCIPLE OF ACCOUNTABILITY

In the science of physics the Third Law of Newton states that "to every action there is an equal and opposite reaction." In the science of organization and management this principle, by analogy, gives added meaning to the leader-follower relationship. As we have seen, managerial activity results only from the directive force which is inherent in authority. From its source at the top of the organization, authority flows downward and outward throughout the entire management structure. Along the channels through which it moves, there are stationed executives of various ranks and functions. It is to them that authority is delegated.

By assuming the rights and powers which are vested in him by virtue of his status, each executive receives, in fact, an impact of responsibility which he can transmit neither up to superiors nor down to subordinates. If, by analogy, then, Newton's law is applicable, to this impact there should be an equal and opposite reaction.

It is fair to say that such a reaction actually takes place, and that it manifests itself in "accountability." Thus, as authority flows down from a superior to a subordinate on the scalar levels of management, accountability flows up responsively in proportion to the responsibility created by such delegated authority. In simpler terms, he who has few responsibilities has little for which he is held accountable, while "to whom much is given, of him shall much be required."

Accountability Defined

By "accountability" is meant "liability for a reckoning of the responsibilities which are received by delegation of authority and accepted by status or office." Such a reckoning may involve a statement of the reasons, causes, or grounds which constitute an explanation or justification of an act, event, or circumstance. In short, to be accountable is to be answerable for one's conduct in respect to obligations fulfilled or unfulfilled.

When this abstract meaning of the term is carried over to designate a principle of organization and management, accountability appears in two forms: not only is an executive answerable *for something*, but he is also answerable *to somebody*. He is answerable for his own acts as an individual who is occupying an executive position, and he is also answerable for the entire unit of the organization under his supervision. Such accountability emphasizes the importance of the managerial function of leadership from the base to the apex of the executive pyramid.

A foreman, for example, who realizes that he is accountable for the efficient and satisfactory fulfillment of a task by the group of employees who are subject to his supervision is stimulated to alertness and care in his job of overseeing. A department head, as, for instance, the division superintendent in a railway system, when conscious that he is answerable for safety and speed in the movement of the streamlined trains flashing over the miles of track under his jurisdiction, makes maintenance of way and other division problems his serious personal concern. When a top executive conceives that out of his responsibility there issues accountability for the profitableness and stability of the entire business, it is not illogical that his personal concern in the welfare of the enterprise extends to the limits of his strength and energy. Finally, when it is realized that ownership—directly or through its representative board of directors—is also accountable for its stewardship of the right to maintain and operate a business enterprise, and to enjoy whatever profits it may be able to make, then private and public interests join.

Accountability Issues from Responsibility

Accountability for performance is, therefore, answerability for carrying out, properly and efficiently, a given task or assignment. Its corollary is accountability to someone superior in executive position from whom authority to perform a task has been received. Thus a foreman reports to a superintendent, a superintendent to a department head, a department head to a major executive, and the latter to his chief at the top, who finally renders an account to ownership directly or to a representative board of directors. The process of accountability does not end at this point. To complete the chain, it must be recognized that ownership itself is answerable to a superior authority outside of its own organization, namely, society. Evidence of such authority is governmental regulation of business. The resulting accountability finds expression in a multitude of inspections, reports, and taxes which are imposed upon business and to which business concerns of every size and character must respond.

The Circuit of Authority and Accountability

It is important to observe, therefore, that as authority is released by delegation and, through the channels established by organization, reaches all parts of the management structure, so also there is a complementary system through which accountability flows back to the source of authority. In a sense, this phase of the management process is analogous to the circulatory system of the blood in a living being (see Fig. 6). From the heart, the center of the system, the bright red blood, charged with energy, is pumped through the arteries to every organ and tissue of the body, distributed widely and in varying quantities as extremities are

reached. But a backflow has also been provided through the veins. At the point where the outflow has spent itself in the capillaries of brain or finger tips, the backflow begins in other channels, which increase in size but reduce in number until the heart is reached again.

This physiological analogy may be carried even farther in other respects. In the first place, organs with special functions appear along the course of the blood stream. The heart, so to speak, does not presume to perform the work assigned to any of these organs, but leaves these responsibilities to them. And yet, should the heart cease to send energy through the channels of the circulatory system, performance would cease in every organ. To some extent the reverse is also true; that is, should an organ cease to function, the heart itself may not be able to go on. This happens when such "vital parts" as the brain and lungs are affected. In a business organization also, there are vital parts whose functions are essential to the very existence of the business.

In the second place, the phenomenon of "circulation" is the secret of the vitality of the blood stream. A break in the system causes bleeding or loss of energy, and, if not checked and stopped, death ensues. Moreover, if the system is clogged and the return flow is obstructed, again serious consequences result. So it is in the circulatory system of business organization. Authority flows outward from top management to departmental heads and on to employees, invigorating and vitalizing each part and member. But outflow is not sufficient. The small channels or lines of authority which lead to actual performance of functional activities, in turn, gather up a return flow of accountability which eventually streams back to the heart of the organization at the top. If this circuit of authority outward and the return flow of accountability inward is broken or obstructed, serious consequences result in the proper functioning of a business organization.

The point of emphasis in this comparison is that an executive who releases authority by delegation must expect and require responsiveness from his subordinates through accountability. Conversely, a subordinate, in accepting a position and an assignment of duty, thereby recognizes the authority to which he is subject and accepts the responsibility which his work entails. At the same time, he should also understand and discharge the obligation of accountability upon which, as the closing link in the circuit of the leader-follower relationship, effectiveness and efficiency in management vitally depend.

AUTHORITY AND LEADERSHIP

One of the main responsibilities of leadership is the establishment of a firm foundation upon which the directive forces of management can be

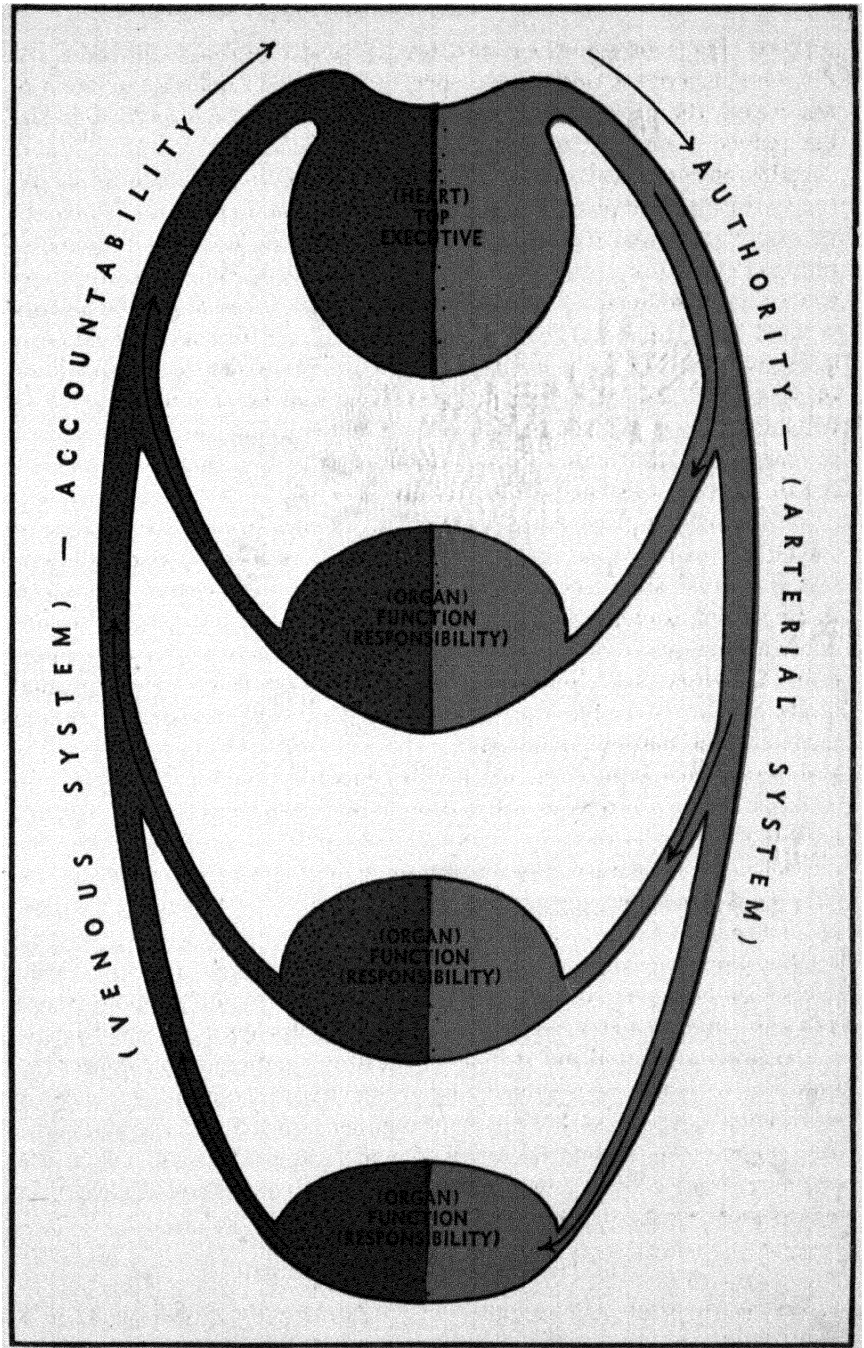


FIG. 6.—Diagrammatic representation of the analogy of the flow of authority and accountability to the circulatory system of the blood.

based. In so doing, it is important that those who respond to authority understand both immediate and ultimate objectives. This is true because for every activity performed by the leader there is a supplementary activity performed by those whom he leads. In other words, the work of the managerial executive in formulating plans and procedures is, obviously, not an end in itself. Such work would have no significance except that it can be translated into useful performance by subordinates. Unless the work of those who are in authority and of those who submit to authority can be harmoniously integrated, the process of management will inevitably fail.

It is at this point that the vital relationship between authority and leadership appears. The successful exercise of the rights and powers of authority involves something more than the creation of acquiescence on the part of minor executives and workers. It demands some participation in the tasks of management by all members of an organization from top to bottom. Human beings are so constituted that they are jealous of their rights, however limited in scope they may be. And since rights imply powers, it follows that authority itself is an attribute which every individual esteems. Therefore, leadership, in releasing authority which flows down through the channels of organized managerial relationships, must recognize that, in so doing, it is necessarily sharing its own prerogatives by the distribution and allocation of rights and powers to the members of the group. When authority is thus transmitted and directed by leadership, it is not only an energizing force, but it is also unifying in its purpose and effect.

Motivation and Coordination of Activities

The example of an orchestra conductor illustrates clearly how leadership both activates and coordinates group action and directs it toward an objective consciously envisioned by leader and followers alike. Both players and audience recognize him as leader. In him is vested the authority to select and perform certain musical productions. Readiness to release his authority is symbolized by the warning tap of his baton by means of which the attention of every player is concentrated upon the task before him. Then, with a decisive gesture or beat, the conductor sets his orchestra in motion; but he is still in control only if the individual members of the group acquiesce to his leadership and willingly strive to interpret the written score as the music is revealed to the mind of the conductor. Thus an orchestra of a hundred players harmonizes, and its leader seems to play on one huge instrument rather than to direct several score of individual players.

Perhaps an orchestra could perform without a conductor, but not for

very long. Without his authority, it would revert to its component parts, both as to program and to the manner in which each musical composition should be played. The great conductor's role is not one of dominance. His players do not respond to his directions out of fear, nor is he recognized by his audience for his ability to coerce or cajole. Rather, he emerges as a great orchestral leader as a result of his own understanding of music, which is coupled with his ability to project that understanding and feeling into the minds of the instrumentalists, who watch the strokes of his baton and are guided by him in every tone and modulation produced.

Ideally, such leadership may also be found in the more prosaic affairs of business management. As one views the operations of a great industry, with its hundreds or thousands of individual performers—each one literally playing upon his own particular instrument—it is something more than a fancy flight of the imagination to compare it to a renowned symphony orchestra. An industry also has its *tempo*, which even a casual observer may detect. Each man, in his place, operates not for his own sake but for the sake of the enterprise as a whole. Somewhere there is a conductor or leader who coordinates, energizes, and unifies all processes to the end that a single product, such as a motor car, may be the outcome. Furthermore, the car, like the orchestral rendition, must meet with the approval of a large portion of the public, the audience, or else in either instance, the consequences resulting from the leader's failure may disrupt or destroy the organization under his direction.

Leadership depends upon authority for its being and its effectiveness. But that authority should find expression in the ability of its possessor to stimulate followership through a clear understanding of basic policies and objectives, a common purpose to achieve them, and a mutual confidence in personalities and anticipated results.

How Leaders Are Chosen

There can be no leadership without authority, and authority is purely an abstraction without leadership. Moreover, to be significant factors in management, both qualities must be focused in one person. The manner in which a leader of a human group is chosen varies according to custom, practice, and type of organization. For example, the hereditary or inheritance method is in common use. Most small business enterprises are transmitted, in this manner, from one owner-manager to the next. Then there is the rotation method of promotion from within the next-in-rank whenever a vacancy occurs. This method is frequently used in military organizations, in government, and in many business enterprises. The head of a partnership is customarily the senior, or oldest, partner.

The committee-selection method is often used by the modern business corporation, by associations, and by many governmental agencies. Where this practice is followed, the board of directors elects the new top executive from a group of eligible candidates, chosen from its own membership, from the membership of the entire organization, or even from the outside. The general election method is rarely used by business, since the stockholders commonly elect the members of the board of directors, who, in turn, select their chief executive. Proprietary businesses owned and operated by the government, however, are often headed by executives elected by the citizen-owners at the polls. (See Chap. XVI.)

A method of indicating who may not become the head of a business concern is developing. This negative method is essentially a phase of governmental regulation of management. By statutory enactment, the government seeks to prevent certain practices, such as interlocking directorates, by prohibiting the directors of one corporation, under certain conditions, from becoming directors of another. This prohibition conceivably limits the eligibility of certain persons for office in an organization and may operate negatively on the selection of the top executive.

The modern business corporation is often accused of being undemocratic in its organization, chiefly because the general election method is not used in the selection of the top executive. In this sense, governmental agencies are also undemocratic because most public officials are appointed or selected, not directly elected by the voters. Likewise, the management of modern business is also accused of excessive and improper generosity to its top executives and associated major executives in the form of pay, bonuses, and perquisites. Some of the reasons for such recognitions are, in the first place, that it is impossible for an individual to serve as the conspicuous leader of a business enterprise without incurring certain unusual expenses inherent in the position. In the second place, the whole structure of pay for services rendered in any particular business—as well as in society in general—grades up from manual labor to the highest compensation for conspicuous services of the skilled leadership type. Doubtless, higher rates of pay for increased assumption of authority tend to furnish incentives to lower-paid employees and executives to prepare for and seek promotion. It is instinctive to expect added remuneration for added responsibilities. Even in socialized Russia, the principle of graded pay, rising up to high earnings for the position of conspicuous leadership, has apparently been restored after experimenting with uniform pay.

One Principal Leader

In any organization, including a business enterprise, there can be only one principal leader. Such a leader, however, may have closely associated

with him a small group of assistants or major executives. Commonly, the managers of the chief functional and staff divisions of a business constitute this group, although there is no fixed rule which determines the practice. In a partnership the partners themselves are collectively both the owners and the executives of the business. Meeting as a group, they can perform those acts of ownership that are the responsibility of the board of directors of a corporation. As executives, the partners are usually organized under the senior partner, who serves as leader or top executive of the business.

In a corporation the management activities of ownership are performed by, or directly for, the board of directors. But the details of management are performed by another group of officers, headed by the top executive or leader. This top executive is comparable to the senior partner in a partnership, and his associated major executives may be thought of as the junior partners.

From a legal standpoint, the top executive derives his position, and therefore his authority, from the nature of corporate organization itself. The stockholders elect their representatives to serve as the board of directors. The board of directors, in turn, select the chief executive to head the management of the business. This executive is then charged with the appointment of the major and minor executives to assist him, delegating to each of them a part of his own management authority.

When the duties performed by the board of directors are weak or unimportant, the top executive of a business enterprise tends to assume the leadership role of a commanding general of an army. On the other hand, when the board of directors pushes itself far into the field of detailed management, the top executive tends toward the leadership role of an appointed official in charge of a publicly owned business. That is to say, he is constantly conscious of his subserviency, often doubtful as to his prerogatives, and therefore he is hesitant and reluctant to make decisions on the basis of his own judgment. The natural and customary relationship is that suggested by the ownership and management activities of partners. Under such conditions, the board of directors neither relinquishes the function of representing ownership and determining major policies nor invades the field of operation management. The major executives neither take orders in military fashion from their top executive nor set themselves up in separate functional compartments independent of each other and of their titular superior. There is, instead, a middle ground where executives of superior and subordinate authority meet on the solid foundation of understanding, each individual confident of his own authority and respected in its exercise by his associates. At the same time, the consciousness of a common purpose prevails under the guidance of a single leader through whose efforts coordinated performance is achieved.

The Flow of Authority

The expression "flow of authority" has been used frequently in this chapter. It is only natural to inquire precisely how this movement takes place. It is a common practice in modern business management to reduce to writing the tangible evidence of the authority that is delegated and the instructions that grow out of such authority. From the standpoint of permanence, prepared statements of this kind may represent basic policies, standing orders, instruction manuals, routine operating instructions, or special instructions to meet a particular temporary situation. They may be applicable to all employees, or they may be restricted to some one group within the organization. Sometimes instructions may be issued by executives or employees who do not have full powers of decision in certain circumstances. In such instances, therefore, they are subject to revocation. In times of emergency, instructions are often issued by persons who have only temporary authority to issue orders and make decisions. Or again, they may be issued to confirm, countermand, or interpret previous instructions prepared by executives in the higher positions of authority.

Printed statements of policies, standing orders, and instructions—like printed books in a modern library—would be worth little without arrangement, classification, or indexing. The subject matter treated originates in a thousand different ways. Each item, order, or set of instructions has its own path to follow in order that the desired performance responses may be realized. The system of handling these written directions, therefore, must be dynamic rather than static. It is not enough to classify them for proper filing. To be effective, they must also be coordinated and codified.

Authority and Responsibility Equated

From the standpoint of the employee who receives an order, there is only one kind of authority, namely, the formal authority to issue the instructions which he must obey. From the standpoint of the legal organization of a business enterprise, there is only one kind of responsibility, namely, the obligation to see to it that the work is done and satisfactory results are obtained in accordance with the authority delegated to each executive. From the standpoint of ownership and the public, there is only one kind of accountability, namely, answerability for the right and power to manage a business concern. Thus the executives who occupy the top of the management pyramid, by virtue of the authority delegated to them, find the responsibilities which they must inescapably assume broadening out to complete accountability for the entire business.

It is important to observe, however, that the direct authority of top executives to issue formal orders is limited by the character of the organization on the lower levels of management. That is, authority can only flow in the channels provided for it. Therefore, while responsibility and accountability of the major executives, jointly, are over-all considerations, their authority is necessarily dispersed through the established specialized functional divisions of management.

At the lower executive levels, the situation is reversed. A supervisor, for example, is responsible and accountable for very little beyond his own acts and the work of a limited personnel directly subordinate to him. He has, however, almost complete formal authority to issue instructions to these employees. Viewed in this light, it becomes clear that authority and responsibility are equated only by means of the interlocking and coordination of executive activity and employee performance at each and all of the various levels of the management structure.

QUESTIONS

1. The words "responsibility" and "accountability" are often used as synonyms. Cite dictionary definitions of each of them that are peculiarly appropriate, in a technical sense, to the field of organization and management. On the basis of the text in this chapter, explain how these terms should be used to indicate different phases of the effect of the delegation of authority in the management of a business enterprise.

2. Enumerate and explain the problems of leadership of business executives that result from the release of authority in the following types of enterprise:
   a) A small business managed by its principal owner.
   b) A large business corporation managed by salaried executives who are directly accountable to a board of directors composed of the principal owners of the company.
   c) A large business concern managed by salaried executives who are directly accountable to a board of directors or a board of trustees composed of members appropriately chosen from among the customers of the enterprise. (Examples of such business concerns are mutual life insurance companies, mutual savings banks, and farmers' cooperative associations.)

3. Explain in your own words—and use examples of your own selection chosen from various management levels within a particular enterprise, such as a store, a bank, a college or university, or a railroad—how and why authority and responsibility may be unequal and not equated in any one executive, and yet is equated when the enterprise is viewed as a whole.

(Choose an actual or simulated example with at least three management levels for your illustration. If charts and diagrams will help to make your argument clear, use them.)

4. It has been asserted in the text and illustrated in Figure 6 that there is a flow of authority and accountability in the management of a business enterprise.
   a) Explain how this statement can be justified when nearly everything representative of the flow of authority and accountability consists of written instructions and reports.
   b) Show how there are two types of this flow or movement illustrated by (1) written evidence of authority and accountability, such as production orders and accounting records; and (2) the actual flow of authority and accountability from one person to his immediate subordinates or to his immediate superior.

5. By means of definitions and examples, distinguish between the following:
   a) "Responsibility for the performance of assigned work" and "responsibility for personal discipline and morale."
   b) "Accountability for the performance of assigned work" and "accountability for personal discipline and morale."

6. In the following described situations, show how a typical business enterprise may be affected with respect to the source and restriction of its managerial authority:
   a) By state legislation, a law is enacted which prescribes minimum factory safety standards and establishes a system of safety inspection by state employees.
   b) Subsequent to issuing a certificate of incorporation to a business concern, a state adopts new tax laws and imposes new taxes upon an enterprise.
   c) By means of appropriate legislation, a state decides to enter a particular field of business with a government proprietary enterprise, publicly owned, that is in direct competition with a previously established private business concern.

7. Following the pattern of Figure 1 in Chapter II, construct a diagram that shows the proper relationships of the following personnel of a large business organization:
   a) Stockholders.
   b) Board of directors.
   c) Executive committee of the board of directors.
   d) Bondholders.
   e) Sales manager.

f) President of the company.

g) The chief clerk who works in the customer-order division of the sales department.

h) A committee consisting of departmental executives who are not members of the board of directors.

i) The chairman of the board of directors.

j) A certified public accountant who is employed once a year to make an annual audit.

k) The legal counsel who is retained by the company to work on an annual basis.

8. State as definitely and as fully as possible the source of the authority of each of the executives and committees included in the organization described in Question 7.

9. With the analysis of the rights of executive authority and their concomitant powers as shown in Figure 5 as a basis, make an outline which divides and allocates such rights and powers among the subdivisions of the organization described in Question 7. Point out instances at different management levels where there is duplication in the exercise of identical rights and powers, and state the reasons for such duplication.

10. Following is a list of typical items that might be found in the annual report to the stockholders of any large business enterprise. From the standpoint of their general or limited applicability to all business enterprises, and their value as fundamental management ideas, discuss their validity and importance:

a) "The production of a quality product for our customers is our primary reason for being in business."

b) "Size, in and of itself, is not an objective with us."

c) "Our management is especially watchful of the items of expense that are within our control."

d) "Our balance sheet and other records of account have been examined and verified by the X firm of certified public accountants whose report is attached."

e) "We believe that our management is competent to handle the affairs of our company, and that it is adequately organized to protect the investments of our stockholders and to maintain satisfactory future earnings."

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Chapter IV

THE LEVELS THEORY OF ORGANIZATION

WHY MANAGEMENT LEVELS EXIST

RANK or title normally identifies status in managerial leadership. Indeed, stratification is the characteristic feature of the architecture of a typical business organization. The levels theory of organization is an explanation of this universal phenomenon. It may be stated in general terms as follows: The organization structure of the management group consists of executives of varying ranks and duties arranged in a series of strata or levels, ranging from those with the highest authority at the top down to those who supervise the workers at the bottom. As a corollary to this general statement, there is the further consideration that the number of management levels tends to increase as the size of an enterprise increases.

Management levels do not come into existence for convenience or for the satisfaction of ambitious "climbers" within an organization. Management levels exist primarily because of the limitations of human capabilities. In short, these limitations may be said to comprise the "span of control" which can be comprehended by an individual executive.

THE SPAN OF CONTROL

The span of control is an underlying principle of business organization. In contemplating it, certain inexorable bounds of human nature and human ingenuity must be taken into account. Just as the physical "reach" of the extended arms of a man can span only a limited number of feet and inches, so his mental reach can span but a limited number of the problems, the situations, and the relationships that make up the activities of management.

The span of control, in a broad sense, has several elements. Its limits are determined by other "spans," such as the span of knowledge, the span of time, the span of energy, and the span of personality. In its narrower sense, the span of control refers to the maximum number of subordinates which may be placed under the jurisdiction of one executive who is immediately superior to them. It has been pointed out that the act of management consists essentially of directives and controls. From the standpoint of the first process, there is probably no limit to the number of persons to which an executive can issue an order. During the last war,

for example, a single general order from a field commander could be, and in some cases was, transmitted to millions of men at once so that a major offensive action might be timed with unity and precision. To see that this general order was properly executed from one end of the army to the other was a different matter. At this point, namely, that of control, the act of management or command was restricted by many limitations, both human and material in character.

By way of a simple example, let us assume an army of one hundred and one men. Having in mind the principle of leadership, the minimum organization possible would be as shown in Figure 7. Here is presented, in effect, the ancient Roman *century* with its commander, the *centurion.* This organization would be effective from the standpoint of issuing orders, but common sense tells us that the captain in the midst of a modern battle could not control one hundred soldiers, especially if they were

Management level:	One captain
Performance level:	One hundred men

FIG. 7.—Management and performance levels in an ancient Roman army unit called "The Century."

deployed along a line where he could not even see all of them. To realize effective command under present-day circumstances, the captain may need as many as ten assistants, such as lieutenants and sergeants, and would also make use of radio and other communication techniques.

Modern Army Organization

Assume, now, that the number of troops engaged in a single theater of operations in modern warfare is increased to millions of men. It is clear that the number of assistants which one commander in chief would require, if our simple type of organization prevailed, would become so great that effective direction and control would be impossible. Therefore, many levels of command, or management, are necessary. This multiplication of management levels is basic to modern army organization. Figure 8 is a striking illustration of its application to the Allied Forces in Europe during World War II. It shows the composition of the top levels of command which existed on V-E Day, May 7, 1945.

In this illustration, General of the Army, Dwight D. Eisenhower, is shown as Supreme Commander of all the Allied Expeditionary Forces. It was the rank assigned to him in the directive issued by the Combined Chiefs of Staff on February 12, 1944, which also specified his task, as follows:

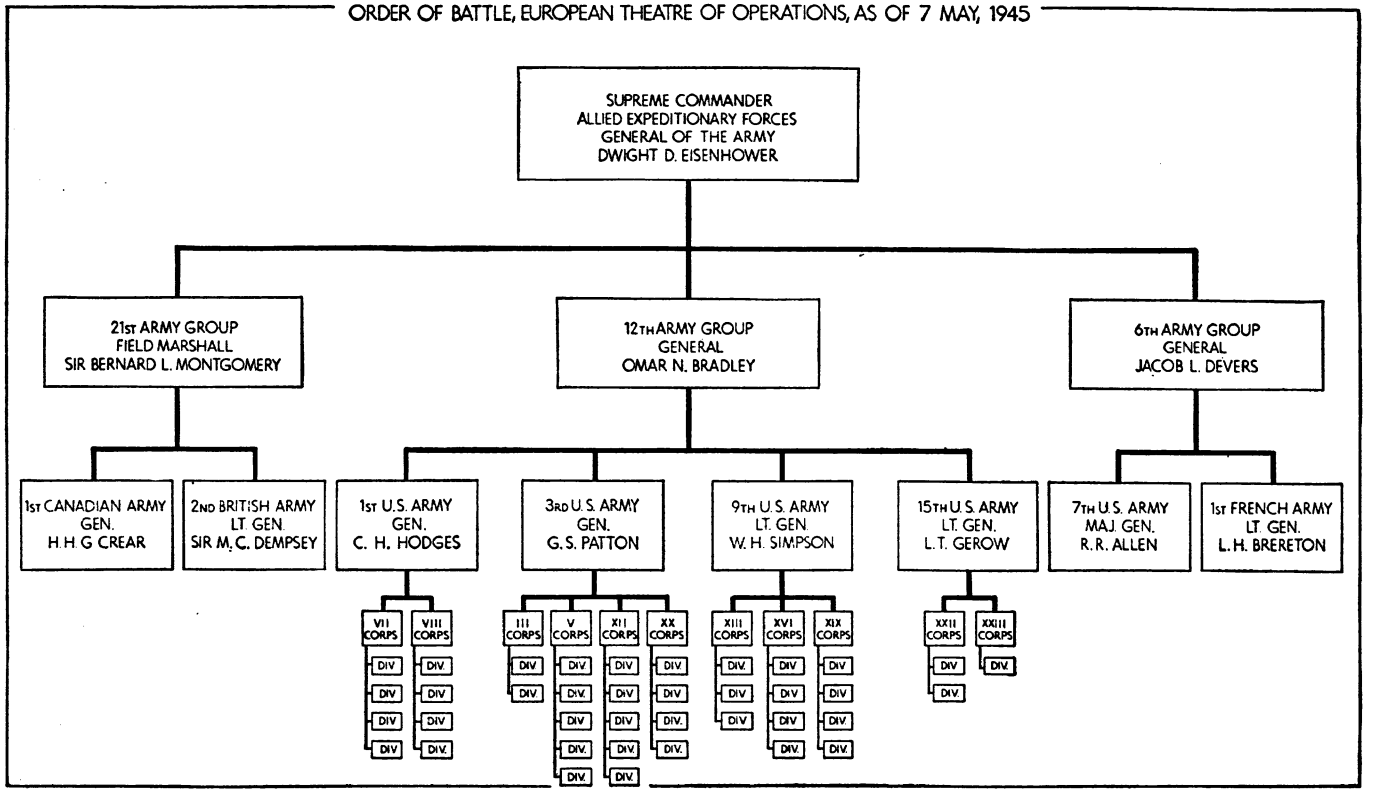


FIG. 8.—Organization of the Allied Expeditionary Force, European Theater of Operations, 1945. From *United States News*, October 10, 1945, pp. 52–53.

You are hereby designated as Supreme Allied Commander of the forces placed under your orders for operations for liberation of Europe from the Germans. Your title will be Supreme Commander Allied Expeditionary Forces.

You will enter the continent of Europe and, in conjunction with the other United Nations, undertake operations aimed at the heart of Germany and the destruction of her armed forces.[1]

In this directive, notice that all the Allied Forces were placed under General Eisenhower's *orders*. His was the authority, as well as the responsibility, to "liberate Europe from the Germans." In this task his *orders* would permeate to every fighting unit engaged in the gigantic operation, but his immediate subordinates consisted of only three officers. They were the men who constituted the next level or order of command, namely, the commanders of three army groups: Field Marshall Sir Bernard L. Montgomery of the Twenty-First Army Group; General Omar N. Bradley of the Twelfth Army Group; and General Jacob L. Devers of the Sixth Army Group.

The next level of command below that of the army groups was composed of units designated as "armies." Again, to make effective the flow of orders from the Supreme Commander, the number of officers accountable to each army group commander were few in number. There were only two officers—General H. H. G. Crear of the First Canadian Army and Lieutenant General Sir M. C. Dempsey of the Second British Army—who were accountable to Field Marshall Montgomery. General Bradley had four officers under his immediate command: General C. H. Hodges of the First U.S. Army, General George S. Patton, Jr. of the Third U.S. Army, Lieutenant General W. H. Simpson of the Ninth U.S. Army, and Lieutenant General L. T. Gerow of the Fifteenth U.S. Army. General Devers also had only two officers directly under him: Major General R. R. Allen of the Seventh U.S. Army and Lieutenant General L. H. Brereton of the First French Army.

Armies were broken down into corps, which constituted the next level of command. Figure 8 shows an example of this arrangement, the organization of the Twelfth Army Group. General Hodges had two immediate subordinates, the commanders of the Seventh and Eighth Corps; General Patton had four, the commanders of the Third, Fifth, Twelfth, and Twentieth Corps; General Simpson had three, the commanders of the Thirteenth, Sixteenth, and Nineteenth Corps; and General Gerow had two, the commanders of the Twenty-second and Twenty-third Corps.

In this major organization of the Allied Forces the next level below the corps was made up of divisions. Corps commanders had from one to

[1] *Report by the Supreme Commander to the Combined Chiefs of Staff of the Operations in Europe of the Allied Expeditionary Force, 6 June, 1944, to 8 May, 1945*, p. vi.

five officers reporting directly to them, thereby carrying out the principle of effective direction and control by a limited number of immediate subordinates.

It would be possible to analyze army organization even further. The size of a division varies, depending upon the character of its arms and its purpose. A typical infantry division may have in it up to 15,000 officers and men, who are usually under the command of a major general. But army organization provides for the separation of a division into brigades, a brigade into regiments, a regiment into battalions, and a battalion into companies, a company being the smallest administrative army unit. A company, however, is further divided into platoons, a platoon into sections, and a section into squads, at which point the individual unit of the army, the private soldier, is reached. Thus, if the chain of command were illustrated graphically from the Supreme Commander to the fighting foot soldier as it existed in the Allied Expeditionary Forces, that command would be found to flow through twelve levels, from a single chief, the commanding general at the top, to the squad leader, a sergeant, at the bottom.

If this analysis were carried out completely, army organization would also show that the span of control in terms of number of immediate subordinates is broader at the bottom of the pyramid of command than at the top. A squad leader may have had a dozen or fifteen men under his jurisdiction, whereas the supreme commander had only three. But the problems of the sergeant in charge of a squad of infantrymen are quite different from those of high-ranking officers. The problem of control of major military units deals primarily with general orders based on policy, strategy, and campaign considerations which are extremely complex in character. At the bottom the squad leader works intimately with his men. His responsibility consists in maintaining readiness to obey orders and immediate compliance with those orders when they are issued. His effectiveness is largely a matter of example.

The foregoing illustration has been used to emphasize the importance and significance of the levels theory of organization. The larger the army unit, the greater the number of management levels. This principle is equally applicable to business organization or any other association of persons in which cooperation under authoritative leadership is required.

Line Organization

The relationships of superiors and subordinates in the command of an army typify line organization. By "line organization" is meant that "authority and responsibility for management flow in an unbroken line from the highest executive down through the successive levels to the private soldier." This plan is not exclusively peculiar to military organiza-

tion. Its counterpart is also found in business. Business, however, is less likely to achieve perfect line organization because its managerial problems generally fall into subdivisions which are principally functional in character, such as production, selling, and accounting. In pure line organization, as found in the command of an army unit, functional considerations are relatively unimportant in the determination of levels of authority. It is the span of control based on the idea of manageable units which is the determining factor.

Because the main purpose of an army when it goes into action is to overcome the enemy, it is difficult to draw an exact analogy between its organization and that of business. Furthermore, business organization differs in details and technical designation from enterprise to enterprise. In other words, no two business units are exactly alike, nor do their executives always have the same titles. In the army, generals, colonels, and captains are traditional, and their respective duties vary only slightly wherever they are found. The significant comparisons which can be made refer to the patterns of management levels. Thus, top management in business compares with the officers in high command in the army. Both groups deal mainly with general policy and grand strategy. In order that these fundamental instructions may be realized, performance in business and command in the army devolve upon subordinate executives and officers with varying degrees of authority and responsibility. To attempt to make further direct comparisons, such as general manager and major general, department head and colonel, or superintendent and captain, would be far-fetched. Yet, it can be said with considerable emphasis that it is the shop foreman in industry and the squad leader, or corporal, in the army who actually command the workmen and soldiers who do the real producing and the actual fighting. Each higher officer, whether in a business or in a military organization, is essentially a coordinating executive responsible for two or more units beneath him and taking orders from someone superior in position.

Theoretical Business Organization

By recognizing this analogy as far as it is pertinent, it is possible to illustrate the levels theory of organization in terms of a business concern, as shown in Figure 9. In this hypothetical case the president of the company, from the standpoint of span of control, supervises three assistants. These officers are the functional managers commonly identified by such designations as "production," "sales," and "financial" managers. They also constitute the major executive group to whom the president may look for aid in the determination of policy and to whom he issues general orders for the operation of the business. Each of these managers supervises five department heads. The character of the responsibilities of these latter

officers may vary widely within this particular level. Some may be functional specialists, while others may be identified with territorial or commodity considerations.

In this illustration it is assumed that each department head has under his jurisdiction five foremen or supervisors. Foremen and supervisors in turn manage groups of twelve employees each; but in exercising such supervision the one in charge not only oversees and directs the work in progress, but also takes part in the activity himself. At this point in the operations of a business, as with the sergeant and his squad in the army, leadership merges with performance.

It hardly should be necessary to point out that the even division of a business organization into departments and groups of personnel as shown in Figure 9 never happens in practical business affairs. Herein business

Level	Number of Personnel	Official Designation	Immediate Subordinates
Ownership:	6	Board of directors	1 president
Leadership:	1	President	3 functional managers
Major executive:	3	(Production) manager	5 department heads
Minor executive:	15	Department head	5 foremen
Supervisory:	75	Foreman	12 employees
Performance:	900	Employees	.....

Fig. 9.—Organization of a theoretical business enterprise.

organization again differs in details from that of the army. Standing orders in the latter specify to a man the composition of the personnel of a military unit as to ranks and numbers. These particulars vary in times of war and peace, but they are in either case prescribed.

There is as yet no clearly accepted rule to indicate the maximum number of subordinates who should report directly to a particular business executive without violating the principle of the span of control. There is general agreement, however, that the higher the executive the smaller should be the number who report directly to him. It is clear that too many management levels would add greatly to the burden of overhead costs, against which responsible business authorities are always on guard. Conversely, too few management levels result in inefficient work and long delays in offices which are overcrowded with details and unfinished tasks. Procrastination, postponement, and indecision are triple evils all too prevalent in management. Like insidious molds, they germinate best in the rubbish on cluttered desks and in the dark recesses of disorderly workrooms.

One student of management sums up the subject of the number of subordinates as follows:

The ideal number of subordinates for all superior authorities appears to be four. At the lowest level of organization, where what is delegated is responsibility for the performance of specific tasks and not for the supervision of others, the number may be eight or twelve. The number of levels in any organization should be a minimum sufficient to permit of this distribution of subordinates. . . . The subdivision of activities into too few levels encounters far more dangers than their subdivision into too many. Centralization of authority should always be regarded as a necessary evil to be kept to a minimum. It is a passport to bureaucracy. . . .[2]

THE SPAN OF KNOWLEDGE

Closely associated with the span of control, and by some authorities considered to be a part of it, is the "span of knowledge." For purposes of analysis, we shall consider the span of knowledge as a separate quality which, to a considerable extent, affects or modifies the levels of management. The term itself signifies the intellectual grasp of an executive. That is, there is a limit to the amount of knowledge of pertinent subject matter about a business enterprise which can be comprehended by one individual. Obviously, the power of an executive to exercise control will be conditioned by his limitations in this respect. The ancient maxim that "knowledge is power" has particular force in executive activity.

This is a delicate subject, since few individuals are willing to recognize their own intellectual limitations. A man's ego flatters him to such an extent that he is ready to believe his mind can encompass and understand all the subject matter which may come to his attention. It must be recognized, of course, that individuals vary in their mental capacities just as they do in physical stamina. Some persons have tremendous capabilities with respect to memory and to the powers of analysis and synthesis. Everyone, however, no matter what his mental development may be, lives in his own intellectual environment, which surrounds him like the atmosphere surrounds the earth. Indeed, the following analogy may be drawn from this comparison.

Meteorologists say that the whole mass of air which envelops the earth is divided into three zones. The first of these zones is the "troposphere," which extends upward about 10 miles. It is the area of temperature changes, clouds, and weather. Its characteristics, conditions, and effects are so well known that they have been reduced to the science of climatology.

The next zone is the "stratosphere," where the air is clear—free of dust and of clouds of vapor and rain. It reaches up another 30–50 miles. The knowledge of this zone is incomplete; but it is known that, at its base, there is a tenuous belt of ozone—probably at a level of 80,000 feet, pro-

[2] L. Urwick, "Axioms of Organization," *Public Administration Magazine* (London, England), October, 1935, pp. 348–49.

tecting life on the earth from the deadly ultraviolet rays which come from the sun. About 95 per cent of the atmosphere, by weight, lies below this belt.

From 40 to 60 miles above the earth the stratosphere merges into the next zone called the "ionosphere." Our knowledge of it is fragmentary,

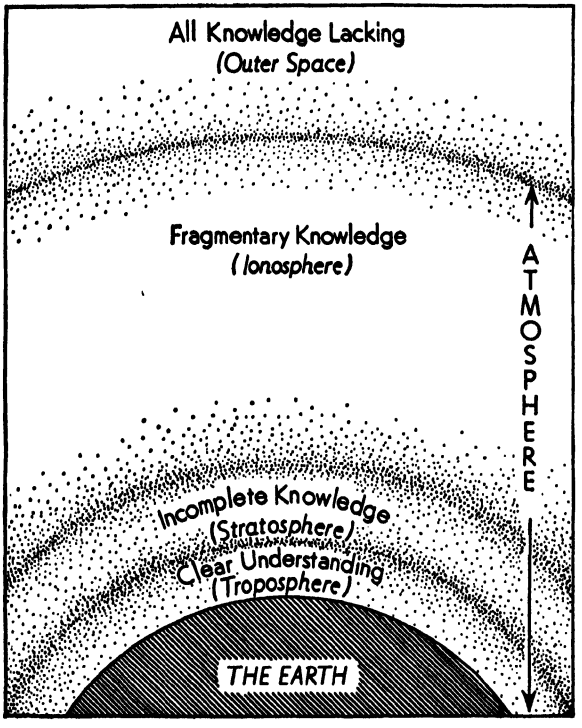


FIG. 10.—Analogy between the earth's atmosphere and an individual's span of knowledge.

but it is the atmospheric region of meteors, noctilucent ("shining-by-night") clouds, the "aurora borealis" or "northern lights," and the "radio mirror," without which long-distance radio could not operate. Short radio waves used in long-distance communication projected into the air are reflected back to the earth by the "ions" in this zone, i.e., atoms of air that have lost their electrons. The ionosphere extends to a height of 250 miles or more beyond which is outer space, about which little or nothing is known.[3]

This analogy between the atmosphere of the earth and the span of knowledge of an individual is illustrated in Figure 10. Every intelligent

[3] F. Barrows Colton, "New Frontier in the Sky," *National Geographic Magazine*, Vol. XC, No. 3 (September, 1946), pp. 379–408.

person is surrounded by an area of clear understanding. It is the first zone of his intellectual atmosphere, perhaps narrowly limited in the beginning, but increasing in breadth as he gains in mental stature by education and experience. This zone merges into another one, where the knowledge he possesses is incomplete or theoretical. As his theories are verified by experiments and facts, learning and understanding move outward, and his span of knowledge increases. Surrounding these inner spheres is a rarefied region of fragmentary knowledge. The individual observes phenomena that he can neither explain nor understand. It is the area of guesses and opinion, one into which logic and reason have not yet been able to penetrate. Beyond this zone, in outer space, lies the "vast unknown," as yet completely unexplored by him and beyond the boundaries of his knowledge.

The Mental Equipment of Management

Since the span of knowledge is, therefore, limited for all men, and since the problems of business are continually evolving and expanding, more and more emphasis is being placed on the importance of the mental equipment of management. This attitude may be called a recognition of the necessity of training for management. Such training takes various forms. In business, as elsewhere, experience is still the best teacher, providing the learners are capable of understanding its precepts. To augment experience, developments in service training programs and formal business education curricula in the professional schools of universities and colleges have expanded rapidly in the last two decades. But even the finest training and the widest and the best experience are not sufficient in themselves. There is a point beyond which they cannot go. It is the moving horizon of human fortune beyond which no navigator has ever ventured and beyond which the course of human events has not been charted.

Business problems are essentially social problems, the solution of which does not lend itself to the application of natural laws, in the sense that such laws apply to the problems of mathematics and physics. Though a person's span of knowledge may broaden with the passing years, the problems which properly come within the purview of management increase in scope and number faster than the pace of the mental growth of any one individual. In view of these considerations, the commonplace assertion that "two heads are better than one" takes on new meaning. Translated into terms of business organization, it implies that two levels of management are better than one when that point is reached, in the affairs of an enterprise, where the span of one executive's knowledge is insufficient to cope with the intellectual problems involved in the management of the enterprise. In such circumstances, a new level supplements the previous one with the seemingly paradoxical result that the combined

span of knowledge of both executives is greater than twice the wisdom of either of them.

One way to gain important knowledge for managerial purposes is by personal observation of events at the time and place in which they occur. There is much truth in the old Chinese proverb that "to see once is better than to hear one hundred times." Despite the perfection of modern means of communication, there is still no adequate substitute for a manager's personal direction and supervision. Yet, by reason of the element of physical space and the limitations which it imposes on an individual owing to distance and the obvious consideration that one cannot be in two places at once, many desirable experiences gained through witnessing performance are denied the business executive. His span of firsthand knowledge, sometimes indispensable in making decisions, is restricted. In fact, many an executive, especially at lower levels of management, owes his position primarily to the necessity for his being on hand as an eyewitness when certain processes and activities take place.

Inadequacy of Line Organization

If proficiency in management were not subject to the limitations of an individual's span of knowledge, the straight line organization of a typical military unit might be applied directly to modern business. But even in the armed forces, the span of knowledge is a modifying factor in organization. How this modification is effected is shown in Figure 11, which illustrates the organization of the General Staff in the War Department of the federal government, prior to September, 1947.

First of all, superior to the General Staff is the President of the United States, who is Commander in Chief of the Army by provision of the Constitution of the United States. His command is exercised through two persons: the Secretary of War, who is a civilian, and the Chief of Staff, a professional soldier, who is the ranking officer of the Army. The Secretary of War is charged with carrying out the broad policies of the President in military matters. The Chief of Staff is the executive through whom the President, as Commander in Chief, exercises his command with respect to strategy, tactics, and military operations.

Subordinate to the Chief of Staff is the Deputy Chief of Staff. He acts for the Chief of Staff in such matters pertaining to the supervision of the various divisions of the General Staff and the three principal commands, as are delegated to him by the Chief of Staff.

It is at the point where the General and Special Staffs are inserted into the organization that the recognition of the limitations of the span of knowledge of any one officer—no matter how capable he may be—appears. The strength of the armed forces and the successful outcome of their operations depend upon numerous factors of a great variety. These

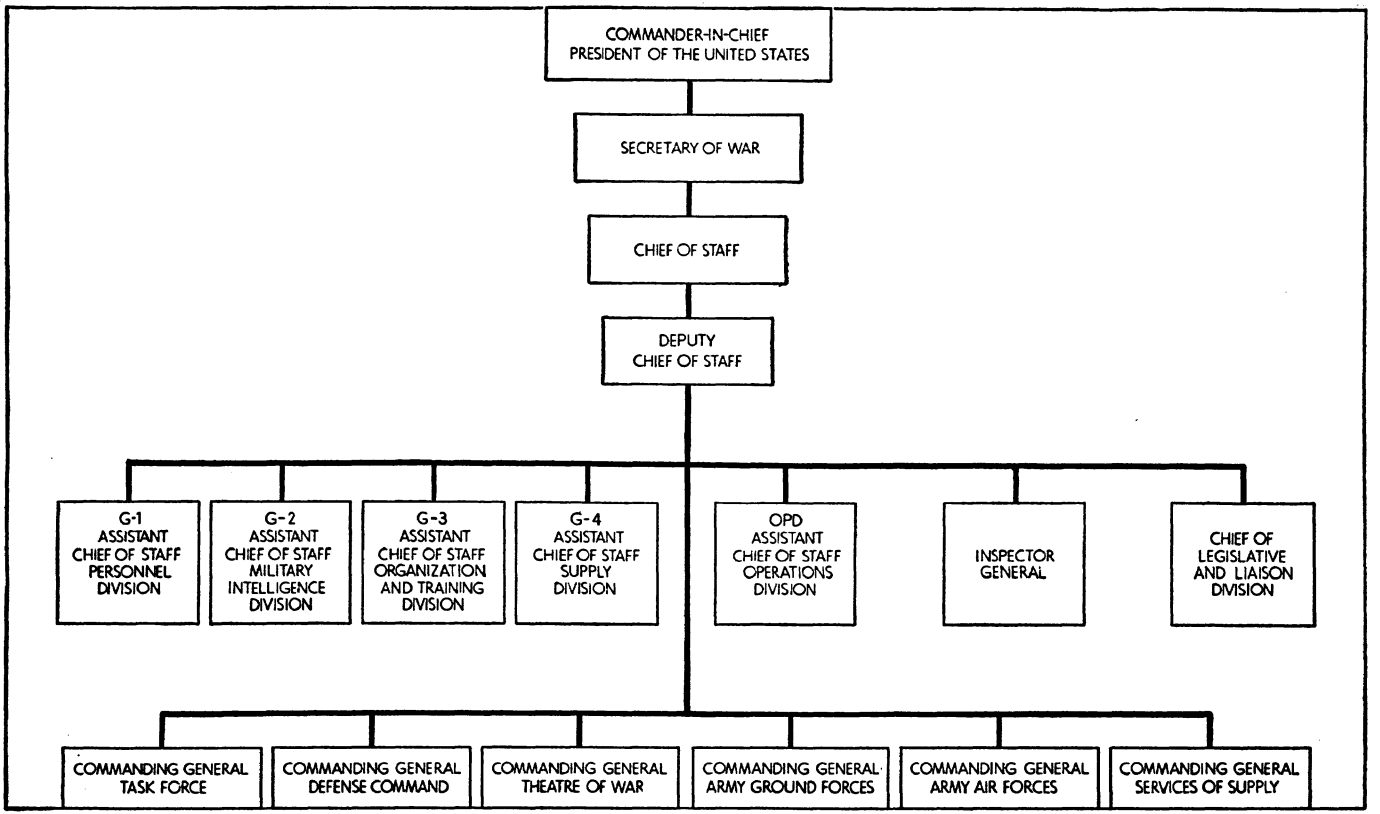


FIG. 11.—Organization of the General Staff in the War Department, 1947.

factors have been classified and allocated to divisions of the General and Special Staffs as specialized functions. Briefly, they are as follows:

1. *G-1, Personnel Division*: Deals with all personnel of all components of the Army.
2. *G-2, Military Intelligence Division*: Deals with all military information.
3. *G-3, Organization and Training Division*: Deals with the organization, training, and operation of troops and their units.
4. *G-4, Supply Division*: Supplies the armed forces with all material requirements of every kind.
5. *OPD, Operations Division*: This is the command post for the strategic direction of the armed forces.
6. *Inspector General's Department*: Inspects and reports on the efficiency and economy of the Army.
7. *Legislative and Liaison Division*: Supervises the preparation of legislation requested by the War Department and establishes liaison with the Congress.

At the lower level shown in the organization chart are the commands of the operating components of the Army. In the United States Army, such operations as the assignment, equipping, and training of troops are divided into commands according to the eventual missions upon which the troops will be sent. There were in 1946 three such commands, namely, the Army Ground Forces, the Army Air Forces, and the Services of Supply. Upon the arrival of the troops in an area of assignment, they pass from the jurisdiction of these three designated commands to that of the commander in charge of particular operations. This commander, under the War Department, assumes full operational and administrative control over the units and personnel assigned to his command. This command organization is based on the military principle of unity of control and rapidity of action together with a rational division of functions and a broad decentralization of details.[4]

Influence upon Departmentation

Because the span of knowledge is a restrictive factor in the managerial capacity of an executive, the segments into which modern business organization divides itself have a tendency to split into an increasing number of vertical lines. These vertical lines do not always start at the topmost level of management in the organization, nor do they always proceed downward all the way to the workers. They may terminate at any intermediate level, depending upon the type and purpose of the departmentation involved. The simplest and perhaps the original method of vertical separation is that of location.

[4] *U.S. Government Manual, 1946* (1st ed.), pp. 192–200. Since September, 1947, the War Department has been known as the Department of the Army.

Territorial Departmentation

This method is usually called "territorial departmentation." As shown in Figure 12, railroads use this type of specialization in establishing different operating divisions. Not only is each division completely separated geographically from other operating units, but its managing personnel is also distinct. Such coordination as may be required for the smooth functioning of the whole railroad system takes place only in the management level of the major executive group. In this way the span of control and the span of knowledge are equated and balanced to a marked degree. Because he is located where train movements take place, the division superintend-

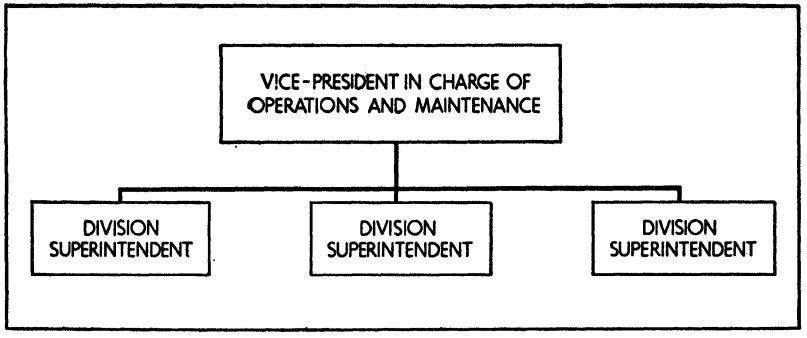


FIG. 12.—Territorial departmentation in a railroad system.

ent, who is the executive in charge of the operating unit, has the advantage of having detailed knowledge concerning performance.

Commodity Departmentation

The second method of vertical separation of management tasks, called "commodity departmentation," is illustrated by Figure 13. Under this plan, specialization in management takes place on the basis of a particular class of products or goods which come within the jurisdiction of a single executive. A typical example of this method appears in the procurement divisions of chain stores, wholesale houses, and other merchandising establishments. Thus, there are provision buyers, canned goods buyers, flour buyers, and so on. Here, again, clash is avoided between the span of control and the span of knowledge because the executive in control has his interests centered on one class of items concerning which he and his subordinates are thoroughly familiar.

Functional Departmentation

A third method of vertical cleavage is determined on the basis of activities performed. This method is called "functional departmentation."

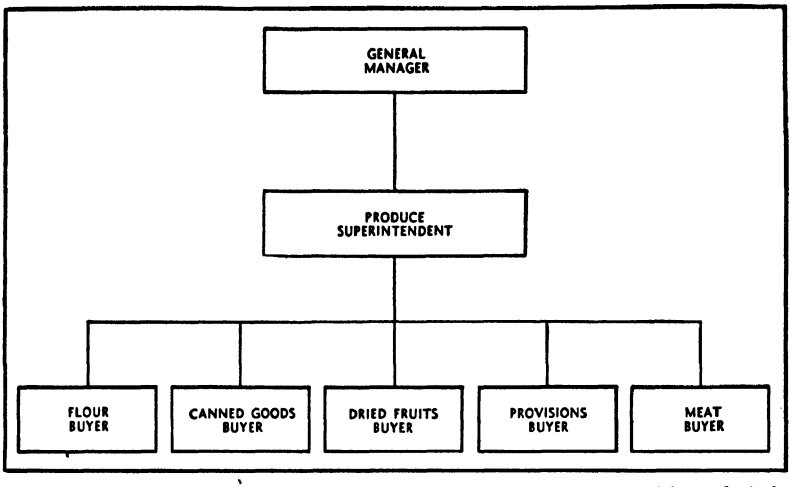


FIG. 13.—Commodity departmentation in the procurement division of chain grocery store organization.

Often responsibility for and control over the functions of production, selling, accounting, transportation, or advertising are assigned to separate specialized executives with appropriate staffs of assistants. By this plan the organization of a business below the level of the top executive and his immediate assistants consists of a number of managerial groups usually of equal rank, which are identified by the special tasks each is to perform (Fig. 14).

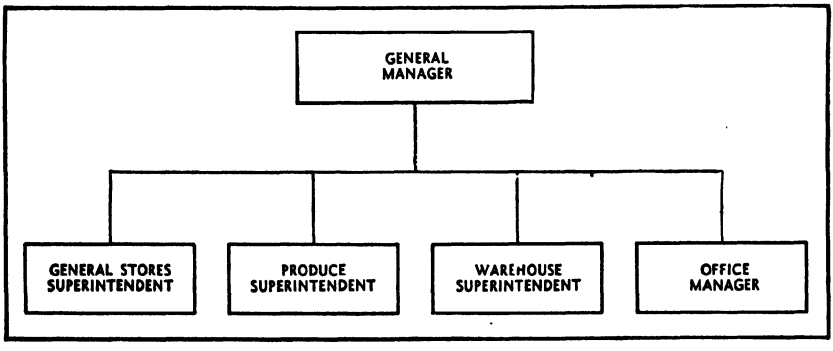


FIG. 14.—Functional departmentation in chain grocery store organization.

As a business enterprise grows in size and scope, there is a tendency to increase the number of functional departments in its management. Sometimes this is done by adding new departments or splitting old ones. When these divisions occur, it is often difficult to determine the precise levels of authority which should prevail. Frequently the result is that each

functional executive who is added merely increases the number of subordinates which report directly to the president, or top executive, of the company. It is at this point that a clash occurs between the span of control and the span of knowledge. Obviously, functional executives are appointed because the span of knowledge of the highest executive, or that of a limited number of assistants immediately subordinate to him, is not sufficient to comprehend and solve all the technical problems which arise in the business. But when the addition of such specialists increases the number of persons in the management group immediately subordinate to the general manager to a point where it violates the principle of the span of control, the benefits of functionalization may be lost in indecision and disorder.

Balance and Judgment in Executive Control

Again, the need for balance and judgment in the responsibilities of executive control is apparent. There must be functionalization. No executive should be expected to deal with an excessive amount of subject matter. Neither should he be required to supervise so large a group of persons that his limitations of time and energy break down in the process. Knowledge, after all, is a nebulous thing. Its boundaries may not be staked out with the exactness of a mining claim on a mountainside. Therefore, the application of the span of knowledge in the determination of management levels in an organization cannot be made on a scientific basis. Nevertheless, certain general observations may be made. When an executive staff contains an insufficient number of individuals, the chances are that the span of knowledge of certain persons in the group presumes to encompass an impracticable variety of subject matter and capabilities. On the other hand, the existence of too many executives may result in the failure of the higher executives to take advantage of latent talents possessed by individual members—talents undeveloped and unobserved because they are not utilized.

SPANS OF TIME, ENERGY, ATTENTION, AND PERSONALITY

While special emphasis has been placed on the significance of the span of control and the span of knowledge in the determination of management levels, there remain certain auxiliary "spans" or limitations which have a bearing on the subject. They have been suggested in the early part of this chapter. Their further elaboration will serve to complete the main considerations involved in the levels theory of organization.

The Span of Time

Time is an inexorable limitation of life. The number of hours in a day are fixed. The power of man can neither increase nor shorten them. To

budget time is as necessary as to budget material resources, for budgeting involves planning, and planning is a guard against waste. Waste of time and lack of time are deterrents to efficient management. The correction of the former is largely a personal problem of every executive; but the lack of time may be due to improper organization beyond the control of the individual affected. The executive must plan the best and wisest use of each working day.

It is at this point that the "span of time" is a determining factor in arriving at the number of levels which should prevail in a management group. An increase in personnel, an expansion of plant, or a growth in patronage—any or all of these conditions—may be sufficient to place such added demands upon the time of an executive that, unless his duties are shared with others, his output as a manager will be seriously affected. In other words, the single consideration of time may be the decisive element in the effectiveness of control in management. Obviously, when the time required to perform an executive task is in excess of the time available to the one whose duty it is to perform such a task, a new level of management must be added in order that efficient service may be rendered. Thus management levels may increase on this basis alone. This characteristic of the span of time which causes an increase in the number of levels is only one of its effects. The span of time also may cause an increase in the number of executives required at any one level.

The Span of Energy

Closely associated with the span of time is the "span of human energy." It has two aspects—physical and mental. There are, of course, limits beyond which human physical endurance cannot go. The recognition of this fact lies at the roots of limitations upon daily and weekly schedules of work. It also relates itself to holidays, vacations, and other respites from the regular routines of employment. Both in practice and opinion, it is generally assumed that a six- or eight-hour day and a forty- or forty-four hour week apply particularly to workmen engaged in the productive processes of an enterprise, and not to the members of the management group. In fact, labor laws which prescribe minimum wages and hours specifically exempt employees who may be classed as executives, administrators, or professionals.

For some reason—perhaps purely traditional—it is felt presumably that executive activity is not such a drain on energy as is manual labor. Or it may be that executives themselves consider that the nature of their work does not lend itself to stated schedules. It is possible that the latter reason is the more valid one. But, whatever the reason for this attitude may be, the fact still remains that occasions do occur when a manager, whether in a major or minor position, is assigned an overload of duties—

when, in plain language, he has more work than he can do. True, the span of time, already discussed, may be a factor of prime importance in determining when the point is reached where the tasks assigned exceed the energy of the person required to do them. However, there are also the considerations of relief and relaxation in their relation to efficient service. The distinction between a lack of time and the lack of sufficient energy may be a fine one, but it is nevertheless real. When the span of physical energy is thus exceeded and further assistance is required, another level or other levels of management are added to an organization. Like the span of time, the span of energy has other effects, particularly in causing an increase in the number of executives with similar duties at the same managerial level.

The Span of Attention

Another phase of the span of energy, in addition to that of physical endurance, is the natural limitation of mental energy. This limitation may be called the "span of attention." When executives are warned against the dangers and wastes of "fiddling with details," what is meant, in more formal language, is that the human brain is able to pay attention, efficiently and effectively, to relatively few items at a time. An attempt to spread the span of attention is the exact reverse of the concept of concentration. The concentration of force—be it mental or physical—multiplies its effectiveness, and, conversely, dispersion weakens its power.

This principle is especially significant, though often overlooked or disregarded, in business organization. Since the tasks of management involve the control and coordination of the activities of many persons whose duties are interrelated, it follows that in making his decisions an executive is inescapably concerned with the reactions of every person under his jurisdiction. These reactions are not only individual in character but they also include the reactions of any possible group of persons of which the individual may be a member. A French consultant in management has elaborated this point in considerable detail.[5] He points out that in the act of management, the burden of the executive is measured by the direct single relationships between himself and those he supervises, and by the additional direct group relationships and cross-relationships which grow out of the human associations involved. Thus, if A supervises merely two persons, B and C, six relationships are thereby created. First, there are the direct single relationships of A to B and A to C; then there are the direct group relationships of A to B with C and A to C with B; and, finally, there are the cross-relationships of B with C and C with B.

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[5] V. A. Graicunas, "Relationship in Organization," *Papers on the Science of Administration* (New York: Institute of Public Administration, Columbia University, 1937), pp. 183–87.

Some realization of the effect of an increase in the number of subordinates which report to a superior officer may be gained from the fact that the number of relationships which must be considered increase in geometrical progression. With each of four subordinates an executive may have eleven relationships. "Just why an executive already having four subordinates should hesitate before adding a fifth member to the group which he controls directly, becomes clear if it is realized that the addition not only brings twenty new relationships with him, but adds nine more relationships to each of his colleagues. The total is raised from forty-four to one hundred possible relationships for the unit, an increase in complexity of 127 per cent in return for a 20 per cent increase in working capacity." [6]

The limitations of the span of attention also have a bearing upon specialization. Specialization is essential in organization. It is the fundamental basis of departmentation. But specialization may hardly be realized without the concentration of attention upon a given task or function. Again we approach near to the concept of the span of knowledge. To become authoritatively informed in a given field or upon a special topic implies sustained and concentrated attention upon it almost to the exclusion of the consideration of other subject matter. Such devotion of mental effort in one direction obviously restricts the span of attention. New products, new problems, and new methods supplementing, but not supplanting, the previous policies and objectives of a business would therefore require new levels in the executive structure. The addition of individuals to the executive personnel at any level increases the number of relationships which arise, as described above. Complexities in organization and management, therefore, multiply as a business increases in size and scope. Yet the principle of span of control is absolute—modified as it is, at various points by knowledge, time, energy, and attention. When this principle is violated, management becomes weaker and tends to degenerate into ineffectiveness.

The Span of Personality

There remains to be mentioned a further human limitation which has a bearing on management levels. It may be characterized as the "span of personality." Less definite in its nature than time and energy, and more difficult to analyze than knowledge and control, the executive capacity of certain individuals is clearly limited by their personalities, especially in instances where certain personal qualities are needed. "Personality" has been defined as "that part of character that is effective in influencing other people." Presumably, the kind of influence which is sought after is favorable influence. Hence, if the elements which make up personality are

[6] *Ibid.*, p. 185.

undeveloped or lacking in an executive, the amount of favorable influence which he can exert will be limited or nonexistent.

The span of personality seems to be pertinent in the field of public relations particularly. In a managerial position where the problem of building and maintaining goodwill is a principal consideration, an executive may be ever so competent in knowledge and energy, have the necessary time at his disposal, and yet, if he is lacking in personality, his *contact* effectiveness will be slight or even negative and harmful. Under such circumstances, the otherwise competent executive must be dismissed or replaced, or else another executive must be delegated to do the contact work.

ORGANIZATION LEVELS DEVELOP BECAUSE OF HUMAN LIMITATIONS

The characteristic feature of the architecture of a business organization is its stratification. These strata are the management levels, existing because of the limitations upon human capabilities. Most general of all these limitations is the span of control. When the span of control is further analyzed, it is found to be conditioned by auxiliary limitations identified as the spans of knowledge, time, energy, attention, and personality.

Discussion has been intentionally limited in this chapter to the levels theory of organization, that is, to consideration of the basic influences within the management structure that cause even the number of management levels to multiply. The counterinfluences that tend to increase the number of like or related executives at the same level rather than to increase the number of levels, have been left for later discussion. The student should bear in mind, however, that the final result, namely "*actual management practice*," is a combination of all forces and influences.

QUESTIONS

1. Assume a hypothetical business concern of medium size in which the organization for management consists of sixty-nine persons. Using Figure 9 as a pattern, make a diagram of this organization showing personnel assignments as follows:
   Forty foremen.
   Six overseers or general foremen (also sometimes called "assistant superintendents").
   Two inspectors.
   One assistant sales manager.
   One plant engineer.
   One paymaster.
   One statistician.

Two sales managers (one for each of two different products manufactured in different factory divisions).
Two factory managers (one for each of two factories located 700 miles apart).
One general production manager.
One secretary of the corporation, also known as the "corporation clerk."
One president of the company.
One treasurer.
Two vice-presidents.
A board of directors consisting of seven persons, four of whom are active executives in the concern—namely, the president, the two vice-presidents, and the chief clerk. The other three members have no connection with the business except as board members.

2. A century ago the corporate form of business organization resembled the partnership in that it had no single executive head like the modern corporation president. If the corporation owned several different properties, each of them was managed at its location by a resident director or by a salaried operating manager commonly called an "agent." Often the top level of management consisted entirely of unpaid board members who, by election, would also serve in such capacities, as chairman, treasurer, and clerk. In the light of the foregoing brief description and the text material in this chapter, discuss the evolution of the top level of management from the following standpoints:
   a) Did the modern top executive level of management evolve because of the need for an effective organization of the board of directors?
   b) Did it evolve because of an increase in the size of business enterprises? (Reconcile your answer with the fact that the salaried top executive system is in common use in modern small business enterprises.)
   c) Did it evolve to meet new legal requirements?

3. Refer to the item in Question 1 which shows that some of the members of the board of directors hold executive positions in the company. As such, they receive salaries from the corporation in addition to any profits to which they may be entitled as stockholders. The problem:

   Explain fully and clearly the different relationships of authority, responsibility, and accountability which obtain between the board of directors and the top management level of higher executives—including the president of the company—(1) when the board of directors includes the salaried executives as indicated above, and (2) when the board of directors consists of persons completely independent of any other official connection with the corporation.

4. Assume the same two different conditions relative to the composition of a board of directors as stated in the problem of Question 3. Show how the circumstances involving the span of control and the span of knowledge vary in each instance on the part of the board of directors and the higher executives—including the president of the company.

5. An old record dated October, 1824, of an American business enterprise still in existence, shows that its original organization included the following:

   A board of directors with headquarters in Boston.

   Two executives, the treasurer and corporation secretary or clerk, resident in Boston.

   Two executives, the agent or general manager and the accountant, at that time called the "bookkeeper and timekeeper," resident at the factory of the company located about forty miles from Boston.

   This particular company did not have a president until 1867. During the period between 1824 and 1867, the presiding officer of the board of directors was the senior director. Both the treasurer of the company and the factory agent were members of the Board. Assignment:

   With suitable diagrams and discussion, show that this actual organization of more than a century ago cannot be considered an example of perfect line organization. Give reasons for the idea that modern American corporations have been drifting away from perfect line organization.

6. Prepare diagrams representing each of the following types of departmentation, using examples of actual organizations familiar to you through your own knowledge or experience:
   a) Territorial departmentation.
   b) Commodity departmentation.
   c) Functional departmentation.

7. As a business enterprise grows larger, an older top executive is sometimes heard to remark: "Our company is no longer a one-man concern."

   Point out the reasons for such a statement, adhering to the terminology of the text in this chapter as closely as possible, particularly with reference to the spans of control, knowledge, time, energy, attention, and personality. Give examples of the effect of company growth upon each of these concepts.

8. The executive career of Samuel Pepys extended from 1660 to 1688. Familiarize yourself with the life of this man by referring to encyclopedia articles or by reading his famous diary.

   a) Discuss evidences of mismanagement in the affairs of the British Royal Navy during the lifetime of Samuel Pepys, and show how better organization might have corrected them.

   b) Contrast the personal honesty of Mr. Pepys with modern standards of ethics.

9. There is good ground for the statement that when an enterprise has been effectively organized on the basis of territorial or commodity departmentation, its evolution and growth often result in the addition of functional departments. Such expansion is frequently accomplished by the creation of a new level of management immediately below that of the president of the concern and above that of the original form of departmentation. Show by

means of diagrams and appropriate explanations what is meant by the foregoing statement, using the following illustrations:

a) A modern railroad company is often organized into nearly autonomous divisions, each one of which may consist of certain tracks, stations, engine houses, locomotives, and car inspection and repair facilities. Such a railroad, as it grows in size, frequently develops a group of vice-presidents whose individuals bear such titles as Vice-President—Operation; Vice-President—Traffic; Vice-President—Finance; and Vice-President —Personnel.

b) A large department store has ten sales floors, each under the control of a different executive called a "buyer." An attempt is made to limit the type of merchandise displayed and sold on each floor to a more or less homogeneous type of goods. Accordingly, men's furnishings are handled on one floor, ladies' ready-to-wear on another, hardware on another, and so on, each floor being different from all others.

This store has its own employment and personnel department which selects and trains its sales clerks and other employees, but it has entered into a cooperative arrangement with other stores in other cities whereby resident buyers of goods are maintained in central markets like New York. These buyers are specialists in the purchase of articles and groups of articles at wholesale. A further cooperative arrangement is a local one in which this store joins with its neighbors in a delivery service of purchases to the homes of its customers.

10. On the basis of the discussion of leadership, as presented in Chapter II, point out similarities and differences in the problems of leadership encountered by companies whose basic pattern of organization is "territorial departmentation" and those that are organized on a basis of "commodity departmentation." Do not fail to take into account Taylor's four principles of scientific management.

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Chapter V

THE BOARD OF DIRECTORS LEVEL OF MANAGEMENT

IN ORDER that a business may exist in our modern society and do the things that are expected of it, it is necessary that rules be established both for its creation and its operation. These rules are of two principal sorts—those established by public law and those made by a business itself. In the brief historical sketch of business (Chap. I), the effect of general incorporation laws upon the growth and development of business corporations was emphasized. Such laws are the "acts of government" in the usual meaning of that term. But a business concern also makes its own rules, enforces them when possible, and changes them when necessary. To the extent that it does so, it has been aptly described as a "private government within the law."[1] It is "within the law" because statutes enacted by legislatures give a business organization a legal status for existence and authorize it to make rules for the conduct of its affairs. It is "private" because, once such rules are made according to law, they are not reviewable by any public body.

THE PLACE OF STOCKHOLDERS IN MANAGEMENT

If a business is a private government, then who makes its rules? As has already been shown (Chap. II), in a large corporation where ownership and leadership are sharply separated, the stockholders, who are the owners, exercise little or no direct personal influence in management. The stockholders, collectively, elect a board of directors; but in general practice, the members of this board are not *chosen* by the stockholders. This is true because the stockholders are usually not organized to nominate candidates for the board, nor are they sufficiently informed as to the merits and qualifications of persons available for such office. Therefore, the actual choice of directors is made by the board itself, often upon the recommendation of top executives within the management group. Once elected, the board of directors assumes the basic authority over and responsibility for management in an incorporated business.

This does not mean that the stockholders of a corporation are entirely without the power of decision in all issues which may arise in a business concern. As regards rule-making, there are questions that are

[1] Beardsley Ruml, *Tomorrow's Business* (New York: Farrar & Rinehart, Inc., 1945), p. 51.

restricted by law to decisions by vote of the stockholders. In the corporation laws of many states, matters of this kind are specifically set down in the statutes as subjects exclusively within the authority of the stockholders. They usually include problems involving all of the property of a business at one time, such as the sale or lease of its total assets, or consolidation with another concern. It is also customarily the exclusive power of the stockholders to amend the charter of the corporation and to make changes in its capital structure. A mere majority vote by the stockholders on such a question usually is not sufficient to carry it. State laws vary on this point, but a two-thirds or three-fourths majority is not uncommon. In the event of bankruptcy, bondholders, through their own representatives, may take the lead in formulating plans for reorganization.

Considering these legal restrictions upon the board of directors and remembering also that the directors are elected periodically by the stockholders, it is a fair statement that the fundamental authority for the management of an incorporated business rests with the stockholders in much the same sense that, in a republic such as our own, the sovereign power of government resides in a certain body of the people called the electorate, which power is exercised by its elected representatives. Nevertheless, the role of the stockholders and the owners of other securities, such as bonds, is rarely important in the broad stream of management affairs. In a successful, stable, going concern, this large group which represents ownership convenes in an annual meeting—personally and by proxy—and accepts or rejects persons nominated to the board of directors. From this point on, it is the latter committee which must assume the burdens of management.

THE BOARD OF DIRECTORS

The real head, therefore, of a typical incorporated business enterprise is a committee—the "board of directors." It is upon this board's decisions and directives with respect to the major aspects of a concern that success or failure depends. Behind such decisions and purposes, of course, is the personnel of the board itself. How wise and prudent the collective action of a board of directors will be hinges upon the wisdom and judgment of each individual member and upon his qualifications to serve in the capacity for which he has been elected.

The board of directors occupies a position between the stockholders and the executive group. Neither in modern theory nor in practice is it assumed that the board will attempt to direct the affairs of a business in any detail. Its function is to exercise broad supervision and to share active leadership in the enterprise with the executives it has appointed. Obviously, the effective performance of this function varies widely among business concerns. Directors are more active in some corporations than

in others. Their role in management may be influenced by the size and the composition of the board, as well as by provisions of the bylaws of the corporation which largely determine their activities and procedures.

Size and Composition of the Board

Under the corporation laws of some states a board of directors may consist of as few as three members. According to one survey, it has been found that the typical board has a membership between five and nine.[2] An odd number is commonly adopted so that tie votes will not be possible. In an analysis of one hundred fifty-five very large corporations, Gordon found that in 1935 the size of boards of directors ranged from six to thirty-five members. The average for the entire group surveyed was approximately thirteen men per board, which seems to be a fairly typical figure for large corporations in this country.[3] Boards much larger than this are likely to be unwieldy and ineffective. The most effective size usually varies from five directors in small concerns to thirteen or fifteen in large corporations. No general rule can be laid down covering this point. It is important that a board of directors be small enough to be effective as a working group and yet large enough to provide diversity in experience and viewpoint on the part of its members.

It is possible for the board of directors of a modern business corporation to consist of three different types of persons. In the first place, it may consist of the principal owners of the business enterprise, each one serving not only as director but usually as one of the executives. This condition was typical during the last century when businesses were still largely controlled by their founders. It is an organization pattern which closely resembles the business firm or partnership.

In the second place, the board of directors may include minority or small owners of the business enterprise, often because of the diffusion of stock ownership following the death of the founders. In a constantly growing proportion of large American business enterprises, every owner is a minority stockholder. Indeed, in some corporations the board of directors cannot muster majority ownership of the company's common stock. The directors, therefore, must manage the business not only for themselves but also for the majority of the stock ownership not represented on the board. Such directors may be said to have "fiduciary responsibility." Directors responsible for large amounts of the money of

[2] Article by Erwin H. Schell on "Trends in the Functions and Composition of Boards of Directors" in W. J. Donald (ed.), *Handbook of Business Administration* (published for the American Management Association by McGraw-Hill Book Co., New York, 1931) p. 405.

[3] Robert A. Gordon, *Business Leadership in the Large Corporation* (Washington, D.C.: Brookings Institution, 1945), p. 117.

other stockholders are, in a very real sense, "trustees" for the nonrepresented shareholders.

In the third place, the board of directors may have members who are not stockholders beyond possessing the minimum number of shares which qualify them for positions on the board. Such persons may, or may not, also serve as executives of the business. The members of the board of directors of any mutual insurance company are responsible for a business enterprise they cannot themselves own, since its assets belong entirely to its policyholders. Such directors are essentially trustees. This form of organization is still relatively uncommon, but it is increasing in incidence.

In order to achieve checks and balances within a board of directors, its members are sometimes chosen in a manner that provides one group which represents the active management and another group which has no direct connection with the concern except in board membership. When this pattern is followed, the first group is important because it brings to the board the firsthand views and attitudes of the executives who are constantly dealing with the operating problems of the company. Its members can personally sponsor for board action proposals that have their origin within the business and are based on a thorough knowledge of its internal affairs.

The importance of the second, or outside, group is that the judgment of such directors will tend to temper prejudiced or biased proposals direct from management by bringing to the board an impartial and somewhat detached viewpoint. As a result of their familiarity with other businesses and interests, these so-called "outsiders" are able to suggest policies and practices followed elsewhere. They may be conversant with conditions and circumstances that can be turned to the advantage of their company which might not otherwise be utilized. Directors of this type can more readily exercise a sound appraisal of results, since the other board members, who are executives of the concern, can hardly pass judgment upon their own accomplishments.

Personal Qualifications of Directors

Related to the size and composition of boards of directors is the question as to why persons are selected for membership on such boards. There are several reasons for such selection. Studies of existing boards show that executive ability is the most important qualification for membership; stock ownership is a less important factor, but trusteeship is becoming a more frequent reason.

The quality of executive ability may be broken down into such elements as knowledge of business details, managerial judgment, financial and legal counsel, and an understanding of general business conditions. When active executives of a concern are chosen to sit as board members, they

are usually persons who have had broad experience in the fundamental fields of management—finance, accounting, production, and marketing. Typically, they hold top positions as president or general manager, ranking vice-presidents, or other officers in charge of the major functions of the business.

Individuals are sometimes chosen for positions on directorates because of their ability to bring prestige to the corporation. Such prestige may be due to their recognized standing in the business world, in their community, or in their own specialized fields. Additional desirable qualifications of outside directors have been found to be the following: [4]

1. A personal financial interest in the enterprise.
2. A limited number of other directorships.
3. A familiarity with the company and its industry.
4. An independent viewpoint.
5. A willingness to criticize.
6. Sufficient interest to insure regular attendance at meetings and thoughtful consideration of company problems.
7. A broad business and executive experience.
8. No adverse interest.

Since it is the responsibility of all boards of directors of incorporated business to sanction the major policies and objectives of business enterprise, it is paramount that board members should be only persons competent to meet their obligations. By their official acts not only do these directorates, to a large extent, shape the pattern which management must follow; but also collectively, they influence the very destiny of private enterprise as a whole.

Therefore, the qualifications of a good director of a business corporation are high—probably too high for any one person to possess all of them. Yet, they are no more than commensurate with the high obligations that, by virtue of office, are his. A good director must be a person of unquestioned personal integrity, motivated by sound principles of ethics. He must have the courage of his convictions in order that he may be independent in his judgment, yet must be cooperative in his actions. He must manifest qualities of leadership by advancing constructive policies for the welfare of the firm he represents, regardless of whether such policies conflict with his own personal interests. From him it is fair to expect loyalty to the business and genuine interest in its success. He will show his devotion by being available for meetings of the board and for consultation with officers and employees of the company.

Because of the social and economic implications of modern business, a

[4] Paul E. Holden, Lounsbury S. Fish, and Hubert L. Smith, *Top-Management Organization and Control* (Stanford University, Calif.: Stanford University Press, 1941), p. 19.

good director must be one who has a broad social point of view, who is aware of change and has no fear of it, and who can adjust his business thinking to changed conditions when necessary. He is conservative in the sense that he is not wasteful or profligate. He does not cling to, or abandon, old policies and methods because they are old; nor does he spurn or embrace new and untried ones because they are new. By reason of his experience, knowledge, and understanding of men and affairs, his background makes him competent to comprehend clearly and quickly the problems of a specific business even though it may be quite different from his own vocation. Profit and stability—twin major concerns of a board of directors of a business institution—are constantly a matter of exploration and development, but "the explorer must know far more of the country than the spot where he pitches his tent."

ORGANIZATION OF THE BOARD OF DIRECTORS

The bylaws customarily provide that the directors shall elect the officers of the corporation. Precisely who these officers shall be will vary among corporations. Usually they are the president, one or more vice-presidents, the treasurer, the secretary, and the legal counsel. It is also not uncommon that provision is made for the election of a chairman of the board of directors distinct from the president of the corporation.

The Chairman of the Board

The chairman of the board of directors, when separate and distinct from the president of the company, sometimes occupies an honorary position. He is often a man whose long experience in the business has brought advancement in position, but who has passed the age when it is practicable for him to assume the responsibilities of the daily problems of management. He has sometimes been called the "Nestor" of the company, after the aged and wise counselor of the Greeks in the Trojan War. As such, his advice is desirable upon questions of policy, particularly as they refer to relations outside of the corporation itself. Therefore, his duties cannot be specified, except that he presides at all meetings of the board.

Since the directors are in session only at intervals, ordinarily a month or more apart, provision must be made to handle the business of the board between meetings. For example, the chairman is usually authorized to sign the name of the board to indicate approval of actions already taken.

The President and Vice-Presidents

The president is the top executive or managerial head of the company. Sometimes he is known as "president and general manager." If a separate chairman of the board is lacking, he will act in that capacity as well. Vice-presidents are generally heads of the main functional departments into

which the organization of the business is divided, though it is not uncommon for such executives not to be vice-presidents. The president is almost always a voting member of the board; often he is the only executive so honored.

The Treasurer

It is the duty of the treasurer to assume responsibility for the receipt, custody, and disbursement of the corporate funds, and as such he must serve under bond, or its equivalent. In fact all executives and many employees occupy "positions of trust" and, like the treasurer, are in the status usually called "bonded," which means that a company reserve or an outside bonding company will make restitution for criminal acts such as theft. A treasurer may be either an active or an inactive managerial executive. If the former, he is also frequently the controller, and as such he is placed at the head of the accounting department. If he is inactive, his duties are more or less formal and nominal, the details of his office having been delegated to some other executive. The treasurer usually makes his reports to the board in person, whether he is a board member or not.

The Secretary

The secretary of a corporation keeps the minutes of the meetings of both the board of directors and the stockholders. He must prepare and distribute appropriate notices of such meetings. He is the custodian of the corporate seal, and he is in charge of the records of issue and transfer of stock certificates. He is the officer who assumes the responsibility for the reports of the corporation which are required by law, and he handles all communications with public officials pertaining to the charter of his company. Usually the secretary is paid a salary for his work. Often he is not a member of the board of directors. Though the practice varies with different corporations, there are no restrictions—legal or otherwise—that exclude the secretary from membership on the board of directors.

The Legal Counsel

The legal counsel, as his title implies, is the attorney of the corporation. He may be appointed on a retainer basis, or he may be employed full time, depending upon the size of the firm and the nature of the legal problems involved in its management. In either instance, he is the legal expert to whom questions of law may be referred at any time. In the event of court trial, it is his duty to prosecute the case in the interest of the corporation, which may then be both his employer and his client. He usually attends board meetings, even when a nonmember participant in its discussions.

Special Committees

To make possible emergency decisions between regular meetings, it is common practice to appoint a standing subcommittee of a few board members, usually called the "executive committee" or "finance committee." In effect, this committee is given blanket power to make decisions of a specified character during the interval between meetings. The board agrees in advance to approve such decisions of its subcommittee. The chairman of the board is one of the members of this executive committee, and the secretary of the board keeps a record of its actions. This record he subsequently transmits to the board to become part of its legally approved minutes at the next regular meeting.

In addition to this device of a standing subcommittee, one or more of the members of the board of directors are often regarded by the members as having specialized ability. Frequently these members are also major executives of the company, but this dual position is not a prerequisite to such recognition within the board.

In actual practice, most of the vital problems considered by the board of directors as a whole have first been studied, and a decision has been reached either by an individual member or by a permanent committee of the board—frequently by both. It follows that board meetings are held for the principal purpose of ratifying action already taken, or about to be taken.

LEGAL POWERS OF THE BOARD OF DIRECTORS

A "corporation" has been defined as an "artificial person created by law, endowed with the rights of ownership and initiative, and with concomitant obligations like those of a natural person." Thus, title to corporate property is vested in the corporation; and since right of ownership of private property is the fundamental basis of authority for management, it follows that such authority is also vested in the corporation. But the corporation, being an artificial person, obviously cannot think and act of itself. It is for this reason that the control of its property and the authority for its management, both inherent in the right of ownership, can only find expression through the corporation's representatives, namely, the board of directors. Therefore, it should be clearly understood that while the stockholders *own* the corporation, the latter is a separate entity, a creature of law, which, in turn, *owns* the corporate property.

To say that the assets of an incorporated business enterprise belong to the corporation and not to the stockholders, who own the corporation, may seem to be making a distinction without a difference. Yet this distinction is important. Such separation of ownership automatically carries with it the separation of obligations. That is, a stockholder cannot be held

liable for the acts of a corporation of which he may be part owner. By the same line of reasoning, until or unless he is legally elected a director of the concern, he has no voice in its management—except indirectly, as further provided by law, namely, the power to participate in the election of the members of the board. Normally, this power consists in one vote for each share of stock owned.

As stated above, the corporation itself, being inarticulate and inanimate, can only speak and act through its legally established representatives—the board of directors. Hence the directors are not the agents of the corporation, but they stand for it and in its place. When they make contracts, or in any other way conduct any business transaction, the corporation itself is acting. Therefore, the directors can authorize anything which the corporation can do, but no more. Their powers are delegated to them by the state which grants the corporate charter under which they act.

Provisions of Statutes and Charter

According to the General Corporation Law of the state of Colorado, which is fairly typical, the position of directors is as follows: "The corporate powers shall be exercised by a board of directors. . . ."[5]

The board of directors of a corporation must exercise its powers as a group, and not singly as individual members of the organization. In this respect the board functions precisely as any other representative body. For instance, a city council elected by the people of a community can act only when in session as a council. Similarly, directors must make their decisions in board meetings, formal minutes of which are required by law, to be kept by a designated officer. Directors may not vote by proxy, but they must be present in board meetings and cast their votes in person. The incorporation laws of the various states specify in general terms what the powers of a corporation, and hence the powers of its board of directors, may be. These powers are more specifically enumerated in the charter, which is issued to make a going concern possible. Taken in combination, the powers of a board of directors, both statutory and chartered, fall into three classes: (1) those definitely specified in the charter; (2) those which are contingent upon or accessory to the expressed powers; and (3) those which are implied by reason of the corporation's creation to carry on a business enterprise. For example, a corporation may be expressly created for the purpose of generating and distributing electrical energy for domestic use. This occupational objective will be clearly set forth in its charter. Contingent upon this service—objective and accessory to it—such a corporation should and,

[5] General Corporation Law of Colorado, Art. I, Sec. 27 (*Colorado Statutes Annotated 1935*, chap. 41, p. 644).

probably would, have the power to sell electrical appliances at retail. Since it is a business institution, it would have authority by its implied powers to own property, enter into contracts, borrow money, and do all such other things which are commonly necessary in the management and operation of a business enterprise.

Such a corporation, however, might not be able to go into the coal-mining business, desirable though it might be to own its own supply of fuel. To do so might be considered an *ultra vires* act by the state which granted its charter in the first place, because coal mining was not mentioned or implied in the charter description of the occupational objective. *Ultra vires,* literally interpreted, means "beyond its strength," hence, outside of its powers. Such an act is, in a sense, a breach of contract with the state, the penalty for which might be the dissolution of the corporation. Furthermore, the owners of the corporation, that is, the stockholders, having a vital stake in the case, could seek to restrain ventures into new undertakings on the ground that capital would be diverted into fields not contemplated when the shareholders invested their money.

Bylaws

Thus far we have seen that the authority of the board of directors of a corporation is regulated, first, by statute and, second, by the charter which is issued in conformity with such statute. Supplementing the charter, there is another document which contains the bylaws of the corporation. These bylaws consist of a formal statement of certain basic organization and management details not stated in either the corporation law or the charter, under which the company must operate. The preparation of the bylaws is not an incidental matter, but it is an essential part in constructing the legal framework of a corporation. So important have the bylaws been deemed that it is an accepted rule of law that the power to make or amend them resides in the members of a group or corporation at large. Stockholders, unless legally forbidden to do so, generally delegate this power to the board of directors. Thus, essential changes in the details of bylaws are expedited without waiting for action to be taken at regular or special meetings of stockholders.

Without going into extensive detail on this subject, suffice it to say that the bylaws usually cover stipulations having to do with the following items: (1) the principal office of the corporation; (2) the date and place of the annual meeting of the stockholders; (3) details concerning the board of directors with respect to number, term of office, qualifications, compensation, meetings, and committees; (4) a listing of the corporate officers, their appointment, terms of office, and duties; (5) provisions for the issuance and transfer of stock certificates; (6) the corporate seal; and (7) the method of amending the bylaws.

Regulatory Laws

It is important, also, to observe that in the economy of the United States there has also developed a different kind of authority, which, from the management standpoint, partially supersedes the board of directors. It consists of a system of regulatory laws which may eventually evolve into a superimposed level of business regulation, that is, management of business conduct in its broader phases. The board may participate in, negotiate with, or yield to, regulatory pressure without any change in its own status, as the head of its own particular organization.

The Framework of Authority

Thus, while the board of directors is, in fact, a committee elected by the stockholders to represent the corporation, it is at the same time a legally constituted body, subject to relatively strict regulations. These regulations are: first, the incorporation statutes of the state which issues the corporate charter; second, the charter itself; third, the bylaws; and, fourth, the federal and state regulations, apart from statutes which authorize such incorporation. Within the limitations prescribed by these measures, the board exercises its authority.

By analysis, this authority can be classified under eight heads, as follows:

1. Interpretation, clarification, and modification of the occupational objective stated in the charter.
2. The determination of major policies.
3. The election of officers, both corporate and managerial.
4. The issuing of stock.
5. The declaration of dividends.
6. The making of contracts in the name of the corporation.
7. The bringing of suits in courts of law and equity.
8. Miscellaneous powers incidental to but necessary for the management of the corporation, but not at variance with the charter and bylaws.

FUNCTIONS OF THE BOARD OF DIRECTORS

The board of directors may be thought of as the pilot of a great ocean liner who stands beside the captain and guides the ship through the narrow channel into the crowded harbor. The pilot does not steer the ship himself, nor does he issue orders to the crew. He tells the captain how the ship should be directed, and the captain converts his general instructions into specific orders. The pilot not only has available all the knowledge and skill of the ship's officers and crew, but he also understands the harbor and its traffic and knows the problems that will be met in docking the vessel. Similarly, the board of directors guides the company president

and his executive group in their management of the business. The board must understand not only its own business enterprise but also its relation to other businesses and to changing business conditions.

The Function of Trusteeship

As long as the corporate form of legal organization of business continues in general use, the board of directors will continue to be the first step in the practical process of management. Its structural position in the organization is that of highest management level, since the board receives an almost complete and legally approved delegation of authority from the stockholders. However, the board of directors is, and should be, more than a mere device to identify ownership. It is more than a titular capstone which lends dignity to the key position of president or top executive by conducting at intervals an investiture or coronation at a prearranged formalized election.

The most vital role of the board of directors is that of sharing in the management process. As such, the board, through its various duties and actions, impresses itself upon the owners of the business and supports their interests in the enterprise. This role in management may be described as the function of "trusteeship." Even when the board is ineffective, and deservedly subject to criticism for its faults, trusteeship cannot be disregarded. Failure to take action is negative performance. Failure to decide does not always prevent decision; nor does it shift responsibility and accountability for results.

Exercise of trusteeship by the board of directors necessarily includes a sort of "overlordship" over every aspect of the business. The board, in other words, may at any time choose to assume direct authority over any financial question or detail, any organization question or detail, and any management question or detail. The board may use the appeal process for this purpose, or it may simply assume original jurisdiction and take the matter out of the hands of its delegates, the top executive and his subordinates.

James O. McKinsey, who had unusual opportunity to observe the actual operation of many boards of directors of modern American business concerns, summarizes the functions of a board of directors as follows:[6]

1. It should be responsible for establishing the general objectives of the business.
2. It should establish the major policies of the business.
3. It should determine the organization structure of the business and select the major executives of this organization.

[6] Article by James O. McKinsey on "Boards of Directors" in *Handbook of Business Administration*, p. 394.

4. It should be responsible for "checking up" on the executives of the business to whom the responsibility for its administration has been delegated.

The Function of Policy Formulation

Of course, the board of directors cannot take up all the details of the business for sheer lack of time and expert knowledge. Therefore, it is at this level of management that a clear separation between policy-making and executive functions is apparent. In the proper discharge of their responsibilities, directors serve principally as a legislative body and devote themselves to broad planning and the development of a philosophy of action. They reserve to themselves only such executive functions for which authority cannot be delegated to the chief executive of the concern and his staff.

"Policy formulation" is, in effect, planning. Major policies of corporate significance that come within the province of the board of directors deal with such matters as the determination of the principal objectives of the business, changes in the capital structure, the payment of dividends, expansion, new products, price policies, labor relations, public relations, loans, and lines of credit.

The Profit Objective

When a business is established as a going concern, its basic objective of making a profit immediately comes into existence. If the business is to continue to live and flourish, it must yield this profit consistently. All sustained profit-yielding is based largely on other major yields of the business which justify, morally and legally, its existence. First, it must supply certain economic values to the community of which it is a part. That is, it must provide a needed commodity or service and do so at a justifiable price. At the same time, the community has a right to expect that the business will be so managed as to avoid waste of the nonreplaceable natural resources, such as petroleum, virgin forests, or fisheries. It must, in other words, yield profits or social values to the whole community. Second, it must supply economic values to ownership. The owners of a business have a right to expect that it will be so managed as to yield a favorable pecuniary difference between income and outgo, namely, a profit. And, third, it must supply certain economic and psychological values to its managerial and operative employees. Those who are paid salaries and wages in a business concern have a right to expect that it will yield, in addition, such material and mental satisfactions as will encourage them to continue to exchange their labor for the rewards they receive.

The achievement of this profit objective, and its subsidiary aspects, translates itself into problems of management which the highest level of management, that is, the board of directors, must unceasingly seek to

solve. Anything short of good faith in their solutions will not be tolerated for long. The personal aggrandizer—alone or in collusion with others of his ilk—who, by virtue of membership in the board, seeks to satiate his own greed will soon be found out.

The Occupational Objective

In addition to the universal objective of financial success, the board of directors of each particular business must develop and announce its specific occupational aim, that is to say, must define what the scope of its activities is to be. Sometimes this objective is indicated in the name of the business; in a corporation, it is always stated, at least in broad outline, in its charter.

The occupational objective is not stable, but shifts with time and conditions. It can be observed, for example, that the aim of a business may change as size increases. Growth may result in expansion in various directions. In its marketing policy, large size may influence the extension of its geographical area of operation. In its financial aspects, growth may cause a business to invest surplus profits in more or less unrelated fields in order to diversify risk. The duPont Company, established in 1802, is a notable instance of this tendency:

> In contrast with its original position as distinctly a gunpowder producer, the duPont Company today is essentially and chiefly a manufacturer of products having no relation to war. Especially in the past sixteen years, it has sought and accomplished development of almost the whole range of chemical manufactures. Industrial explosives and sporting powders; paints . . . ; pyroxylin cements . . . ; rubberized fabrics; . . . plastics; dyestuffs . . . ; industrial alcohol . . . ; acids, pigments and heavy chemicals; rayon . . . ; fixed nitrogen . . . ; electro-chemicals . . . go to make up your company's present business, and all these are peace-time products . . . from the crucial viewpoint of profits, the peace-time products of your company now outweigh its military explosives business in the ratio of about fifty to one.[7]

Then, again, the occupational objective of a business may change with population migration, growth, or decline. As a general thing, a rapid growth of the population in a portion of the country which is served by a particular business has a broadening effect upon the objective of that business. Conversely, a slight growth or a decline in the population will tend to result in restriction. When the St. Louis and San Francisco Railroad was organized, its corporate name indicated its objective—the construction and operation of a railroad between St. Louis, Missouri, and San

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[7] *E. I. duPont de Nemours and Company, Inc.* (pamphlet addressed to the stockholders and employees on the duPont company munitions) (Wilmington, Delaware, September, 1934), p. 6.

Francisco, California. It was an objective which was never realized. The sparseness of population over a wide region in western Texas, New Mexico, and Arizona, was an effective barrier to the extension of the railroad toward its original goal. Instead, it found a more profitable territory in central Oklahoma and northern Texas where the population increased rapidly. A brief account of this change in objective follows:

> It started at St. Louis in the fifties, and was completed to Vinita in Indian Territory (now Oklahoma) by the Atlantic and Pacific Railroad Company . . . the St. Louis and San Francisco joined with the Sante Fe. . . . The plan agreed upon at this period would have produced in time a through line with one western and two eastern segments. . . . Unfortunately for the St. Louis and San Francisco these plans were only partially carried out. . . . The Atlantic and Pacific at this time (1895) passed entirely under the control of the Santa Fe, and the Frisco, on its separation from the latter company, found itself entirely divorced from its Far Western lines. . . . Had the credit of the Frisco been a little more secure or its management a little more enterprising, that company might have occupied the position which the Santa Fe now holds. We have seen that the St. Louis and San Francisco first faced west. After separation from the Santa Fe in 1895, the company seems to have looked south and southwest for its future development, and with some success. . . . Results showed that a railroad concentrated in Illinois, Missouri, Kansas, Oklahoma, and northern Arkansas and northern Texas was capable of great progress. . . .[8]

Finally, the occupational objective of a business may change in response to concurrent developments in competition. Some of these trends are due to the evolution of a particular industry. Others may be attributed to laws, regulations, and public opinion. An example of the effect of the change in attitude on the part of customers is found in the policies of the E. I. duPont de Nemours Company already referred to:

> As of June 1, 1933, company acquired a controlling interest in the Remington Arms Company; and on May 15, 1934, Remington, which was of course several times the larger concern, purchased the principal assets and business of the Peters Cartridge Company . . . this investment was justified as a necessary means of defense for the company's sporting powder business. Unmistakable indications were apparent that the intent was taking final shape within the ammunition industry to enter aggressively into the manufacture of sporting smokeless powder. There are no other customers for sporting powders except the producers of ammunition. If the ammunition manufacturers were going to integrate their business backward into powder, then it appeared quite plain that

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[8] Stuart Daggett, *Railroad Consolidation West of the Mississippi River* (University of California Publications in Economics, Vol. II, No. 2) (Berkeley: University of California Press, 1933), pp. 236–37.

the duPont Company must either integrate its business forward into ammunition or else eventually be crowded out of the sporting powder business. . . .[9]

How changes in the occupational objective come about by reason of new laws, regulations, and a shift in public opinion is shown in a report of J. P. Morgan and Company:

The banking business of private bankers, the receiving of deposits, the making of loans, buying and selling of exchange, making of acceptances, has on the whole been conservatively conducted, and in spite of casualties, private bankers have given a good account of themselves here and abroad, over a period beginning a couple of hundred years before corporate banking began. . . . Issuing bankers are really merchants of securities. Some of them are wholesale merchants like ourselves who have no salesmen, and others are retail merchants. . . .

Private bankers seek and receive no charter from the State. They do not solicit capital from the public, but venture their own capital. . . . They do a private banking business with their private clients, who number perhaps a few hundreds. . . .

It seems extraordinary that, after seventy years devoted to building up a good will which had made it true that our clients are men of affairs and of leadership, we should be taken to task for perfectly sound, honorable and straightforward business transactions with them, simply because chance has brought some of them into high office and mischance has impaired the fortunes of others. . . .

The precise facts as to our payment of income taxes seems to have been misunderstood by a portion of the community. Since 1917, the partners of our firm have, as stated, paid upwards of $51,000,000 in income taxes. . . . There can be no doubt that many persons, failing to realize that during prosperous times we have paid heavy taxes upon our profits, felt it to be unjust that during the last three years we paid no income taxes; again failing to realize that our losses had more than wiped out our taxable income. . . .

The question has been raised whether a private banker should be permitted to accept deposits. The laws of the State of New York, very wisely, as I think, and under careful restrictions have sanctioned the practice. . . .

In my experience of over forty years, I cannot remember any partner of the house taking a directorship except at the earnest request of the board of directors of the company in question. It is often useful for the directors of a company who are not financial experts to have an expert of that sort, in whom they have confidence, at hand for consultation. This is why I regret the tendency of so much present-day legislation which endeavors to prevent bankers from being directors of one thing or another; or which throws on directors

[9] *E. I. duPont de Nemours and Company, Inc.*, pp. 9–11.

such liabilities for errors for which they could not be responsible as to make it too dangerous for any man of experience or means to assume such responsibilities. . . .[10]

Financial and Legal Functions

Without digressing too far into the field of corporation finance, it is desirable to note, at this point, the specified powers of the board of directors which deal with this subject. At the outset of a corporation's life, the authorized capital stock is stated in the charter. The amount of this stock may be increased or decreased by charter amendment in the manner provided by law, that is, by vote of the stockholders. When such a change takes place, however, if additional funds are sought through a new issue of stock, it is within the authority of the directors to decide upon the time, the amount, and the terms of the new issue. Likewise, when the reverse action has been taken by the stockholders, the directors decide how and when the old stock shall be contracted or retired.

The directors also have the authority to decide whether a dividend shall be declared and how it shall be paid. Earned profits, however, do not necessarily mean that dividends will be paid to shareholders. If the directors believe that the business will be served best by reinvesting earnings, it is within their power to withhold an authorization for the payment of dividends. This power has been supported in the courts, where it has been declared that the directors of a corporation may exercise such discretion with assurance, unless it can be proved that their acts were "fraudulent, collusive, and destructive of the rights of the shareholders."[11]

Since the directors act for the corporation, and the corporation is a person in the eyes of the law, it follows that the directors may enter into binding agreements and contracts in the name of the corporation. Likewise the directors, representing the corporation, may sue and be sued in courts of law and equity.

Executive Functions

Even though the efficient management of a corporation requires the separation of legislative and executive activities at the level of the board of directors, there are certain basic functions of an executive nature which must be performed by an effective board. It is the duty of the board to select the chief executive and senior officers (commonly, major department heads) of the company and to see to it that able young ex-

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[10] *Statements of Members of J. P. Morgan and Company to the U.S. Senate Committee on Banking and Currency, May and June, 1933* (New York: J. P. Morgan & Co., 1933), pp. 41, 40, 20, 15–16, 6, and 5, in the order given.

[11] *Hunter* vs. *Roberts, Throop and Co.*, 83 Mich. 63; *Ochs* vs. *Maydole Hammer Co.*, 246 N.Y. Supp. 539.

ecutives are being developed. The board of directors also controls the compensation of the members of the executive personnel and establishes pension and retirement policies for their benefit.

Another executive function of the directors is to check on the operations of the company and to exercise appraisal and judgment as to whether the results achieved are satisfactory from the standpoint of both profits and the responsibilities of trusteeship. This function is performed by means of periodical budgets, reports of officers, and inspections of plant and procedures.

In a small corporation in which both ownership and executive management are represented in the membership of the board of directors, the board may exercise significant leadership in initiating policies and in deciding what actions shall be taken to carry them out. In a large corporation, in the broad range of nonfinancial considerations, directors exercise little or no such initiative and decisions with respect to specific matters. The approval of proposals brought to it by ranking officers of the company, or the exercise of its veto power over such recommendations, is the function expected of the board of directors.

Equating Authority and Responsibility

It is often stated that, under sound management conditions, authority and responsibility must be equal. That is, an executive should not be given a responsibility unless he is vested at the same time with complete authority for its accomplishment. Under the complex management conditions of a large enterprise, the equating of authority and responsibility in one person may not be practical. Often such balance can be realized only through the cooperation of several executives.

This complication also appears at the level of the board of directors. As has been said, the board is charged with the complete responsibility for the success or failure of the business. In order to equate this responsibility with commensurate authority, it would seem necessary for the board to exercise the closest direction and supervision of every phase of the enterprise. In practice, it cannot do so; rather, it voluntarily restricts its direct concern to matters that are of special interest to ownership and of the broadest importance to the business as a whole. The board of directors has ultimate authority, to be sure; but such authority is equated with similar responsibility only in the sense that the executive group—created at the demand and with the approval of the board—has been delegated adequate authority to carry on the manifold activities of the business in the name of, and for, the board.

PROCEDURE OF THE BOARD OF DIRECTORS

Since the board of directors is chiefly concerned with matters of broad policies and major objectives, its duties are of such a nature that

they can be satisfactorily performed at periodic meetings. The frequency of such meetings varies with different corporations. Some boards meet quarterly, others monthly, and still others more often. Directors' meetings are not regulated by law; but in order that they may not be considered incidental or casual, provisions for meetings at stated intervals are included in corporation bylaws.

A careful study has been made by President John C. Baker of Ohio University, for the Graduate School of Business Administration of Harvard University, of the procedures followed by active and successful boards of directors. In this investigation, it was found that four types of procedure are indicated in the way effective boards handle different matters. These types are described by the terms "decide," "confirm," "counsel," and "review."[12] By using these terms for the transactions of a board of directors it is possible to describe its functions more clearly. No matter how small the enterprise, these four procedures have full validity and application.

Acts of Decision

Whenever a board of directors takes jurisdiction of an issue, deliberates upon its implications and consequences, and determines a course of action, it engages in decision-making. This procedure is usually restricted to those areas in which the board, for legal or other reasons, cannot delegate authority. The selection of a president of the concern, making a radical change in the occupational objective, the issuance of capital stock, and the payment of dividends, are examples of such acts. In dealing with them, the board may, or may not, initiate additional steps, such as further investigation or legal advice. In any event, the board does receive and weigh evidence, and, on its own motion, effects decisions.

Acts of Confirmation

One of the most common procedures is to receive tentative recommendations and decisions already made by executives of the concern, *subject to the approval of the board.* In instances of this kind, the board still assumes jurisdiction in that it can approve, or disapprove, the proposals submitted to it. The first step of initiation, however, has been delegated to the executives of the business. In so doing, it is presumed that the need, the ways and means, and the anticipated results have been carefully studied to show that the board's approval would work to the advantage of the company. In such circumstances, the duty of the board is to probe the thoroughness with which executives have analyzed their problems and the validity of their proposed solutions.

After questioning, the board confirms the tentative decisions which

[12] John C. Baker, *Directors and Their Functions* (Boston: Division of Research, Graduate School of Business Administration, Harvard University, 1945), p. 16.

the executives have made. This confirmation results not only in approval but also in authentication and validation as the official acts of the corporation, itself. If executives are competent and worthy of the authority delegated to them, it is rare that their recommendations will not be confirmed by the board, though usually with many suggestions as to vital aspects.

The criticism is often made that this customary procedure reduces the board of directors to a "rubber stamp." This charge is not necessarily true. Effective directors, because of their knowledge, experience, and sober judgment, can, and do, ask discerning questions about the issues involved. Because the executives under the jurisdiction of the board realize that their proposals may be subjected to vigorous questioning, they will support their recommendations with adequate and thoroughgoing diagnosis and planning. They will anticipate questions in advance of their being asked, and prepare answers for these questions that can be defended in the interest of their company.

At this point, most boards of directors demonstrate their effectiveness, or ineffectiveness, in the management process. As indicated previously, the members of the board are, usually and properly, separated from the operations of the concern. Therefore, the significant contribution a board member is expected to make is an independent viewpoint. He cannot have personal knowledge of the details of the management of the business, but he can weigh evidence and ask searching questions that may reveal "blind spots" in the proposals which he has been asked to approve.

Courts of law have generally held that a corporation is ordinarily bound only by the resolutions adopted by the board of directors at a legally called meeting at which a quorum of the directors is present. Therefore, many actions, most of which board members could not have initiated because of insufficient time and inadequate knowledge, have to be taken at such meetings. Hence, by adopting the procedure of confirmation, after scrutiny by discerning questions, directors do not get involved in making the decisions that are rightly the responsibility of the executive personnel. Thus directors keep themselves out of operating management, and thereby afford themselves a better opportunity to focus their attention on major policies and objectives.

Acts of Counseling

To "counsel" means "to advise and to give aid in making decisions." Used in connection with the procedures of a board of directors, such counsel usually consists of informal conferences between directors and executives. No formal actions or commitments on the part of the board are involved. Rather, it is a method of exploration which is employed in the initial stages of policy formation. It is a process by means of which

the top executives of a concern may discuss important questions with board members for the purpose of securing the latter's reactions and points of view. Counsel precedes acts of confirmation; and good counsel may actually strengthen policies which are adopted later because the result of preliminary conferences is often a refinement of contemplated proposals which are subsequently brought to the board for approval. Should there exist an element of uncertainty as to the confirmation of a particular issue by the board, the danger of embarrassment, because of disapproval, can often be avoided by securing the counsel of board members before a formal presentation of the matter is made.

Examples of the application of this procedure are considerations which affect expansion of the plant; development of new products; extension of markets; preparation or revision of budgets; sanction of operating results; negotiations concerning labor contracts; and changes in executive personnel, especially new appointments, reassignments, and promotions. When such changes and ventures are contemplated, it is often advantageous for responsible executives to secure the advice of influential directors, whether such counsel be encouragement or caution.

Acts of Review

In order to discharge the broad obligations of guidance and trusteeship effectively, it is necessary that the members of a board of directors keep abreast of executive acts and company affairs. This duty is performed by the review of reports and the inspection of the plant and other facilities. Personal inspections are generally both inconvenient and infrequent. Therefore, written reports, statements, and summaries are the most effective means of apprizing board members of the condition and progress of their company. These documents may vary as to form, purpose, and frequency; but they serve to keep directors informed about company operations. By receiving these reports, the board tacitly approves or, at least, accepts the acts of the executives who supply them.

These data may be furnished to the directors in the form of letters, typed and duplicated reports, or formal printed statements as the occasion may require. Their purpose may be of a general informative character, or they may deal with specific problems to which special attention is directed. These data are not all used with the same frequency; sometimes they serve as interim reports between board meetings, and sometimes they are prepared for presentation at regular board meetings to supplement or explain the agenda which have been set up for consideration and action.

The wide range of subjects and purposes covered by reports to boards of directors is illustrated by the following groups into which they may be classified:

1. The board receives legal documents for its consideration and, in many cases, for its approval in the name of the business. These documents vary from routine contracts to problems of vital importance. The board is frequently called upon to make decisions as to the advisable and legal policy to follow.

2. The board receives many statistical and accounting reports, ranging from routine statements of the current financial and operative situation, to exhaustive studies of trends and analysis of deviations from instructions. The board of directors knows about the business for which it is responsible through analysis of financial and production records of this sort rather than by direct contact.

3. The board receives many reports which apply particular ascertainable facts to current and future business situations. If the business operates a mine, it receives reports concerning the amount and quality of ore in reserve and the cost of mining. If the board of directors considers purchase of a newly invented device, it receives reports of its engineering merits and defects. If a downtown store is operated, studies are made as to the shifting of retail patronage from downtown toward uptown locations. If unions demand a wage increase because of rising costs of living, economic index numbers will be consulted. Usually such semiscientific research is clothed with its practical application.

A Summary of Procedures

In the report on directors and their functions, already referred to, President Baker has summarized typical board procedures. This summary is reproduced in Figure 15.[13]

LIABILITIES OF DIRECTORS

Directors not only have authority; they also have liabilities. Many of these liabilities hinge upon the honesty and fair dealing of each individual director. Even though the board, as a committee, represents the corporation, and no member of the board acts for himself, every director is personally liable for the abuse of the powers granted to him. As has already been emphasized, directors are placed in a position of trust in the highest level of the management of an enterprise. As such, they are required to exercise the same care over the property and other interests of the business as a prudent man would exercise over his personal property. Therefore, directors are prohibited by law from engaging in many acts which might properly come under the head of manipulation. Specifically, some of these acts may be enumerated as follows:

Speculation

A director may not engage in speculation in the stock of the corporation which he represents. It is recognized that the position he occupies affords a chance for "inside information" not available to the shareholders

[13] *Ibid.*, p. 18.

or the public. If it can be proved that by manipulation of funds and records a director has secured advantages to himself at the expense of the corporation or its stockholders, he is subject to severe penalties.

Transfer of Corporate Property

Directors may not transfer corporate property to themselves, to stockholders, or to others for the purpose of defrauding creditors in the event the business appears to be insolvent.

Problems	Methods Used by Directors		
	In Most Companies	In Many Companies	In Few Companies
Selection of president—his remuneration (and removal)	Decide		
Nomination of directors	Decide		
Changes in capital structure	Decide		
Capital budget or expenditures	Decide	Confirm	
Selection of outside auditors	Decide	Confirm	
Determination of dividends	Decide	Confirm	
Selection and remuneration of other executives	Confirm	Decide	
Formation of postwar plans	Counsel	Confirm	Decide
Formation of major policies in production, marketing, finance, and personnel	Counsel	Confirm	Decide
Addition of new products	Review	Counsel	Confirm
Preparation of operating budget	Review	Counsel	Confirm
Union negotiations and settlement	Review	Counsel	Confirm
Reports on competitive position and operating results		Review	Counsel
Decisions on detailed advertising program			Review

Fig. 15.—Methods used by directors in different companies to deal with illustrative problems. From John C. Baker, *Directors and Their Functions* (Boston: Division of Research, Graduate School of Business Administration, Harvard University, 1945).

False Financial Statements

Under the Securities Exchange Act, directors are liable for false statements of the financial condition of their corporation and for the omission of any material fact in the registration of its securities.

Illegal Dividends

Directors may not declare illegal dividends. "Illegal dividends" are usually construed to mean those which are paid out of capital rather than out of earnings. The payment of such dividends would result in the impairment of assets to the detriment of both owners and creditors.

Illegal Lending of Corporation Funds

Directors may not lend the funds of a corporation to the members of the board or to the stockholders. This prohibition is also intended to

prevent preferment and undue advantage for those intimately connected with the enterprise.

Personal Liability

Each director is personally liable for any act of the board of directors, representing the corporation or in the name of the company, which is specifically prohibited by law. In other words, a director may not plead personal immunity from the effects of a law which prohibits a corporation from engaging in certain acts. As was pointed out previously, a corporation can act only through its board of directors. While it is true that legally both the corporation and each director are recognized as separate and distinct persons, nevertheless, in his official capacity as spokesman and sponsor of the corporation, a director cannot divest himself of his moral and lawful responsibilities.

Stock Watering

Directors are also prohibited from engaging in certain types of excesses, such as stock watering and gross overvaluation of assets, selling corporate property at excessive valuation, and gross mismanagement. For example, if it can be established that, by word and deed, the directors are personally responsible for causes which lead to the failure of a business, they may be held accountable to those who thereby suffer injury.

CRITICISMS OF THE BOARD OF DIRECTORS

In recent years, there has been a widespread tendency to criticize the device of the board of directors as an inadequate instrument of power in business management. For example, a businessman of prominence has written:

> It is a vestigial remain of a time when investors paid attention to their businesses and when offensive and defensive alliances in business were the order of the day. The most that can be said for the board of directors as it exists today is that it provides an arena in which the ablest, most powerful, and most persistent members of the board can generally have their way. Such men have the traits that make business successful, and their survival in the shifting locus of power in a company means that they survive not only for their own good but for the good of the company, too. The board of directors tends to screen the fit from the unfit, and to that extent to provide the rule of the fit for the conduct of the business.[14]

Early Criticism by Adam Smith

This criticism recalls an attitude and a point of view that has had a long tradition. In dealing with this subject, Adam Smith, in his *Wealth of Nations* published in 1776, made the following observations:

[14] Ruml, *op. cit.*, pp. 83–84.

The trade of a joint stock company is always managed by a court of directors. This court, indeed, is frequently subject, in many respects, to the control of a general court of proprietors. But the greater part of those proprietors seldom pretend to understand anything of the business of the company; and when the spirit of faction happens not to prevail among them, give themselves no trouble about it, but receive contentedly such half-yearly or yearly dividend as the directors think proper to make them. This total exemption from trouble and from risk, beyond a limited sum, encourages many people. . . . Such companies, therefore, commonly draw to themselves much greater stocks than any private copartnery can boast of. . . . The directors of such companies, however, being the managers rather of other people's money than of their own, it cannot well be expected that they should watch over it with the same anxious vigilance with which the partners in a private copartnery frequently watch over their own. . . . Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company. It is upon this account that joint stock companies for foreign trade have seldom been able to maintain the competition against private adventurers. . . .

The only trades which it seems possible for a joint stock company to carry on successfully, without an exclusive privilege, are those of which all operations are capable of being reduced to what is called a routine, or to such uniformity of method as admits little or no variation. Of this kind is, first, the banking trade; secondly, the trade of insurance from fire, and from sea risk and capture in time of war; thirdly, trade of making and maintaining a navigable cut or canal; and fourthly, the similar trade of bringing water for the supply of a great city. . . . To establish a joint stock company . . . merely because such a company might be capable of managing it successfully . . . would certainly not be reasonable. . . . First it ought to appear with the clearest evidence, that the undertaking is of greater and more general utility than the greater part of common trades; and secondly, that it requires a greater capital than can easily be collected into a private copartnery. In the four trades above mentioned, both these circumstances concur. . . .

The joint stock companies, which are established for the public-spirited purpose of promoting some particular manufacture, over and above managing their own affairs, . . . can in other respects scarce ever fail to do more harm than good. Notwithstanding the most upright intentions, the avoidable partiality of their directors to particular branches of the manufacture . . . necessarily breaks, more or less, that natural proportion which would otherwise establish itself between judicious industry and profit. . . .[15]

Criticism by Veblen

The oft-quoted work of Veblen, *The Theory of Business Enterprise*, written nearly one hundred and fifty years after the classic of Adam Smith appeared, takes the same critical position with regard to the management of business corporations in the United States.[16] In it, the general

[15] Adam Smith, *Wealth of Nations*, pp. 586–87, 598–99, and 600.

[16] Thorstein Veblen, *The Theory of Business Enterprise* (New York: Chas. Scribner's Sons, 1921), p. 159.

argument is that, since the connection of the members of a board of directors with the firm is not permanent, the best interests of the business are commonly dissociated from the private interests of the directors themselves. It is pointed out that the motives of personal acquisitiveness are opposed to the long-run success of the concern and that the members of the directorate can make more for themselves by manipulating the company's stock than by relying upon ordinary profits.

It would be fatuous to hold that such manipulation has not, at one time or another, occurred, but the bulk of the examples cited in support of this assertion are taken from the past and not the present. To draw conclusions on this basis is about as valid as to reason that, because buccaneering was once profitable on the high seas, shipping masters still find it advantageous to engage in piracy rather than to serve their companies honestly in the maritime transport of goods. It is true that there seems to be historical evidence that a few freebooters accumulated vast riches, perhaps to be buried somewhere on an unknown isle. But as governments became stronger and the demand for safety and assurance in international trade became more insistent, the pursuits of the buccaneer lost both allurement and profit.

The same may be said with respect to the manipulator of the securities of a corporation. His career would hold little promise of success today. Not only are the moral standards of businessmen generally higher than they were in previous generations; but by reason of legal restrictions and regulations evidenced by such laws as the Securities Exchange Act, irregularities in the management of a corporation's financial affairs, on the part of the members of the board of directors are uninviting, to say the least. Under modern conditions it is becoming an absurdity to argue that the directorate of a corporation can foist upon an unsuspecting public a putative earning capacity at variance with actual experience with respect to profits and losses.

Alleged Defects of Committee Management

Aside from charges of dishonesty, corruption, and manipulation, much is written and said today about the alleged inherent defects of the plural executive, or management committee. It is urged that a committee delays executive decisions by its debates and political intrigues; that it frequently reverses itself; that it kills the initiative of its salaried executives through its criticisms and bickerings; and that it wastes time on details. It is pointed out that a top committee may lose all sense of responsibility—except to itself—and that it may become honorary through the inheritance process and thus lose all direct contact with the business it controls. These disadvantages are of exceptional character and grow out of the defects in human nature.

Nevertheless, at the highest management level of a business enterprise the use of the committee, as the organization device, has become almost universal. It is difficult to visualize a method of organization of business enterprise that does not have at its head a highest management level of the committee type. A business enterprise is itself a group, consisting of workers and executives. A group of executives, in any particular business, succeeds or fails in ratio to the success of its group-thinking. The board of directors is logically a committee which represents the best of the group-thinking and skill available at this highest management level.

It is possible for the board of directors of a corporation to degenerate into a club of rich descendants of the founders, a group detached from the business as a whole, paying no attention to the business beyond the declaration of dividends and the re-election of the president of the company, who manages the entire business. The typical business enterprise could not be so organized for very long because of the quickly resulting deficits. Actually, membership on most boards is more of a responsibility than an honor. Board members, in return for the small director's fee for each meeting attended, must keep in touch with the business as a whole and be prepared to make decisions that determine future profits or losses.

A New Ethical Concept of Board Membership

A new ethical concept concerning board members has developed because of the lessening importance of stock ownership as a reason for membership. Formerly the board of directors, composed entirely of principal stockholders, could make decisions as to what they desired to do with their property without regard for others. Under present conditions, however, board members must constantly decide what is to be done with other people's property as well as with their own. This situation involves the ethical and legal responsibility of trusteeship and the necessity for board members to give closer, more efficient attention to the problems and needs of their business enterprise.

As the following quotation from President Baker's analysis indicates, much remains to be done if the board of directors is to maintain and develop its natural position at the top of the management hierarchy:

> To assume that responsibilities of directors have remained the same as they were two decades ago or that they have decreased is to ignore history and the economic development of this country. If there ever was any doubt of the importance of directors or the latent possibilities of their contributions to corporate and social welfare, it should have been dispelled by events occurring during the last decade. Directors are one of the important keys to the solution of present-day social and economic problems, and it is no exaggeration to state that national welfare, even political security and liberty, may well depend on

some of their decisions concerning such matters as products, expansion, and employment.

The essential concern of corporation directors, particularly in our large corporations, is not today, nor should it ever have been, merely protection of stockholders and their interests. These functions are simply more in evidence than others. The problem is vastly more important. It is the reconciliation of private enterprise with the smooth functioning of a democratic society with justice to all groups: stockholders, executives, employees, creditors, customers, and the public. Such a broad concept of the functions of directors is frequently overlooked. Nevertheless, this should be the contribution of directors in our national life.[17]

QUESTIONS

1. In the text of this chapter there is this statement, "Neither in modern theory nor in practice is it assumed that the board (of directors) will attempt to direct the affairs of a business in any detail." Expand upon this statement from the following standpoints:
   a) The change in the relationship of the board of directors to business details as a concern increases in size.
   b) The evidence of an evolutionary trend during the last century in the relationship of boards of directors to their respective enterprises.
2. Assume that a meeting of the stockholders of a successful locally owned business corporation is in progress in which the business in hand is the election of directors. Nominations for board membership have been made, and you are to second, or oppose their election, with concise but adequate reasoning respecting the following described persons:
   a) A local bank executive.
   b) The president of the local university.
   c) A substantial resident of the town, but one who owns not to exceed 3 per cent of the common stock of the corporation.
   d) The general manager of one of the factories owned by the corporation.
   e) A man who is recognized as one of the more important customers of the corporation.
3. Assume that you are a member of the board of directors of a certain business corporation. As such, express your opinions on the function of trusteeship in the following typical situations:
   a) A decision to declare dividends out of current earnings.
   b) A decision to declare dividends out of the past earnings that have been set aside as surplus, even though current operations are being conducted at a loss.
   c) A decision to declare dividends out of capital since there are neither

[17] Baker, *op. cit.*, p. 138.

surplus nor profits and since the company has always operated at a loss.

d) A refusal to declare dividends even though the company has always made a profit and is currently earning more than enough to cover satisfactory returns to stockholders.

4. Set up your own list of the activities of a typical board of directors of a business concern by combining, or adding to, all of the following analyses given in this chapter:
   a) The procedures described in Figure 15.
   b) The summary of functions as indicated by J. O. McKinsey, shown on pages 118–19.
   c) The analysis of the authority of directors shown in the classification on page 117.
5. Make a list of regular and special committees that you believe should be created within the theoretical board of directors of a medium-sized business corporation. Take into account the following problems, and give adequate reasons for the committee service you propose:
   a) The personnel problems involved in the handling and settlement of labor strikes.
   b) A procedure for reviewing and determining the compensation of company executives.
   c) The responsibilities of the board of directors in matters of plant location and construction.
6. Prepare an analysis of the limitations that have been imposed, or that may be imposed, upon the powers of the typical corporate board of directors in the management of a business with respect to the following:
   a) Limitations inherent in incorporation laws.
   b) Limitations inherent in governmental power to tax and to regulate.
   c) Limitations that result from custom and experience, but which are not imposed by law.
7. Distinguish clearly between the "profit objective" and the "occupational objective," and apply your explanation to the following examples:
   a) A bankrupt railroad that is required by law to continue in operation even though it is unable to earn a profit.
   b) A department store that has gone heavily into debt in order to install escalators and air conditioning equipment.
8. The procedures of the board of directors include acts of decision, confirmation, counseling, and review. Explain the relationship of the function of policy formulation to each of these acts, and present your own illustrations of policy formulation within each procedural group.
9. Explain the problems that are inherent in determining and giving effect to the liability of a director in the following situations:

a) The board approves the purchase of large quantities of raw materials. Some months later there is a severe drop in the market price of these materials and the finished product, with the result that the company suffers heavy losses.

b) By a majority vote, the board approves an increase in the number of shares of stock of the company, with the full knowledge that certain members of the board intend to take advantage of this issue for their own personal gain through stock market manipulations.

c) By a majority vote, the board approves an increase in the number of shares of stock of the company, and, then, secretly and without the knowledge of all of the directors, certain members of the board use this issue of stock for their own personal gain through stock market manipulations.

10. Concisely, but adequately, summarize the criticisms of boards of directors by Ruml, Smith, and Veblen. If you believe that the corporate form of business organization is necessary in our modern economy, then defend the method of committee management at its highest managerial level. If you feel that the corporate form of organization is obsolete—or for some other reason undesirable and unnecessary—and that it can and should be replaced, then explain what, in your opinion, should be substituted for it, and whether the committee form of top management should be abolished or retained. (Note that this question is based on the assumption that the system of private enterprise in business management is to be continued.)

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Chapter VI

THE EXECUTIVE LEVEL OF MANAGEMENT

IN THE explanation of the levels theory of organization (Chap. IV), it was shown that stratification is the characteristic feature of the architecture of organization for management. A business organization, to be efficient and effective, must be a logical structure. That is to say, it must have a top as well as a base, with the intermediate units of management in between. That is why a pyramid, usually drawn in two dimensions (Fig. 3, Chap. II), instead of the more accurate form of three dimensions, is commonly considered the best graphical illustration of a business organization.

It has been further shown that the acts of management proceed from certain allocations of authority and responsibility and that orderly performance requires a system of transmission of authority by a process of delegation. To be purposeful, such transmission implies both origin and destination. As in an electrical power system, a central power plant from which energy flows over transmission lines must be provided, but the work to be performed is not at the place where the turbines and generators, for example, are located.

So, also, in organization for management, the energy of authority issues from a center of power, namely, the board of directors at the top. It is the legislative or rule-making body; but like any other legislative group, its laws, rules, or policies—by whatever name the product of its deliberations may be called—are of no significance unless and until they are enforced. It is for this purpose that the executive level is established in the organization structure.

ELEMENTS OF THE EXECUTIVE LEVEL

In its verb form, "to execute" means "to perform or to do what is required to achieve objectives according to predetermined plans." Hence, an "executive" is one who achieves; but as the term is used in the language of management, he is a "person who is responsible for the work performed by others." He must necessarily have the qualities of leadership explained in Chapter II, and he must also have authority commensurate with his responsibilities.

The Chief Executive

The first element of the executive level is the top or chief executive. All executive work in any type or size of organization must head up in one person. In a business organization, he is generally known as the president or general manager, or by the combined title of these two terms. He stands between the directors above him and his subordinate officers and employees below him. He must not only interpret the major policies and objectives determined by the board to persons lower in rank, but he is, at the same time, the medium through which flow orders and directives designed to carry out the policies and achieve the objectives of the business. In a sense, he is the main center of communication within the organization, because often the chief executive is the only one who represents management to the governing board and the governing board to the management.

In most of the affairs of a concern, the chief executive is the boss. By working through his subordinates, he sees to it that the things that have to be done are accomplished. Except in matters specifically restricted by public laws or the bylaws of the corporation, his position permits him to exercise authority over all aspects of the business. Beyond this authority the president of a company generally recommends to the board of directors those things which he thinks it should do. Directors very commonly recognize presidential recommendations that require only routine confirmation by them. Should such a matter encounter an irreconcilable difference of opinion by a majority of the board, the resulting reversal, or disapproval, of the president's recommendation might be regarded as a "vote of no confidence." Resignation of the president would follow as a matter of course.

In a small business, the top executive can know much about the details of management and operations. His personal span of control is adequate to his task. The larger the business the more impracticable it is for one person to attempt to comprehend and decide, on his own initiative, all of the problems of the entire concern. It follows that one of the natural results of increased size is that the president seeks to surround himself with a number of diverse experts through whom he can maintain his grasp of the complex affairs of his business.

Major Executives

The second element of the executive level is, therefore, composed of the higher, or major, executives. These are the topmost management individuals directly accountable to the chief executive. They provide the active management of the major divisions or departments of the business within the scope of the authority delegated to them. They are designated

by various titles, such as vice-presidents, department managers, and directors. When the title of "director" of some division of the organization of a business is used, the designation does not imply that the position carries with it membership on the board of directors of the company. These variously titled officers head up operating departments, such as production, sales, purchasing, accounting, and others, depending upon the type of business they serve. As such, they have line authority within the limitations of their specialties. In small concerns, this executive group is usually limited to such operating heads. As companies increase in size, other executives of coordinate rank are included in this level. They may be staff officers who have special advisory authority in designated areas of the management, such as research, engineering, planning, and other fields.

Whatever may be the nature of the assignment to a particular major executive, it is essential that it be a logical and distinctive part of the whole concern. Unless a reasonably clear-cut definition is provided, effective management fails from the standpoint of both direction and control. A responsible and efficient executive must be able to have a clear conception of his functions, the objectives of his company, and his proper relationships to other members of the executive personnel. Moreover, since records and reports of performance are transmitted upward to them, and from these highest managers to the chief executive at the top, limitation of such topmost organization to major functions of the business permits unrestricted flow of communication through natural managerial channels.

The number of major executives that constitute this highest level of management varies widely, depending upon the size and the character of the company, as well as upon the type of individual persons who comprise its personnel. In small concerns, there may be at this level as few as four executives—department heads in charge of such functions as manufacturing, marketing, purchasing, and financial activities. At the other extreme, but equally well organized, is a large corporation like Swift & Company, which has fourteen executives reporting directly to the president. Obviously, in the latter case, were it not for the fact that the individuals who occupy their respective positions in the organization are of exceptionally high quality as executives, the demands upon the president for maintaining effective contact with them would overburden him. Because of the limitations of an individual's span of control, it is generally considered to be good management to limit the number of subordinates reporting to a single executive to a few persons in order that each one may receive from his superior officer the attention that he deserves. It is an evidence of faulty organization when an immediately subordinate executive cannot have reasonably free access to his superior on all matters of mutual concern in the interest of the management and success of the enterprise.

Staff Executives

An important part of the major executive level is the "staff" or "facilitative" phase of the organization. Generally, the group of staff executives in a business consists of fewer individuals than the operating group, but it is, for that reason, no less important. As the management process increases in complexity, the spans of time, energy, and knowledge of a single executive become inadequate. He must, therefore, strengthen his position, as well as his organization, by adding staff agencies to furnish specialized assistance and advice. Staff individuals or departments do not create new functional organization problems except as the top executive may thereby overstrain his spans of control, knowledge, and time by serving as a clearing house for managerial details of a functional type.

Staff executives have no power to command, but only the power to investigate and recommend. They aid in formulating and enforcing policies, including certain tactical, strategic, and skillful derivatives which determine the direction and intensity of effort. Policy-making is part of the background of staff work. It helps to make the leadership of the chief executive effective among divisional and operating executives. Staff executives would not be fulfilling their full responsibility if they contented themselves with the formulation of policy and took no interest in making that policy effective. Therefore, another of their duties is the task of evaluating and improving the work done by other executives.

In army organization the use of staff officers is an established practice. In military language, its purpose is as follows:

> The staff is an aid to command. It is provided to relieve the commander of details by providing basic information and technical advice by which he may arrive at decisions; by developing the basic decision into adequate plans, translating plans into orders, and transmitting them to subordinate leaders; by insuring compliance of these orders by constructive inspection and observation for the commander; by keeping the commander informed of everything he ought to know; by anticipating future needs and drafting tentative plans to meet them; and by supplementing the commander's efforts to secure unity of action throughout the command.[1]

Full-Time and Temporary Executives

Major executives are usually full-time officers of a company. Their job is to see that the operating departments are kept going. In large concerns the staff executives are also full-time and have no other assignments

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[1] *The Officer's Guide* (9th ed.; Harrisburg, Pa.: Military Service Publishing Co., 1942), p. 295.

or duties. For example, some businesses may employ economists to analyze and forecast business trends. Some have specialists engaged in electrical or metallurgical research. Sometimes personnel executives, safety and methods engineers, and even corporation attorneys are given no authority beyond investigation and recommendation, thereby putting them on a true staff basis.

Sometimes operating executives have staff duties assigned to them. When this is done, it is usually on a part-time, temporary basis. For instance, a sales manager may be asked to investigate the skill and qualifications of a warehouseman or a branch manager as an incidental task when he visits a division of the business situated in a distant city. The treasurer of the company may be called upon to make analyses and report findings upon the financial advisability of buying certain raw materials. The purchasing agent may be instructed, when attending a convention, to interview a prospective candidate for executive employment in another part of the business. All of these tasks, and many others like them, are essentially staff work, since they involve only investigation, reports, and recommendations.

Outside Staff Services

There is another type of staff work often of considerable importance to business concerns. Since it is performed by persons not regular company executives, it may not be technically proper to include them in the executive level. Yet, at least in businesses too small to maintain full-time staff organizations, they play an important role in management.

For example, a company which sells office or factory machinery may offer to install the machinery and train employees to operate it efficiently. An inventor may ask for the manufacture and sale of his invention. A real estate broker may ask permission to review all rented property in order to recommend savings in rentals by using property under his control. A salesman may make a survey and write a report showing that his product would result in better quality or lower cost. Obviously, the number of suggestions and recommendations made by such volunteer staff members is large. Consideration and decisions concerning each of these many ideas is one of the important tasks of management, especially since the recommendations are likely to be tinged with prejudice.

Another, and in some respects a more important, source of outside staff services is the consultant. The "consultant" is an "expert who offers his services to business management." If he is accepted and employed on a retainer or per diem fee basis, the consultant acquires, in an almost perfect manner, the position and relationship of a staff executive in the organization. He is independent of internal politics. Since he is not a full-time executive himself, there need be no fear of his usurping authority of

other executives. He does not have the prejudicial self-interest of a salesman, or of an inventor, who might volunteer his services without fee. If he is a reputable consultant, he is bound by ethical considerations to serve his client well and faithfully. His experience facilitates his investigations, and his reputation increases the ease with which his recommendations are accepted by operating executives.

Regardless of the method, or lack of method, used to provide staff services, they serve a useful purpose in the management of a business. The increasing technical complexities of business require staff investigations and recommendations, even in small concerns. But as the size of a company increases, the development of a formal staff executive organization is required.

The Selection of Executives

A major executive activity is the selection of personnel. As we have seen, it is the duty of the board of directors to appoint the chief executive, who, in turn, is charged with the responsibility of selecting his own immediate subordinates. He chooses them either by full authority delegated to him or subject only to confirmation by the board. Vested with such authority, one of his basic problems is whether to pick weak or strong subordinate executives.

The terms "weak" and "strong" are used here in a colloquial sense to indicate the "degree of dependence upon the top executive." In this sense, a "weak" executive is one who leans upon his superior officer for advice and guidance. He does not assume responsibility or authority except as determined by the man above him. The weak executive may be very successful as long as this relationship continues; but whenever it ends—for instance, when a new chief executive is selected—the inability of the subordinate to stand on his own feet becomes serious.

It is a natural human trait for a competent executive to choose subordinates who will lean on him. Under modern business conditions, this is a bad practice because it leads to instability in both organization and operation. It does not relieve any of the strain upon the span of control and the span of knowledge which is required of the top executive, but instead it increases his burdens until they become too great for him to bear. A common and recurring criticism of many otherwise strong business leaders is that they have surrounded themselves with high-salaried "yes-men" who do no independent thinking but who always try to make the decisions that will please the "big boss." Executive groups, so organized, face inevitable reorganization if the particular enterprise is to survive beyond the time when the dominating executive will be replaced.

Weakness in executive selection also results from failure to fill vital gaps in the management organization. In such cases the weakness is not in

degree of delegation of authority and responsibility but in organization architecture.

Defects in the pattern of an organization will cause the level at which certain policies are decided to be shifted both upward and downward as a matter of expediency rather than logic. For example, before purchasing came to be recognized as a specialized function of management worthy of separate departmental status, it was decentralized and scattered among various groups and executives. This practice left a gap in the management structure. Since no framework had been erected to carry this important activity, its load was shifted to various levels, and diverse executives were charged with the responsibility of making uncoordinated purchasing decisions. The purchase of the most important commodities was commonly shifted upward to the president or general manager, or to divisional executives, thereby imposing an added burden on them. The purchase of less important items was shifted downward to foremen or chief clerks, thereby requiring them to make decisions for which they were ill-fitted. This sort of organizational error is corrected in modern management, and the responsibility of procurement is centered in a purchasing agent, who may be either a functional or a staff executive, but, in either case, he is an expert in the complicated field of buying.

Since the purpose of business organization is to secure efficient and profitable operation, the proper selection of executives and the clear definition of their duties are matters of paramount importance to management. The ideal executive is one whose specialized work is needed, who is highly competent, who is "strong" in the sense of standing on his own feet, and yet who is a genuinely cooperative member of the executive group as a whole.

There is conviction among business executives that theoretical perfection of organization is unimportant as compared with the selection of the right executive personnel. This attitude is apparently justified by the fact that relations between major executives and their top management, while appearing to be highly complex on paper, can, in fact, be thoroughly practical and efficient. Therefore, too much emphasis should not be laid upon a precisely charted organization pattern, but rather upon a plan which is workable in its practical application to a particular business and yet which does not violate sound and tested executive relationships and requirements.

CLASSIFICATION OF EXECUTIVE ACTIVITIES

In general terms, the tasks of management may be divided into five major fields. These divisions may be called: policy management, executive personnel management, employee personnel management, operating management, and financial management. "Policy management" includes

the determination of objectives and the formulation of plans and procedures to achieve them. It includes executive strategy and the enforcement of policies designed to accomplish efficient and profitable operation.

"Executive personnel management" has to do with the selection of major and minor officials and the determination of the organization architecture, in general and in detail. Not only must such persons be selected, but they must be assigned to various functions and duties, and their activities coordinated. It is in this area that specializing the work of management is in greatest evidence. Similarly, employee personnel management involves the selection, assignment, training, compensation, and promotion of workers, as distinguished from executives. External regulations affecting labor relations, such as negotiations with unions and governmental agencies, have forced much of this field of personnel management—even to details—into the scope of duties of higher executives.

"Operating management" is concerned with the problems of the production and sale of the products or services of the business. Among other things, attention must be given to the procurement of raw materials for manufacture of goods for resale. Plant equipment must be supplied, erected, and maintained, and costs of operation must be kept within prescribed limits. Customers' claims and complaints must be looked after, and trade relations with other businesses sustained through such means as trade associations and conventions.

"Financial management" assumes responsibility for contracting the funded debt and for the allocation of company investments and surpluses. Included in its scope are accounting and budgetary control.

Each of these five major fields of management may be divided into three subgroups. First, there are activities of primary importance to ownership, which tend to be performed in detail by the board of directors or under its immediate supervision. Second, there are management problems peculiarly coordinative in character. Finally, there are executive activities—more or less routine in their nature—which are called "direction and control" if performed by major executives and "supervision" if performed by minor executives.

A schematic arrangement of the tasks of management, as described thus far, is presented in Figure 16. It should be read both vertically and horizontally. When reading the columns from left to right, the first one lists the five major fields into which management activities fall. The second column indicates the phases of these activities which are a primary concern to ownership and, therefore, the immediate responsibility of the board of directors. In the third column are found those activities that are assigned to the major executives and can not usually be delegated to subordinates. The last column contains a list of activities for which departmental executives are generally responsible. When the chart is read

horizontally, that is, by levels, each level indicates a major executive activity and the three subgroups of activities into which it may be divided.

It should be noted, however, that in the daily routine of actual business affairs, the work of management does not fall so readily into compartments as this chart seems to indicate. As has been explained elsewhere, border lines which describe analytical concepts, especially in business

Field of Management	Ownership Activities	Coordination Activities	Direction and Control Activities
Objectives and policies:	Determine objectives and administrative policies	Coordinate objectives and all policies, including strategy and tactics	Determine departmental policies, enforce all policies, and accomplish efficient operation
Executive personnel:	Select major executives and determine general organization structure	Coordinate staff, functional, and line executives	Select minor executives and determine detailed organization
Employee personnel:	Determine basic working conditions	Join in collective bargaining, adjust employee complaints, and coordinate personnel with operation and finance	Selection, training, transfer, promotion, protection, and compensation of individual workers
Operation:	Make all basic operating and selling decisions	Join in trade association discussions, adjust customer complaints, and coordinate operating departments	Efficient production, inspection, advertising, sales of, and collection for, individual products or services
Finance:	Pass upon all important financial problems	Coordination, or budget control, of income and expense	Preparation and analysis of audits, accounting reports, and financial statements

Fig. 16.—Classification of management tasks. (This chart should be read both up and down and from left to right.)

organization, are not boundaries beyond which one group may not go without violating the prerogatives of another. Rather, such demarcations are like the imaginary lines on a baseball diamond which designate each player's position and the ground he normally covers. When the game is on, to win the contest is each man's main purpose. In its accomplishment, naturally he must play his own position ably and fully; but in an emergency, the shortstop, for example, does not hesitate to cover second base when a play calls that baseman out of position; nor does the center fielder let a ball go by if he can get it, even though he ends up in left field when

the catch is made. Positions in baseball, as in management, have been developed in order to take advantage of human specialization. Field designations have been made to avoid interference between players. Yet, as the game is played, it is not nine individual men against nine individual competitors; it is team against team, which is a way of describing coordination in action.

THE SCOPE OF EXECUTIVE ACTIVITIES

In order to understand fully the scope of executive activities, it is necessary to examine the interests affected by them and to see how the obligations of authority and responsibility, thus implied, are allocated to the various executives. Referring again to Figure 16, it is seen that first in order are the management activities which are of primary significance to ownership. As was explained in Chapter V, such activities are usually performed, even to details, by the board of directors. They lie outside and above the level of the executives of the business.

Personnel Activities

In the organization of the executive personnel it is the exclusive duty of the board of directors to select the chief executive of the company. As was pointed out previously, other members of the executive group may be chosen outright by the chief executive, or their appointment may be subject to the confirmation of the board. While the titles of these latter individuals may vary in different firms, such major executives usually include the sales manager, the production manager, and the financial manager. By the selection and appointment of such officials, the broad outlines of the executive organization are determined.

The selection of minor executives and the routines of employee management are distinctly the concerns of the responsible officers of a company. Upon their shoulders fall the responsibilities of securing, training, and promoting employees of various grades and assignments, and fitting them into their proper places in the organization. It is the job of executives to provide compensation for employees, including collective bargaining and contracts with labor unions. In addition, they must hear and adjust grievances, determine working conditions, and arrange for insurance, retirement, and pension plans.

Financial and Operational Activities

The board of directors, in its official capacity, must perform all important acts pertaining to financial management. In the whole scheme of business management, the board has retained more detailed control over financial management than over any other managerial activity. The reason

for this traditional policy is not hard to find, because the control of the purse is ownership's natural way to control the business. After general financial policies have once been formulated, and budgets and other procedures have been determined, the executives receive, expend, and account for the funds of the concern.

"Direction and control" is the executive process of issuing orders and then following them up to make sure they are promptly and properly executed. Orders vary in type, origin, and points of execution. As we have seen, the basic objectives and major policies are expressions of the will of the board of directors. They are translated into plans and orders by the higher executives. It is their responsibility to see that these directions or orders are universally understood and obeyed throughout the organization.

The particular current situation in which a business finds itself determines a large number of executive commands of a less basic nature. If, for example, a competitor is found to be engaged in price-cutting in a certain territory, to decide whether to meet the reduction or to withdraw from the depressed area is primarily the function of department heads. The daily flow of sales to be delivered, of production to be put through the factory, purchases initiated, credits allowed, and collections followed up —all of these details and many others require thousands of instructions. Someone must conceive the ideas and plans back of them. They must be reduced to orders of varying importance. They must be directed into proper channels for execution, and the results which follow must be inspected, recorded in most instances, and appraised. All of these activities require direction and control, which, when performed by minor executives such as supervisors, foremen, and chief clerks, are designated as "supervision and inspection" activities.

Coordination Activities

"Coordination" means "concurrence in purpose and performance to secure harmony in action toward a common end." Problems of coordination are found in all fields of management. In the field of policy management, there is the problem of coordinating the strategy of the moment with the basic objectives of the business. Suppose, for instance, that a basic policy of long standing provides that sales shall be made only through established wholesalers and that no other outlets for goods shall be sought or accepted. In the face of this policy, a current situation arises which unquestionably makes it desirable to sell a large order direct to a retailer. If such an opportunity is to be seized, obviously an established policy will have to be violated. It is a problem which must be solved by the major executives of the business, but in its solution there must be concurrence between purpose and performance. If the situation involves

only a single instance, its execution may be considered merely to be an exception to a general rule. If, however, the exception presents so many elements of advantage over previous practices that a change in the occupational objective seems imperative, then it becomes a matter for the board of directors to settle.

Executives are chosen, for the most part, to manage their specially assigned portion of a business. Exceptions are the top executive, or general manager, and certain major executives, the scope of whose jurisdiction is general in nature, as, for example, the vice-president in charge of operations. The coordination of the work of specialized executives is a constantly recurring phase of executive personnel management. For instance, the credit manager may refuse to approve the credit of an important customer believed by a salesman and the sales manager to be solvent and a good risk. Obviously, if a sale to such an individual or concern is to be consummated and future business relations are to be established, the credit and sales executives of the business will have to be coordinated or brought into agreement on the problem.

Management of employees is also subject to coordination. The personnel manager may sometimes reduce employee turn-over by studying and correcting the justifiable complaints of those who resign. Dissatisfaction and inefficiency may be minimized—if not entirely remedied—by eliminating misfits in the organization and by the coordination of employees with jobs. Similarly, in the field of operating management, balance is necessary. For example, the production department may desire to build up a large inventory in advance of sales. The sales department, on the other hand, may insist that such a policy is a mistake. In order to meet market fluctuations in price and quantity, it insists that the production department should provide itself with excess capacity rather than goods and thus be ready to produce quickly after orders have been received. It is conceivable that there could be merit in both contentions; but as long as they are contentions, operations are obstructed. Only coordinated effort can rectify a situation of this kind.

Financial management is affected in the same way. A common problem is the coordination of income and expense, known as "budgeting." A "budget," in the language of accounting, is "a plan for financing an enterprise during a definite period. It is prepared and submitted by a responsible executive to a representative body whose approval and authorization are necessary before the plan may be executed."[2] This definition itself implies that budgetary control is essentially a matter of balancing income and outgo in order that an enterprise may use its capital effectively and remain in a liquid position.

[2] W. A. Paton (ed), *Accountant's Handbook* (2d ed.: New York: Ronald Press Co., 1934), p. 1178.

Coordination a Distinctive Executive Task

Coordination emerges as the distinctive task of top management only when the business becomes too large to be controlled through personal leadership. There is no fixed point in growth at which this occurs. Rather there is a transitional zone, within which the two management methods overlap. Some of the rules-of-thumb that indicate the dividing line between management by personal leadership and management by systematic coordination may be suggested. When the number of important customers or employees exceeds a few hundred, it becomes impossible for top management to know everybody personally; hence the influence of personal leadership becomes diluted. Or, again, when the branch factories or important branch sales offices are more than a few miles apart, it becomes impossible for the minor executives and employees to fraternize. It is thus difficult for them to become an integrated group under their natural leader, that is, the top executive, or one of the major executives.

When the number who report directly to the top executive exceeds about ten, it becomes difficult for him to function as a personal leader. His development of special machinery of coordination shifts his own activity away from personal leadership. Likewise, when a supervisor or employee is required to obey two or more executives, it becomes impossible for the subordinate to recognize his leader without the aid of coordination devices. And in a business where practically no employee works without written instructions, personal leadership tends to disappear. In essence, therefore, coordination becomes the technique of top management in a large, or even in a medium-sized business simply because personal leadership has become impracticable.

Like the board of directors, the top executive has full responsibility for the success of every phase of the business. To be most effective, his authority must be equal to his responsibility. In practice, however, it is impossible for him to execute in person all of the details implied by his executive position. His personal span of control is too limited to permit him to be in touch with every detail of the business. His personal span of knowledge cannot possibly cover all phases of all business operations. He cannot be an expert accountant, production manager, sales manager, traffic manager, purchasing agent, and corporation attorney, all at the same time. As a result, his management activities at this top level of the business tend more and more to be limited to the tasks of coordination.

The interrelation between personal leadership and executive coordination varies between two extremes. If a business were organized like the theoretical army, with only line executives, personal leadership would be paramount. If, on the other hand, a business were organized like our national government, with only functional executives, executive coordina-

tion would predominate. This is true because perfect line organization assumes that all commands can originate at the very top of the organization. In any army, the highest general can give the order to go into action against a particular enemy position. His immediately subordinate executives then transmit the order to those next below, with necessary amplification as to details, and so on down to the enlisted men who perform the assigned task. It also assumes that the organization will be divided into similar units, such as regiments, and that the regiments will consist of a number of identical companies. This principle of uniformity of the units into which the perfect line organization must be divided is essential to permit interchangeability.

Two top executives, each in charge of his own large business enterprise, discussed at length their own duties. Their conclusion was that they were performing their own tasks best when they had nothing to do. They meant that their work consisted chiefly of coordinating the work of others. If this task were poorly done, many problems of coordination such as the settlement of disputes over policy, the selection of subordinate executives to fill gaps, and the adjustment of jurisdictional controversies between executives would arise. If this task were efficiently done, particularly with respect to plan and organization, the necessary coordination would be smooth and orderly. Therefore, there would be no current problems to occupy their minds. Each executive could busy himself with the problems of the future to the end that when the future became the present, his tasks would in turn be well coordinated. It has often been said of Andrew Carnegie that he preferred to manage his business from his estate in Scotland because nothing could be referred to him there. This anecdote illustrates the same point. Mr. Carnegie so regulated his business that the affairs of the present could be adequately handled by the major executives next in line to himself. Moreover, in such circumstances, his presence would be a prop on which his subordinates could lean—a condition repugnant to his sensibilities. It was his desire to be left free to plan for the future without being restrained by the problems of the present, a realization impossible without a high degree of delegation of authority and of consequent coordination approaching perfection.

Coordination and Executive Discretion

The relation of one operating executive to another within a business institution resembles the relation of one citizen to another in a democracy like the United States. Each citizen is free, and his personal liberty is regarded as a precious heritage. However, this personal liberty is circumscribed by regulations, called "laws," which set limits within which one is free. Beyond these limits, the citizen is considered to be interfering with the rights of others. If he violates these laws, he may be put in prison or

prevented by legal injunction from pursuing his occupation. Similarly, the business executive in charge of one operating division, such as personnel, is free to perform his tasks within certain limits. These limitations upon his own discretion are for the purpose of coordinating his effort with the purposes of the entire business. Limitations which permit him freedom within his own sphere but forbid his interference with the activities of other executives outside of his jurisdiction are a necessary part of organization technique.

The top executive of a business comes into direct contact with the actual routine of business operations chiefly through his power to determine the limits of subordinate executive discretion. Through the approval of such limits and by means of the delegation of authority, he decides how the details of the business shall be performed. He also determines what is beyond the scope of subordinate executive decision, in which event questions for settlement must be appealed upward to himself or to his major assistants.

The simplest, and probably the most common, form of limitation upon subordinate executive discretion has to do with magnitude or importance. Operating problems meeting this test must be referred to the higher executives for decision. Examples of such limitations are as follows:

1. The purchasing agent is usually instructed to obtain approval of superior executives before making a purchase in excess of a certain amount, say, $10,000.
2. The production manager is usually instructed to obtain the approval of someone above himself in authority before hiring an extra shift of workers or before shutting down the plant.
3. A salesman is usually instructed to obtain approval of the credit manager (or sometimes the sales manager) before quoting any other than the customary discounts and credit terms.
4. All executives are usually instructed to obtain approval from their superiors before making any addition to the physical plant and equipment; before selling any used equipment or surplus material; and before expenditures of any sort are made beyond the amount allowed in the current budget for the particular purpose.

In some departments of a business, every decision must have the approval of the head of the department. No legal decision can be made by an assistant to the counsel of a corporation without first considering its possible effect upon, or relationships to, other decisions previously made or pending. Furthermore, a legal decision may have a bearing on more than one problem or situation. When questions of law enter into management, the necessity for coordination is particularly apparent. Therefore, to centralize final approval of all legal matters in the chief counsel is an inviolable policy. Similarly, no assistant purchasing agent may make an

offer to buy which does not take into consideration all other offers for similar materials.

Technique of Executive Discretion

A simple technique in common use for limiting the discretion of subordinates is to require that the signature of the department head appear on all letters and orders issued by the department. When this is done, every subordinate performs his work merely as agent for the executive in charge. His work is inspected by the executive and is approved or sent back for revision. This method effectively coordinates the work of minor officials, but it also slows down the work of the department and places a heavy burden of detail upon the shoulders of its head. Every new question is automatically held up through refusal of subordinates to make any new decision. It is a technique which is justifiable only where close coordination is absolutely necessary. Its application is not conducive to the stimulation of initiative and self-confidence in subordinates, and its general or unnecessary adoption should be avoided.

When the limitations upon the discretion of subordinate executives are highly restrictive, it becomes necessary to make special provisions for the exercise of authority in times of emergency. In fact, under a policy of complete, or nearly complete, subordination, self-direction almost vanishes and decision-making by minor executives becomes a lost art. When an emergency arises and time and circumstances do not permit instructions to be received from superiors, delay may prove disastrous. Provision against such eventualities is made by allowing abnormal power to cope with abnormal situations. Employees of a city like Los Angeles or Cincinnati have strict limitations placed upon their executive discretion in such matters as purchasing, employment, and the issuance of peremptory orders to the public. In the event of an emergency, such as a flood or an earthquake, it becomes necessary for these employees to take drastic steps and to go into immediate action with almost no limitations. The same principle applies in a business enterprise. If the operating executive is given definite limitations in order to coordinate his work with others, he must likewise be given full discretion to meet any emergencies which may arise.

The interest of the general manager of a business is to coordinate the entire enterprise so that its output with respect to quality and quantity will come within the most profitable commercial limits obtainable. To make products higher in quality than similar products on the open market may be profitable if a new patronage is thereby secured, or an old clientele is better served. But higher quality may entail higher costs at a level which will be unprofitable to the manufacturer. Similar conditions exist with respect to quantity. In one case, to curtail quantity may con-

strict the market with an ensuing loss of customers. On the other hand, an increase in quantity may result in unsold inventories of stagnant goods with all their attendant losses. Efficient management always seeks balance, and the techniques of coordination are designed to accomplish this end.

EXECUTIVE TOOLS AND PROCEDURES

In order to perform the work of management, executives have developed and perfected many different tools and techniques. One of the most important of these is policy formulation.

A well-established, going concern has generally set before itself several basic objectives. Among them are such considerations as the type of products to be made or services to be performed (occupational objective); the reputation and character of the firm to be maintained; the competitive position in the industry to be held; and the profits that the business aims to make. The determination of these objectives is, in itself, a phase of policy-forming. All other policies of an enterprise hinge upon, and are conditioned by these ultimate goals. Each policy is a guide to executive action—a directive by means of which the course of the particular business is charted.

How Policies Are Made

Because of the varying importance of different business problems, a particular policy may have broad application within the business, and, therefore, it may be relatively fixed. A policy may be outlined to cover an unusual situation which, though important, may never occur again. All the policies which are collectively in effect at one time must be recognized as representing an interpretation of the basic objectives of a particular business enterprise.

A policy should not be confused with an executive command or order. A "policy" is a "written or unwritten decision setting forth the proper course of action to be followed in a given situation." Though often phrased as an order or set of instructions, a policy is the basis for a command, not the command itself. For instance, fire insurance protection may be considered in one of two ways: (1) it may be deemed advisable to purchase such insurance rather than to use any form of self-insurance; or (2) it may be decided to accept a particular offer of a fire insurance program, thereby adopting a new policy by abandoning a former one which provided for self-insurance.

Both of these actions outline the same policy of purchasing insurance from an outside source. The first one merely provides for a change in an established practice of self-insurance to one of purchased insurance. The second one includes, with the change in policy, the specific order or command to put it into effect. The larger the business enterprise, the greater

the tendency is for the board of directors and higher executives to outline policy in general terms, leaving the formulation of specific instructions or commands to subordinates.

A combination of basic policies and objectives is sometimes spoken of as a "master plan." Like the constitution of a modern nation, this master plan may be unwritten or it may be written in considerable detail. The latter method is more and more becoming the standard practice of the large corporations. The reason for its adoption is that a written master plan serves the dual purpose of information and education for stockholders and employees with respect to the underlying principles of the business. It is also useful in meeting the insistent demand of governmental agencies in matters of inquiry and investigation. The term "master plan" is not in common use in actual business situations and circumstances. What is here called the "master plan" usually consists of fundamental pronouncements and announcements, such as the annual report of the company, speeches made by top executives, and the reports of newspaper interviews.

The Use of Staff in Policy-Making

More and more the trend in management is toward greater use of staff investigation and planning before policies are formulated. Problems that need solutions before executive decisions can be safely made are continually arising. Modern business is carried on under relatively stabilized conditions, with potential losses from "taking chances" without knowing possible future outcomes, too great to justify the risk. Therefore, in order to have assurance, if possible, that future outcomes will conform to present executive decisions, constant research, analysis, and study are required before any significant action is taken.

Stable and continuous operation of a business also requires close direction and control of subordinate executives by top management. Executive leadership must be enforced and recognized from the top to the bottom of the organization. Subordinate executives generally do not exercise so much discretion and caution with respect to "taking chances" as do their superior officers. Years of service under conditions of stabilized operation cause junior executives to be less alert to the possibilities and need of new and better methods and practices in such matters as lower costs, increased production, wider markets, and greater benefits to owners, workers, and customers.

The responsibility of executives in operating their divisions of the enterprise preclude them from engaging in researches and long-time planning. The problems involved in such activities, therefore, come within the proper sphere of staff services. There are six principal groups of such problems that are commonly referred to staff executives for

investigation, study, and recommendation before decisions are made concerning matters which they affect. These groups are: major policies, product design, methods engineering, special training of employees, executive morale, and appealed problems.

The Staff and Major Policies

If executives are to lead their enterprises on to success and profitable operation, their decisions affecting policies must be right. Knowing this, executives tend more and more to verify their judgment through staff investigation and planning. An example of this practice is market research, which is undertaken for the purpose of discovering reliable information about sales potentials, customer acceptance, and prospective results from entry into a new territory.

Product Design and Methods Engineering

Product design, or redesign, is a problem involving future production plans. It therefore lends itself peculiarly to staff investigation and recommendation. Sometimes such organization devices as "suggestion committees" and "design committees" of appropriate operating executives are often created in order that they may study critical matters of this kind with staff specialists of proved knowledge and ability.

Methods engineering is closely related to product design. "Product design" considers such matters as market competition, while "methods engineering" is concerned with the details of the cost of production. Inasmuch as both activities look to future change and improvement, the solutions to the problems they create are properly matters for staff consideration.

Special Training of Employees

When special knowledge and skills are required at any place in the organization, it is the function of staff members to furnish them. Since such needs are generally intermittent, they are frequently supplied by temporary outside services. Two examples may be cited to illustrate this point. Assume that a food products manufacturer has been sued by a consumer on the charge that a food preparation on the manufacturer's list has made the consumer ill by poisoning. If the defendant in this case requires a special technician to analyze the product in question to detect if poison were present in it, such advice would probably be provided by an expert consultant, temporarily employed as an addition to the regular staff analysts of the company's food-testing laboratory.

If a street railway company should decide to change its operating equipment from a rail to a bus system of transportation, a qualified representative of the firm that would supply the new busses would

probably serve for a time in a staff capacity, as teacher of the trolley-car operators who must now learn how to drive busses. In these two situations the top executive exercises his leadership by providing a supply of needed ability and knowledge to his staff. He works through that staff, both as a convenience and as a matter of economy, avoiding the expense of permanent additional personnel in his operating organization to care for such exceptional nonrecurring problems.

Influence of Staff Executives on Morale

The relation of staff executives and consultants to the morale of the executives who operate the business is especially important. If operating executives look on the staff members with alarm or suspicion, morale is adversely affected. This often happens when the top executive decides to employ an outside expert or consultant to install a so-called "scientific" wage system. Operating executives who are accustomed to the good old-fashioned piece-work or day-work plan of compensation may become resentful and antagonistic to both the system proposed and the person who is employed to install it.

Sometimes the top executive employs his staff to stimulate and improve the morale of his subordinates. By his actions, and even by plain warnings, he lets it be known to members of his organization that they must respond favorably to the suggestions of his adviser or consultant if they wish to keep their jobs. For example, the head of the business may tell his operating executives that they can, and must, hold the quality of output and the percentage of waste and rejections within the limits suggested by the consultant. Under such circumstances, if the consultant is not only an expert but also a diplomat and teacher, the new limits will be attained and executive morale will improve from pride of achievement.

An even more difficult situation develops when the top executive frankly abandons the plan of bringing about improvement by gradual evolutionary means. He then uses a staff executive or an outside consultant as a "trouble shooter" and sends him into the particular division of the firm with instructions likely to cause revolt among the persons affected. In this instance, the consultant would be given full authority to make and enforce operating decisions. Under such circumstances, some operating executives become sullen, others pugnacious, while still others settle down to learn the new way and to cooperate with the staff executive. This sorting process opens the way for "house cleaning" by the top executive. It gives him an opportunity to rebuild his organization by replacing obstructive and recalcitrant persons with a group of more cooperative and better-trained subordinates.

In such a "revolutionary" process the staff does its task by issuing and enforcing orders. This is the dividing line between staff and line activities.

When such authority is assumed, it changes the staff into an operating-executive group. This is a danger to be avoided. It leads to excessive development of the staff system and, in many cases, threatens to reduce otherwise capable and responsible operating executives to mere figureheads.

The Function of Staff in Appealed Problems

A chief executive or general manager must be successful in handling knotty appealed problems brought to him by his subordinates. His personal span of knowledge and his regular duties force him to seek others with requisite skill and sound judgment, who can advise him how and what to decide. The quality of the advice he receives is most important, since an incorrect or unfortunate decision on his part will either mislead or repudiate his subordinate executive who has instituted the appeal. In either case, the top executive has his own leadership at stake. He cannot expect to force his executive orders on unwilling subordinates if experience proves his decisions are consistently wrong.

EXECUTIVE COORDINATION PROCEDURES

The point at which coordination between different executive activities must take place is of great importance. Only a small number of problems of greatest significance should be coordinated by the company president or top executive. It follows that the top executive of a business must select executives and assign their duties in such manner as to keep at a minimum his own personal coordination problems. He must also strike a balance between functional centralization and decentralization, since excessive tendencies in either direction increase greatly the stresses and strains to which the head of a concern will be subjected.

Degree of Centralization

It would seem that a high degree of centralization of management in the top executive would tend to simplify the work of coordination. In an extreme situation a managerial dictator would have to harmonize the ideas and purposes of no one but himself. His subordinates would be mere order-takers who would manifest unquestioned compliance with directives from above. But we have already seen that such concentration of power in one person will not work because of his natural limitations of time, energy, and knowledge. When the span of control of an executive is inadequate and, hence, lacking in effectiveness, coordination of activities consequently suffers. Control and coordination are mutually dependent phases of good management.

On the other hand, too much decentralization or overfunctionalization in a business organization likewise tends to destroy coordination. Such a

condition would mean that problems of like nature arising at different points would not be given similar treatment. Some examples may be cited.

Under decentralized purchasing, one department may accumulate raw materials too far ahead, whereas another may buy from hand to mouth. If the latter department is in production sequence with the former, the result may be that, in the one, capital will be tied up in excess material while both are shut down waiting for deliveries for the other.

Again, too much decentralization causes two different departments within the organization to attempt to perform the same task. The sales department may guarantee delivery of merchandise at a certain time. The traffic department may choose a method of transportation making such delivery impossible. If the problem is important, such a departmental dispute should be coordinated by some higher executive to whom it is appealed. If the problem is unimportant, the functionalization which made the dispute possible is not worth while.

Overfunctionalization reduces the flexibility of the executive organization and, therefore, its ability to adjust itself rapidly to new conditions. This is true because disputes between two different functional activities are often jurisdictional in character; that is, they involve the question of which department has the major responsibility and authority over the particular problem. In many businesses, the personnel department has extended its functional authority to cover discharge of employees. An operating department cannot fire a worker. It can only transfer him to the personnel department, which may merely shift him into another part of the business. The settlement of jurisdictional disputes concerning such a separation of power gradually develops a line of decisions which indicates the boundaries.

In so far as functions are important, establishment of these boundaries is a step toward more perfect coordination. Executives have a clearer understanding of their respective duties. However, if an increase in the number of separate activities divides the organization into a great number of functions, each under an executive, the settlement of jurisdictional disputes develops a situation in business organization similar in character to that of government organization. An enterprise comes to consist of many distinct functions, each bounded by a line of decisions from all others. This creates a mass of internal red tape which has no advantage, but which only serves to retard the business.

Geographical Coordination

In addition to selection of executives capable of operating the business in coordinated fashion and arranging their duties in relation to each other, the top executive must consider the problem of coordination of geographically separated executives. This problem arises in clear-cut form—

for example, when one business located primarily in one city purchases another business located primarily in another city. The question arises as to whether the executive organization of the parent company is to become the executive organization of the subsidiary. Typical problems that must be solved are as follows:

1. Assuming that the subsidiary is to have a sales executive of its own reporting to the major executive in charge of sales for the parent company, is the subsidiary to have its own sales force or is it to use the sales organization of the parent company? Is the subsidiary to do its own advertising? Is it to determine the sales price of its products? Is it to follow its own former policies, or the policies of its new owner in traffic routing and shipping?

2. Assuming that the subsidiary is to have its own production executive who reports to the major executive in charge of the production of the parent company, is the subsidiary going to make a complete product, or is it to process semifinished materials furnished by the parent company? Will the subsidiary have its own personnel department? Will personnel policies be determined by the parent company? Will it do its own purchasing? Will it hire its own expert chemists or other consultants on technical problems?

3. Assuming that the subsidiary is to have a financial major executive of its own, reporting to the company treasurer, is the subsidiary to have its own accounting organization, or are all billing, collecting, and accounting to be performed by the parent company at the home office? If accounting is centralized at the home office, how will payroll checks be made up? What records will be kept that are not required for home-office use?

The range within which a geographically separate portion of a business may be organized is from complete built-in status to complete corporate independence. Illustrations of these two extremes often appear in electrical utility corporations. At one extreme is the method of supplying service to a suburban community on the border of a large city. Aside from a few substation operators, the entire production, sales, and financial operation is performed by home-office executives and employees as part of their regular duties. At the other extreme is the practically independent subsidiary corporation. Coordination of a built-in subsidiary is accomplished within the parent business. Coordination of the parent company with independent subsidiary is accomplished by the top executive and his major executives through their dual position in both organizations.

Management of separate units involves many distinct coordination problems, which may be solved only by selection of executives and assignment of their duties and by proper interrelation or coordination with the entire business.

Factual Bases of Coordination

Successful coordination depends upon the ability of the top management to visualize all the probable implications of a proposed action. This requires knowledge of the past. Such knowledge, with respect to any particular business enterprise, consists in knowing the principles and precedents derived from the history of the company, industry, and the nation.

If business management were an exact science, all executive decisions could be made on the basis of known and precisely stated principles. This is not possible. Most business decisions are therefore related to past experience. Precedent, after repeated experimental proof of its validity in particular situations, may crystallize into a principle or fundamental rule.

The skill of executive coordination is developed by continuous study of the work performed by subordinates. The materials for such study include reports dealing with audits, budgets, and operating ratios. The financial audit not only reveals improper accounting for money but also helps to disclose inconsistencies or deviations in application of policies to operating problems. Good practice requires that final or summation audits be made at regular intervals by outside professional firms of public accountants. Since audits are in the nature of financial inspections, they must always be free from the influence and control of those who are inspected.

The "budget" is the "predetermined plan or forecast of the financial details of the business for a stated period," usually twelve months. The relation between actual results as they develop and the original plan or budget throws light upon detailed operational problems and accomplishments.

Operating ratios are prepared to show various significant relationships, such as current assets to current liabilities; fixed assets to total assets; net profits to gross sales; net sales to total assets; working capital to total assets; net worth to fixed assets; surplus and reserves to total assets; and earnings before interest to total capitalization. In substance, such ratios provide an understanding of trends and accomplishments in relation to the objectives, policies, and plans of the enterprise.

Systems in Coordination Procedure

A chief executive is rarely concerned with or interested in the various systems used in the operation of the business. He is, however, vitally concerned with the encouragement of system. The more systematic the operations, and the sounder and better the systems that are in use, the more profitable the business is likely to be.

A "system" is a "method of accomplishing work," but its significant implication is *order*. When a business concern installs or revises a systema-

tized work routine, it does so in order to improve procedures, facilitate processes, establish order, or effect economies by eliminating confusion and unnecessary work.

A good illustration of the importance of systematized management are the methods of operation in a large modern retail department store. In every phase of such a store's activity, there is an important system. But all of its systems must be coordinated because the work of employees in one department interlocks with the duties of many others. Therefore, store employees must be trained to discharge their responsibilities accurately and rapidly. It is as if it were a highly organized mechanism with its working parts carefully synchronized. An obstruction or breakdown at any point would throw all of it out of gear.

Thus, in a great store there is, first, a system of purchasing merchandise. Upon delivery of the goods bought, there is a system for receiving and preparing them for sale. Concurrent with this system is another one of recording purchases and withdrawals from stock and of establishing inventory. Then follows the actual selling of merchandise, also according to a system. A store will have a system for the packaging and delivering of goods to customers, and a system of opening, recording, and collecting charge accounts. And, finally, it will have an over-all accounting system peculiarly adapted to its own requirements.

Here there have been enumerated seven distinct systems, each of them highly important in the successful operation of the store. Yet none of them has any use by itself. Nor can the full benefit of any one system be realized except as it contributes to the whole process of selling merchandise in an orderly and profitable manner. This is the real significance of systems in the procedures of coordination. Systems are designed to produce order and economy, but it is coordination—a task of the executives who use them—that make systems effective.

The Budget as a Device of Coordination

The one system with which the top executive is directly and personally concerned is the budget. Viewed as a system, a "budget" is simply a "tabulation or compilation of anticipated receipts and expenditures over some future period." It is as detailed as its makers desire. It is as worth while and effective as the top executive of the business cares to make it.

In its least valuable and passive form a budget is an assembly or summary of the estimates of income and the desires of operating executives for expenditure. Such a budget cannot have much value as a management technique or device because the various estimates and requests are not coordinated. Nevertheless, it is better than no budget at all, and in this simple form, it is often used when more careful and worth-while methods have not been adopted. As we have seen, a department store is a closely

knit type of business. The general manager of such a business may spend most of his time in personal contact with the heads of the several departments of the store. He personally watches their sales income and approves their purchases. Under such circumstances the top executive and his operating subordinates make and revise the budget, detail by detail. The budget system merely assembles the results into a store-wide summary for ready reference by all concerned.

A truly fundamental principle of budget-making is that it must be built up from the detailed estimates of all the operating executives, each reporting on the items of income and expense in his own department. Only in this way can all the detailed problems of the business be taken into account. Only in this way can the operating executives be "sold on the budget." If they feel that the budget is something "crammed down their throats" by top management, their morale is undermined. If they do not participate in making up the budget, the operating executives feel under no obligation to live up to its terms.

However, a workable budget cannot be obtained by merely assembling the estimates of all the details or items of income and expense submitted by the departmental executives. Two defects are usually present in this simple, or "passive," type of budget. One characteristic weakness is that the estimated income from sales usually runs much less than the sum of all the estimated or requested items of expense. Operating executives, in other words, are so close to the needs of their own work that they often feel a need for construction, or maintenance expenditures, or for expansion of personnel that is out of proportion to the possible income from revenue.

The other weakness of the passive type of budget is that operating executives are different, individual human beings. Some ride expensive hobbies. Other are penurious. Some are noncommittal and retiring in attitude. Others are aggressive in promoting their ideas for expenditures.

The passive budget must obviously be coordinated in order to overcome its natural weaknesses. Its income estimate must be brought in line with its proposed future expenditures, by raising the former or cutting the latter, or both. The needs of the various parts of the business for expense allowances must be brought into balance with each other, raising some and cutting others. This is a procedure of coordination. The top executive takes the unrelated estimates made by his subordinates, and coordinates them into a unified and properly interrelated budget for the future period.

Coordinating the Budget

This process of coordinating the budget is best done by means of individual conferences between the top executive or his authorized staff rep-

resentative, namely, the budget director, or controller, and each of the operating executives. The aim is to get each operating executive to join wholeheartedly in revision of his own estimates in order to adjust them to the completed total budget. The successful budget, when completed, represents the will and influence of the top executive only in bringing about revision. The actual details of coordination have been decided by the operating executives themselves. This budget then becomes the creation and the responsibility of the operating executives. This procedure stimulates morale and encourages enforcement of the budget to the fullest possible extent.

A budget becomes an instrument of greatest usefulness as a management device when it serves as a complete plan or interpretation of future policy in terms of future results.

The Campaign Method of Coordination

Every business enterprise is always in the midst of a campaign. Often several different campaigns are under way at the same time. They may cover several different activities, such as manufacturing, storing, selling, and financing. Some businesses with strong seasonal variation in both sales and production tend to spend certain months each year planning their annual campaigns. In others, the campaigns may have no fixed time for beginning or ending. Campaigning is a complex problem of coordination both as to time schedules and plans.

A "campaign" is a "concerted drive toward some aspect or portion of the occupational objective of a business." It may be planned as a frontal attack upon competition in general, or as a measure to offset specific competitor aggressiveness. Whatever its nature, a campaign must be planned in conformity with and in terms of the current policies of the business.

Strategy, Tactics, and Diplomacy

"Strategy" is essentially a military term. In its literal interpretation the term means "the art of the leader or general." When employed in military operations, strategy is a phase of a campaign, or combat, in which an attempt is made to impose upon the enemy selected battle conditions of disadvantage to him. It also includes taking advantage of conditions and situations extraneous to the opposing armies themselves. Strategy has many aspects, outstanding among which are courage, duty, readiness, mobility, and sagacity on the part of the leader. Strategy is the broad aspect of the problem of "how to execute policy." A related term is "tactics," that is, the detailed steps of policy execution.

Applied to the campaign of a business, strategy and tactics involve techniques and qualities of leadership similar in character to those necessary in military management. In a competitive situation in business, to be

successful, the operating strength, position, and reserve forces of rivals in the field must be known or carefully estimated. As in army maneuvers, there are considerations of movement and timing, and obstacles to be surmounted and situations to be seized upon. The qualities of courage and readiness, and the ability to "get there first," also must be present. Strategy and tactics probably can never be reduced to a science but must remain essentially an art. For this reason, strategy and tactics are conditioned to a marked degree by the genius of the one who exercises them. Rendered no less important by this characterization, they are indispensable tools in the hands of a business executive.

"Diplomacy" connotes settlement of disagreements through negotiation and compromise. Between unyielding rigidity and spineless vacillation in the dealings between men and institutions stands diplomacy—flexible but not soft, courteous but not pompous, ready to give and take. The diplomatic executive is one who realizes that most matters in which there are important differences of opinion are settled by compromise rather than by force. He adopts this attitude as a handy tool.

THE EXECUTIVE TASK OF EFFICIENCY

A major task of management is to secure efficiency in the operating processes of a business. This responsibility embraces the installation and enforcement of system and order in handling production so that it will flow through the plant without waste of time, money, or effort. It may be well to point out that, while the figure of speech here adopted seems to apply particularly to manufacturing enterprises, no such exclusive interpretation is intended. There is a "flow of production" in every business, be it manufacturing, retailing, wholesaling, or transportation. This concept of systematic and orderly movement may even be recognized as an essential attribute in the management of the affairs of professional offices, government, and charitable and educational institutions. All of these agencies are, in the truest sense, engaged in production. In the discussion which immediately follows, the aim has been to state the principles, couched by way of example in railroad phraseology, which are applicable to all routine operations in which the relationship of costs and returns are of material importance. Systematized flow of production is based on certain fundamental principles. For the sake of efficient operation, these principles, representing steps in a process, must always be undertaken in a sequential order.

Sequences in Routine Operations

Planning.—In the production process the basic management act is the "order." But no order can be sound unless preceded by a plan or conscious procedure. If a railroad decides to operate its principal passenger

trains on a new and faster schedule between terminals, it must plan in advance what motive power to use, what speeds to maintain on curves as well as on straight track, and what reconstruction of track and roadbed may be necessary to accommodate the new conditions. If increased costs are necessary, it must also plan how they may be financed and what fares ought to be charged for its new service. Finally, it must plan its improvement program so that its new trains and its reconditioned track may be ready for use at the same time.

Preparation.—A plan may exist entirely on paper or, even less tangibly, in the mind of an executive. The first step in its realization is "preparation." This step is the act of assembling men, materials, machinery, and perhaps money, in order that the purpose of the plan may be carried out. To continue the illustration of the railroad: Its plan is complete, it has been tested by scientific study, it has withstood the searching scrutiny of skilled and experienced executives. The time has now arrived to make final preparations for the new train service. The needed money must be obtained and materials purchased, including the new trains themselves. The track and right-of-way improvements must be undertaken and completed, and their safety proved by careful tests.

Scheduling.—Scheduling is the process of arranging the desired work so that it can be performed with dispatch and efficiency and with the minimum interference with other work. A new train may be ready to run upon the new track; but before it may be put under way, the railroad's timetable must be revised. Not only must the time schedules of the new trains be worked out to the last detail, but also the schedules of other trains, both passenger and freight. Such scheduling is for the purpose of establishing coordination throughout the whole railway system. The new, faster trains must be given the right of way over all other trains; yet they must not impede the rest of the company's operations. It is only through the total operation of all of its facilities that the railroad can be justified or made to pay.

Performance.—Having taken these three preliminary steps, it is now possible for production to be accomplished. The new trains may be put into service utilizing new equipment and improved roadbed. They will operate on faster schedules which are coordinated with the running time and services of other trains in the system. Production of faster transportation under these circumstances then becomes simply a matter of effectuating the original predetermined plan.

The chief executive of the company has no direct interest in the details of this plan-prepare-schedule-perform sequence of routine operations. He is vitally concerned, however, that its four phases be properly recognized, understood, related, and carried out, to the end that profitable and efficient operation of his business may result. Failure to do so would result

in loss to the business because of clogged, unworkable conditions of production.

Sequences in the Act of Command

The characteristic act of the executive is the preparation and issuance of a command or order which results in performance by subordinates. This act, like those of routine operations, is also composed of four steps, which must be undertaken sequentially. Three of these steps are identical in principle with those previously discussed, namely, planning, preparation, and performance. One step is added, however, and one is omitted. In leadership, investigation always precedes planning, and scheduling can hardly be conceived to be one of its elements.

Investigation.—No management decision or order can be sound unless preceded by detailed investigation and study of the present and the probable future situations which may affect a given business. "Investigation" includes two elements—the assembly of all pertinent facts and their reduction to a scientific basis.

Planning.—Planning follows investigation, since it is impossible to plan without the knowledge of the situation or problem under consideration. "Planning" may be regarded as the "mental process of solving management problems."

Preparation.—After the business problem has been investigated and appraised, and the plan for its solution formulated and adopted, there must be preparation before management may go into action. "Preparation" is a complex activity which involves the assembly of man power and its training, organization, and assignment to duty. Likewise, the material resources of the business must be gathered, tested, and allocated. Preparation often requires the raising of money, the assurance of legal authority, and timing. It is always relative to such factors as invention, population, legislation, and the business cycle.

Performance.—The last step in the sequence which describes the act of command is "performance." By it is meant the actual and efficient execution of managerial orders. Performance is always quantitative, since an order calls for an amount of work or product. It is qualitative, since the order also will require—specifically or by implication—an optimum of perfection or, perhaps, arbitrary limits within which quality may fluctuate.

QUESTIONS

1. As of a given date, a report of a small commercial airline shows its organization to be as follows:
   President and General Manager.

Vice-President in charge of traffic.
Vice-President in charge of operations.

As of the same date, a large commercial airline reported its organization to be as follows:

Chairman of the Board and Manager of Foreign Lines.
President.
Executive Vice-President.
Senior Vice-President.
Vice-Presidents, respectively, in charge of transportation; engineering and maintenance; operations; traffic; public relations; and three vice-presidents with unstated duties. (Therefore, the total number of vice-presidents, other than the executive and senior vice-presidents, is eight.)
Treasurer.
Secretary.
General Traffic Manager.
Director of Ticket Offices.
Director of International Traffic.

a) Show by diagram and descriptive discussion that the organization of the large airline could have been evolved from the organization of the small airline by a process of growth evidenced by the addition of executives and the redelegation of duties.

b) Elaborate upon the statement that the duties of the chief executive of a business enterprise vary from one concern to another, even in the same field of business. Illustrate your discussion with examples that may be known to you through your observation or reading.

2. Analyze and explain fully the similarities and differences between the following:

a) The four methods used by directors in performing their functions, as outlined in Figure 15, Chapter V.

b) The four steps involved in the executive task of efficiency in routine operations, as explained on pages 165–67.

c) The four steps involved in the executive act of command, as explained on page 167.

3. By referring again to Figure 15, Chapter V, it will be noted that fourteen problems of business management are listed as representative of the responsibilities of a board of directors. State, in a sentence or two, the role of the chief executive, his major executives, and staff assistants in the consideration and solution of each of these problems.

4. Distinguish coordination activities from direction and control activities in each of the following assumed problems prevalent in a typical commercial airline, and give reasons for the distinctions you have made:

a) Training pilots to fly a new type of plane.

b) Scheduling the work of flying personnel.

c) Employing a caterer as consultant on menus and food service to passengers aloft.

d) Balancing the distance traveled by planes between refueling stops, and taking into account the resulting heavy take-off load of fuel in relation to the compensating reduction in the pay load of passengers—mail, express, or freight.

5. Analyze and restate the following incorrect statements:
   a) The reason small airlines get along with fewer vice-presidents is that the executives of small airlines are more competent than the ones that can be obtained by large airlines.
   b) As the executive organization of a business enterprise more nearly approaches perfection, the less need there is for competent major executives.
   c) The outstanding characteristic of effective personal leadership on the part of a chief executive is his tendency to impose no limitations upon the planning work done by his subordinates, but to place narrow and rigid limits upon the routine acts of management of the executives who are accountable to him.

6. Explain fully the relationship of budgets of income and expense to the effectiveness of coordination on the part of a chief executive and his immediate subordinates.

7. Assume that X Company in one city has 1 store and 100 employees, and that Y Company in another city has 10 stores, in several cities, and 1,000 employees. Assume further that the 2 companies merge into a new concern. Answer the following questions and give reasons for your conclusions:
   a) Would you retain the general offices of both of the former companies, or would you centralize their activities in one new main office?
   b) Do you believe that the new company that has resulted from the merger is large enough to justify the appointment of an additional functional executive who will be responsible for the selection and training of sales employees for the whole firm?
   c) Suppose that, after consolidation has been effected, neither president of the original companies will agree to retire. How, then, might the problem of securing a chief executive for the new concern be solved?

8. Assume that a domestic commercial airline has petitioned the appropriate government agencies to extend its services to a foreign country. Use this hypothesis as the basis for a list of problems that will illustrate the meaning of the statement that "successful coordination depends upon the ability of the top management to visualize all the probable implications of a proposed action."

9. The board of trustees of a large mutual life insurance company customarily appoints an examining committee of policyholders (i.e., a com-

mittee of customers) to examine annually the affairs of the company. Answer the following questions bearing upon the probable duties of this committee, and give reasons for your answers:

a) Should this committee inquire into the safety of investments and the continuity of earnings therefrom?

b) Should this committee attempt to appraise the competency of management?

c) Should this committee make suggestions for improved relationships and services to the company's customers?

10. Define concisely, but adequately, the following terms as they apply to executive functions:

a) Executive discretion.

b) Policy.

c) Appealed problems.

d) Strategy.

e) Tactics.

f) Diplomacy.

g) Investigation.

h) Scheduling.

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CHAPTER VII

THE SUPERVISORY LEVEL OF MANAGEMENT

FROM the analysis of the executive tasks of management it is clear that direction is a basic element of authority and responsibility. The structure of an organization is static; it is the individuals who compose it that possess the potential energy which can set an organization in motion. Such activation is management. But the full utilization of that energy depends upon a directive factor which will release it and guide it into channels of useful and concerted action. Hence, "direction" denotes guidance and coordination of the activities of subordinates for the purpose of accomplishing desired results.

Now, supervision is the indispensable complement of direction. "Supervision" means "to oversee and to instruct persons in the detailed performance of their work." Closely associated with supervision is "inspection," which involves examination, testing, and appraisal. In order that supervision may be effective, not only must executive decisions be made and enforced, but there must also be an assumption of the responsibility for the satisfactory performance of the work that is to be done. This responsibility is the essential task of the supervisory level of management.

Supervision, then, can be compared to the engineering function in a power plant. The material and mechanical elements of the plant furnish the essential power; but in order that the full potentiality of that power may be realized for the purposes for which it is generated, it must be supplemented by the regulatory control of an engineer. So, also, in a business organization, the top executive level of management provides the motive force that stimulates all parts of the organization into action. It is the duty of the personnel at the supervisory level to insure the efficient and effective application of that motive force to the accomplishment of the predetermined objectives of the business. Specifically, the goals of management are consummated through supervision.

THE ELEMENTS OF THE SUPERVISORY LEVEL

It may be stated as a basic principle that actual management of a group of employees can be accomplished only by means of personal supervision. Such words as "supervise," "superintend," and "oversee" all have to do with the process of managing workers through personal observation and contact. These words have come down to us from ancient

languages, indicating that the supervision level of management has been recognized for thousands of years. At first, as the words suggest, "supervision" may have meant "looking down from above," the way an overseer might watch a group of slaves or the master craftsman managed his indentured apprentices.

Today the supervision level of management does not manage from above, but it participates as on-the-spot management in actual operations. Supervisors, overseers, and foremen are associated with the workers themselves in the joint task of doing the work in question. If the business enterprise is very small, the different levels of management are all merged into one executive. From the standpoint of the worker, this one executive is his supervisor. Conversely, no matter how many upper levels of management are developed within a large business, there must always be a level composed of executives, not regular production employees, who keep in personal touch with all workers and direct and participate in all work.

Classification of Supervisory Personnel

The personnel at the supervisory level of management may be grouped into three broad categories on the basis of the kind of work supervised and the extent to which a supervisor participates in it. A scalar arrangement of organization prevails at this level somewhat as it does in the ranks of higher executives.

The highest level of supervision, immediately below that of departmental executives, is that of the typical superintendent. His duties are commonly limited to participation in the environment, or general working conditions, of the particular segment of the business which he serves. He performs none of the physical work and little, if any, of the routine clerical tasks of his department, but he must be "on the job." He cannot discharge his responsibilities by proxy or *in absentia.* If he is in charge of a construction project, for example, the superintendent must live in the vicinity of the job and must come into regular contact with the job itself.

The next level of supervision is typically the one of the foreman, or overseer. He does little or none of the physical work that he supervises, but he participates in a portion, at least, of the actual routine clerical work of his office. His task may seem simple and unimportant, but the reverse is true. Despite the fact that he is relatively inconspicuous, he occupies a key position in the organization. His is the job of providing face-to-face leadership and supervision to a particular group of employees who perform a portion of the productive work of the enterprise. He is the connecting link between the higher executives of the concern and the operating personnel. He is expected to interpret company policies and objectives to workers and the interests of workers to management. Conse-

quently, he can be a strong influence, either affirmatively or negatively, in the development of the attitudes and morale of the working force. Not only does management above him look to the foreman for stability, discipline, and loyalty in the personnel which he supervises, but it also holds him responsible for quality, quantity, and costs of the products turned out under his observation. The leadership, craft ability, and coordinating skill of a foreman play a significant role in operating economy and effectiveness.

While in most organizations the foremanship level may be considered to be at the bottom of the scalar structure of management, in some instances still another supervisory level exists. It is that of the assistant or working foreman, sometimes called the "gang boss." His duties may involve regular work in preparation for the actual physical labor of the persons he supervises. For example, in a machine shop the gang boss makes all preparations for getting the work to the workmen. He collects jigs, tools, drawings, and other material and sees that the work is properly set in the machine. He relieves the workmen of all planning on the job and participates in the work itself to the extent that he sees to it that the specifications on a given instruction card or sheet are fulfilled.

Another type of gang boss is the tie boss in a track maintenance and repair crew for a railroad. He works with that crew under the general supervision of the section boss who is the foreman. In a utility like a telephone company, the gang boss may be a head linesman who not only supervises but also assists in the work of keeping telephone lines open and in working order.

The titles of supervisors vary with different types of organizations. Generally, such titles tend to be descriptive of the work performed. Figure 17 illustrates this tendency. No matter what their titles may be, the general nature of their duties is the same. In their responsibility for performance, they are held accountable for the methods of production and the quality of the product of the processes under their supervision. In their responsibility for persons, they are held accountable for the company employees whom they supervise. They are, in each instance, directly accountable to their immediate department heads.

The concept of unity of management from highest to lowest levels, requires a clear-cut demarcation between lowest supervision executives and workers. The test of separation is production activity—supervisors, even at the lowest level, perform no productive processes except those involved in job instructions and preparation or equipment testing.

Size of Supervisory Personnel

The size of the supervisory personnel, in terms of the number of persons that compose it, tends to vary with the number of employees in

a concern. Ten or less supervisory executives of all grades—excluding the department heads and their immediate assistants—for every one hundred workers is a fairly accurate rule-of-thumb. The number of supervisory executives is always several times greater than the total number of higher executives of all ranks. Entirely apart from their somewhat different duties, supervisors are so numerous as to be regarded as a distinct group within the business. In general, the larger the number of workers employed by a particular business, the larger will be the number of executives required to supervise them. This ratio is merely the result of the practical application, at this level, of the principle of the span of control.

Type of Organization	Superintendency Level	Foreman or Overseer Level	Assistant Foreman Level
Railroad (train operation)	Division superintendent	Trainmaster	Train conductor
Public utility	Superintendent	Assistant superintendent	Gang boss or group foreman
Factory	Assistant superintendent	Foreman	Assistant foreman
Retail department stor	Floorwalker or floor superintendent	Department buyer	Assistant buyer
Government office	Bureau head	Chief clerk	Assistant chief clerk
Insurance sales offices	Traveling agency supervisor	Insurance agency manager	Assistant agency manager
Army	Lieutenant	Lieutenant	Sergeant
Wholesale sales force	Traveling supervisor	Traveling zone manager	Traveling salesman
Public school	Superintendent	Principal	Supervisor
University (instruction)	Provost	Dean	Department chairman

Fig. 17.—Typical titles of supervisory executives.

More specifically, the extent of the supervisory level will depend not only upon the number of employees who must be supervised but also upon the geographical dispersion of the operations of the business and the character of the technical and mechanical equipment used in its productive processes. Every remote center of operation, such as a branch store or a sales warehouse, must have at least one supervisory executive. Often, therefore, the number of executives per one hundred employees is larger when company operations are widely scattered. Conversely, a supervisory executive at a remote subcenter may be more important than a supervisor in a corresponding position in the home office or factory. Thus, train conductors and traveling salesmen have relatively greater responsibilities because their work is remote from the supervision of higher executives. Although included in Figure 17, such occupations as train conductor and

others at the assistant foreman level, who both supervise and perform regular production work, are commonly regarded as employees.

Or, again, depending upon the skill required, large numbers of machine operators may readily be supervised by an assistant foreman. The most highly skilled employees, such as tool-makers, die-cutters, and the makers of delicate instruments, have personal abilities of such excellent qualities that mechanical devices are merely supplementary aids to them. Obviously, very little supervision is required or desired by them. Then there are machines whose processes are technologically perfect only so long as certain human routine tasks are performed in connection with their operations. Since such tasks require little or no skill on the part of those who provide them, the supervisory requirements involved are also of a routine character. In both instances, supervision is simplified, and the optimum number of persons who may be properly assigned to one supervisor is increased.

Selection of Supervisors

Important qualities in the major executive are unquenchable ambition and personal pride in successful achievement. These qualities lead him to seek advancement for himself while he devotes his energies and talents to the best interests of his firm. An important quality in the typical supervisor is unswerving, enthusiastic loyalty, since this attribute will lead him to take advantage of every opportunity to improve the position of his company with respect to production, sales, and prestige. Another important quality in the supervisor is strong love of family and home, since this will root him to his position and will win the respect and loyalty of those who must work beside him and under him.

The tendency to develop an upper executive group separate from the lower has been much discussed. It is often referred to as the growing aristocracy of brains. This is an illogical implication because chance and environment have certainly left many a keen mind in the lower group of employees and supervisors. It is decried also as an arbitrary denial of opportunity to the workman. In fact, management at the higher levels is becoming a sort of profession, involving different and longer training than is the natural lot of the employee and supervisor. In a similar manner, the legal profession is being restricted to the college and law-school graduate. The court clerk and law clerk who find advancement more and more difficult because of the complexity of the body of legal knowledge are being denied opportunity to reach the top of the legal profession. To state this in another way, the medical, legal, and higher business executive positions in society are increasingly reserved for those who have the courage, the time, the funds, the opportunity, and the ability to prepare themselves by prolonged and diligent effort for these important careers.

This is self-selection, not aristocracy. Through ability and the hardest kind of personal self-training, supervisors can and do break across this imaginary line. Conversely, children of competent executives, born in the lap of opportunity, sometimes are, through indolence or inaptitude, scarcely worthy of modest supervisory posts.

Promotion from within to supervisory positions in an organization is an established practice. This is true of field and branch supervisory executives as well as of factory foremen and superintendents. Experience counts heavily in the qualifications of a supervisor, because he must instill in his assistants and employees confidence that the expected performance is attainable, and confidence grows chiefly out of experience.

The factory supervisor or office chief clerk learns largely in the school of hard knocks. Something must be done in a hurry or in a special way, and the supervisor is instructed to get it done. When routine is neglected, or performance is allowed to drop below current work-flow standards, the supervisor is called "on the carpet" to explain his negligence to his superior. He and his superior must work out a solution, or appeal the problem to a higher executive who has the necessary authority to adjust or otherwise dispose of the matter.

The supervisor is rarely praised, but he is often criticized or condemned. Employees expect their foreman or chief clerk to pull their chestnuts, such as pay raises or days-off, out of the fire. His superior executives expect him to maintain or increase production per employee, improve quality, reduce errors, and cut unit costs.

Fifty years ago the typical foreman, gang boss, or supervisor of a group of male employees was a husky "hard guy." His commands were obeyed because he was a physical giant, who did not hesitate to use violent disciplinary measures. If not physically strong, the foreman often developed the art of bullying his men. Of course this picture is overdrawn. Nevertheless, American business looks back without pride to the past in which every group supervisor was a petty and often arrogant ruler, who hired, fired, and punished his employees as he saw fit. The foreman was responsible for his group of employees and had complete and sole authority over them. No provision was made in management to aid or check him in his activities as supervisor. He was, in fact, a petty ruler over workers—men and women alike—whom he could discharge from their jobs on the slightest provocation and without a moment's notice.

Criteria of Supervisory Promotions

Supervisory executives generally obtain their positions by promotion from other tasks within an organization. The selection of an employee to begin as an assistant supervisor is usually made by the superintendent or

by a foreman who has such authority. There are certain accepted criteria that influence these selections. The candidate may be a first-class journeyman (a higher stage than an apprentice) in the particular craft or unit of work for which supervision is needed. He may be a workman who has accomplished a high volume of production and who has demonstrated special ability in meeting established standards and requirements.

Other qualifications that lead to the promotion of workers to supervisory positions are: a low ratio of rejections in proportion to the total units of finished product of a workman—especially under conditions of complete and rigid tests; the evidence of leadership and the ability to secure the cooperation of other people; and, sometimes a relationship of friendship or family with some higher executive in the company.

Assistant supervisors are rarely chosen for their proved or probable ability to teach employees—important as authoritative education has become. Nor is it likely that a supervisor, in selecting an assistant, would find among his employees individuals with the broad training in business required at the higher executive levels. It follows, therefore, that the process of selection is, itself, a barrier to promotion into the higher management. The assistant supervisor, once he has been selected, must learn through experience how to teach and lead employees.

After an employee has been advanced to the position of assistant foreman or to a similar assignment, whatever the exact title may be, he is usually promoted to the next higher rank whenever an appropriate vacancy occurs. When he has reached the top supervisory position, his path to further advancement tends to be more difficult. He is handicapped or entirely stopped by the age which he has by then attained and by insufficient experience in and knowledge of the techniques of management that would qualify him for a managerial position at a higher executive level.

There is much to be said in favor of the foregoing method of selecting supervisory executives. As they come up through the ranks, they must, of necessity, come into close contact with the work which they will later supervise. Furthermore, this process conforms to the principle of self-selection of a vocation. There is, as yet, no universally satisfactory prevocational, scientific method of sorting persons into vocational groups on the basis of native ability. The fact that certain individuals have stood out among their fellow employees, and on that account have been placed in supervisory positions, is strong evidence of their fitness for advancement.

FOREMANSHIP EDUCATION AND TRAINING

It has already been pointed out that the foreman occupies a key position in a business organization. If such a supervisor has been advanced to his present position principally because of his exceptional skill in the

operative processes of his department, such experience—valuable as it is within its own limitations—affords no assurance of subsequent executive effectiveness. "Craft ability" and "executive ability" are not synonymous. The foreman's job is fundamentally one of executive leadership; therefore craftmanship is helpful but is not a sufficient qualification for the position. The supervisor who can skillfully perform the actual work which he requires of his subordinates has a clear advantage over one who cannot do so. Nevertheless, in numerous instances inefficiency and dissatisfaction among employees can often be traced to a supervisor's incompetence as a leader. It is the purpose of foremanship educational and training programs to correct this fault. No matter how small the enterprise, there is an important place in it for foremanship education and training.

The distinction between an educational and a training program is found in method and purpose rather than in content. Both programs are informative, but educational foremanship courses are intended to develop supervisors of different ranks for advancement, while training courses are established to enhance the effectiveness of a foreman on his present job. Of course the latter may also contribute to his chances for advancement, but one of the basic aims of education is to afford a familiarity with and an understanding of new areas of knowledge.

Content and Objectives of Training Courses

Since it is the purpose of foremanship training courses to improve the work of the supervisor in his immediate job, the content of such courses is designed to cover the problems most common to supervisory activities. These problems are of two kinds: first, there are those which have to do with personnel. In this group, training courses deal with such things as methods of adjusting grievances, techniques of handling persons to secure and maintain loyalty and cooperation, principles of disciplinary action, and the proper observance of interdepartmental relationships. The second group has to do with operative processes. Here the topics studied include the maintenance of quality, standards of output, reduction and elimination of waste, job analyses, time and motion studies, and safety precautions.

The immediate objectives of such courses is apparent from the subjects they cover. Both the anticipation and the solution of the personnel problems indicated result in better morale and stability of employment. Adequate answers to the operative problems serve to reduce costs, increase production, prevent delays, and generally improve the product or services supplied by the firm. It is clear that the achievement of these immediate objectives will at the same time result in realizing the ultimate goal of a high degree of effectiveness in departmental management.

Methods of Foremanship Training

Three methods are used in carrying on formal supervisory training. Of these, the most successful plan is the conference method. It is called the "conference method" because its procedure is based on a joint analysis and discussion of problems common to all the members of the group that participate in it. No prepared text material is used. Rather, it is assumed that the solutions to the problems considered are to be found in the combined experiences of those who are confronted with them. This method enables the individual group member to use the background which he already has and to supplement it with the experiences of his associates in similar circumstances. As he takes part in the discussions, the foreman is forced to think and reason about his job and to clarify his ideas as he presents them to the conference. In effect, a conference of this sort develops into a staff committee at the supervisory level. It brings together facts, weighs evidence, and hears arguments as to ways and means of doing the best job of supervision. It has no authority to issue orders or directives, but the conclusions reached in conference very naturally take the form of advice and recommendations.

A conference of this kind, established on a regular schedule of frequent meetings, will not run of itself. Like any other organization, it requires a leader. A competent conference leader is indispensable to its success. While the supervisors taking part are expected to express their views with a minimum of guidance, the leader must be able to stimulate both thinking and discussion. He may not dominate the conference, nor is he expected to supply the answers to the problems presented. By his appearance, personality, and mental ability the leader must merit the respect of the members of the group. This conference method of foremanship training can be especially useful in small companies in which a major executive, or even the top executive, can take the time to serve as a group discussion leader.

Another plan of supervisory training is the study method. It may vary as to form. In some instances, it is based on a correspondence study course given by an outside agency, such as a university extension division or a private correspondence study school. In either case, it requires individual home study in the preparation of formal lessons received and sent by mail.

The study method may also be undertaken as formal classwork based on available textbooks and taught by employed instructors. Such classes may depend upon the voluntary enrollment of foremen with or without the encouragement of higher executives. Membership in the classes may be more or less compulsory in some instances, especially if the cost of organizing and operating them is borne by the company.

A third plan is the lecture method by means of which different speak-

ers present various phases of the problems of supervision. These speakers may be selected from outside sources or from the executive group of the concern. The lectures may be intermittent, or they may constitute a coordinated program. Also, each lecture may be followed by a discussion period or by a group conference at a later date.

Each one of these methods has merit and a place in supervisory training. In general, it may be said that the less personalized the instruction, the less valuable will be its results. The formal study and lectures plans have their greatest usefulness in education for technical staff positions and for supervisory responsibilities beyond an individual's immediate experience. The conference method is best adapted to training on the job.

Organization of a foremanship training course is usually undertaken at the level of the superintendent. If it is successful at this level, the chances are that it can be instituted farther down in the management scale because subordinates are subject to the influence of the practices of their superiors. Whatever the method of foremanship training adopted, there are certain dangers and pitfalls that must be avoided if a plan is to yield practical results. Lasting returns of value cannot be realized from superficial lesson sheets or mimeographed "pep" letters produced for mass distribution on a fee basis by an outside agency or prepared for their intended users by a clerk in the office of a company executive. Any plan of foremanship training must guard against lack of appropriate material for study and discussion and against concentration on the psychology of emotion. The one results in loss of interest, and the other, while retaining attention, speedily drops to the level of psychological quackery.

The statement is often made by executives that no system of training is needed because "we employ only experienced supervisors." This means that chance determines how the particular supervisor has trained himself. In general, a methodical plan for training is likely to produce better results than chance. Every supervisor is undergoing constant training in the routines, techniques, and processes which he oversees. He is subjected to an occupational environment characterized by continual change. Technological advances bring about new developments in equipment and processes, and even the behavior of employees varies with time and personnel turnover. Because of the strong incentive provided by curiosity and mechanical interest, the operation of a new machine is most readily learned by the supervisor. After mastering the operation himself, the supervisor teaches it to his employees. But new routines and operational methods for prevailing facilities and equipment are less likely to be taught or learned on the job. The incentive of curiosity is lacking as well as the tangible and immediate evidence of results which are demonstrated by the absorbing operations of a complicated machine. For this reason, the requirements of personal leadership, in addition to the mechanical skills

demanded of a supervisor, can best be acquired through training programs that run concurrently with but apart from routine foremanship tasks.

Education in Company Policy

The most important subjects to be taught in executive educational programs are a groundwork in company policies, objectives, strategy, and tactics, as well as company organization and company channels and procedures for communication of orders, reports, and information. Such instruction is best provided by appropriate major executives or department heads, preferably in small conferences and discussion groups. It is a program sometimes described as the "understudy system." Its purpose is to develop stability and continuity in the management group. It is based on the principle that for every executive position in the organization there should be at least one understudy who, by virtue of experience, education, and personal qualities, is available to fill such an office when it becomes vacant. A vacancy might be a temporary one resulting from the absence of its regular incumbent, or it might be of such a nature as to leave the position open for the permanent appointment of a new executive. It is a pathway for promotion of supervisors.

By this plan the executive in charge of a division or department is expected to teach an understudy the policies, practices, and objectives of the business which apply to his special task. In this way a competent substitute or successor is always available when required. Obviously, this method implies promotion from within the organization. In some companies where this system is in effect, an executive will not be promoted himself unless he has taught another person to take his place. The program involved is properly a phase or part of the whole educational plan of the firm.

THE SCOPE OF SUPERVISORY ACTIVITIES

The supervisor occupies the position in the management structure closest to the actual performance of production processes. In this capacity he is the manager of the employees who produce the goods or services of the concern. In simple language, it is the job of the supervisor to see that work is done. In the execution of this task, he must first direct the flow of work. Unplanned and unguided work, like a stream following the line of least resistance, is sluggish and runs crookedly.

In the second place, the supervisor is a coordinator. The output of workers must be in harmony with the policies and objectives of the business as a whole, or else its productive units will tend to "ride off in all directions." Moreover, the activities of all divisions of work must be synchronized into unified performance in order to prevent discord, confu-

sion, and inefficiency in operations. As a coordinator, the supervisor is in control of performance.

Finally, the supervisor, by his personal influence, motivates each individual employee. This duty requires the exercise of leadership, which is his most important responsibility. Without such leadership, cooperation of workers among themselves, as well as with the management of the business, is unlikely.

The Flow of Work

Supervision of the flow of work is accomplished by production orders. By "production order" is meant a "clerical instrument designed to facilitate and control the quantity and character of work to be performed according to a predetermined schedule." In some types of business it may be a simple memorandum that recites the sequential steps to be taken to accomplish a given task in a specified period of time. In other types of manufacturing concerns it is a complicated document which distinguishes individual units or groups of units whose identity must be kept separate during a carefully scheduled production process. Regardless of its form, if the nature of the work to be done depends upon a schedule of sequential operations, the production order is an important tool of the supervisor. It not only releases authority for production from a proper executive source but also is an instrument for control of the flow of work.

In general, from the standpoint of priority of time in the production process, all work may be classified into three broad groups. The group with the highest priority takes precedence over all other work. It includes rush orders in factories, nonstop flights of airplanes between terminals, fast freights on railroads, special deliveries of mail and goods, and advance reservations at restaurants and hotels. All of these circumstances are frequent occurrences in business which must be scheduled and controlled at the level of supervision.

The second group is routine work. Most of the work done by every concern is necessarily routine in nature. It is the steady stream which flows along day by day and upon which the real stability of the business depends. Such work must also be scheduled and controlled even though it may, intermittently and temporarily, be interrupted by work orders of higher priority. But it is the duty of the supervisor to direct into production channels the priorities that will disrupt routine operations the least and will, at the same time, fulfill commitments. If, for example, in an excess of enthusiasm some department head should promise rush or preferred treatment to all of the company's customers—and such promises could be carried out—the unusual would then become the routine situation, though such a possibility is difficult to imagine.

A third group of activities is work which can be delayed. It is per-

formed when preferential orders and normal operations slacken. It is fill-in work that is performed when workers and facilities are not otherwise busy. In factories, such work may be "production for stock" to be held in reserve and stored. Another example is the power utilities that seek customers who are willing to delay and restrict consumption of electricity to off-peak hours. In many enterprises preferential, routine, and fill-in work flow side by side, but the central current is the steady stream of normal operations. To keep the channels clear for all work is a responsibility of supervisory executives.

Conditions of Flow of Work Supervision

The task of supervision of the flow of work is conditioned by the layouts of plants, by mechanical devices and equipment, and by established policies of production and service. In factories the character of the supervision required will vary with such factors as the extent to which mass production is developed, the type of product that moves through the plant, and the way the plant itself is built to facilitate production processes. For example, continuous manufacture with little or no storage of the finished product requires supervision different from that needed in a system of alternating production and storage. The mechanical devices of assembly lines, conveyor belts, and vertical processing by means of gravity feed—all tend to speed up and standardize the flow of work to which the particular supervision must be adapted.

Again, a different type of supervision is required in the single-machine method of mass production. It is illustrated by a generating plant of a modern electric utility. Such a plant mechanically conveys into itself coal, water, oil, and other materials and produces electricity. No employee does any important physical labor. The entire plant is one huge integrated machine, operated by employees who maintain the machinery, regulate its operation, and dispatch its product along high-tension lines to points of use. Factories for other purposes are now designed, as far as possible, in a similar manner. In factory design the modern goal is intake of raw material and output of finished product within one continuously producing machine. Because of the high degree of technological efficiency of such a factory, the need for human supervision of its detailed processes of production is minimized. At the next higher supervision level—that of the superintendent and his associates—greater skill and knowledge are required, despite the lessened minor supervisory activities.

Methods of Work Assignment

Supervision of the flow of work involves the assignment of work to employees; and if equipment is to be used—whether machines or otherwise—it, too, must be specified. There are five methods of such assign-

ment. They vary with different types of enterprises according to the purpose of their respective operations. For instance, in factories where the conditions of mass production are highly developed, the "automatic method" is used. Here the character of the product automatically determines both the employees and the equipment that will be required to do the work. In other manufacturing concerns the "job shop" or "flying-squadron method" is a common practice. Under this plan, each employee must be capable of performing a variety of tasks. With each new production order or assignment, the worker may have to follow a production path involving skilled operation of different machinery. The term "flying squadron" designates a variation of this method. In some large factories, groups or squadrons of workers are trained in several operations so that absent employees may be replaced, or the output of a particular process increased, as circumstances may require.

Another plan of work assignment is the "performance rating method." It can be used in a wide variety of businesses. Certain criteria of excellence against which the efficiency of workers is measured are established by means of various tests and research studies. Then, in the assignment of work to be performed, those who have the highest rating, that is, demonstrated ability, are designated to do the work that is contemplated. The plan followed by most transportation companies is the "seniority method." This system provides that employees in the order of length of service are permitted to choose what tasks they will undertake within the range of their particular skills and training.

Finally, there is the "experience method." Under this plan the supervisor assigns employees and machines as he sees fit. As a result of long experience, he feels that he knows who should do a particular job.

Supervision of Performance

Technically, the supervisor is a line executive. That is, the authority delegated to him is essentially the power to give and enforce whatever orders are necessary to get the work done. But, as has already been pointed out, he is also a coordinator of the decisions of higher management and the work performed by employees. The combination of these responsibilities makes him a functional specialist in his own craft within the organization of which he is a part. The acceptance of this enlarged role by supervisory executives and the efficient discharge of their responsibilities in accordance with it have together resulted in greater output and better quality of goods and services.

Today, the task of supervision includes the maintenance of existing high production standards of quality and quantity and the fostering of improvement. Since much has been accomplished, the supervisor who achieves even higher performance is indeed skilled in his task.

Of course this improvement cannot be brought about by the supervisor alone, important as his role in the process must be. Development of efficiency in operation is a joint task of the higher management, the supervisors, and the workers. There must be close cooperation and free communication between them. It will not do for one department to make promises involving another which the latter is unable to fulfill. To make sure that such a situation will not arise, it is necessary for the various functional divisions of the concern to be thoroughly familiar with the capacity of the firm in terms of equipment and workers in every unit of the business. Such departmental executives must have up-to-date knowledge of inventories and previous commitments, so that bottlenecks are avoided and supervisors be not embarrassed because employees find themselves in a situation where it is impossible for them to perform the duties expected of them.

This cooperation between the higher management and the supervisors is facilitated by the development of an accurate and concurrently posted record of all facts essential to smooth and efficient operation. Such a record is created by the supervisors who furnish the original data, but the record itself must be used and interpreted by superior department heads. Through them the information becomes available to the personnel that is responsible for the actual work of the enterprise.

Perfection in performance is an ideal toward which management always strives. Since performance, in large part, depends upon human beings, its ideal achievement can never be fully realized. Nevertheless, many defects and deficiencies can be remedied and avoided by adequate supervision. Often the individual foreman who experiences trouble is not the one responsible for it. It may be that someone else in the supervisory group has contributed to the problem. And there are faults in performance which are chargeable jointly to supervision and higher executive management. This joint responsibility is illustrated in the examples which follow.

Joint Responsibilities of Supervisors and Executive Management

When changes and additions in products or services are decided, the decisions involved are clearly those of higher management. If delay and confusion are the result of such decisions, the trouble can be charged to department heads who have failed to properly implement such departures and innovations at the level of performance. However, supervisors can help or hinder in transitions of this kind in proportion to the effectiveness of their skill and cooperation. When operating departments have to curtail operations because of inadequate supplies, equipment, facilities, or personnel, the basic failure is the fault of management higher up. Yet, individual supervisors are partly to blame in such circumstances. Their

fault may be neglect in informing their superiors of the things that are lacking or their own errors in judgment and full use of the facilities at their disposal. Other difficulties akin to the foregoing and, jointly, a managerial and supervisory responsibility are: continued use of antiquated equipment, the failure to take advantage of new devices and methods, and deficient training courses for employees or the complete absence of such programs.

Again, when management is unable to obtain accurate costs because its system is defective or to obtain accurate time studies of individual employees and machine operations, the failure is executive—but with contributory supervisory negligence or ignorance. There is much that cooperative supervisors can do to insure accuracy in costing and in time study. Also, when a supervisor finds that a high proportion of the output of his department will not stand critical inspection, he, as well as higher management, is at fault. If the material with which he has to work is defective, or if the inspection to which he is subjected is not valid or defensible, it is his duty to discover ways and means by which such difficulties can be corrected.

Responsibilities Solely Supervisory

In addition to problems that are jointly managerial and supervisory, there are some that are primarily due to faulty supervision alone. In this category the outstanding weakness is defective workmanship. The foreman or supervisor is employed by his particular enterprise to see to it that the employees turn out satisfactory work. Failure to accomplish this end is an invitation to the management to find some other supervisor.

Closely related to defective workmanship are the failures in timing the flow of work. If the supervisor who has that particular work under his charge fails to expedite and arrange the flow of work in order to prevent delay, the embarrassment, confusion, and extra cost that result are his own responsibility. If, within a particular operating department, production is not planned so as to reduce to a minimum the delays resulting from obstacles in mechanical and other processes, obviously the foreman or superintendent is accountable for the failure to meet promised deliveries. If the final assembly of a product is not synchronized, it is probable that, somewhere along the line, someone under the jurisdiction of a supervisor was off schedule.

In most enterprises, final responsibility for an adequate supply of trained labor rests with the individual supervisor. Where such a policy prevails, failure to have such a supply is the fault of the supervisor alone, and he must answer for the consequences.

One of the difficult problems of management is to settle fights and feuds between otherwise competent supervisors. One foreman may hate

another foreman, and say so whenever he has an opportunity. When such a difference results in faulty coordination of operations or in unnecessary costs and wastes, the failure clearly lies with the supervisors. They must be required to settle their quarrels amicably or else be removed from their jobs.

One of the best techniques for developing efficiency of performance is the standing committee of foremen and supervisors. Often such a committee is organized along semivoluntary lines as a quasi-social club of the supervisors. It is also frequently linked with the foremanship training program, or with activities of the personnel department devised to handle employee complaints or to develop safety measures. However organized, it is an association of foremen and supervisors—with or without a membership of higher executives—established for the purpose of discussing common problems. To accomplish the best results, such a committee or association should have a preplanned program, and its meetings should be conducted like a panel or forum. Much of its value comes from free and full discussion, or "post-mortem" review, of the errors that have been made, and of the criticism of the management concerning the quality of supervision in particular cases. Such committees can be the best possible conference method of foremanship training.

Supervision of Employees

The relationship of the supervisor to the employees under his jurisdiction depends upon his status. If, because of the work he performs, the supervisor considers himself to be nonmanagerial in rank, his executive influence upon the personnel under his supervision will be narrowly limited. This is true, for example, of the train conductor. Only in emergencies does his authority allow him to exercise control of the remainder of the train crew beyond certain traditional, well-recognized limits.

On the other hand, if the supervisor is regarded as the personal representative of the higher management, his power to direct and control his subordinates may be very great. This is the case, for example, of the supervisor of a small chain store unit remote from headquarters. Such a store manager must be given broad powers to manage his employees.

For various reasons, executives at the lowest supervision level of management may be regarded as either employees or management. There is a tendency for some labor unions to seek to annex assistant foremen and similar supervisors as regular employee members of their organizations. On the other hand, employers identify as "management" all supervisors who do not perform regular production work. Both efforts emphasize the marginal character of the assistant supervisor on the border line between management and employees.

The relation of the supervisor to his employees depends likewise upon the size of the particular business enterprise. In general, the smaller the enterprise, the more complete is the authority and responsibility of the supervisor for all personnel matters, such as selection, training, instruction, and motivation through transfer, promotion, discipline, and discharge. As the size of the particular business increases, it becomes necessary to employ functional specialists to handle such problems as employment, safety, workmen's compensation for accidents, apprenticeship training, and wage rates. These functional specialists divide the total authority over personnel with the various supervisors. The authority of the supervisor is apparently weakened by this division. Actually it is increased, since he has more time for concentration upon his main task, that of motivating the individual employees to do their work as efficiently as possible.

Selection and Training of Employees

The selection of employees consists of two steps: first, it is necessary to find persons who meet particular job specifications; and, second, from among those who meet the qualifications of eligibility, it is necessary to select employees who seem to offer the best potentialities. In small enterprises, both activities tend to be performed by the supervisor. When a business has become large enough to have a central employment office for recruiting and interviewing, the two steps are divided between the employment office and the supervisor. The supervisor does not have to take valuable time away from his department for recruiting; but he still possesses final veto power and can, therefore, select, from among the eligible candidates, the employees he desires to have in his group.

The training of employees is partly the responsibility of the supervisor and partly outside of his province. To an increasing extent, instruction in various trades and occupations is offered by many schools, both public and private, prior to any employment. In many instances, business concerns themselves maintain regularly organized and scheduled schoolwork for apprentices and other new employees under the supervision of specially employed educational directors.

However, just as educational and training programs for foremen are recognized as an essential element in management at the supervisory level, so has the instruction of employees come to be a responsibility of the supervisor. This responsibility has two aspects: First, there is instruction in connection with the job itself. A worker can hardly be expected to conform to increasingly exacting standards of performance unless he is taught how he can best apply his talents and skill to the work which is assigned to him. His workplace is his laboratory, but he needs guidance if he is to learn by his experience. Therefore, the supervisor is constantly teaching his employees the fine points of their work. He is

striving to help them to correct their minor faults or to avoid developing bad habits that will result in accidents or damaged material.

The able supervisor also engages in another type of instruction, which may be called "authoritative education." This term is used because it describes the process of being taught by one who is an expert in his field or craft, such as a good supervisor is expected to be. In this capacity he not only shows employees how work must be done, but he explains as he demonstrates.

Authoritative education also conforms to conditions in large business firms in which individuals rarely see any executive other than their immediate supervisor. In such concerns, operations are carried out by means of written orders that are actually formal instructions of an educational character. The individual knows exactly what performance is expected of him when adequate written instructions have been supplied. It is usually easier for the employee to accept and to comply with the instructions from a competent and sympathetic supervisor than to contrive how to disobey the orders to which he is subjected.

Furthermore, this type of instruction may extend to an explanation of company policies and objectives in order that employees may have an intelligent conception of the whole enterprise. Work becomes dull, monotonous, and irksome when the one who performs it conceives of no other purpose of his efforts than his pay envelope and the firm's profits. Too often it is assumed that a generous wage supplies an adequate incentive to work. This assumption is merely a half-truth, for there are other compensations equally as important as the remuneration one receives for his labors. A supervisor who has the ability to instill in his employees the desire to learn can make a significant contribution through authoritative education.

Motivation of Employees

To most workers, because of his immediacy and close association, the supervisor is "the management." For this reason the latter is in a position to exert strong influence upon the motivation of the individuals under his supervisory jurisdiction. In other words, the supervisor can incite in his employees ideas and emotions which affect their morale and their operational efficiency. The means he can use to produce such attitudes are both positive and negative in character. They are positive when a supervisor uses his influence to transfer and promote employees to more favorable assignments, and they are negative when the reactions of workers are induced by discipline or fear of discharge.

Even though the final authority for the determination of wages, hours, and working conditions rests with executives of higher management, every employee feels that the supervisor is responsible for his earnings

and the circumstances under which he works. It is only natural that he should feel this way toward his "boss." Therefore, when the supervisor assigns an employee to better and more profitable work, he thereby creates an added inducement for increased productive effort and a greater loyalty to the company itself.

Likewise, a supervisor can encourage the transfer of an employee to more desirable employment; he can request an increase in pay for him; or he can use his influence to secure a promotion for anyone who, in his opinion, deserves such recognition.

These activities are all devices of positive and desirable motivation, properly at the disposal of the supervisor. It follows that by means of them he is equipped with his greatest power in the management process. Wisely used, this power enables him to weld his organization into an effective and happy group. If this power is not realized or used, or if it is improperly applied, the influence of the supervisor, or the lack of it, in the important matters of assignment, transfer, and promotion, may stultify and actually ruin departmental efficiency and morale. Employees react favorably to fair, considerate treatment. They have their own notions as to when they are treated fairly. The supervisor must be capable of sensing such feelings, and, where merit exists, anticipating them by positive action without yielding to pressure and flattery or engaging in favoritism.

As has been said, supervisors also motivate employees through the negative means of fear of disciplinary action or of discharge. Discipline no longer includes physical punishment but is accomplished by means of a formal or informal system of ratings, demerits, or "black marks." When mere warnings and threats are of no avail, the employee may be laid off for a period or even discharged.

This negative device of discipline and discharge was formerly one of the principal techniques of supervision. Today it is losing its force. On the one hand, union rules protect the employee from unreasonable or arbitrary use of the power to discharge. On the other hand, the tendency is for management to take this authority away from the supervisor and to vest it in the hands of a specialized personnel manager. Furthermore, fair dealing on the basis of recognized merit is an instrument of self-discipline which is more effective in securing orderly conduct than are imposed rules, regulations, and threats.

THE AUTHORITATIVE STATUS OF THE SUPERVISOR

The authority that is delegated to the supervisor is limited to routine operations. He determines no basic policies, and he makes no broad managerial decisions. Within the framework of the established managerial organization, he takes his work as he finds it, and plays his part in

the achievement of predetermined goals through the execution of orders that come to him from higher management.

Influence upon Authoritative Management

The supervisor is not without the power of exerting forceful influence upon the character of the managerial decisions that affect him and his work. By means of his interpretation and application of such decisions, he may be instrumental in their modification or even in the gradual creation of a basis upon which they are built by his superior officers. For example, he may receive orders that a certain product shall be made or a service rendered by the employment of specified equipment or facilities. The supervisor may find it impossible to carry out such orders precisely. His inability to make prescribed deliveries may be due to repeated breakdowns in equipment or to the unfitness of the facilities which were designated to perform the required work. When successive failures of this kind are followed by requests from the supervisor for the modification of instructions to conform to actual working conditions, his suggestions and recommendations will eventually result in revisions in the orders he is expected to follow or will actually form the basis upon which future instructions are prepared.

The main purpose of interpretation by the supervisor is not to cause review by the higher management but to get the assigned task accomplished. Operation happens over and over again under modern industrial conditions. Nature, however, is constantly changing, so that raw materials are not absolutely uniform, weather conditions are different every day, machines operate differently from time to time, and employees have varying moods. To the supervisor, therefore, routine operation represents an exciting series of conquests of actual conditions in order to maintain unvarying quality and quantity of performance.

If the conditions under which operations must take place did not change, it might be possible to set up a business organization with fewer skilled supervisory executives. But because these conditions are changing constantly, the supervisor, by the exercise of his own judgment and skill, must manipulate the facts of the moment to achieve the results desired. In this adjustment process, business management ability is more than mere knowledge. It is an intuitive process not unlike the genius of the military commander.

In modern armies likewise, this responsibility and authority at the lower levels of command is to interpret and to modify orders received from superior officers to meet actual battle conditions. The purpose, rather than the exact wording of an order is the significant fact. Every subordinate officer is expected to make his own estimate of the actual situation and to interpret his instructions accordingly. For example,

troops may be told to advance at a particular time, protected and aided by an advancing screen of artillery fire. If the artillery fire is improperly timed or aimed, the subordinate infantry commanders in the front line of battle must make the best of the actual situation. Their purpose is to win the battle—a purpose unlikely to be furthered by ordering their men forward to be killed from behind by their own artillery—and the subordinate officers at the front must make the decision since communication with

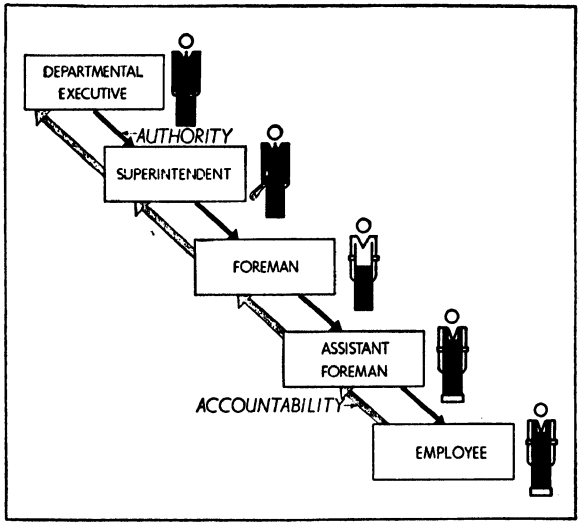


FIG. 18.—The flow of authority and accountability in a simple line organization at the supervisory level.

superior officers would waste precious time and accomplish nothing. Thus the skilled appraisal of actual conditions and the trained initiative of subordinate officers multiply the strength of the army.

The Nature of Supervisory Authority

The characteristic relationship of supervisory levels to a departmental head and to each other is that of line organization. If several such levels are involved, the normal flow of authority is from a departmental executive to a superintendent and through him to a foreman. The foreman, in turn, instructs an assistant foreman, who supervises the employees. In the reverse direction, accountability flows up from the worker to the assistant foreman, who reports to his foreman. The foreman is accountable to the superintendent, who is immediately subordinate to the departmental executive. Figure 18 illustrates this simple arrangement.

In a modern complex organization the flow of authority and accountability is not so simple. As the scope of management has been forced to include the supervision of increasing numbers of individuals, the old

concept that an employee should take orders from and be accountable to but one superior executive has had to be modified. In large concerns it is now the common practice to require a worker, and even other persons of various executive ranks, to recognize multiple authority. That is to say, *more than one line of authority* may descend directly to a particular employee; and by reason of this fact, such a person may, in turn, be required to be answerable for his work and conduct to more than one superior. At the supervisory level, however, and from the standpoint of the worker or other recipient of instructions, all technically titled authority blends into one, namely, the right and power to give orders and to exact obedience.

Analysis of Supervisory Authority

From the standpoint of management technique, multiple authority can be analyzed and justified. It is obvious that normal line authority must always prevail. That is, the right and power to command and to exact obedience are indispensable. In small concerns this type of authority is usually sufficient: it can properly encompass all the phases of direction, supervision, control, and inspection that are required at the level of work performance. But as enterprises become larger, such managerial activities grow more complex and supervisory specialization is necessary.

One of the basic principles of departmentation is that responsibility for inspection should be distinct from the corresponding responsibility for production. Even in a small factory, the product inspector should report directly to the production manager—independent of the foreman. In a large business, the inspection department may be organized under an independent department head, reporting to the appropriate major executive. In the case of factories, the chief chemist often is head of this department, because of the importance of skilled chemical control in production. In a public utility, inspection is primarily related to public relations, or to rate-making, thus making it most appropriate to place the inspection activity under the department head in charge of public relations.

It is usually true that a particular employee comes under one inspection line of authority for routine production inspection and under other lines for various nonroutine purposes. The audit method of inspection, for example, comes down to the employee from a major executive.

At intervals, portions of the activities of planning, preparation, and scheduling which are involved in the processes of producing goods and services reach all employees. The selection of an employee by the personnel department and his possible training in the educational department are necessary aspects of planning and preparation. The classification of work to be performed—getting it into its proper channels and directing its flow from inception to accomplishment—requires scheduling in which

workers are obviously involved. Here processing and timing are two very distinct activities, often each being the responsibility of a different person. It may be very good management procedure to require a worker to look to a production foreman for instructions pertaining to processing and to a route clerk for the sequence of operations.

Minimizing Multiple Authority

Many different organization plans have been suggested for the purpose of preserving the exercise of complete authority and responsibility over a particular employee by only one supervisor, in compliance with the principle of line organization. Such plans consist, in general, of provision for terminating the multiple lines of authority and responsibility at one of the supervisory levels above the employee. Instructions may be given that the foreman is to receive all orders intended for the employee beneath him. Attempts of this sort are sometimes unrealistic and add cumbersome organization machinery without commensurate advantage.

The primary task of the supervisor is to interpret instructions to the employee so that production may be accomplished. When a foreman is required to transmit to the employee technical instructions without interpretation, he serves merely as a channel of communication rather than as an interpreter. He may even be antagonistic to the seeming interference with his own prerogatives. If the multiple lines of authority are not allowed to reach down to the employee, crosscurrents are set up within the organization and duplication of managerial effort is increased. Two types of multiple management organization are illustrated in Figure 19.

From an organization standpoint, a plan that reduces confusion is to permit authority to take its turn. The following examples may serve to illustrate this method: (1) The personnel executive has nothing to do with an employee unless the latter is fired by the foreman or supervisor. Then, according to practice in many companies, the employee is merely transferred out of the department, and the personnel executive has the authority to confirm the discharge or to place the employee in another department or in different work. (2) A sales department may wish to take offered business but must defer to the veto power of the credit department. (3) A locomotive engineer must obey the orders of the dispatcher and the conductor in his movement of the train, but he must also follow the instructions of the superintendent of motive power in the operation of his locomotive.

The rotation plan of multiple authority grows in effectiveness as the employee becomes used to the presence of several bosses. He will look to different supervisors for instructions as different problems arise. When the successive instructions of various executives are in conflict with each other, the situation becomes confusing and requires coordination by the

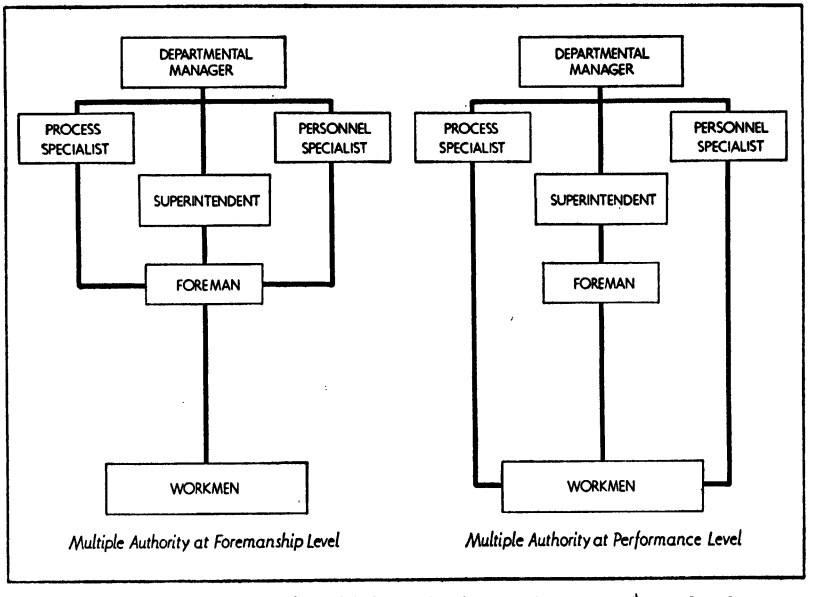


FIG. 19.—Two types of multiple authority at the supervisory level.

major executive only because the employee necessarily obeys the nearest executive or the one whom he most fears or respects.

In the last analysis, therefore, the problem of multiple lines of authority reaching down through the organization toward or even to the individual employee cannot be solved solely through organization. Its solution depends upon intelligent and effective coordination by the responsible supervisors.

THE SUPERVISOR'S SHARE IN MANAGEMENT

Complexities in the development of organization for management have changed many of the duties and tasks of supervision, and the traditional status of the supervisor in the management structure has changed with them. Half a century ago, when the supervisor was an autocrat exercising authority over his work force without consulting the higher management, he was "the management" in the eyes of those under his oversight. In modern management, many within the executive organization participate and share with him in his detailed supervision. However, this does not mean that the supervisor is being relegated to the status of "leading hand" or "number one employee."

The present-day supervisor must have more ability and skill than his predecessors. Less of his time and energy is taken up with details and problems outside of the scope of supervision, and more time must be given to the immediate problems of performance. The modern super-

visor must regulate the production of goods and services within closer limits in order to realize higher quality and greater efficiency. He must direct the flow of work more carefully in order to meet delivery promises. He must interpret to his employees the instructions and orders that come down from higher management and, especially, avoid snarls in the multiple lines of authority that reach down from numerous executives to the workers. He must use positive rather than negative methods in the training of employees and in providing them with adequate incentives to do their work properly and efficiently.

Therefore, it may be said that the position of the supervisor is increasing in significance. More and more he is being accepted and regarded as an important part of the management group. This improvement in status is a manifestation of the recognition of his increased ability and skill, but it should not be allowed to result in a widening gulf between supervisors and their employees. Somehow, the supervisor must continue to be part of management, yet close to his workers. He must fraternize with his subordinates, but he must also interpret and represent the management to them. He must lead by example and motivate without force; yet he must also respond to the pressure of the higher management for greater efficiency and better operating results.

QUESTIONS

1. It has been said that foremen, though considered a part of the organization for management, are not, in fact, *treated* as a part of management. Discuss this view fully, using the following points as an outline, indicating the extent to which you believe each point to be true:
   a) The relatively low earnings of foremen as compared with the earnings of the workers under their immediate supervision.
   b) The failure of foremen to share in any bonus or other benefits that result from the prosperity of the company that employs them.
   c) The humiliating treatment of foremen by superior executives, and their subservience to rules promulgated by the higher management.

2. On the basis of the two types of multiple authority at the supervisory level that are graphically illustrated in Figure 19, explain the different procedures that must be followed in dealing with the worker under each of the following circumstances:
   a) A new employee is introduced to his fellow workers and is taught to do the work required of him.
   b) An employee is discharged for cause.
   c) An employee has a grievance against the company which he takes up through a designated representative of the labor union to which he belongs.

3. The statement which follows below may be true, partially true, or wholly false. Study it carefully, and then rewrite it at greater length so that it becomes a true and explicit statement according to your understanding, bearing in mind that negotiations between employees and unions are required by law:

   "Since the average worker looks upon his immediate supervisor as his employer, the foreman loses prestige when negotiations between an employer and a labor union take place at a higher management level, even though the particular foreman is kept fully informed by his superior executives of such negotiations and their progress."

4. As elements in the training and development of foremen, give examples that illustrate the importance of the following considerations:
   a) Foremen must be honest and fair in dealing with—
      (1) Higher executives.
      (2) Other foremen.
      (3) Employees, whether or not such employees report directly to the foremen in question.
   b) Foremen must be willing and conscientious in—
      (1) Assuming responsibility for mistakes.
      (2) Avoiding "buck-passing," or shifting blame to others.
      (3) Studying and adopting improvements in procedures and processes.

5. Explain the proper role of the supervisory level of management in the settlement of employee grievances, taking into account the following points:
   a) The attitude of the foreman and his knowledge of company policy influence significantly the number, kind, and importance of employee grievances.
   b) Experience with union-employer contracts that provide for grievance procedures beginning with foremen at the supervisory level reveals that about half of all grievances can be settled at that level without further appeal to higher management executives or to higher union representatives.

6. Indicate fully your views on the following supervisory personnel practices:
   a) Supervisors should always be paid more than the highest-paid workers under their supervision.
   b) Supervisors should have managerial status with respect to vacations, sick leaves, and retirement plans; and they should receive monthly salaries rather than wages on an hourly basis.
   c) When supervisors are returned to the status of workers for such reasons as the closing of their shops or the discontinuance of their type of work, they should have their seniority rights fully protected by the management and, if necessary, by union agreement.

7. "Favoritism" is often a troublesome problem at the supervisory level. State fully your views on this subject in the following instances:

a) Should foremen be prohibited from accepting gifts of any kind from their subordinates, such as a box of cigars at Christmas time?

b) Is it improper for foremen to "share the ride" to and from work in a subordinate worker's car?

c) What is "nepotism," and what is its relation to "favoritism"?

8. Contrast the following statements of the purposes of the supervisory level of management, and indicate clearly how the two different aims or goals are not inconsistent with each other:

a) The basic tasks of employee supervision are to obtain desired output, raise standards of quality, avoid waste, lessen accidents, reduce unit costs of production, and bring about improvements in procedures, processes, and products.

b) The basic tasks of employee supervision are to teach, guide, and adjust workers to their jobs so that they may have the opportunity to obtain the maximum possible satisfactions of life and living.

9. Outline your own views as to what the qualifications and skills of a typical foreman or supervisor should be, using the following points as a check list:

a) Effectively assume responsibility for worker morale.

b) Understand company policy, at least to the extent of knowing what results must come from the work done under his direct supervision.

c) Know the limits of his own executive discretion as a foreman or supervisor.

d) Know where to go for information and guidance.

e) Know how to serve as a channel for establishing and maintaining two-way communication between individual employees and the higher management.

10. Rewrite the following incorrect statements, indicating fully the reasons for your corrections:

a) Foremen have no difficulty in doing their work properly even though the company's management, viewed as a whole, has areas of faulty organization, tolerates improper personnel practices, is beset with personal clashes between executives, and has many clogged lines of communication between the higher and lower levels of management.

b) Supervisory executives, such as foremen, have such excellent morale that they can generally surmount such minor obstacles to management unity as the following typical actions of a certain kind of senior executive:

(1) High-pressure or driving tactics, such as ordering that some work be performed within a certain time without inquiring as to the burden imposed thereby upon the foreman and his workers.

(2) The imposition of training and study responsibilities upon foremen in such a way as to make the supervisors feel they are being re-

garded as inferior to the higher executives, rather than as equal partners in the management of the enterprise.

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Chapter VIII

PRIMARY DEPARTMENTATION

THE PRINCIPLE OF DEPARTMENTATION

DEPARTMENTATION is a major principle in the theory of business organization. It may be defined as the "dividing and arranging of the managing and working forces, together with the processes involved, of a business enterprise into specialized units or groups." Departmentation includes the combining of activities for the purpose of harmonious and efficient operation, thus embracing the principles of functionalization and coordination. It also results from the creation of levels of management with their attendant lines of authority by means of which internal relationships are maintained.

"Departmentation" should be distinguished from "division of labor" as this term is commonly used by economists. In its simplest form, "division of labor" refers to the division of employments, such as farming, fishing, shipbuilding, selling, and other occupations. In its more complex meaning, it indicates the characteristic separation of tasks in the factory system, as, for example, in shoemaking, where one task involves the making of soles, another the uppers, another combining them, and so on until the manufacturing process is complete. A "department," in the language of business organization, is a term which includes in its meaning such units as sections, divisions, districts, or any grouping of personnel for the purpose of management. It is true that such units represent a division of the work of management in that different members of the management group perform different tasks which, when coordinated, have the same end or objective in view. Yet, a department, so conceived, may at the same time comprise groups of workers engaged in a production process in which there is a high division of labor.

Thus departments form the framework of a business organization; that is to say, a department is an agency or vehicle of management. The "departments" of the executive branch of our federal government furnish an analogy. They are: State, Defense, Interior, Agriculture, Commerce, Labor, Post Office, Treasury, and Justice. The heads of these departments are generally called "secretaries" except for the Postmaster General and the Attorney General. Together these executives form the President's Cabinet, though they have no concern with the departmental problems of one another. Similarly, army organization is also a composite of

specialized units which properly may be called "departments." These units include the infantry, artillery, cavalry, air force, engineers, medical corps, intelligence, communication, supply, and others. In fact, wherever there is orderly and purposeful direction and supervision of human affairs, there also will be found organization based on departmentation.

The Purpose of Departmentation

The purpose of departmentation is threefold: (1) to specialize executive activity, (2) to simplify the tasks of management, and (3) to group employees for the purpose of direction and control. The limitations upon executive capacity to direct and control were discussed at length in a previous chapter. It was shown that, as soon as any phase of management passes beyond the capabilities of a single executive, departmentation becomes imperative. Modern business requires that work be done systematically, efficiently, and methodically. In fact, the whole principle of departmentation rests upon a foundation of expeditious performance. Therefore by grouping employees under responsible unit heads, each sphere of executive activity is narrowed to limits commensurate with managerial capacity.

Types of Primary Departmentation

This grouping of personnel into departments is accomplished in different ways. Three primary methods prevail, namely, territorial, commodity, and functional. But seldom, if ever, do we find a single organization which typifies any one of these plans to the exclusion of one or both of the other two. Most organizations—excepting perhaps very small ones —are so departmentized that all of these types are represented in combination to a lesser or greater degree. For the purposes of critical analysis and study, each of them will be considered separately.

TERRITORIAL DEPARTMENTATION

Reference has been made to the tendency manifested by the segments of business organization to break into vertical lines, the simplest of which is separation by location. The reason for this tendency is that, in some instances, it is possible that managerial efficiency may best be effected by grouping together under one responsible head all the activities which are performed within a prescribed area. Such grouping is called "territorial departmentation." It is a frank recognition of the human limitations of knowledge, time, and energy in the affairs of management.

This geographical separation is most apparent in a large business whose occupational objective is to serve a clientele on a national scale, or in one whose international trade has reached large proportions. We have already

observed the application of this principle to railroad transportation.[1] The same method is commonly used in the management of so-called "old-line" life insurance companies. The home office of a life insurance company is usually located in a large business center like New York, Philadelphia, Chicago, or Toronto. Radiating from such a center are district offices in strategic cities which dominate the areas surrounding them. Denver, San Francisco, Seattle, Dallas, and St. Louis are examples. A district office, in turn, is the focus of many small agencies, or even individual agents, located in the towns and smaller cities within the territory served by the district office. This method is illustrated in Figure 20. When this scheme of

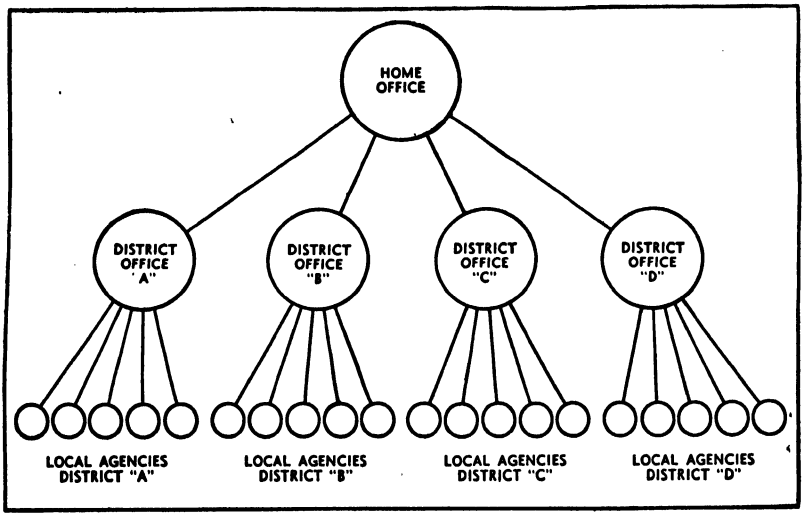


FIG. 20.—Schematic representation of the territorial departmentation of a typical life insurance company.

territorial departmentation is highly developed and instituted in all parts of the country, it forms a managerial network which explains to a great extent the enormous coverage—paralleled nowhere in the world—which the life insurance business enjoys in the United States.

Governmental Territorial Departmentation

Whether the prototype of territorial departmentation is to be found in government organization cannot be proved with assurance. Nevertheless, government does furnish an analogy which is useful by comparison. In the United States we have a central government surrounded, in a sense, by those of the various states and territories. Within the states there are counties, municipalities, townships, and school districts. Each of these

[1] Chap. IV, Fig. 12.

units is essentially autonomous, it is true, and not a branch of a central government. At the same time, they represent the geographical division and distribution of the authority and responsibility of organized society in governmental management. The acceptance of this method of geographical separation has been so widespread that, when territorial departmentation has been adopted by business enterprises with centralized authority, political boundary lines between states and between counties within states have been designated, more frequently than not, as delineating the limits of sales territories and other areas established for management purposes. Because political boundary lines have little or no bearing on the determination of economic territorial units in a democracy like the United States, this practice has been followed more as a result of habit and tradition than logic.

More nearly to the point, perhaps, is the territorial departmentation employed by the service and regulatory agencies of the federal government in their far-flung activities over an area as large as the United States. In their management, it is generally found that a central office is maintained in Washington, with district offices distributed geographically on a regional or, in exceptional cases, on a state-wide basis. The main purpose of such departmentation is clearly that of efficient and expeditious supervision and control. The Federal Reserve System is an example. The act creating it was passed in 1913. By its terms, provision was made for the establishment of Federal Reserve Districts, each of which was to have one Federal Reserve Bank. When the law was put into effect, twelve districts each with its own bank, were accordingly created. While each bank is self-governing as far as its operations are concerned, and distinct from any other Federal Reserve Bank, authority for the formulation of major policies for the whole system is centered in the Federal Reserve Board. There is, therefore, no central reserve bank with twelve branches. Rather, there is a central coordinating agency established to direct twelve major banking units, each of which, with the exception of Boston and Philadelphia, has one or more branches. These branches, as well as the parent banks, serve definite areas whose boundaries do not, in all instances, follow political boundary lines but cut across states in the interests of the localities served. The complete territorial departmentation of the Federal Reserve System is shown in Figure 21.

Chain-Store Territorial Departmentation

Territorial departmentation is basic in the organization of chain-store companies for the reason that the occupational objective of such a business implies geographical dispersion. The extent to which management will be broken down by regions and districts will depend upon the size of the concern and the extent of the area served. In general, however, the

diagram shown in Figure 22, representing a chain grocery store system, is fairly typical. In this instance, territorial departmentation is shown to appear below the first level of major executives, which is functional in character. The first territorial division is by districts, with a manager in charge of each. The extent of each district follows no fixed or traditional pattern. Sometimes—as in some of the larger chains—a district may include several states, or parts of them. In other instances, a district may be much smaller in area. Whatever its size, the principle of departmentation involved is the same, namely, that a balance is sought between spatial con-

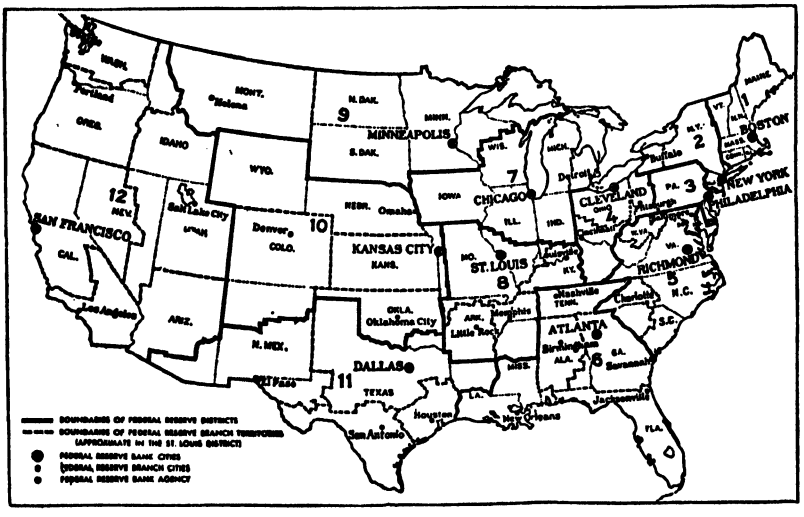


FIG. 21.—Federal Reserve districts: territorial departmentation in the Federal Reserve System.

siderations and the span of control by having subordinates report to one superior officer.

As shown in Figure 22, each district manager has under his direction a number of supervisors. Each supervisor is responsible for the stores located in a prescribed segment of the district of which it is a part. Such a segment may embrace several counties in a rural region, or it may be confined to a part of a metropolitan area where the density of population is high. Subordinate to each supervisor are several store superintendents, who, in turn are immediately superior to the store managers who operate the individual units. Thus, a store superintendent may direct the store managers in several small towns, or, as is the case in a large city, his duties may limit his territory to a matter of blocks, depending upon the number of stores involved.

This description serves to emphasize the fact that in contemplating the

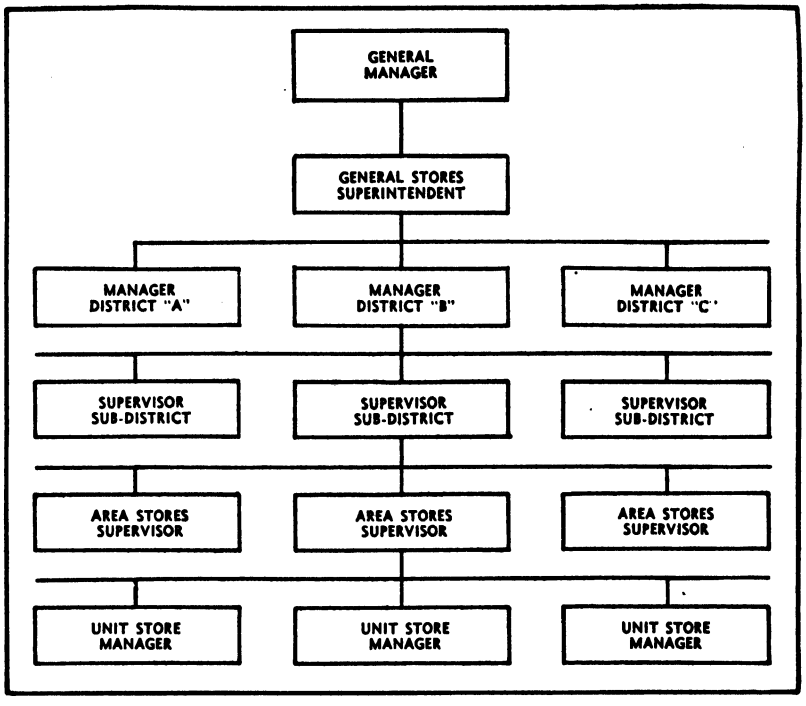


FIG. 22.—Territorial departmentation in chain grocery store organization.

levels of management from the standpoint of space or territory, other phases of the concept of the span of control are inescapably involved. This is particularly true with respect to the number of subordinates under supervision, but it may also have to do with knowledge, time, energy, and attention.

Territorial Departmentation in International Trade

Business concerns operating on an international scale also find territorial departmentation indispensable. One such concern is the General Motors Overseas Operations, Division of General Motors Corporation. This organization is charged with the manufacture and distribution of the products of the corporation in all parts of the world, especially outside of the United States.

To accomplish this objective, a central office in charge of a general manager is maintained in New York. Subordinate to him in line of authority are seven regional managers, each in charge of a major territorial division as follows: Pan-American Region, for the Argentine, Mexico, Brazil, and other undesignated Latin American countries; General Motors Inter-America Corporation, for Venezuela, Cuba, Peru, Chile, and Uru-

guay; British Isles Region, for Great Britain and Ireland; Australian Region, for Australia and New Zealand; Far Eastern Region, for India, the Malay States, the Netherlands East Indies, the Philippines, China, and Japan; European Region, for the Scandinavian and Low countries, France, Germany, the Soviet Union, and the Balkans; and the Mediterranean-African Region, for Switzerland, the Iberian Peninsula, Italy and other undesignated Mediterranean countries, the Near East, and South Africa.

Each regional manager supervises and directs from two to six managing directors, who are, in reality, local company managers, of whom, in 1946 there were thirty-one. A local branch or office has the responsibility of serving a district which may be coextensive with a nation or may be larger or smaller than a single country. To render such service, each managing director may have at his disposal zone managers who, as their designation indicates, undertake the handling of General Motors products in areas smaller than a district. To do this work, each zone manager, in turn, may have under his immediate direction a corps of field or local representatives who supply the local market. Thus markets constitute zones, zones make up districts. districts form regions, and regions comprise the portions of the earth in which General Motors carries on its overseas operations.[2]

In this, as in other examples of geographical separation of the tasks of management, location is the basic factor in departmentation. Furthermore, departments formed in this manner are identified by definite physical limitations as well as by other considerations.

Advantages of Territorial Departmentation

While territorial departmentation is a recognition of the physical limitations of executive capacity, it may be supported on other grounds. The area over which an executive may extend his influence effectively varies with his relative familiarity with the details required of him. In the consideration of the span of knowledge, the significance to an executive of witnessing performance was emphasized. Thus, the "section boss" on a railroad may find that the requirements of his job restrict his "territory," that is, his section, to ten or twenty miles of track, while the division superintendent, who is his immediate superior, relieved of many details by his subordinates, can supervise many hundreds of miles and not find his assignment excessive.

Territorial departmentation may also be found to be advantageous in times of emergency. Upon such occasions, executive authority, immediately at hand, may mean the difference between order and confusion

[2] "The Organization of General Motors Overseas Operations, Division of General Motors Corporation, April 4, 1946" (Supplied by Edgar W. Smith, administrative assistant).

or between profit and loss. For example, it is possible for the management of a manufacturing concern to direct the operations of a branch plant located in another area from a central office in the parent establishment. Such a policy might work satisfactorily under normal circumstances. But in case of break downs, labor troubles, or other difficulties, local management may be found to be exceedingly more desirable than an arrangement whereby orders and decisions can only be issued from the headquarters, situated remotely from the scene of the branch plant operations. Similar considerations are involved when favorable business opportunities of a local character present themselves and demand immediate decisions.

A third advantage of territorial departmentation arises when different areas present widely different problems of management. A wholesale house, for example, may find that the problems of selling in a congested area are quite different from those encountered in a sparsely settled region. Or, to return to railroad management again, the problems of railroad operation in a mountainous section of the country have no parallel in the prairie states.

COMMODITY DEPARTMENTATION

A second type of primary departmentation is separation of management activities on the basis of goods or services, that is, "commodity departmentation." It is apparent that specialization by this method has its genesis in the ancient handicraft system in which each artisan was an expert in his own occupation. He manufactured only that product in the making of which he was most skilled. His trade, and even his name were identified by the commodity which he produced. With the development of the factory system, skills likewise became the basis of the division of labor already referred to, and it has been but a natural step to extend the same idea to management.

Commodity Departmentation in Manufacturing

Thus, it often happens that certain kinds of direction and supervision can be exercised to the best advantage by grouping together activities which deal with particular commodities. Vertical separation in this manner takes place most frequently in production processes. As a rule, both the human skills and the mechanical facilities required in the manufacture of one commodity in a plant differ considerably from those required in the production of another. Even the raw materials involved may be quite different and unrelated in each case. In the meat-packing industry these distinctions are very clearly drawn. Even in the smaller plants, it is common to find three primary divisions, designated as the beef department, provision (pork) department, and the small stock (veal and mutton)

department. In the manufacture of automobiles there are also many divisions which are identified with particular reference to the commodities produced. Thus, in an automobile plant we find a body department, motor department, radiator department, wheel department, painting department, and so on.

In the examples given, the factor which distinguishes each department is the commodity which that department produces. Since special skills and special equipment are required in processing and handling the materials as they pass through the factory, specialization is carried one step farther to include management. Therefore, in the production division of an organization, the executive in charge of a commodity department is made responsible only for those activities which are peculiarly associated with the manufacture of a particular product. He has no jurisdiction over activities common to the production of all commodities. Problems of management, such as engineering, research, planning, inspection, storage, and numerous other considerations which relate to the whole plant, are the concern of functional executives whose authority and responsibility may cut across many commodity or territorial groupings which are otherwise separate and distinct.

Commodity Departmentation in Merchandising

Commodity departmentation also is often found in the sales organization of a business. The adoption of this method of specialization explains to a large extent the distinctive department store organization. The merchandising function in a department store is a combination of buying and selling activities. That is, the executive at the head of a department whose main purpose is to sell merchandise to customers is more often than not also the buyer of merchandise for that department. But buyers are specialized in terms of commodities. So well established is this policy in the merchandising field that specialization in buying has almost reached a professional stage. Buyers of furniture for sale at retail are obviously confronted with problems quite unlike those encountered by the purchasers of shoes, jewelry, house dresses, or men's furnishings. The mere mention of these classifications of goods is sufficient to suggest how vitally each type of merchandise, or commodity, determines the character of the management required for its purchase and sale.

Examples of the application of this principle are manifold. In wholesale houses it is common in both buying and selling activities. The practice of railroads in separating the freight department from the passenger department is a commodity distinction in the sense that these two types of service are recognized as economic goods. At the risk of stretching the analogy to the point of strain, perhaps it is not too farfetched to suggest that the separation of the fields of knowledge into departments in our

colleges and universities is an application of the principle of commodity differentiation to the business of academic teaching and research.

Distinction between Territorial and Commodity Departmentation

From the foregoing discussions of territorial and commodity departmentation, the distinction between them should be clear. The span of control in its spatial conception sets the bounds of managerial effectiveness, in the one instance, and the bounds of the span of knowledge in the other. In both, however, the factors involved are tangible and capable of being comprehended with definiteness and precision. Yet, distinct as these two methods of specialization are, they may easily overlap in their practical application. Such overlapping appears in an industry in which the production of different commodities takes place in different factories. Decentralization of plant implies geographical separation; hence territorial as well as commodity distinctions may be responsible for the method of departmentation employed.

The International Harvester Company has been cited as a case in point.[8] In this industry, tractors, harvesting machinery, and motor trucks are manufactured in separate plants located in widely separated localities. Each plant is practically an independent division of the central production department, completely separated on both commodity and territorial bases as far as processing is concerned. After the formation of the consolidated company, certainly these two principles exerted an influence upon the present character of the organization of the industry which hardly can be attributed to tradition alone. This combination is graphically represented in Figure 23.

FUNCTIONAL DEPARTMENTATION

The bases of primary departmentation by territorial and commodity considerations are largely material in character. That is to say, in applying these principles to the organization of an enterprise, executive activity is specialized according to the objects or things dealt with, whether such objects are a particular kind of goods or a limited geographical area. But there is also a subjective basis for departmentation. It is specialization in management based upon a classification of activities performed by groups of workers. This method is commonly called "functional departmentation."

Functional departmentation, by its very nature, is to be found in every organization where even a rudimentary separation in the managerial tasks is undertaken. Consider, for example, the kinds of activities

[8] W. N. Mitchell, *Production Management* (Chicago: University of Chicago Press, 1931), p. 216.

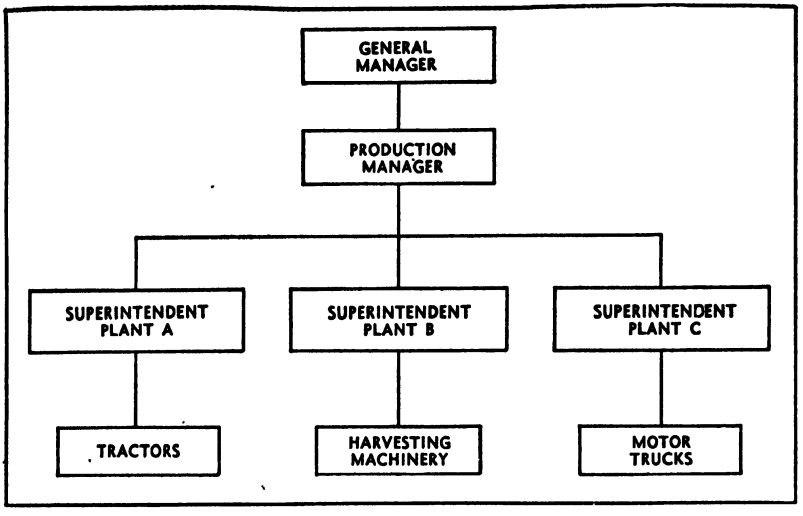


FIG. 23.—Territorial and commodity separation.

which are immediately evident when the establishment and operation of any business is contemplated. Invariably, if it is a merchandising institution, there are four such groups of activities: financing, buying, selling, and accounting. If a factory is considered, a group of production activities must be added to the list. It may well be that the cleavage between these distinctive aspects of management are the only ones which prevail. If so, we should expect to find departments with titles somewhat as follows: finance, purchasing, production, sales, and accounting. In a very small business, it is conceivable that only three separate divisions would be recognized, purchasing having been merged with production and accounting with finance.

As a business grows in size and scope, there is a tendency for each of these basic functions to become subdivided into several more highly specialized tasks. For example, personnel and traffic activities may emerge from the production department, advertising from sales, credits and collections from finance, auditing and claims from accounting, and warehousing and stores from purchasing. As these various activities are enumerated, a normal reaction is to think of each of them as a natural unit of management. And so it is in common practice: a functional department is a natural division of executive responsibility.

Rationalization of Industry

"Rationalization of industry" is a phrase sometimes used in the literature of management. It refers to functionalization, that is, the natural tendency for the activities of management to be placed in categories

identified by the special skills and techniques required in the various operations of an enterprise. "Rationalization" expresses an attempt to avoid the difficulties which are encountered in supervision and control when a multiplicity of tasks are branded with the same label and included within the jurisdiction of a single executive to such an extent that his responsibilities exceed the tolerable range of his span of control.

This is a point of danger, all too typical, in departmentation on an objective basis such as has been described. In other words, to expect an executive to manage efficiently a large number of workers engaged in miscellaneous operations is an irrational procedure. Here, again, reference to the "intellectual requisite" and the "span of knowledge" in executive competence recurs. It is the point at which functional departmentation parallels, if it does not actually join, the concept of scientific management as promulgated by Frederick W. Taylor and his followers.

Taylor's System

Taylor is credited with introducing the term "functional organization." When he conceived it, his interest had to do principally with the lower levels of authority in a shop, and he directed his efforts to correct what he considered to be the traditionally bad practices of foremanship in the industries with which he was familiar. As a basis upon which to establish his work, he enunciated the principle of functional foremanship, or multiple supervision at the foreman level. This principle is summarized in one sentence from his writings: "Functional management consists in so dividing the work of management that each man from the assistant superintendent down shall have as few functions as possible to perform."[4]

On its face, Taylor's principle suggests a close parallel with the span of control and the span of knowledge as these concepts relate to functional departmentation. But Taylor attempted to make a thoroughgoing application of his idea. As he studied and analyzed the duties of the foremen who came under his observation, he concluded he could classify their activities into eight groups, which, in turn, were separated into two levels —the upper level, planning, and the lower level performance:

PLANNING LEVEL

1. Order of work and routing
2. Instruction cards
3. Time and cost

PERFORMANCE LEVEL

4. Gang boss
5. Speed boss
6. Repair boss
7. Inspector
8. Disciplinarian

[4] *Shop Management* (New York: Harper & Bros., 1911), p. 99.

Figure 24 illustrates graphically functional foremanship as Taylor saw it. He visualized that the customary single foreman would be superseded by eight new ones, each of whom was to be limited in his sphere of activities to the special duties suggested in the diagram. When put into practice, Taylor's plan was a radical departure from custom because, instead of each employee having one boss, he would have eight.

It was, perhaps, on the rock of multiple bosses that the Taylor scheme of functional foremanship eventually foundered. While commendable

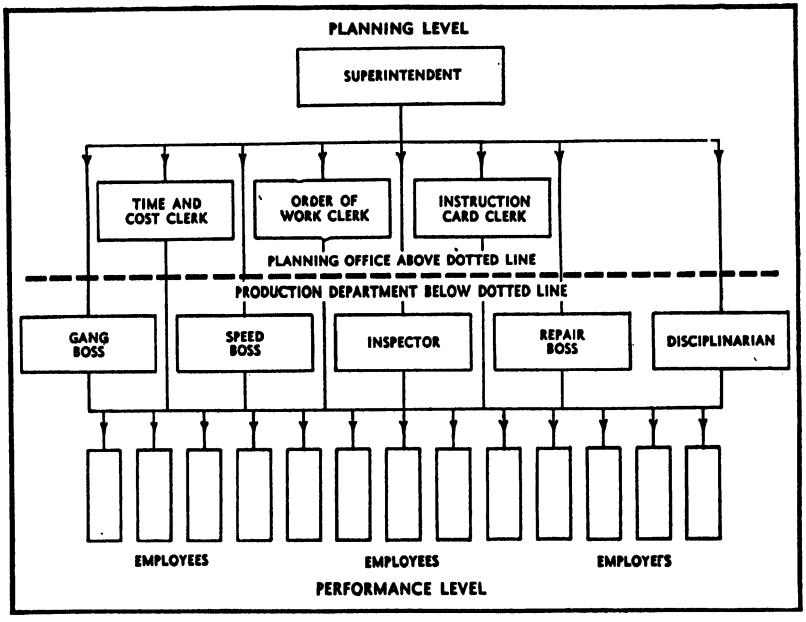


FIG. 24.—Functional foremanship according to Taylor. Adapted from Dexter S. Kimball, *Principles of Industrial Organization* (5th ed.; New York: McGraw-Hill Book Co., 1939), p. 190.

in its underlying theory that the duties required of a foreman should be restricted to one activity in which he could be reasonably expected to be expert, the line separating one task from another—and therefore the jurisdiction of one foreman from that of another—is exceedingly fine and sometimes impossible to determine. Therefore, friction and embarrassment ensue, and questions of authority which are difficult to settle arise. Where such confusion exists, an employee is placed in the dilemma of choosing whose orders shall be obeyed and to which boss his allegiance is required. No matter how carefully the lines of authority and responsibility in an organization are drawn, issues of jurisdiction cannot always be avoided; but it is better that such differences be adjusted at a higher managerial level than that of the foreman.

Despite this weakness in his plan of scientific management, Taylor made a substantial contribution to the theory of business organization, particularly in emphasizing the separation of planning and performance and the recognition of functional distinctions in the structure of departments. His attack upon excessive managerial responsibilities resulting from the irrational scope of duties assigned to certain executives under territorial and commodity departmentation was doubtless justified. While the ends Taylor sought were not realized in the manner in which he had planned, the most significant features of them have been achieved through staff and line organization, which will be discussed at some length in Chapter X.

The two extremes in organization of foremanship, "nonfunctional" and "functional," are contrasted in Figure 25. The aim of management is to strike a reasonable and effective compromise between these two extremes.

COMBINATIONS IN PRIMARY DEPARTMENTATION

Modifications in primary departmentation have resulted in certain desirable types of specialization. These modifications are the result of various combinations of territorial, commodity, and functional distinctions. For example, it is possible to have functional departmentation in the major levels of management, followed by territorial departmentation in the lower levels or operating units. Thus, in chain grocery store organization previously illustrated in Figure 14, departmentation at the level of the major executives is necessarily functional. That is, subordinate to the general manager, there are such executives as (1) the general stores superintendent in charge of sales; (2) the produce superintendent in charge of purchasing; (3) the warehouse superintendent in charge of storage and requisitions; and (4) the office manager in charge of accounts and records.

If, now, one of these functional departments of a chain grocery store organization is analyzed, it is possible to see how territorial departmentation fits in to specialize further the work of management. By dividing the territory served into designated areas and placing a district manager in charge of each area, this purpose has been accomplished. Each such district manager is subordinate to the general stores superintendent, since the function involved is the main one, selling merchandise. Likewise, it is possible to utilize commodity departmentation in the same organization. Since the produce superintendent is, in reality, the chief purchasing agent of the business, the great variety and number of commodities with which his department has to deal necessitate specialization in procurement. He is the chief executive over a number of buyers who are typically commodity experts in such lines as canned goods, dried fruits, flour, provisions, meat, and many others. A combination of all three of these basic

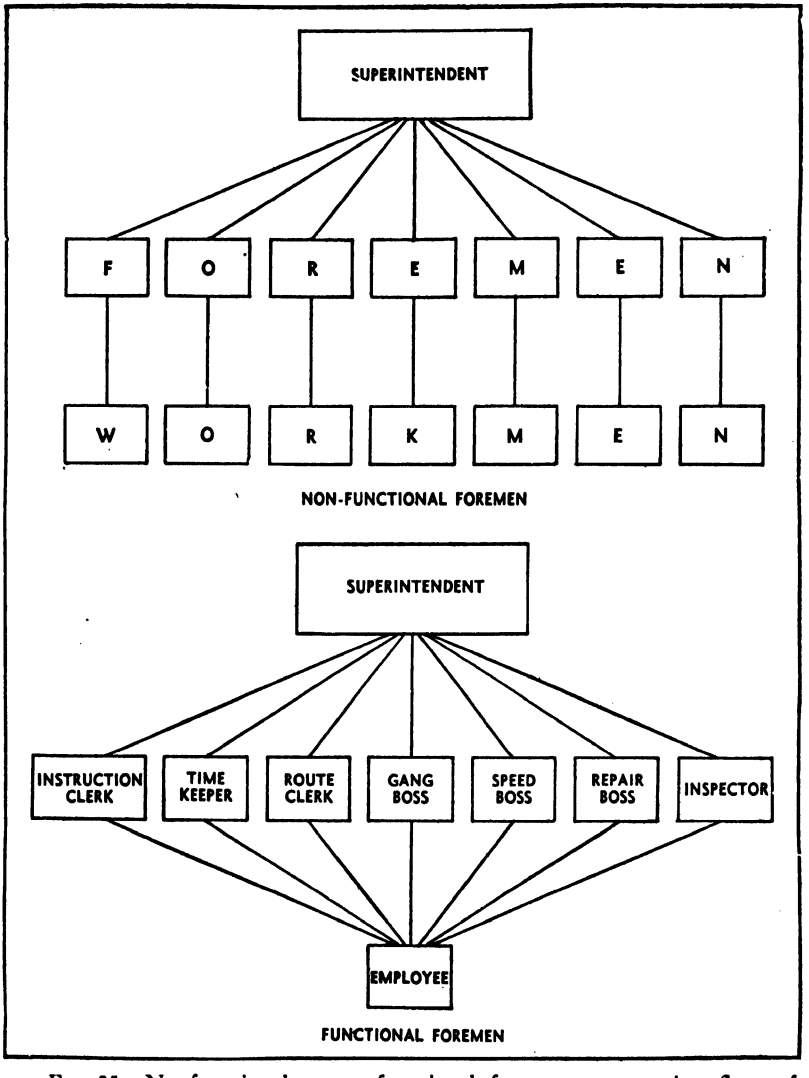


FIG. 25.—Nonfunctional versus functional foremen: contrasting flow of authority, responsibility, and accountability.

types of departmentation—territorial, commodity, and functional—is illustrated in Figure 26.

Many other combinations of primary departmentation are possible. Some of these are illustrated in Figures 27–30, inclusive. In Figure 27 there is presented a form of departmentation with functional differences at the top and territorial separation at the level of operations. In Figure 28 this situation is reversed. The first level of management tasks is deter-

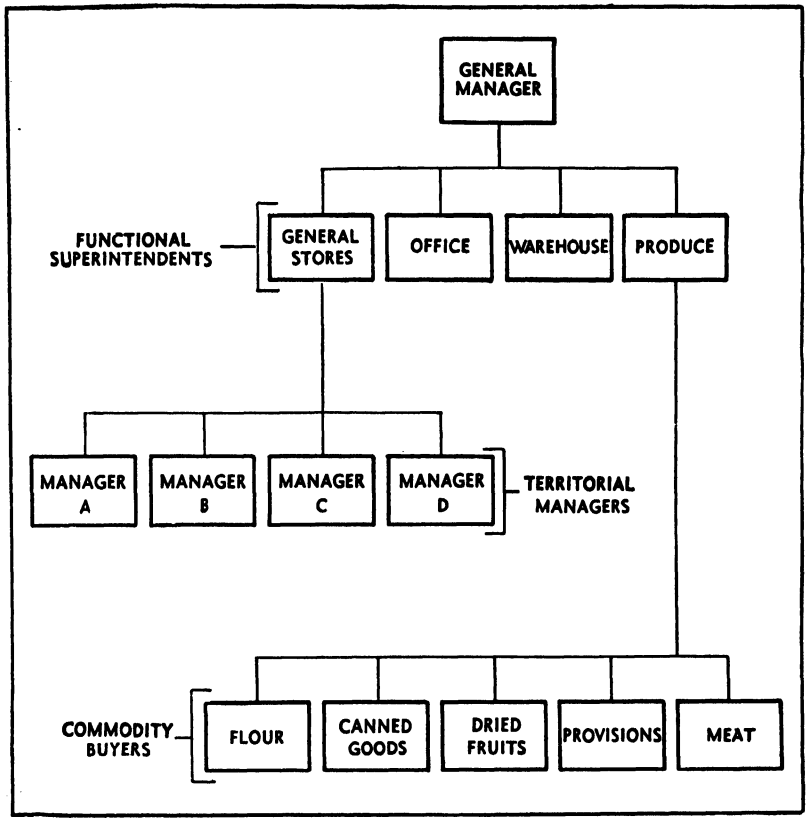


FIG. 26.—Combination of basic types of departmentation in a chain grocery store organization.

mined on a territorial basis with regional managers, designated as departmental heads immediately responsible to the general manager of the company. Functional departmentation, therefore, does not appear except in each regional office. This arrangement is conceivable in theory but is relatively uncommon. An example would be a group of hotels or theaters —each in a different community—all owned by the same parent company but each under the complete management of either a resident vice-president or a manager.

Figure 29 is a representation of a combination of commodity and territorial differences in the first level below the general manager. That is to say, the plants of the company are specialized by product as well as separated by location. Functional departmentation follows and is confined to each under the direction of the plant manager. A much more complex situation is illustrated in Figure 30. Here the plants are un-

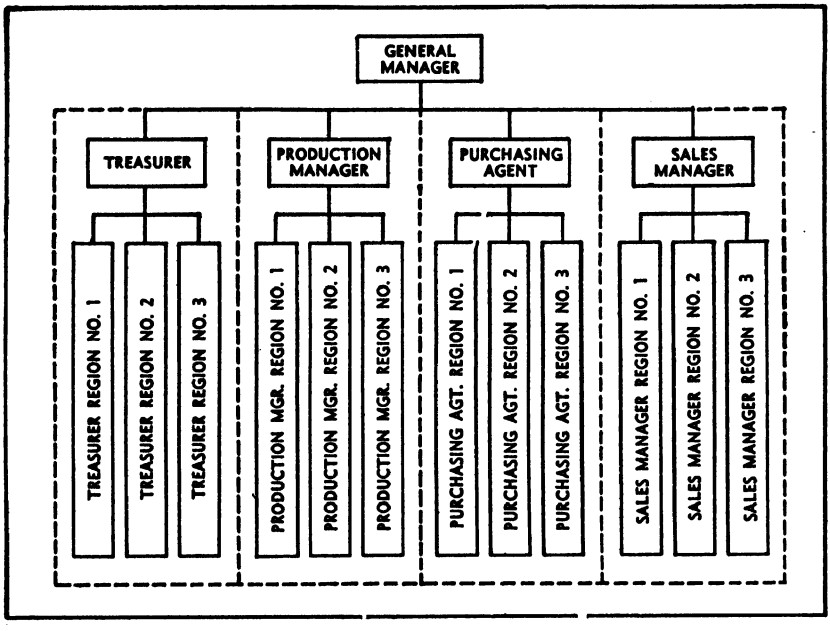


FIG. 27.—Departmentation showing primary functional differences.

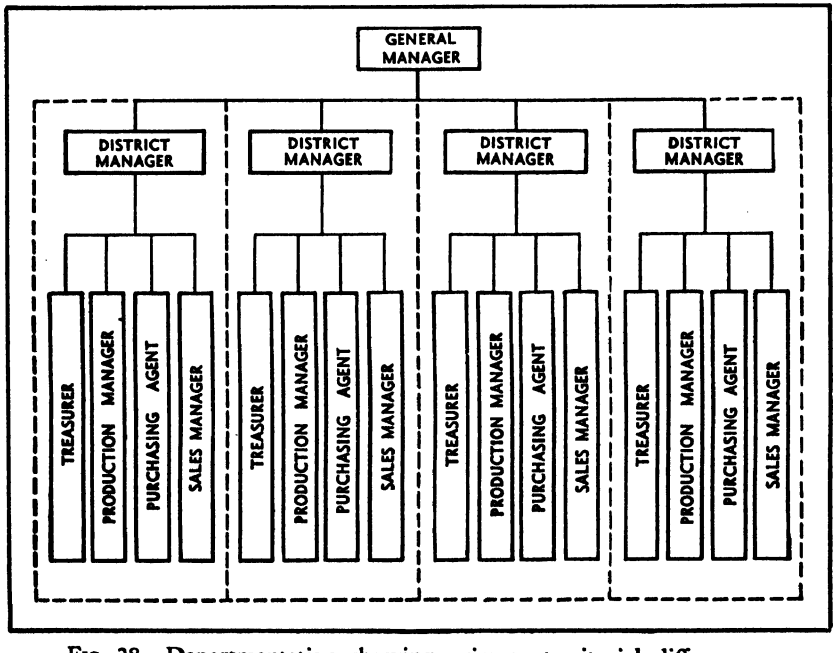


FIG. 28.—Departmentation showing primary territorial differences.

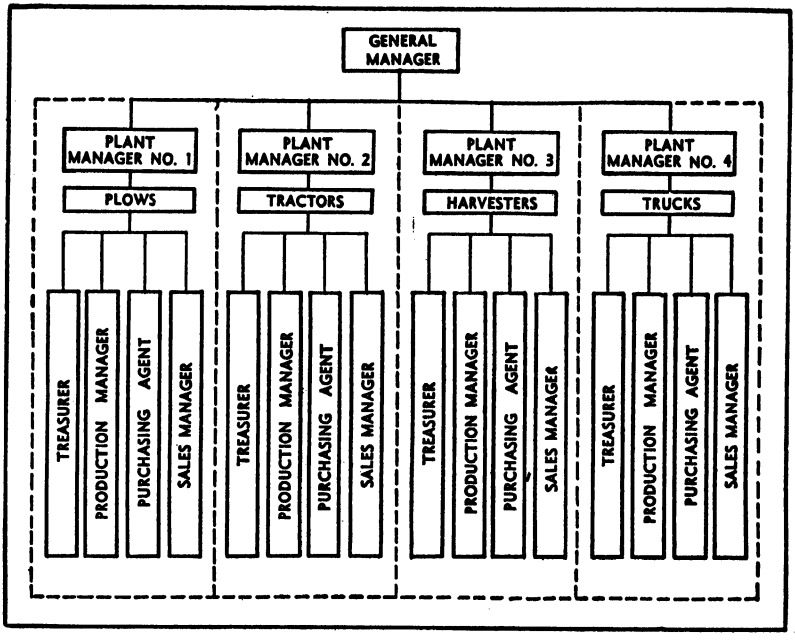


FIG. 29.—Departmentation showing primary commodity differences—plants specialized.

specialized, and the first level of departmentation is purely territorial in character. But there is a combination of commodity and functional differences within each factory. Even though each plant produces four commodities—plows, tractors, harvesters, and trucks—each one of these lines is assumed to have its own production manager, purchasing agent, and sales manager. Presumably, there would also be a plant superintendent in charge of each commodity division to whom these three functional executives would be accountable. Such an arrangement approaches in its functional aspects Taylor's concept of high specialization but applied to the levels above those of foremen.

Use of the Three Types of Departmentation

Early in this chapter it was pointed out that seldom, if ever, does one type of primary departmentation prevail to the exclusion of one or both of the others. Balance and simplicity in management are desirable, and these ends can be best achieved by the wise use of all three of these departmental devices. A desirable method of combination is shown in Figure 31. In this illustration territorial departmentation is shown to take place first. Then comes functional departmentation, in which the executives in charge are immediately subordinate to each plant manager. Com-

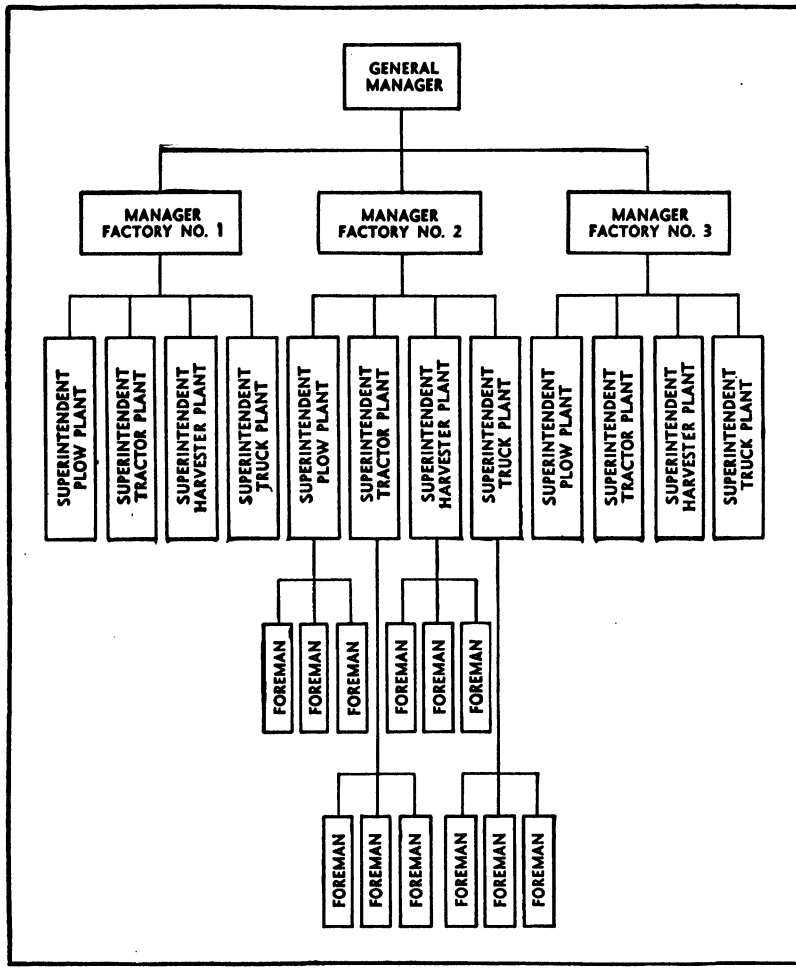


FIG. 30.—Departmentation showing primary commodity differences—plants unspecialized.

modity departmentation is not undertaken until the level of the factory superintendent, which is one step above that of the foremen, is reached. Though it probably would not be involved in financing and purchasing, this division of executive activity on a commodity basis may, or may not, be extended to the sales function.

Despite the foregoing illustrations, no organization chart of a given business concern which would fit exactly the requirements of every other business in its class can be drawn. Every business institution, like every human being, differs in certain details of organic structure and physiognomy. Only trends and fundamental characteristics in organization and

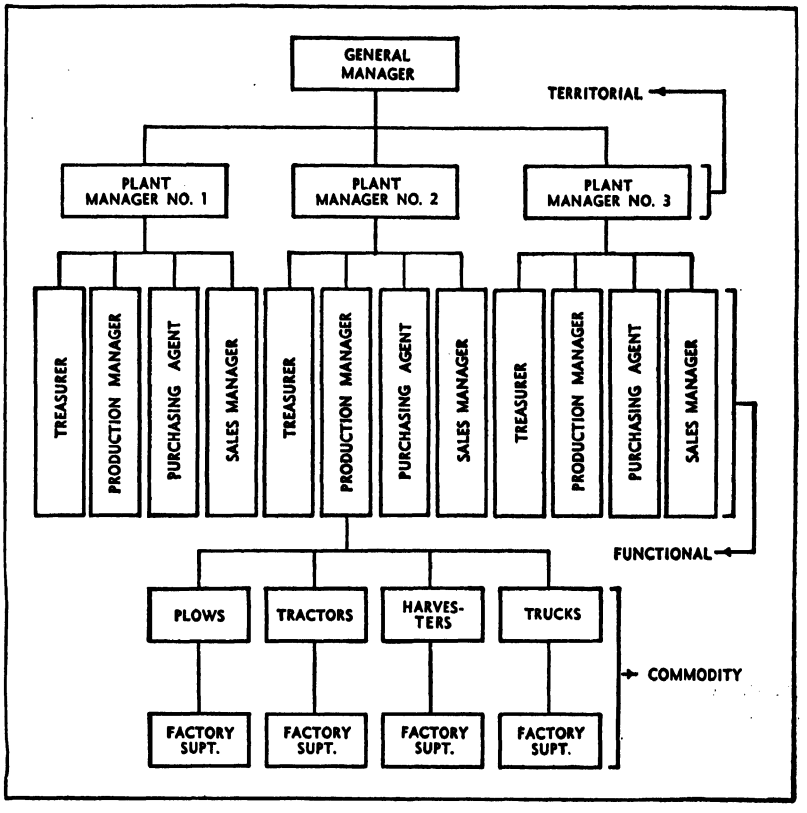


FIG. 31.—Combination of territorial, functional, and commodity differences in departmental organization.

the underlying principles which bring them into being are subject to analytical and expository treatment. However, these trends and fundamental characteristics of departmentation apply to companies of any size. The illustrations seem to emphasize large-scale enterprises only because such examples are easier to present and to understand.

TRENDS IN ORGANIZATION ARCHITECTURE

Just as the organization chart of one business differs from that of another, so does the organization of an individual concern differ from time to time. Hence, it is difficult to draw an accurate organization chart of even a medium-sized business. Organization details change almost daily. Much of the actual organization of the moment results from "give and take" within the executive group and from the management problems which are uppermost. Organization actually looks different and, in a sense, is different when viewed from different levels within a particular

enterprise. In like manner, the impressions one receives of a building vary when it is looked upon from different angles and from different elevations. The common type of organization chart usually prepared for a business is a summary of the organization relationships viewed from the level of the board of directors. Such a chart presents the interrelations of the board of directors, the president (or general manager), the major executives, and the heads of departments. It must be noted that frequently there is no distinction between major executives and heads of departments; that is, major executives are often themselves the department heads.

If management were completely scientific, it would be possible to outline the one best organization for a given business at a given time. In reality, organization charts are usually drawn up as a matter of history to show what the actual organization has been. A series of such diagrams prepared annually for a particular company would reveal certain distinct trends. If it were a growing concern, an increase would be shown in the number of permanent functional executives. It would also be apparent that the organization had a tendency to be built around the strongest major executives. There is a saying that "authority gravitates to those who can." This is characteristically true in the evolution of the pattern of the internal organization of a business. Finally, it would be observed that the organization of one concern would tend to conform more and more closely to a general pattern which would be found to prevail in the particular field or class of institutions of which it was a part.

Patterns of Departmental Organization

There is such a characteristic pattern of departmental organization for every type of business, at least in broad and basic outline. A certain typical arrangement of departmentation has evolved out of experience and has been generally accepted. It is perpetuated by the transfer of trained executives from one business enterprise to another within the field. It evolves gradually through experimental organizational modification by executives who are, at the moment, regarded as leaders of the industry or business. Some examples of the typical patterns of departmentation which obtain in the organization for management in a selected group of businesses are presented in the following outline:

1. Department Store Organization
   - Accounting department
   - Advertising department
   - Merchandising department
   - Personnel department
   - Receiving and warehousing department
   - Store service and delivery department

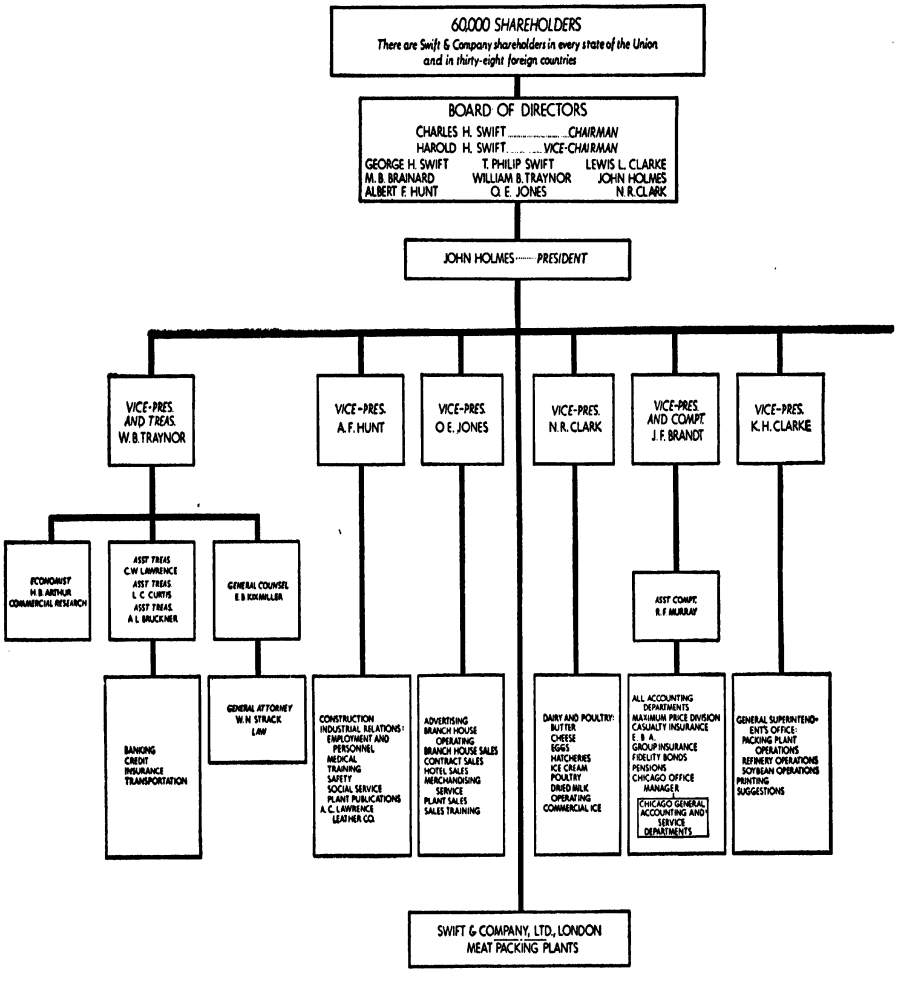
2. Life Insurance Company Organization
   - Accounting department
   - Actuarial department
   - Advertising department
   - Agency supervision department
   - Claim adjustment department
   - Investments department

3. Manufacturing Company Organization
   - Accounting department
   - Advertising department
   - Engineering department
   - Personnel department
   - Production department
   - Purchasing department
   - Research and control laboratory
   - Sales department
   - Traffic department
   - Warehousing and stores department

4. Railroad Organization
   - Accounting department
   - Engineering department
   - Motive power department
   - Operating and maintenance department
   - Purchasing department
   - Traffic department
   - Transportation department

5. Water Utility Organization
   - Accounting department
   - Engineering department
   - Maintenance and operating department
   - Personnel department
   - Purchasing department
   - Service department
   - Water purification departmen

When a business deviates from the common pattern of departmentation, it is often said to be experimenting with an "organization frill." Like a fad or a style in clothing, furniture, or architecture, such an innovation may prove unpopular or it may gradually be adopted as part of the organization pattern of the particular field of business. Variations from typical departmentation—whether by innovation or by custom—are the result of the degree of importance which is placed on particular problems by those

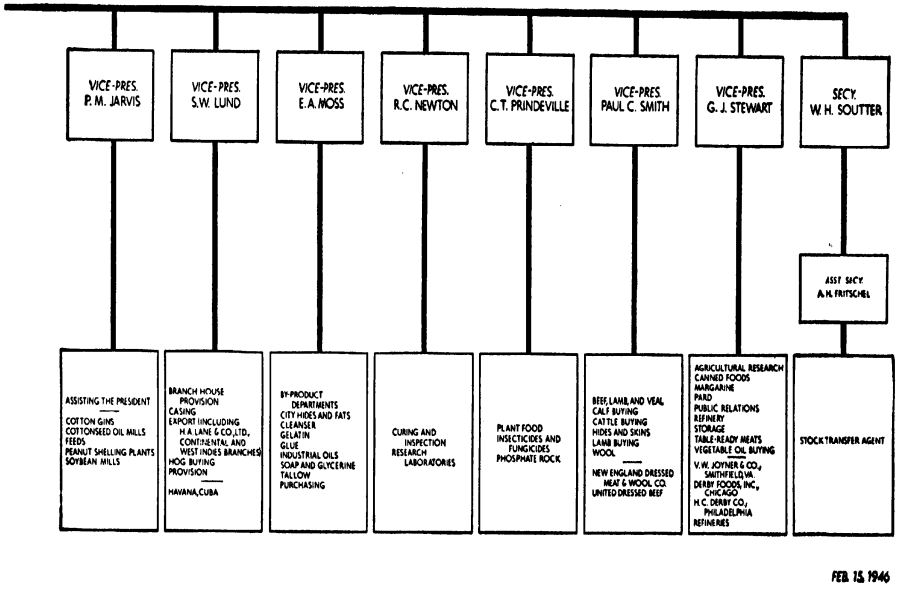


who determine the organization policies of the business. Which activities merit departmental segregation because of their very nature and which because of association with other executive tasks cannot be stated categorically. In some businesses, the activities are relatively few in number; in others, a schedule of them assumes large proportions. How extensive such a list may be is shown in Figure 32, illustrating the organization of Swift & Company, one of the largest meat-packing firms in the world.

Departmental Organization of Swift & Company

In order to show the principles involved, the diagrammatic illustrations of various organization situations and types of departmentation used up to this point have been simplified. In Figure 32, however, there is a complete summary of the actual organization of a large business enterprise. As shown in the chart, Swift & Company is now owned by approximately

FIG. 32.—Organization chart of Swift & Company. Courtesy of Swift & Company.



60,000 stockholders who are scattered throughout the United States and 38 foreign countries.

The company has a board of directors of eleven members, seven of whom hold corporate offices in addition to their posts as directors. The titles of the corporate officers are chairman of the board, vice-chairman, president, and treasurer, all members of the board of directors. Other general officers of the company are the secretary, comptroller, general counsel, and economist. For the sake of complete description, it should be added that there are also three assistant treasurers, one assistant comptroller, one general attorney, and one assistant secretary, all specifically mentioned by names and titles. There are thirteen vice-presidents, one of whom is treasurer and one comptroller. Three vice-presidents, in addition to the treasurer, are members of the board of directors. The vice-presidents, while technically corporate officers, are essentially major managerial

executives to whom authority has been delegated for particular purposes in order to extend and strengthen the power of the president in the management of the business.

Another important factor in the organization of the board of directors is also illustrated by Swift & Company, namely, continuity of membership of the natural leaders of a particular business. Charles H. Swift, chairman of the board of directors, is a son of the founder, Gustavus Franklin Swift. Throughout his lifetime he has followed closely in the footsteps of his father. Moreover, four of the nine members of the board bear the name of Swift, hence are obviously related to, or descended from, "The Yankee of the Yards."[5] Thus the founding family still has a prominent place in the directorate of the company, and a study of the company's literature shows that this continued relationship has given stability to policy and consistency to management and has aided in the development of pride and morale on the part of Swift & Company executives and employees.

Division of Management

The four principal members of the Swift & Company board of directors divide up the management of the business in a somewhat independent—though closely interrelated and coordinated, fashion. The chairman of the board devotes himself to general company affairs, particularly the broad problems of the "owning" corporation. The vice-chairman, according to a yearbook of the company,[6] gives his attention to internal problems, spending much time in direct contacts with the thirteen vice-presidents of the company, with the more important of the numerous packing-house, branch-house, and factory managers, and with foreign representatives of the company. He performs these activities in order that he can report to the board firsthand information concerning the major management problems of the concern.

Both the president of the Company and the treasurer are members of the board of directors as well as executives. As a board member the treasurer ranks with the president, but he, also, serves under the president as vice-president and treasurer.

The seeming discrepancies in coordination involved in the dual relation of board member and executive are deliberate rather than accidental. They have come into existence for the purpose of increasing the effectiveness of the company by permitting these highest executives to work together at all management levels, including that of the board of

[5] For an absorbing biography of Gustavus Franklin Swift, see *The Yankee of the Yards*, by Louis F. Swift in collaboration with Arthur Van Vlissingen, Jr. (New York: A. W. Shaw Co., 1927).

[6] *Yearbook of Swift & Company, 1937*, p. 3.

directors. This close personal association, together with voluntary submission by each of these independent board members to the necessary degree of managerial discipline in their executive interrelationships, assures the necessary coordination of the business.

Figure 32 shows that the president is the top executive of Swift & Company. All other executives report to him, directly or indirectly. The president has partially delegated his authority and responsibility for management and operation of this enormous business enterprise to fourteen executives.

Primary Departmentation of the Company

The basic or primary departmentation of Swift & Company consists of ninety-three separate management activities, as listed in Figure 32. These are assigned in varying numbers to the twelve operating vice-presidents, to the thirteenth vice-president, who is also treasurer, to the secretary, and to the president himself. The president reserves direct management of the London office of the company and all the Swift & Company meat-packing plants. Thus, directly under the president are placed the thousands of employees, supervisors, and executives in the company's plants which are scattered throughout the United States and Canada. In addition to this territorial departmentation of the meat-packing plants under the president, there are several hundred more branch houses, dairy, poultry, and ice-cream plants, refineries, fertilizer plants, and oil mills—all under the executive management of various vice-presidents.

Enough has been presented concerning the organization of Swift & Company to leave no doubt that its actual departmentation consists of a combination of territorial, commodity, and functional methods all mixed up together and applied in whatever manner has seemed desirable to the top management of this company. The test of good organization is that it yields desired results, not that it conforms to some preconceived pattern. "Organization" is a management technique, not management's master.

This discussion of the actual departmentation of a large business enterprise can best be summed up by Swift & Company itself, by quoting the section on management from its 1939 yearbook:

> The direction of the affairs of a large and complicated business imposes a tremendous and unavoidable responsibility upon its managers. The managers of Swift & Company have the task of making the human and physical resources at their disposal function as an efficient organization. That organization must be able to operate so efficiently that its essential processing and distributing functions will result not only in a maximum service to producers and consumers but in a profit to the shareholders who own the business.
>
> Under the company's promotion policy, almost the entire management

staff of the company—foremen, superintendents, managers, and officers (with the exception of a few holding technical and professional positions)—is made up of workers who started at the bottom with Swift & Company and secured their present positions through promotion. Their advancement has been an inspiration to other workers and a distinct benefit to the company.

Below is a table which gives some idea of the leadership required to conduct the business:

Officers and Assistant Officers (In charge of important branches of the business.)	21
Heads of Commercial and Operating Departments (Home office only.)	35
Heads of Professional and Service Departments (Accounting, credit, finance, law, advertising, construction, research, etc. Home office only.)	33
Plant Managers and Superintendents (Meat-packing plants, dairy and poultry plants, oil mills, refineries, fertilizer works, soap factories, etc.)	384
Sales Managers (Districts, branch houses, plant sales territories.)	448

In addition to the numbers listed above is a corps of competent assistants, together with those charged with the more direct supervision of particular operations. This is a small staff when we consider the number of operating units of the company and the fact that the company sells and delivers its products at frequent intervals to several hundred thousand customers.

Compensation of officers and managers must be such as to attract capable men—men who are fully capable of doing the job they are given. On the other hand, it would be an economic waste to employ workers who did not render services equal to the compensation they are paid.

It is safe to say that the officials of the company receiving the highest salaries could not be replaced by men of equal competence even at a substantially higher rate. And it is also true that their positions exist only because their functions are of such importance that they add much more than this amount to the income of the company. . . .[7]

DEPARTMENTATION: BASIC STRUCTURE OF ORGANIZATION

Departmentation," then, is the basis upon which the structure of a business organization is built. By its application the work of management is specialized, and authority and responsibility for its efficient performance are assigned to executives of various ranks and titles. Several methods are employed to achieve such specialization, of which three are of primary importance. They are separation by territorial, commodity, and functional differences.

"Territorial departmentation" recognizes the necessity of simplifying the tasks of management on the basis of location, on the ground that geography is a conditioning factor in human and economic relationships.

[7] *Yearbook of Swift & Company, 1939*, pp. 14–15.

"Commodity departmentation," like that of location, is material in character. It takes into account the advantages which come from effort concentrated upon the processing or sale of a given class of goods or services. "Functional departmentation," the most pervasive method of specialization in all types of business organization, is subjective in character. It is based upon the assumption that workers naturally group themselves into managerial units by reason of the similarity, or necessary association, of the skills and techniques required of them. But seldom, if ever, does any one of these primary types of departmentation stand alone. It is a combination of two, or all, of them which establishes balance in organization.

In spite of the fact that the basic principles of departmentation in management are common to all businesses, it is impossible to reduce business organization to an inflexible formula. The individuality of establishments and companies preclude such treatment. Even the organization chart of a single concern changes with the lapse of time. At best, it is a historical presentation of relationships in management on given date, thereby serving as a guide for the future but not as a prophecy which promises to be fulfilled. Yet different classes of businesses, such as banks, department stores, insurance companies, manufacturing concerns, and others, conform to certain types of organization representative of their class. Innovations, or radical departures, occur only as a result of the special importance of problems restricted in scope and incidence to particular enterprises. The trend in modern business organization is toward rationalized departmentation well grounded on recognized principles and techniques.

QUESTIONS

1. In 1947 the number of departments in the President's Cabinet of our federal government was reduced from ten to nine by the merger of the former War and Navy Departments into a single Department of Defense, with one instead of two cabinet officers. This new officer is known as the Secretary for Defense. His department now consists of three major divisions in charge of the Secretaries for Army, Navy, and Air, respectively. Explain what effect this change in organization has upon the following:
   a) The spans of control, knowledge, attention, time, and energy of the President of the United States.
   b) The problems of management involved in so-called "combined operations," such as a military campaign which requires coordinated action by the army, navy, and air forces.
2. In the United States, telegraph service is principally furnished to all parts of the country by one company, whereas telephone service is chiefly supplied by a group of regional companies, each one of which limits its operations to a definite geographical area. These regional companies are

subsidiaries of a larger corporation, national in scope, which, in turn, supplies research and coordination services. It also provides for the facilities and connections that make possible efficient long distance telephone communication.

a) What is the correct official full name of the telegraph company that serves your local community?

b) What is the correct official full name of your local telephone company, and in what city are its headquarters situated? If the local company is a subsidiary of a larger corporation, what is the name of the latter, and where is its principal office?

c) Illustrate with a diagram the territorial departmentation of the telephone service in your locality at the regional, district, and local levels.

d) Explain and defend the statement that our national telegraph service must necessarily be organized on the basis of territorial departmentation at the regional, district, and local levels.

3. Reference has been made to the General Motors Overseas Operations as a "division" of the General Motors Corporation. Typical domestic divisions of this corporation are Buick, Cadillac, Chevrolet, Pontiac, and Oldsmobile —all of which manufacture automobiles; Fisher Body, which makes motor car bodies; Frigidaire, a manufacturer of refrigerators; and Electro-Motive, which produces diesel-electric railroad locomotives.

a) With Figure 27 or Figure 28 (select one) as your model, diagram the organization of a typical "region" of the General Motors Overseas Operations.

b) With Figure 29 as a model, diagram the domestic organization of the General Motors Corporation, omitting its Overseas Division.

4. Study carefully the text material and Figure 32 with reference to the organization of Swift & Company.

a) With Figure 26 as your model, prepare a diagram that properly illustrates Swift & Company, viewed as a whole.

b) With Figure 30 as a model, prepare a diagram which will properly illustrate that part of the organization of Swift & Company that deals with its larger meat-packing plants—each of which processes all of the different food animals. (Note: Do not attempt to include the entire organization of Swift & Company in either of the above diagrams. Merely include enough of the organization to bring out the points represented by each of Figures 26 and 30.)

5. Explain fully each of the following statements with respect to the organization of Swift & Company, and give appropriate examples derived from Figure 32:

a) Swift & Company uses territorial departmentation to a large extent.

b) Swift & Company uses commodity departmentation to a large extent.

c) Swift & Company uses functional departmentation to a large extent.

d) It is logical and proper for a large business enterprise to use all three forms of departmentation to a large extent.

6. In the pattern of typical departmental organization for different groups of businesses as shown on pages 220–21 in the text, an accounting department is not only included but it heads the list in each instance. Likewise, the organization chart of Swift & Company, Figure 32, shows that "all accounting departments" are placed under the jurisdiction of the assistant comptroller and his superior officer, the comptroller, who is also a vice-president of the corporation. Figure 32 further shows that the latter executive reports directly to the president of the company and, through him, to the board of directors. With the foregoing facts in mind, answer fully the following questions:

   a) Why is accounting set up as a functional department in the top level of the organization of a business enterprise?

   b) Did Frederick W. Taylor in his scheme of functional foremanship propose to carry the function of accounting down to the level of the worker? (See "Time and Cost Clerk," Figure 24.)

   c) What is the distinction between the treasury and accounting functions in the organization of Swift & Company, as shown in Figure 32?

   d) Note that the term "treasurer" has been used to indicate both the treasury and the accounting functions in the theoretical organizations illustrated in Figures 27, 28, 29, and 31. Explain why this particular combination of functions tends to become separated into two distinct departments as a business enterprise increases in size.

7. There are approximately one hundred business activities that are named in the principal and subheadings of the organization chart of Swift & Company in Figure 32. Separate these activities into three groups and list them under the three dominant departmental categories—territorial, commodity, and functional.

8. In the descriptive reference to Swift & Company in the text of this chapter on page 226, there are tabulated more than 900 executives who have the responsibility for the leadership and management of the company's 60,000 employees, scattered throughout hundreds of separate plants and offices all over the world. These executives and employees do not include numerous assistant executives and supervisors. The total number of foremen and other subordinate executives may be estimated at about 5,000. Considering these data, perform the following exercises, using diagrams where desirable:

   a) Describe the following levels of the Swift & Company organization: ownership, top executive, major executive, minor executive, and supervisory and employee levels.

   b) From the standpoint of the principles of "span of control," describe briefly the activities and responsibilities of the president and each of the thirteen vice-presidents of Swift & Company.

9. On the basis of the analysis of the functions of a board of directors as explained in Chapter V, prepare a chart showing the probable duties and activities of the Board of Directors of Swift & Company. For a pattern, follow Figure 15 on page 129, the summary by J. O. McKensey on page 118, or the classification on page 128. In your analysis, note particularly the effect on board activities that result from the fact that five of its members are salaried executives who bring to board meetings their detailed knowledge of meat packing, dairy and poultry processing, advertising, sales, industrial relations, and financial and legal problems.

10. Interpret fully the following statements:
    a) Since organization charts are rarely of more than historical interest, it is not desirable to attempt to make and keep current detailed organization charts covering every aspect of the management of a particular business enterprise.
    b) The actual organizational interrelationships of the seven members of the board of directors who are also salaried executives of Swift & Company cannot be accurately portrayed on a single diagram or organization chart. (These executives are: Chairman of the Board; Vice-Chairman of the Board; President; Vice-President and Treasurer; Vice-President in Charge of Industrial Relations; Vice-President in Charge of Sales; and Vice-President in Charge of Dairy and Poultry Products.)

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Chapter IX

THE CRITERIA OF DEPARTMENTATION

THE CONCEPT OF FUNCTIONALIZATION

BECAUSE of their objective character, it is not difficult to make departmental classifications on the basis of territory and commodities. Geographical locations are definite, and the boundaries which surround production and trade areas, being tangible, can be determined with accuracy sufficient for all practical purposes. Likewise, commodities are distinguishable from one another by their physical qualities and by the uses to which they are adapted. Not so simple are the recognition and classification of functions for the purposes of departmentation.

That functional departmentation is the most common and the most pervasive of all forms of primary separation of executive activities has already been demonstrated. Rationalized or scientific management can be achieved only by the specialization and classification of managerial tasks and by limiting the number of tasks which are assigned to any one individual to the activities which are inherently similar and distinguishable by reason of place, product, or process. If we disregard the activities which distinguish themselves on the bases of place and product, the problem then becomes one of determining the best way of combining functions into workable departments.

Function Defined

In the terminology of management a "function" may be defined as "any task involved in the performance of the activities of an enterprise that can be clearly distinguished from any other task." It denotes an activity, more or less specialized in character, that is assigned to and performed by an individual or group of individuals within the organization. The term "function" as used in physiology means the "chief activity of an organ. "Organs" are essentially collections of specialized cells, created by organic evolution, which in their normal healthy state perform certain processes. The structure and arrangement of these cells determine their function. Thus, when the histologist observes a specimen under his microscope, his practiced eye easily identifies it as being cells from the skin, muscles, digestive tract, heart, brain, or blood. Having confirmed the structure and arrangement of the cells in the specimen under observation, the function or activity of the organ from which it was taken fol-

lows logically and without variation. Skin cells cannot generate nervous energy, nor can muscle cells digest food. Hence the physiological scientist can reason from organization to function with complete assurance.

It is a valid analogy to assert that departments are the organs of the business body. Likewise, the individual persons who make up its personnel represent its cells. But beyond this point the analogy breaks down, for the obvious reason that the tasks which a man may perform cannot be detected by looking at him. Furthermore, similar tasks may be found in different departments. It is the combination of functions, rather than that of particular persons, which determines a healthy department. The management scientist, to continue the comparison, must, therefore, reason almost entirely from function to organization. In so doing, he is confronted with a host of variations, exceptions, and modifications unknown to the specialist who deals with the laws and phenomena of nature. Exceptions to this generalization are mainly those functions, broad in scope, which are derived from organization levels. Certain management tasks, like the determination of objectives, the formulation of policies, and the supervision of production or performance, are largely, if not entirely, confined to specific executive levels of the management hierarchy.

Recognition and Combination of Functions

Successful departmentation, therefore, involves two techniques: the first of these is the ability to recognize functions by their distinctive characteristics, and the second is the ability to combine functions so as to realize coordinated and efficient performance without unduly increasing the number of management levels. There is, clearly, a balance between functional departmentation and the necessary resultant of increased layers or management levels. To go beyond this point means extra cost and more difficult control without compensating advantage.

The first of these techniques is the simplest. Functions are readily distinguished one from another in various ways with respect to the skills, processes, and activities which they entail. Sometimes the personal qualities of those who perform these functions are also factors which may not be overlooked, although training, experience, physique, and personality rarely determine the service to be rendered. However, it is usually the other way around—the work to be performed will require a certain type of individual.

Assuming that the problem of distinguishing between functions can readily be solved in most instances, its solution is merely the first step in functional departmentation. Obviously, it would be impracticable to create and sustain as many departments as there are special processes in the operation and management of a business. This is particularly true at the level of the major executives. If the primary departmentation of a

concern is brought about on a functional basis, excluding entirely the territorial and commodity methods of specialization, then its major divisions of organization, such as the production, sales, and accounting departments, will each be found to consist of a combination of many subsidiary activities narrower in scope and more definitely circumscribed. There will be the difficult problem of determining a satisfactory basis for each combination undertaken. That is to say, management must decide which departments shall be coordinate in rank and which shall be subordinate. The problem of functional departmentation could be simplified and reduced to the vanishing point if the question of coordinate and subordinate

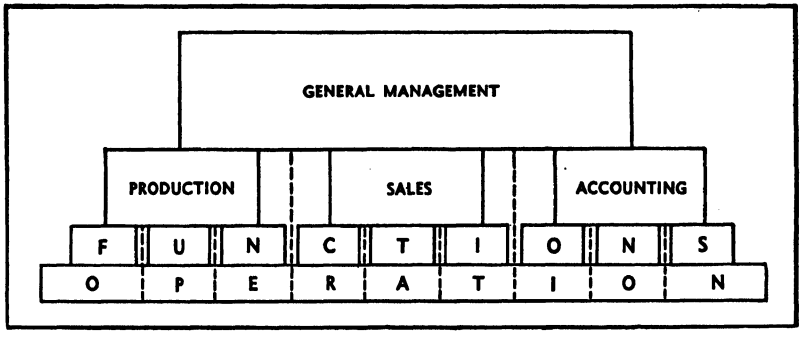


FIG. 33.—Functional pyramid.

departments could be disregarded. But because there are levels of authority and responsibility in management, and because there must be leadership and followership in all directive effort, distinctions in rank and standing between executive groups automatically follow.

Thus the pyramid of business organization is constructed, one tier of functions resting upon another tier, level upon level, with a single capstone at the top, as shown in Figure 33. Assuming functional departmentation throughout the structure as suggested above, the first tier below the crown will consist of the major departments, each of which will consist of several functional groups clearly distinguished from one another. The designer's problem is that of planning the arrangement and of choosing the materials to go into each level of construction.

1. SIMILARITY AS A BASIS FOR DEPARTMENTATION

An obvious basis for grouping activities into departments is that of similarity or likeness. If no other plan is adopted, likeness suggests classification. In the application of likeness to the functions of management, however, it is difficult to determine what tests of similarity are valid. In the first place, the likeness of the personal qualities of the employees or executives who are required to perform a group of given tasks may be

considered. These qualities include training, aptitude, skill, experience, judgment, or even physical strength and stature. It is admitted that this basis of combination is superficial and of little significance as an aid in solving the problems of departmentation on a large scale. Its effect can be traced, however, in small organizations where the pattern of specialization forms itself to fit the personnel already employed. The tasks which are performed by the strongest individuals and which perhaps require very little skill or training in their execution will be grouped together and placed under a single superintendent or foreman. The tasks themselves may be unlike, but the labor force required to perform them may be similar in character.

A second test of similarity is unity of purpose. That is, employees whose activities are directed toward a similar and specific goal or purpose may be grouped together. Sometimes in small businesses this method is the basis for both major and minor departmentation. For example, all processes which pertain directly to selling are grouped into a sales department; all those whose object is processing or manufacture are combined into a production department; and all "office work," including such activities as accounting, correspondence, filing, billing, credits, collections, and sometimes even financing, are assembled in a department commonly called the "general office," with an office manager in charge.

The opposite of likeness is, of course, unlikeness. Inconsistent as it may seem, the element of likeness may be a consideration when unlike activities are grouped together. It sometimes happens that it is desirable to combine activities which are unlike in procedure and direct purpose but complementary in their execution. That is, individually, they are unlike, but with respect to their relationships, they are more like each other than are any other tasks in the business. The selling and buying functions in department stores fall into this classification. While selling and buying are quite dissimilar, the responsibility for their successful performance may rightly be joined in one department under one head because goods which are not properly bought may be difficult to sell.

ASSOCIATION AS A BASIS FOR DEPARTMENTATION

The technique most significant in determining satisfactory allocation and combination of activities is based on the idea of intimate association of functions rather than on their characteristics of likeness or unlikeness. This method goes beyond the technique of "similarity." Its use is justified because the patterns of departmentation that result are more logical and rational and less haphazard and fortuitous. Association, when applied as a basis for departmentation, tends to avoid the shifting of activities from department to department merely because of the accidental interest of one executive or the effort toward disownment on the part of another. Over-

loading a department with many tasks to satisfy a whim for ostentation or the pride of much authority is another abuse which proper functional allocation may help to prevent. Vested interests in certain functions also may be detrimental to good management. Unless precautionary measures are adopted, allocation of activities by inheritance rather than by reason of fitness may ensue. The result is that a selfish and obstinate executive may insist upon the retention of a function or activity when, for the sake of efficiency in supervision and coordination, it should be placed elsewhere.

Eight criteria or tests of association are of proved value in guiding management in the building of an organization from the standpoint of functional departmentation. These eight criteria will be discussed below under their respective titles. These criteria have reality and validity, it is worth emphasizing, regardless of the size of the business under consideration.

The Criterion of Use

It is usually considered proper to place a given activity in that department which makes the most use of it. For example, the question arises in many large industries as to the proper departmental allocation of safety work. Obviously, it is desirable that all the employees of an establishment should be protected against bodily injury. But it is equally clear that the employees engaged in the productive processes need such protection more than any other group of persons. Hence, by the application of the criterion of use, the safety activities would logically belong in the production department.

Within this major department there are usually several subdivisions. It is, then, a question of deciding to which of these subordinate divisions the task of maintaining adequate safety precautions should be assigned. There are three alternative choices which suggest themselves, once the decision to apply the criterion of use has been made. To some extent, safety measures in a manufacturing plant are engineering problems which might be properly assigned to the engineering department. On the other hand, it is the duty of the personnel department to recruit, train, and provide for the welfare of these employees; hence it could be argued that the safety department is logically a responsibility of the personnel manager to whom should be given the authority for its management. But it can also be argued that safety measures are ineffectual unless they are enforced. Rules of enforcement in services of this kind often are embodied in standing orders which cover the work of the inspection department. Therefore, the authority and responsibility for the protection of the work force against injury may conceivably be assigned to the plant inspector.

Another application of the criterion of use is employed in the division

of available floor space in a building. Different activities may be grouped together into a department simply because they use the same general area. In a department store, the Christmas toy department is often placed under the supervision of the furniture buyer because the furniture department most readily offers the necessary space for seasonal display of toys. A more logical application of this criterion is the grouping of a factory's processing activities into a department because all of these activities make use of the same machinery. This is a common basis for factory subdepartmentation at the foreman level.

Industrial traffic functions, for the same reason, are also frequently included in departments bearing other designations. A study of industrial traffic management by the United States Bureau of Foreign and Domestic Commerce shows that, while 75 per cent of the enterprises surveyed maintained independent or coordinate traffic departments, where such departments were combined with others it was usually on the basis of use.[1] One example bearing on this point may be cited. Traffic functions were found to be handled by the production department in 9 per cent of the firms reporting. The reason given for this association is "the close tie-up necessary between the two classes of work." This relationship is further explained as being due to the fact that "raw materials and fuel reach the production department through the traffic department. Finished goods are taken away by the traffic department. This results in the constant meeting of the two departments." In other words, the traffic function has been associated with that of production rather than with that of some other department, on the principle that it should be placed where it could be of the greatest use.

The Criterion of Executive Interest

Another course to pursue in the allocation of functions is to assign a particular activity to the department whose executive is most willing and able to exercise authority over that activity. Stated negatively, it is inefficient and often detrimental to hold an executive responsible for a functional task in which he has no interest and to which he may even be antagonistic. This concept explains why cost accounting in an industrial enterprise is sometimes separated from the general accounting department and placed under the jurisdiction of the production department.

Costing is a matter of first concern to the production manager. The main consideration in scheduling and routing an order through a plant is

[1] *Industrial Traffic Management: A Survey of Its Relation to Business*, U.S. Department of Commerce, Bureau of Foreign and Domestic Commerce, Domestic Commerce Series, No. 39 (Washington, D.C.: U.S. Government Printing Office, 1930), p. 51.

that of completing the job within a specified time limit and at a cost not destructive to profits at the time the product will be sold. The speed of operations and the quality of the goods produced depend upon the materials, processes, and equipment, as well as the work force. All of these factors are costly, and their wise use involves planning on a basis as nearly factual as possible. Close cooperation and coordination between planning, production, and costing functions are therefore essential. The collection of cost data may be a function of the planning department; their classification and interpretation, the duty of the cost accounting department; and their application, a task which the production department must assume.

It should be noted at this point that the proper allocation of cost accounting in a business organization is not a settled question among accountants. There are those who take the view that costing, like all other phases of accounting, should not be divorced from the office of the controller or chief accountant. This position is taken from the standpoint of policy control, to be discussed later. Suffice it to say here that the argument asserts that the chief accountant is interested in, and responsible for, the acounts and records of the business as a whole, not for merely a part of it. In determining its gains and losses, in preparing its budgets, and in rendering the various accounting documents and statements required by the management, cost accounting may not be disregarded.

The criterion of executive interest finds expression in another way. Functionally specialized executives tend to emphasize the importance of their own activities. By their very titles their interests are prominently stressed. When new functions requiring special ability and experience in management are added or when old ones are split off from existing departments by reason of growth, the problem of allocation appears. It is then that existing executive titles become signposts which point the way. Thus the legal counsel, purchasing agent, credit manager, accountant, personnel manager, traffic manager, advertising manager, and factory engineer—all automatically identify themselves and influence organization policy.

In a modern business enterprise the department head is properly considered to be an executive who has been placed in charge of a particular area of managerial responsibility with a clearly defined central purpose, which, on all sides, shades off into other fields. The particular interest and ability of such an executive will, over a period of years, extend his area of specialization in one direction or another. His ability along one line may carry him so far from his own peculiar sphere as to cause his services to be borrowed if he is tactful, or to be rebuffed if he is too aggressive. If he displays weakness in any direction, his lack of strength will similarly permit invited or uninvited encroachment into his own realm by neigh-

boring department heads. Thus the entire management group of any company covers its entire field of problems, and performs its entire managerial task.

The Criterion of Competition

Segregation of activities is often as important a consideration in departmentation as is association. It is conceivable that some activities are afforded the greatest opportunity for development only when they are dissociated from others. The purpose of such dissociation is to provide a stimulus to greater productive effort through competition. Not only is a given division of management freed from domination by another, but rivalry between departments tends to motivate each toward its best possible efforts.

Such a departmentation policy recognizes the fact that rivalry is a natural human phenomenon. Everyone likes contests, and the desire to win is a wholesome virtue. For that reason, contests and prizes are common devices utilized by business management to stimulate men and women to prideful accomplishments.

There are many examples where a line of cleavage has been utilized as the basis for competition between departments. A manufacturer of tires may sell his products under one trade-mark to small garages and tire dealers and under another brand to wholesalers and department stores. To stimulate the sale of both makes of tires in these distinct markets, they may be placed in separate divisions of the sales department under different executives. In this manner, the two brands of tires will tend to compete with each other, and those responsible for their sales will fight for the opportunity to develop their respective divisions to the point of adequate participation in the market served.

A parallel arrangement of executive authority involving coordination at the level of the major executives only is often found in firms engaged extensively in both domestic and foreign trade. In such instances the domestic sales division is entirely separated from the export sales division. The two sales managers concerned are thereby subordinate only to the general manager. Such departmentation is based upon the theory that, if both types of sales activity were in the hands of one sales manager, either one or the other would languish because of personal preference or prejudice. For example, domestic sales might be pressed at the expense of foreign business, but with the introduction of rivalry into the organization, competition will spur each sales manager to make the best possible showing in volume of sales.

The General Motors Corporation, in its policy of separate management of each of its units, has consciously applied the principle of competition to its organization. To the average customer, Buick may seem to

be in competition with Pontiac, Oldsmobile, or Chevrolet; but in the final analysis, the value of the sales of all the products of the corporation finds its way to the consolidated operating statement of the company. This competitive effort has its source in basic policy, deliberately and carefully planned. An executive of the General Motors Corporation explains this policy as follows:

> If the advantages of such a type of organization (that is, decentralized operations in individualized plants or units) are to be enjoyed fully, it is absolutely essential that each unit be constituted so that it represents a self-contained business enterprise. The capital placed under its jurisdiction must be identified definitely with its own business and no other; and prices at which its products are sold must be based upon actual competitive values. Otherwise there is no tangible basis upon which the general effectiveness of the direct management can be gaged reliably.[2]

The same sort of dissociation is to be found when a railroad owns and operates motorbuses for passenger transportation upon highways in apparent competition with its own passenger trains. In such instances the authority responsible for bus passenger traffic is often not the same as the one responsible for the train service. To be sure, there may be coordination of schedules, but departmental management is divided. Competition thus becomes a spur to each of the agencies to improve the service rendered, to reduce costs, and to show a profit if possible.

The Criterion of Suppressed Competition

It is important to notice that rivalry in the management of the internal affairs of an enterprise is not always desirable. Therefore, activities are sometimes grouped within one department in order to avoid a sharp line of cleavage between them. Instead of deliberately creating and stimulating competitive effort, the purpose is to strive for harmony and cooperation. In a department store, for example, it may be desirable for the buyer in the main shoe department to exercise authority over, and assume responsibility for, the bargain basement shoe department as well. Otherwise questions pertaining to the classification of a particular proposed purchase would constantly arise. Would such a purchase be so attractive as to draw customers from the regular line of shoes down to lower-priced items in the basement? Should the upstairs department display a cheap line of shoes priced at the upper level of the bargain basement offerings? In circumstances like these, the line of cleavage between two departments is the result of the natural tendency of two activities to compete with each

[2] Donaldson Brown, Vice-President, *Decentralized Operations and Responsibilities with Coordinated Control*, American Management Association, Annual Convention Series, No. 57 (New York, 1927), p. 10.

other and thus cause unnecessary managerial friction unless they are combined under one executive head.

Another example of the same situation may be observed when a large-scale retail distributor seeks to maintain balance in operation and volume between branch retail stores and an established mail-order department. By coordinating the management of both of these agencies under one sales executive, the tendency for one type of merchandising to dominate the market at the expense of the other is prevented. Where rivalry is encouraged, it is a very natural human proclivity for competing managers to strive for favors from superior officers. An energetic department head might, by diplomacy and persuasion, conceivably receive better appropriations for buying and larger funds for advertising than his rival could secure. The favored child would thus fatten while the other would grow lean. To obviate circumstances of this kind, both types of selling are combined for direct supervision and control into one sales department.

Harmony is unquestionably a necessary element in the management of any successful enterprise. But a policy of suppressed competition may be applied so rigorously and so universally throughout an organization that the desirable natural instincts—to excel and to win—are stifled. When such a state of affairs prevails, initiative is dulled and an organization degenerates into an aggregation of "yes-men." Top management is all too often accused by commentators on modern business of fostering such a deadening policy. One writer is exceedingly blunt in his assertion that "captains of industry, whether they wish it or not, surround themselves with yes-men, yes-women, and even yes-children. One of the basic faults of modern business is that its great men don't get a tenth of the cracks across the knuckles that they deserve."[3]

There is doubtless some truth in this observation. Harmony is essential, but to find the middle ground between bitter rivalry and spineless yes-men is obviously an optimum that should be the goal of good management. Such an optimum may be characterized as "cooperative competition" between departments. Its achievement is by proper use of both criteria—of competition and suppressed competition—each with suitable emphasis and in its proper place.

The Criterion of Policy Control

A function may be assigned to a department because of considerations of policy control. That is to say, when the development and enforcement of certain policies demand careful and constant supervision, wide cleavage between specific activities must be avoided. Thus a function may be placed in an established department because it seems wise to control its

[3] Edward Hope in the *Saturday Evening Post*, April 22, 1933, p. 17.

activities, mainly in the interest of the division of the business to which it is assigned. For example, installation and repair services incidental to the production and sale of heavy or technical machinery and appliances are commonly the responsibility of the manufacturing department. Or again, when permanent patronage is greatly to be desired, the development of customer goodwill through highly specialized customer service and, in less technical situations, the promotion of amiable customer relations are customarily the responsibility of the sales department.

In the separation of functions this criterion is also taken into account. Such a cleavage may be necessary in order to prevent the undue influence of one department upon another. The department of credits and collections is a case in point. This function is a very necessary one in most businesses of medium and large size, but it consists of a group of activities which are often not large enough to be coordinate with the major departments in the organization. The question then is: "With which major division shall it be combined?"

In answering this question, several alternatives are possible. From the standpoint of use and executive interest, a combination with the sales department suggests itself. The extension of credit is necessary to effectuate sales, and unless collections are made upon such accounts, the revenue from sales will suffer. But from the standpoint of policy, this arrangement is not satisfactory. In an effort to expand sales and to make a good showing—at least on paper—a tendency toward unwarranted liberality in the extension of unwise and unsound credit to customers is not inconceivable. For this reason, credits and collections activities are usually placed in another department, such as accounting or, more frequently, the treasurer's department. Either of these is coordinate with the sales department and, therefore, is in a position to operate both as an aid to the function of selling and as a check upon tendencies to abuse credit privileges.

Other examples of the application of the same criterion may be cited. It is undesirable for a certified public accountant who has been employed to audit the books of a company to be a salaried employee of the accounting department which he is retained to check. In the production department, inspectors of product and processes should not report to the foremen under whom the manufacturing operations take place. Often the work of one man is automatically checked by the work of another. One employee may make a particular item which must fit and become an essential part of another's output. If the two employees are subordinate to different executives, they are less likely to combine forces to circumvent the specifications or instructions contained in the original work order. Maintenance of lines of cleavage between activities that should check each other is an important basis for subdividing departments from the standpoint of policy control. Out of this principle there has developed

the maxim of organization that *an inspector should never be subordinate to the one inspected.*

The "Clean Break" Criterion

It should be clear that the main purpose of considering the various criteria of association is to explore the field of possibilities in order to find the best solution to the problem of functional departmentation. Oftentimes this solution remains obscure and exceedingly hard to find even by the expensive trial-and-error method. Despite its difficulty, however, it is the inescapable responsibility of every executive whose task involves the organization of the management group, in whole or in part.

Ease in departmentation is obviously enhanced whenever it is clear that a distinct cleavage between functions exists and that their allocation in different departments can be justified. But sometimes conditions in which the cleavage between activities is not sufficiently apparent to warrant segregation are encountered. In other words, there are instances where considerations of good management require that dissimilar activities remain associated simply because a "clean break" between them is impossible if adequate responsibility and orderly performance are to be maintained. The association of the buying and selling activities in a department store may be explained in part on this basis. When a buyer lays in a stock of merchandise, he selects the items or lines of which it is composed with an "eye" to its favorable reception by the customer. His patrons, in a sense, are as consciously before him when he buys as they are when he sells.

This lack of cleavage between buying and selling is particularly evident with respect to shopping goods, as contrasted with convenience goods. The latter presents no such problem of selection, either in the purchase or in the sale of merchandise. It is therefore legitimate to separate provision buyers from provision sellers in wholesale grocery houses. The same is true in retail establishments where the expense of multiplying the levels of management can be justified by the volume of business enjoyed. A buyer of sugar, for example, would be expected to specify and to secure uniform quality and price in every order of the commodity which he purchased. Subsequently, it would be sold under similar conditions. One bag of sugar would therefore be like every other bag in the lot, and therein would lie its merchandising significance. In contrast, consider the millinery buyer. No buyer of ladies' hats would think it wise to stock many numbers exactly alike. To the same customer, a bag of sugar may be a bag of sugar, but headgear is quite a different thing.

Business organizations are replete with many other examples where functions are combined because a clean break between them is impracticable and undesirable. The relationship between intraplant transporta-

tion and manufacturing operations in a factory may often be explained in this way. An operating department can neither faithfully nor efficiently carry on its work unless the intraplant carrier system is synchronized and coordinated with the production processes. These activities are dissimilar in all of their characteristics, but no cleavage between them in their management can safely be undertaken.

Likewise, certain other traffic functions are sometimes inseparably bound up with those of warehousing and shipping. For example, the manager of a department whose responsibility it is to secure the most economical rates and service, both for incoming and outgoing freight, may be hampered in his work unless he has the cooperation of those in charge of receiving and shipping. The best way to insure such cooperation may be to subject these latter departments to instructions from the traffic manager. Another way is to use the "appeal of exceptions" method, which will be discussed in Chapter XI. Figuring rates, making schedules, and contracting for transportation service are activities quite unlike warehousing and packing, but storage facilities and packing practices intimately affect rates and shipments both into and out of a plant. Hence, from a practical standpoint, a clean break between them is impossible.

Personnel work presents the same problem. If an autonomous personnel manager can force an employee upon an unwilling or dissatisfied foreman, the latter's capacity and authority, at least in matters of discipline, are impaired to an extent which may prove to be serious. To prevent such a situation, the employment officer may be put in a position subordinate to the production manager along with the heads of the manufacturing departments for whom a work force is recruited.

In some types of manufacturing establishments, as, for example, those which make soap, the inspection department may be merged with other tasks of the chemical laboratory technicians under the chief chemist. The reason for this combination is that there is no sharp line of cleavage between the work of chemical control in the regular productive processes of the industry and the work of product inspection. For instance, consider so simple a matter as the leakage of powdered soap from paper packages. This loss may be stopped by better machine operations in the carton plant, or it may be rectified by a change in the chemical composition of the glue which is used to seal the container.

To some extent, the difficulty of making a clean break between activities pervades all departmentized business. But it seems that the functioning of some divisions in an organization are more interrelated than others. The solutions to the problems which arise as a result of these associations find expression in another principle of organization so fundamental that it may be regarded as a maxim: When a department executive is charged with the responsibility of efficient and successful management, he must

also be given adequate authority for discipline and supervision of all the activities immediately essential to the objective of his department. Some of his authority may come from the appeal system, but in any case, *his authority must be adequate to equate the responsibility with which he is charged.*

The Criterion of Separation

In the foregoing section the emphasis was laid upon the importance of the close association of functions to the point of inseparability under certain circumstances. In direct contrast, the criterion of separation provides that good organization may also proceed from a determination of associations which should not be made.

At first glance, such a negative postulate may not seem to be significant or helpful. If troublesome organization problems are rationalized on this basis, however, the force of this method may be realized. In spite of the several bases of association already discussed, uncertainty may still persist as to where, in an organization, a function should go. The chances of making a wrong decision may be materially reduced if the combinations which should not be made are clear and indisputable. By this process of elimination, if no other way seems open, satisfactory departmentation may be effected.

One kind of functional grouping which should always be avoided has already been mentioned, namely, that two activities should not be associated when the task of one of them is to check the other. This principle assumes that checks and balances in a business organization are wholesome devices. There is a limit, however, to the extent to which these devices may be employed. When too great emphasis is placed upon restrictive organization, self-reliance on the part of subordinate executives may be destroyed, or antagonistic and retaliatory attitudes may be engendered. In either case, voluntary responsibility disappears, with the result that coordination in management becomes difficult if not impossible.

The complete absence of restraints would, of course, be equally disastrous to coordinated effort. The problem of determining the bounds of free initiative, on the one hand, and imposed control, on the other, again defies solution of pragmatic formula. Rather, the correct answer depends upon the good judgment of the managing executive whose responsibilities include the task of departmentation. Good judgment is an intangible quality lying somewhere between impulsive action and procrastination. Philosophically, it is probably correct to say that it results from one's ability to consider and to weigh all the factors involved in a given situation.

In addition to its application in the consideration of checks and balances, the criterion of separation manifests itself in numerous other ways

in departmentation. Association of functions is often avoided for no other reason than the sufficient one of executive incompatibility. In other words, it is obviously a bad practice to assign an activity to the jurisdiction of a departmental head who by training and experience is unfitted to manage it. Likewise, sound judgment would be violated if a disinterested or antagonistic executive were placed in charge of a necessary function, the effectiveness of which depended upon sympathetic understanding and direction. By the same reasoning, it is sometimes undesirable to place an older executive under the jurisdiction of a younger one. Questions of space, location, and available facilities are often deciding factors in departmental separation. It is also conceivable that to associate an activity of a certain type with that of another could result in hindrance and obstruction in the normal processes of the latter. Hence a combination of this kind would be objectionable.

Again it is reiterated that if a debatable question of departmentation resolves itself into the creation of a new and coordinate division of management, responsible only to the chief executive, the problem solves itself after the first step in the elimination process. That is, in deciding what association should not be made, the conclusion is reached that an independent department must be established. But, generally, such a step cannot be taken; some kind of association must be made. It is in such circumstances that departmentation by separation may prove to be a helpful method. Knowing what not to do in the first instance may lead to positive action in the end.

The Criterion of Coordination

The recurring reference to coordination, not only as an activity but as a condition of management, emphasizes the important position which concurrence in purpose and harmony in action occupy in business organization. In previous chapters it has been emphasized repeatedly that problems of coordination are to be found in all levels of management. Indeed, it is upon this factor, above all others, that orderly executive procedure depends. Because of its pervasiveness, therefore, it may seem unnecessary, or even out of place, to belabor the term further by using it to denominate a criterion of association.

Coordination is potentially a tool with which a top executive may deliberately bring about an association of functions in order to prevent friction and, at the same time, to secure harmonious and concerted performance. These desirable ends are achieved by utilizing a technique which insures proper discipline and direction under a responsible department head in circumstances which involve many specialized activities. Such circumstances are always present when a business finds it necessary to carry on its affairs through branches or other decentralized units. There

are many examples. They include manufacturing concerns with plants located in various parts of the country, wholesalers with branch houses, and banks engaged in branch banking—to mention only a few. Whatever the type of business may be, each branch of the parent company includes, in its operation, several specialized functions. Each function, in turn, may require a sizeable personnel in order that its activities may be properly performed.

When a business is decentralized in this manner, questions arise as to how coordinated action, both as to performance and product, may be best achieved. Not only must unity of purpose prevail within each branch of the business, but it must also obtain throughout the whole enterprise. In seeking the solutions to problems of this kind, two possibilities present themselves. In the first place, coordination may be effected through the decentralization of executive authority. That is, each branch manager may be recognized as the chief executive of the local establishment in which he is placed. By such an arrangement he becomes an officer whose task involves the coordination of all the activities of the plant under his jurisdiction. Coordination of the dispersed units of the company as a whole then takes place in the central office through the collaboration of the branch executives who are subordinate only to the general manager or president of the concern.[4]

In the second place, coordination might be effected by establishing centralized executive authority over dispersed, specialized functions. In this case, vertical cleavage in management would cut through from the major executives of the business to the functional departments in all of the branch plants.[5] Such a plan, while conceivable in theory, might be cumbersome in practice because responsibility for coordination would be lacking in each branch establishment. Unified and harmonious action between functional departments within each branch and, again, between branches can be realized only through perfect coordination at the higher executive levels.

Similar problems are to be found in railroad organization, especially in the operating and maintenance departments where coordination is indispensable. Maintenance of way and repair of rolling stock are obviously prerequisites to any movement of freight and passengers. In order that such coordination may be realized, one of two methods is employed.[6] The first of these is called the "departmental system." It is, in fact, the application of a vertical cleavage between functional activities from the level of

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[4] See above, Fig. 28, Chap. VIII.

[5] See above, Fig. 27, Chap. VIII.

[6] L. C. Sorrell, "Organization of Traffic Activities," in *Transportation, Production and Marketing*, reprinted from *Traffic World* (Chicago: Traffic Service Corp., 1931), pp. 78–79.

the major executive in charge of operation and maintenance down through the whole supervisory structure to yard and section bosses. As shown in Figure 34, it envisions three subdepartments, purely functional in character and subordinate to the central department, but each one embracing its own specialized activity throughout the territorial divisions of the railroad. Thus the chief engineer has supervision over as many division engineers as there are operating districts in the management of the system. Likewise, the master mechanic and the superintendent of transportation control their respective specialized functions through separated division master mechanics and division superintendents of transportation.

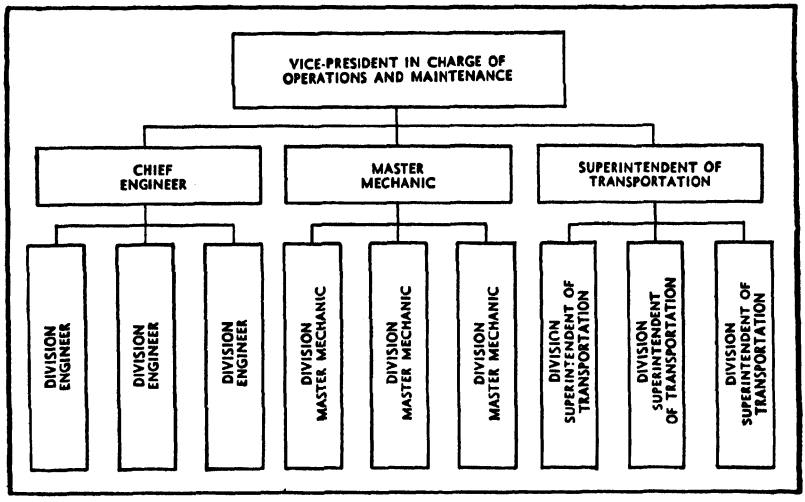


FIG. 34.—Example of territorial departmentation in railroad management, showing correct organization for divisional coordination.

This method of organization leaves each division superintendent without authority over the division master mechanic and division engineer. Coordination can therefore be effected only at the upper level of the office of the central executive—commonly by the vice-president in charge of operations and maintenance as shown in Figure 34.

The other method of securing coordination in railroad organization is called the "divisional system." This method has already been alluded to in connection with the discussion of the span of knowledge. The three necessary functions of engineering, mechanical, and operating supervision are identified as before, but the divisional system ties them together at the level of the division superintendent.[7] In this way, unified action is assured at each division point where problems requiring immediate and, perhaps special, attention and decisions are most likely to occur.

[7] See above, Fig. 12, Chap. IV.

To attempt to enumerate and illustrate all types of conditions and circumstances in which the criterion of coordination is useful to the formation of functional departments would be both impracticable and unnecessary. Coordination is a fundamental principle in organization and management to which emphasis must be given at every point in the chain of executive activity. It is the lubricant which overcomes friction in the highly sensitive human mechanism of management. It is also the cement which binds the elements of an enterprise together, transforming a collection of differentiated parts into an integrated whole.

THE SCOPE OF FUNCTIONAL DEPARTMENTS

On the theory that functional departmentation results from the grouping of activities which are similar or closely associated, it is pertinent to inquire into the scope of functions. That is to say, in designing a business organization, the question invariably arises whether, out of experience, patterns have not been developed which tend to establish sound managerial practices with respect to the activities which should be included in each of the major functional departments of an enterprise.

It is difficult to generalize on this subject with any great degree of assurance. Yet analyses of many organizations, both large and small, supply evidence which suggests tendencies and types in this matter of combinations of functions. Consciously or otherwise, activities have been grouped according to the criteria discussed in the foregoing sections, with the result that characteristic departmental designs have taken shape. These patterns do not in all instances fit all businesses. They are representative, however, of groupings which have been adopted and found workable in practice.

For purposes of illustration, a typical result of functionalization is submitted below. Its basis is a hypothetical manufacturing industry. It purports to show, by analysis, the scope of functions in five major departments. This outline should not be considered to be an ironbound mold into which every industrial organization can be cast. Business organization is plastic, flexible, and yielding, particularly at its periphery. Nevertheless, it has developed a core which gives it strength and stability. The pattern presented is more core than cast and should be so considered.

Typical Pattern of Industrial Functionalization

I. *Finance*:
  1. Raising funds—
    a) Disposing of shares of stock
    b) Issuing bonds
    c) Establishing bank lines

2. Custody of funds—
   a) Selecting depositories
   b) Authorizing expenditures
3. Investing funds—
   a) Dealing in securities
   b) Investments in real estate

II. *Production*:
1. Engineering—
   a) Research
   b) Designing
   c) Preparing production standards
2. Planning—
   a) Inventory control
   b) Preparing production budgets
   c) Routing
   d) Scheduling
   e) Dispatching
3. Costing—
   a) Preparation of standard costs
   b) Process cost keeping
   c) Analyses of variations from standard costs
4. Personnel management—
   a) Hiring
   b) Training
   c) Dismissal
   d) Welfare activities
5. Operations—
   a) Manufacturing services:
      (1) Power generation and distribution
      (2) Plant transportation
      (3) Maintenance of equipment and tools
      (4) Maintenance of grounds and buildings
      (5) Machinery setup
      (6) Repair services
   b) Manufacturing processes:
      (1) Foundry operations
      (2) Machine-shop operations
      (3) Assembling
6. Inspection
   a) Of materials
   b) Of equipment
   c) Of work place
   d) Of product
   e) Safety work

III. *Purchasing*:
1. Procurement—
   a) Of raw materials
   b) Of parts
   c) Of supplies
   d) Of equipment
2. Storekeeping—
   a) Receiving
   b) Storing
   c) Taking inventory
   d) Requisitioning and issuing
3. Shipping—
   a) Packing
   b) Loading and dispatching

IV. *Sales*:
1. Selling—
   a) Sales management, territory
   b) Sales management, house
2. Advertising—
   a) General publicity
   b) Display advertising
   c) Catalogue preparation and distribution
3. Traffic management—
   a) Routing shipments
   b) Rate-making
   c) Freight classification

V. *Controllership*:
1. Accounting
2. Credits and collections
3. Auditing
4. General office services—
   a) Clerical activities
   b) Insurance procurement and claims
   c) Taxation research
   d) Subscriptions and donations

It should be observed that the foregoing analysis is merely a grouping of activities and is, in no sense, an organization chart. Functional analysis is one thing, and organization analysis is quite another. An analysis of a business by functions, however, may well take the form of a chart or outline, but such a design can seldom, if ever, be transformed into an organization without modification. Organization involves the human element as well as the tangible functions which the personnel performs. Therefore, in perfecting a business organization, the activities of the

organization are best indicated by the careful selection of the titles and other descriptive words that are applied to departmental executives.

4. In the discussions of the subject of departmentation that have been presented, it has been implied that functional departmentation is not only more complex in its application but is also more scientific from the standpoint of management theory than either territorial or commodity departmentation. Discuss the validity of this implication with reference to each of the following statements:
   a) The application of relatively simple considerations of appropriate location and similarity of product determines territorial and commodity departmentation.
   b) The application of relatively complex considerations of association is required in order to determine proper functional departmentation.
5. By definition, distinguish between the "criterion of use" and the "criterion of executive interest." Taking the distinction you have made into account and referring to the outline of the typical pattern of industrial functionalization on pages 248–50, answer the following questions:
   a) Why are the functions of real estate investments and the purchase of display advertising not placed under the purchasing department?
   b) Why are these functions placed under finance and sales, respectively, as shown in the outline?
   c) The function of shipping has been assigned to the purchasing department; on what grounds could it be argued that it should be a function of the production department?
6. By definition, distinguish between the "criterion of competition" and the "criterion of suppressed competition." Taking the distinction you have made into account and referring to the outline of the typical pattern of industrial functionalization on pages 248–50, proceed as follows:
   a) In nine instances in the outline, the smallest departmental units are listed as dual functions, for example, credits and collections. List all nine of these dual functions and indicate in each case the nature and extent of suppressed competition involved.
   b) In terms of the criterion of competition, justify the separation of the following functions in departmental organization:
      (1) Inspection of equipment and safety work.
      (2) Hiring and dismissal of employees.
      (3) Selling and advertising.
      (4) Production and sales.
7. Define the "criterion of policy control." Taking your definition into account and referring to the outline of the typical pattern of industrial functionalization on pages 248–50, discuss the validity of the following propositions:
   a) When a customer makes a claim for a reduction in the price that has been charged for a product that shows defective workmanship, it is

sound policy to have this claim settled by the sales manager rather than by the production manager.

b) Even though appropriations for such purposes as salaries, material purchases, and plant investments have been approved by the proper executives, including the president and board of directors, it is nevertheless good policy not to make cash expenditures for them except by direct authorization of the treasurer of the company.

c) It is axiomatic that poor tools tend to reduce both the skill and the productiveness of workers. Hence the functions of procurement and storekeeping, in so far as tools are concerned, should be subdepartments under production rather than purchasing as shown in the outline of industrial functionalization.

8. Define the "clean break" criterion of departmentation. Taking your definition into account and referring to the outline of the typical pattern of industrial functionalization on pages 248–50, explain the following:

a) Why a "clean break" is undesirable between the preparation of standard costs and the analysis of variations from standard costs in the production department.

b) Why a "clean break" is undesirable between power generation and power distribution in the operations division of the production department.

c) Why a "clean break" is undesirable between insurance procurement and the collection of insurance claims in the department of controllership.

d) The functions of selling, advertising, and traffic all appear as divisions of the sales department. Explain why the "clean break" concept requires the close association of selling and advertising, but the function of traffic has been placed in the sales department for other reasons.

9. Define the "criterion of separation." Taking your definition into account and referring to the outline of the typical pattern of industrial functionalization on pages 248–50, give your answers to the following:

a) Assume that the head of the finance department of the company is a young man with limited experience in handling real estate, whereas the chairman of the board of directors, a former president of the company, is very familiar with the concern's investments in real estate. Under these circumstances, where should the department handling investments in real estate be placed?

b) Note that the function of dismissal of employees is separated from the operations of production, which means that foremen and supervisors do not have the authority to discharge workers under their immediate supervision. What is the reason that the function of dismissal has been assigned to the personnel management?

10. Define the "criterion of coordination." Taking your definition into account, rewrite the following partially true statements in a manner and form that clearly and fully impart the meaning intended in each instance:

a) The best way to coordinate all the functions of a business enterprise is to have all the executives of the major departments meet with the president in his office every morning for two hours.

b) If the head of a functional department becomes belligerent toward fellow executives, the proper procedure is to dismiss him or to abolish his department. It would be an evidence of weak management to assume that a troublesome executive might be right in his requests or demands.

c) Since intelligent willingness to cooperate is the essence of effective coordination, it is not necessary to insist upon the best possible arrangement of functional activities into departments and subdepartments.

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Chapter X

LINE, STAFF, AND FUNCTIONAL ORGANIZATION

UP TO this point in our discussion of the theory of business organization and management, major emphasis has been placed on the concept of a hierarchy in management and the consequent division of managerial tasks. These differentiations are brought into existence to insure the purposeful, orderly, and efficient performance of the activities which are involved in the production and distribution of goods and services. The hierarchy itself is derived from a scalar process in organization. That is, practical business management consists of a system of internal government in which there is a gradation of duties determined according to degrees of authority and responsibility. Thus, levels of management imply superiors and subordinates, leaders and followers, commanders and subalterns. Differentiation between the kinds of duties which are performed by the individual members of the management group results in departmentation.

It will be recalled that the scope of executive activities is a broad one. Plans must be made, organization effected, and coordination realized. All of these duties vary in range and force according to official rank; but they are, nevertheless, present in some degree in all levels of the executive pyramid. From plan to procedure, they are an integral part of the responsibilities of a business executive.

THE LINE AND STAFF CONCEPT

The basic fabric of management is line organization. That is, in every organization there must be a single head who, to use a military expression, commands it and who alone is ultimately responsible for results—for all that it does and all that it fails to do. Whatever the architecture of such an organization eventually may be, it represents a growth downward in authority and responsibility from the chief executive to the humblest employee. Each successive subordinate in such a scalar structure is a "station" in the transmission of managerial energy, and the relationships which join them are the lines of jurisdiction through which authority flows from inception to execution.

Whenever the development of an enterprise can be traced to a small beginning, the characteristics of a true line organization are clearly apparent. At its birth, such a business usually emerges merely as an

owner-manager concern. The tasks of management are few and simple, overshadowed by, and subordinate to, the processing functions of the establishment. If it is a store, the owner-manager is usually found behind his counter, serving his trade. If it is a machine shop, he is at the bench or lathe, side by side with whoever his shop personnel may be. In such circumstances, the management of the enterprise is relatively easy, even though the owner may be more proficient in his trade than in his executive ability.

In such a business, organization for management is simple. In all respects it is a line organization. Authority and responsibility for its functions in all particulars, operative as well as managerial, are vested in the owner-manager. All other members of the personnel are subordinate and accountable to him. Policies, decisions, and orders—all flow downward from him. Official ranking may be slight or apparently lacking; yet, to the extent that final jurisdiction is vested in this one man, the scalar principle exists.

Assume now, that the little business prospers and grows. (And be it said in passing that such an assumption is more than academic imagination. Many modern business institutions of all sizes have had precisely such humble origins.) The work involved consequently increases in volume, scope, and complexity. Eventually, the burdens which the developing enterprise imposes upon the owner-manager exceed his physical and mental energies. In the language of our previous discussion, his span of control and possibly his span of knowledge are insufficient to encompass the tasks required of him. He reaches the point where he must delegate a certain amount of authority and responsibility to others in order that the work of the business may be performed. In this way, specialization in management takes form and departmentation appears.

Functional Differentiation

As we have previously noted, the first stage in specializing the tasks of management usually consists of functional differentiation. Department heads are created and are charged with the responsibility for the satisfactory operation of more or less clearly defined activities, such as production, selling, and accounting. In spite of such distinctive assignments, however, these new division heads, conforming to the original system of line relationships, will still take orders from, and report directly to the head of the firm. Should it be found necessary to specialize the tasks of management even further, the department heads may be provided with subordinates to supervise and direct activities narrower in scope and more technical in character.

With each increase in the managerial group, not only are the scalar levels multiplied, but the managerial pyramid is extended at its base. Such

expansion may relieve the manager-owner at the top of many details, but his load of responsibilities is materially increased. As long as a line organization is retained without much modification, expansion in an enterprise tends to increase both the scope and the complexity of the problems which demand the attention of the top executive. The reason for this tendency is that highly centralized management is characteristic of line organization. Its features are those of direct command emanating from an unquestioned superior officer who must be accepted as competent to initiate policies and procedures, direct their execution, and appraise their results. Such omniscience and omnipotence on the part of one man may be possible in a small concern; but, obviously, they transcend the powers of one individual when a business passes beyond a certain stage in its growth. Just when this point is reached may be difficult to determine with precision. However, it is safe to say that, short of a serious breakdown in the internal affairs of an establishment, or its actual failure, top management will normally sense the need of specialists to supplement its knowledge and strengthen its hands. These managerial experts are known as a "staff."

Staff Differentiation

The avowed purpose of a staff is to relieve the chief or top executive, or any executive to whom staff assistants are assigned, of a multitude of details which his post inevitably entails. This does not mean that, by the addition of a staff, the principal executive can divest himself of his responsibilities in certain areas of management below him in scalar position. Such divestiture is impossible since the duties of a leader are inseparable from his authority. Authority may be delegated to subordinates, but not relinquished; responsibility may be assigned, but not avoided.

Sometimes staff members may be largely nominal in character. That is, they support their chiefs in name only rather than by functions. In such instances they are known as "assistants," and speak and act directly for the executives to whom they are attached. Delegation of authority over specific tasks is not involved, but the effect is rather a projection of executive personality. It is as if the span of an executive's capacity had been extended by the addition of new arms and hands to his official body. This device is common in organization and suffices where more elaborate staff requirements are not necessary. It may also prevail by the side of formal staff arrangements.

Formal Staff Organization

Formal staff organization results from the establishment of a distinct managerial group to whom authority covering special fields of action has been delegated. Each formal staff executive, therefore, is a specialized functionary charged with the responsibility of the development of plans

and methods for the performance of certain tasks identified by their operations or purposes. Thus, the chief executive may assign to an immediate subordinate authority regarding the details of policies and procedure with respect to sales; to another, authority regarding production; and to a third, authority concerning the technical problems of procurement.

Personnel management in a large concern is a good example of a staff department. In it are involved numerous considerations which are preliminary and basic to the actual employment of and performance by the labor group. For example, the recruiting of a satisfactory work force is dependent upon a proper job analysis of the operations to be undertaken. Job analysis is an investigative function which can be intrusted only to competent specialists. Similarly, the personnel department may prepare plans for the control of wages and hours in conformity with agreements with labor unions and with the regulations imposed by federal and local laws. It may advise with line executives in matters of seniority, tenure, and promotions. It may facilitate employment itself by engaging in hiring workers, subject to the acceptance of the executive for whom such persons are tentatively secured. This leaves the way open for a line executive to reject any or all of the employees which have been selected for him—a situation which would rarely occur if the employment section of the personnel department is competent and its interdepartmental relationships are prearranged and mutually understood.

Distinctions between Line and Staff Executives

Distinctions between staff and line executives have been attempted in various ways. It is sometimes said that the activity of a staff executive is to *think*, while that of a line executive is to *act*. Such a differentiation is too simple, and it is obviously inaccurate because it is a half-truth. Both types of executives must think and act; the distinction between them is determined by the spheres of interest which govern their thinking and the areas of control which govern their acts. It is more nearly correct to say that staff officers are assigned to an "authority of ideas," while line officers are charged with the "authority to command."

In a sense, therefore, staff organization follows line organization in order of precedence. It is a facilitating structure both superimposed upon and incorporated into a going concern at that point in its development where highly specialized managerial services become indispensable.

LINE AND STAFF IN MILITARY ORGANIZATION

In practice a clear understanding of line and staff organization may be facilitated by analysis and study of these relationships as they prevail in the United States Army. It is unimportant to argue whether the addition of a staff to the basic line organization appeared first in business or in

military organization. Military organization, as it exemplifies the establishment of clear-cut differentiations between superiors and subordinates in authority and responsibility, is undoubtedly the oldest type of complex human grouping.

Because of its ancient origin as well as its universality among all peoples, military organization has contributed much to modern business organization. Moreover, armies have been laboratories in which the management of men has been tested relentlessly. Despite the horrors of war and the aversion of peaceful men to all its works, intellectual honesty compels us to recognize the fact that armies have borne the brunt of the bitter struggle which man has waged against his own baser instincts throughout the ages. Therefore, the efficient performance of military units—unlike other human organizations—has meant the actual life and death of men and of nations. It may be because of such testing in the crucible of history that military organization has not only persisted for twenty centuries and longer but has improved as armies have increased in size and complexity. Military organization is often decried by certain people because of its severe discipline, regimentation, and inflexible rule of authority. These elements are obviously matters of necessity in the very nature of the conditions which armies face. Their effectiveness is undeniable; hence they are often imitated, if not adopted, by business as well as by other organizations where a high degree of order and direction in management seem necessary.

Line and Staff Differentiation

In recent years, military authorities have also learned from business. In their modifications of the organization of the armies of today, they have, in part at least, profited by the experiments and experiences of large business enterprises. Command in an army, like executive authority in a business, is established fundamentally on line organization. In the army unit, of course, the ranks of officers and the limits of their powers are more clearly defined than is true in a business.

Pure line organization, however, does not adequately describe the management structure of an army. In addition to the "officers of the line," modern military units are also provided with a "staff." The staff officers of a military unit and the staff executives of a business concern are identical in principle and purpose. That is to say, the members of both groups are specialists who occupy positions which are so designed that they may give aid and advice to superiors in important technical matters relating to policies, strategy, and procedure. They issue no orders; neither do they supervise or control performance. From them suggestions move *up* to superior officers in whom rests the power to transform such suggestions into orders, which, in turn, flow *down* through the line. The fact that the

suggestions of the staff—when transmitted upward to the "line" or commanding officer—are expressed in their final form as prepared orders, in no way lessens the accuracy of this important differentiation.

Duties of the Staff

Thus a general, in order to exercise his authority and responsibility efficiently, is always assisted by a staff of highly trained officers, each of whom possesses specialized skill or knowledge. The staff implements the authority and responsibility of the commanding officer. It investigates, plans, and formulates the orders which may later be issued by the officer in command to his subordinates in the line. This use of a staff of experts in army organization has given rise to the descriptive term, "line and staff organization," and by simple definition the two types of authority thereby implied may be distinguished. Hence it may be said that "staff authority" is "authority to plan," while "line authority" is "authority to command."

Line and Staff in a Division of Infantry

To illustrate the use of staff in army organization, Figure 35 is presented. It shows that the authority of the commanding general of a division of infantry in the United States Army is not limited to the direct command of four subordinate line officers who are in charge of combat units. Such fighting units must have the support of many other types of troops. These specialized troops constitute the staff organization of the division.

According to the Tables of Organization of the United States Army as of June 1, 1945, the aggregate number of persons in an infantry division, including attached units, is 15,838 officers and enlisted men.[1] Of this total number, there are 12,959 men in the four combat units—namely, three regiments of infantry and a division of artillery. Thus there are only 2,879 officers and enlisted men in the special units which support and supply the actual fighting troops and the headquarters of the division. (See also Fig. 36.)

One reason for the staff organization is to provide the commanding general with assistants whose aid will make his span of control over line officers and their commands effective at all times. Another equally significant reason for the staff is to augment the commanding general's span of knowledge. The activities undertaken by the line officers and the units under their commands are so varied, so complex, and so nearly simultaneous in action as to make comprehension of them impossible in the mind of the division commander alone. Even a cursory examination of Figure 35 will emphasize this fact. The very titles of the units provided

[1] *ROTC Manuals, Supplement, Infantry Organization, 1945–1946* (Harrisburg, Pa.: Military Service Publishing Co.), p. 4.

in the staff organization suggest their highly specialized character and necessary purposes: troops to service the headquarters of the division; police to maintain order and discipline; ordnance to provide ammunition and arms; quartermaster troops to obtain food, clothing, and other subsistence requirements; the signal company to maintain communications; medical units to take care of the sick and wounded; reconnaissance to secure strategic information; engineers to build roads, railroads, bridges,

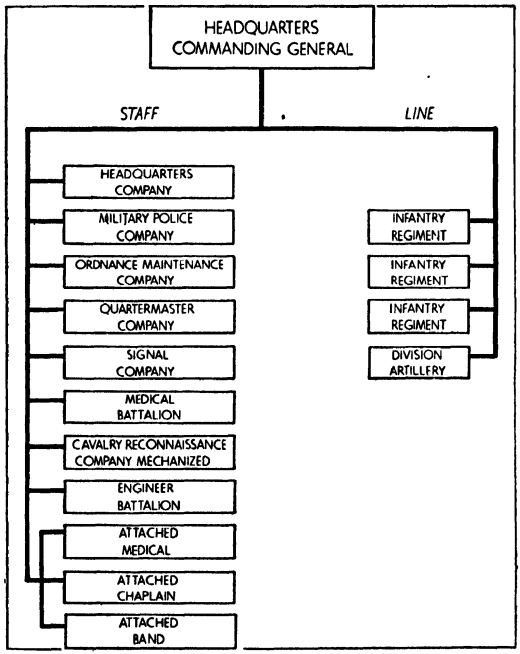


FIG. 35—Infantry Division, T/O & E7, June 1, 1945.

and other works; the chaplains and band to provide psychological and nonmaterial support; and a small group of officers who serve as "staff" assistants to the commanding officer.

The major function of the staff organization of a military unit, therefore, is twofold: (1) without this support it would be impossible for combat troops to successfully engage an enemy, and (2) with staff assistance the commanding general's span of knowledge is extended so that he may comprehend every aspect of his command whether the prevailing circumstances are the normal ones of peacetime or the complicated and critical ones of battle. This illustration brings out the fact that the staff includes both an executive and a worker group, the latter corresponding, in part, to the so-called service departments of a business enterprise.

Unit	Strength	Rank of Commander
Army group	Two or more armies	General
Army	Two or more corps	General
Corps	Two or more divisions	Lieutenant general
Division	15,838	Major general
Brigade	6,516	Brigadier general
Regiment	3,258	Colonel
Battalion	1,014	Lieutenant colonel or major
Company	193	Captain
Platoon	41	First or second lieutenant
Section	12–17	Sergeant
Squad	12	Sergeant

Fig. 36.—Typical units of the United States Army as of October 1, 1945. (Information supplied by the Adjutant General's Office, War Department, Edward F. Witsell, Major General.)

Functional Organization of a "Combat Team"

The knowledge military leaders have gained in the stress of modern warfare has emphasized the necessity for the coordination of infantry units with other types of armed forces in the progress of actual ground battle. Therefore, there has been developed within a division of infantry what is known as a "combat team." Usually it is composed of infantrymen and artillery, the latter with both light and heavy weapons. But circumstances may require that light or heavy tanks, or both, be employed in order to gain certain objectives. Even units of engineers and the signal corps, equipped with arms, may be included in such a team, depending upon the character of the operation to be performed.

Thus there is no such thing as a typical combat team. Size, character, and composition vary with battle requirements. Nevertheless, it is possible to illustrate the command relationships which prevail when a combat team is organized within a division and sent into action against opposing forces. Such a hypothetical situation is shown in Figure 37.

For purposes of illustration, let it be assumed that a given situation has called for a combat team of which the effective units shall be three battalions of infantry and one battalion of light artillery. The ranks of the commanding officers of these units will be lieutenant colonel for the infantry units and major for the battalion of light artillery. In command of the entire combat team there will be a colonel of infantry, since the three battalions of riflemen constitute a regiment. Thus, at the battalion level, the immediate subordinates of the colonel are three lieutenant colonels of infantry and one major of artillery.

Not only does it appear that the formal, theoretical chain of command is violated, but also that two diverse functional units are merged under the authority of an officer of one of them. That is, first, a major theoretically should report to a lieutenant colonel, next higher in rank, rather

than to a colonel; and second, an officer of infantry is commanding an officer of artillery.

The point is that in battle action the requirements of the moment supersede all other considerations. The command of this hypothetical combat team is an example of the modification of the traditional line and staff military organization. Under stress of battle, when lives and military success are at stake, there is not time to use the machinery of line organization, in accordance with which the colonel of infantry could call into action his supporting artillery only by way of divisional headquarters, through which, in turn, orders would be issued to the colonel of artillery. In the development of the combat team, the point at which coordination between infantry and artillery is to take place is brought down from the top executive level to the major executive level. This shift of responsibility is clearly illustrated in Figure 37. In the plan of the combat team,

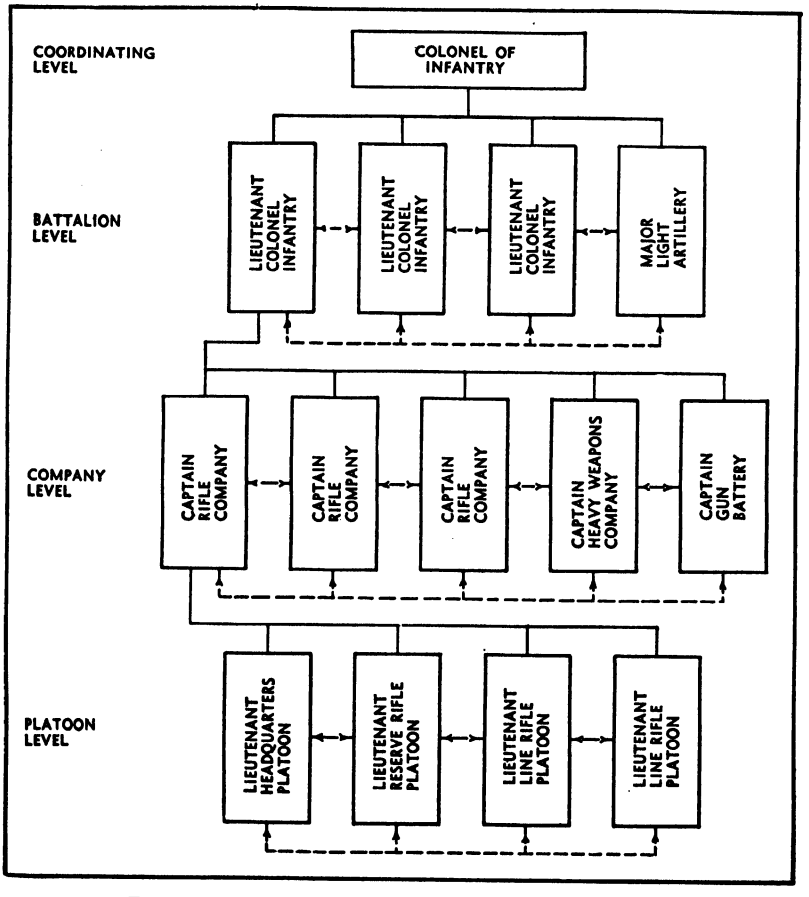


FIG. 37.—Functional organization of the combat team.

authority and responsibility for the coordination of the infantry and the supporting light artillery rests in the colonel of infantry. This change in the point at which interrelated, but functionally different, activities are to be coordinated is in accordance with the experience of large-scale business enterprises in the development of their major executive level. For example, the vice-president in charge of sales is quite commonly also the executive whose responsibility includes the coordination of such different sales functions as advertising and selling in the field.

Increase in Functionalization

New problems involved in mechanized combat have greatly increased the degree of functionalization which must prevail in army organization. In the hypothetical combat team illustrated in Figure 37, this development is particularly apparent at the company level. At this level a complete combat unit consists of three rifle companies, one heavy weapons company, and one gun battery. The three rifle companies and the heavy weapons company collectively form an infantry battalion. The gun battery is taken from the artillery battalion. Since it is no longer possible to arm all troops alike, specialization of a functional character has even developed within the infantry itself. Thus, a rifle company consists primarily of men armed with rifles together with a few machine guns; a heavy weapons company is armed with machine guns and small mortars; and a gun battery consists of artillery light enough to advance rapidly and to keep fairly close to the front lines in order to support the particular infantry unit to which it is attached.

It is clear that this complicated arrangement, with its highly diversified forces, would become chaotic in action were it not for coordination centered in the battalion commander. Technically, this officer is a lieutenant colonel of infantry—originally conceived to be chief of foot soldiers who were armed with hand weapons, such as swords, muskets, or rifles. In modern warfare, such troops are insufficient by themselves. Their effectiveness is enhanced by the sustaining power which they are given by highly mechanized weapons. Thus the lieutenant colonel of infantry in action has now become a commander of artillery as well.

DEVELOPMENT OF FUNCTIONAL AUTHORITY IN MANAGEMENT

Thus far we have traced the development of business organization from its simplest form, that of the pure line authority of the owner-manager of a small establishment, to a stage in its growth where the addition of a staff has become necessary. At this stage, to affirm the outline of the foregoing sections, the organization structure consists of two managerial groups identified by their respective obligations. First, there are the line executives, each of whom exercises complete authority of execution

over all of that part of the organization which lies beneath him in rank and is within the scope of the responsibilities assigned to him. Second, there is the staff, a managerial group of experts created to support the line executives to whom they are attached. Such support is informational and advisory in nature. The power exerted by a staff executive outside of his own department, so far as it is authoritative, is, as has been previously said, merely an authority of ideas, even when such staff ideas are promulgated and accepted by line executives unchanged.

Formal Line and Staff Authority

It is important to grasp the significance of staff and line relationships at this point because it is a stage in the evolution of organization from which a final transition emerges—final, that is, as far as present-day business organization has evolved. The staff executives are formally responsible advisers to their respective line superiors—formal because obviously they exist neither in a vacuum nor in incommunicative compartments. Their special knowledge and advice is available to corresponding staff executives in subordinate organization strata, and to coordinate executives on their own management levels. But any direct line instructions which such staff executives might wish to see promulgated and enforced may only be advanced back through their line of direct contact with their superiors and thence down through line executives to the next subordinate levels.

This flow of advice, information, ideas, or plans—whatever the contribution of the staff may be called—*up* to a superior who has the authority to transform such technical suggestions into orders and then *down* in the form of instructions to be executed, may be illustrated in Figure 38. In this hypothetical case, the staff executive concerned is a specialist in market research. Let us assume that his findings with respect to a certain problem relate especially to the activities of a sales force in a given territory. In order that the ideas of the research expert may be transformed into action, they must first go up to his superior, the chief executive. By the executive's approval and order, they in turn flow down through line authority to the branch manager, a line executive, and through him to his subordinate sales manager, who transmits the instructions to be carried out to the sales force under his immediate jurisdiction.

As a management group increases in size and the scope of its activities expands in the number and complexity of the tasks to be performed, the procedure described in the preceding paragraph becomes both cumbersome and wasteful of executive time and energy. It is like a crooked stream, the angles and turns of which slow down its velocity and hence reduce its force. To realize its maximum power, its channel must be straightened and obstacles which impede the free flow of its current must

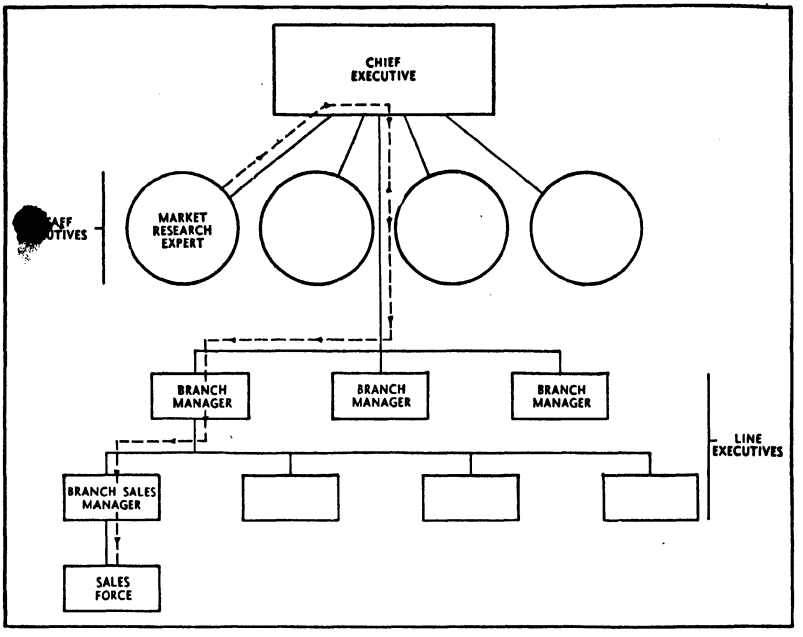


FIG. 38.—Theoretical flow of staff authority through the chief executive to line executives.

be removed. When such a straightening process takes place in the channels of the flow of specialized managerial authority, another stage in the refinement of organization takes place. It is the evolution of staff into functional authority. Similar evolution from line and staff to a functional "combat team" has already been discussed above.

Transition from Staff to Functional Authority

The staff members, for example, may now become executives identified by functional titles to which is appended the word "manager." No longer do they merely serve as advisers to the top executive. They are charged with additional broader responsibilities for the particular functions of the business which they represent. They may carry such designations as general sales manager, general financial manager, general traffic manager, and others of similar character. As such, they occupy positions of major importance in the organization structure. They are pre-eminently the planners and prescribers of methods and procedures within their own fields of specialization. They are, of course, without authority to command beyond their own departments, and they are subordinate to the chief executive. Each such manager owes his post to the inability of the

top executive to add all these specialized fields to his own span of knowledge.

At this point a second difference appears. The chief executive, instead of requiring all details of an informational and advisory nature to pass through his hands for consideration and review, may divert them. In place of such requirements, provision is made for direct contact between the major functional executives and the executives concerned in the lower managerial levels. Thus the channel is cleared for the free flow of work of a technical nature, and the chief executive is relieved of a mass of details relevant to particular functions as distinct from those of over-all managerial significance.

This development is illustrated in Figure 39. In this diagram three levels of management are shown, tied together from top to bottom by line authority and responsibility. But these levels are reinforced functionally by four main vertical bonds corresponding to the major functions of the

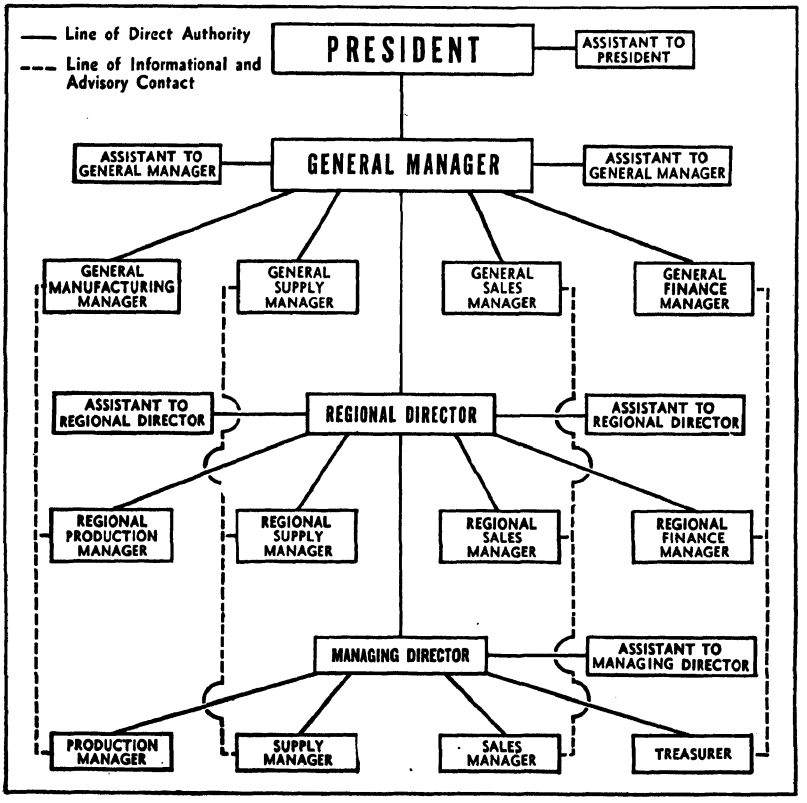


FIG. 39.—A schematic representation showing staff authority in the organization of a manufacturing concern operating on an international basis.

business. These bonds are represented by the broken lines in the drawing. They are projected directly downward without having to pass through the office of the general manager. The dual relationship which exists in this particular enterprise, therefore, may be characterized as a line "organization of execution" and functional-staff "organization of ideas."

Functional Organization Completed

The complete transition from staff to functional organization is shown in Figure 40.[2] This is accomplished by vesting in the functional executives

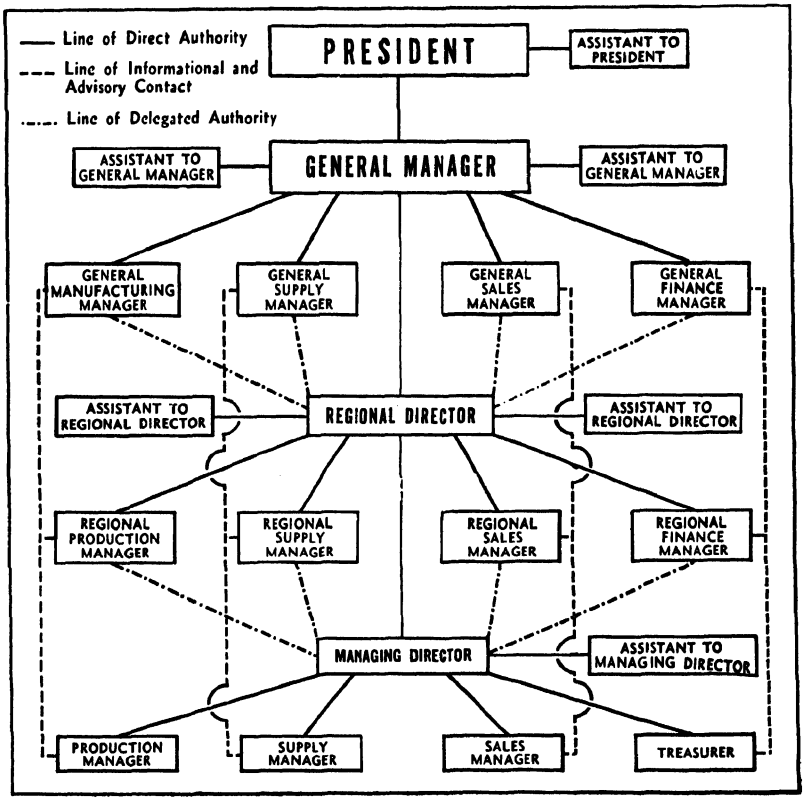


FIG. 40—A schematic representation showing functional authority in the organization of a manufacturing concern operating on an international basis.

[2] Figures 39 and 40 are adaptations of the staff and functional organization of the former General Motors Export Co. as presented by Edgar W. Smith in *Handbook of Business Administration* (New York: McGraw-Hill Book Co., 1931), p. 1484. The General Motors Export Co. has been succeeded by General Motors Overseas Operations, Division of General Motors Corp. According to a communication from Mr. Smith, now administrative assistant of this Division, while technical refinements have been made, the essential structure of the Overseas Division remains the same as it was for the previous organization.

something more than merely informational and advisory obligations. To them has been delegated special authority over the plans, procedures, and results of the activities represented by them. Thus the general manufacturing manager, by specific designation from the general manager, exercises authority over the manufacturing processes of the company under the jurisdiction of the general manager, but superior to the line officers next in rank on the management pyramid. Therefore he is always in a position to command as well as to advise within the limits of the special authority delegated to him. This distinction applies to each of the other functional executives occupying positions on the same level—in this instance, the general supply manager, the general sales manager, and the general finance manager.

It should be carefully observed, however, that established line relationships remain intact. What has happened is that line and functional executives are jointly responsible for performance, the former with respect to direct action involving all subordinates and their activities, and the latter with respect to technical problems involving a given phase of the business.

The fact that *functional executives do not extend their delegated authority below the first level of line executives to which their authority flows* is an important point. As a result of this restriction, each line executive retains his original authority—the authority of command over all of the body of the organization lying beneath him. However, with respect to his source of authority, a line executive must look in two directions: first, to his immediate line superior, and second, to his superior functional executives. In a highly functionalized organization it is clearly apparent, therefore, that a line executive may have more than one "boss." In the practical affairs of the management of an enterprise of any considerable size, the fact is that he usually does have more than one, for reasons already suggested, namely, the limitations of an individual's span of control or span of knowledge. The highest or chief executive must of necessity *delegate* authority over particular functions to specialists or functional executives. These act for him; or, as it has been put, they are his "vicars."

COMPOSITE LINE, STAFF, AND FUNCTIONAL ORGANIZATION

In this chapter the discussion has been concerned with a consideration of the evolution of organization for management from the simple, basic form of line relationships to the more complicated structure which results when the addition of staff and functional positions are built into it. Line organization is the typical management device which exists as long as authority flows directly from superiors to subordinates, free from the interference of lateral or subsidiary influences. That is, a line executive is one who has complete charge of a given division, department, or section

of a business, or of the enterprise as a whole, as in the case of the chief executive. As such he exercises authority over all of the body of the organization which lies beneath him in the management group. He is identified especially by the characteristic of command over persons by means of which performance is accomplished. In all instances, the authority of a line officer is delegated to him by his superior (or superiors) in rank, and he must discharge his obligations within more or less definitely prescribed limits.

Purpose of Staff Authority

As the tasks of management increase in number and complexity, staff authority is added to the organization to strengthen and support the span of control of line executives. Staff authority is concerned chiefly with ideas and plans. This type of authority grows out of investigative activities and flows to the line executive, providing him with information and advice. Staff authority is highly specialized in character and originates as a result of delegated authority from the official to whom such information and advice is given. In other words, fundamentally, the line executive is responsible for both plans and procedures; but since the human capacities of knowledge, time, and attention are limited, increasing burdens of management make it imperative that assistance be sought and secured to lighten the load. The strain almost always appears first in the span of knowledge. As has been noted previously, although there is almost no limit to the number of persons to which commands or orders may be given, it is obvious that in the realm of considered judgment, where decisions must be based upon facts and formulas often highly technical in character, any individual's range of effectiveness is much narrower. To illustrate this point, attention was directed to modern military organization in which the staff is an indispensable device. Without staff assistance, commanding officers of military units would now be impotent to cope with the intricate problems and movements which continually confront the armed forces of any nation.

In a business organization, a refinement of staff authority is effected through the establishment of direct authority relationships with coordinate line executives or with staff positions of lower rank. By means of such contacts within the management structure, channels are provided for the free flow of specialized information and advice directly from the staff executives charged with the responsibilities of origination to points in the management where performance takes place. Consequently, superior line executives are relieved of many details to which attention would otherwise have to be given, even though by the very nature of such matters themselves the consideration accorded them would be largely formal, if not superficial.

Limitations of Functional Authority

Functional authority represents the farthest advance to which specialization in management has gone. It is the stage in the development of organization where it becomes desirable to bring the talents of certain staff executives, who are experts in particular activities, into more direct relationship with the functions which they serve. To accomplish this end, such executives are delegated a greater measure of authority and control over such functions than was possible under the staff system of organization. They become vested with power to control processes within their own fields of specialization, but they may not usurp the authority of the line executives with whom they are associated. Top management has adopted this method to further relieve itself of important details and, at the same time, to strengthen its span of control.

With well-developed functionalization, in keeping with the size of the particular enterprise, many advantages appear. For instance, if all functional experts have uniform rank, it is impossible for the instructions of one expert to take precedence over the instructions of another. Thus, if the purchasing agent is satisfied with a certain grade of raw material which does not meet the specifications of the chief chemist, the chemist cannot prevent the purchase, nor can the purchasing agent insist upon approval by the laboratory. If the production superintendent decides to use the material, the chemist cannot prevent such action by direct instructions. He can, however, appeal to the appropriate major executive for final decision on the dispute. On the other hand, if the production superintendent decides not to use the material, the purchasing agent cannot force its acceptance. His only recourse is to appeal the whole subject to the higher management. If all functional experts have uniform rank within the organization, coordination authority and responsibility tend to concentrate at the major executive level. Since functions overlap within the organization in different ways—and in ways that change constantly with conditions—such concentration increases the efficiency of coordination. It places coordination of operation at the same level as coordination of major policies and company objectives, thus assuring consideration of all aspects of any particular decision.

Complete functionalization in management, however, is seldom, if ever, accomplished. It would be if all the specialized activities of an enterprise were so organized and controlled. Before this stage is reached, the point of "diminishing returns" in effectiveness probably would be passed. Prerogatives in position are imponderable values always jealously guarded; and since each extension of functional authority tends to divide and share such "rights," the resulting human friction is not easily avoided or overcome. Increasing size in organization has tended toward increasing func-

tionalization, but there are practical limits—not easily defined because they are intangible—beyond which the establishment of functional authority in management should not go.

THE PRINCIPLE OF PARAMOUNT NECESSITY

The principle of "paramount necessity" may be said to dominate and determine the process of organization architecture of every business. In other words, no executive position is created and filled for any other reason than that the business would suffer or would make less progress without it. At the supervision level, for example, there is a *paramount necessity* for executives competent to interpret the orders, policies, and natural conditions so that the employees may do the desired work. At the supervisory level, the organization pattern is developed primarily to provide such competence in interpretation at the necessary points among the operating employees.

At every management level, all three methods of organization—staff, line, and functional—are necessarily in use. Thus the assistant foreman of the punch-press room in a large factory is part of the line organization of his particular department. If the punch presses must perform operations for several different portions of the production process, this assistant foreman may also be a functional expert in charge of such work for the entire business. He must usually plan, which is a staff activity, the work done by various employees under his control.

There is developing a strong tendency toward concentration of the different types of authority at the most suitable management levels. Coordination authority, for example, is primarily exercised and assumed at the highest management levels. There is a similar strong tendency toward concentration of functional authority and responsibility at the department head management level.

With coordination and functional type management largely concentrated at the higher management levels, there is a natural offsetting tendency toward concentration of line management at the supervisory levels. The "paramount necessity," at the supervisory levels, is for management, in a "line" sense, to direct and control the production efforts of particular groups of employees.

TOTAL AUTHORITY FOR MANAGEMENT

From a study of the steps in the development of the staff and line concept of organization, it should be clear that an evolutionary process emerges. Through delegation of authority, top management consolidates its position and supports its span of control by assigning both power and responsibility to subordinates upon whom reliance is placed. This development is illustrated in Figure 41. Total authority for management, as in

the smallest business, involves four major activities: coordination, planning, command over persons, and control over processes. The first detachment from complete centralized control, as the size of the enterprise increases, is the delegation of line authority, with its command over persons. A portion of the tasks of management is assigned to executives below the rank of the top executive, and to that extent the span of control of the latter is narrowed and strengthened by concentration. The second segment to be delegated is staff authority, which involves investigation, information, and advice. Finally, the third step is delegation of functional authority, concerned particularly with control over specialized processes. Coordination remains as the residual element, the main task of top man-

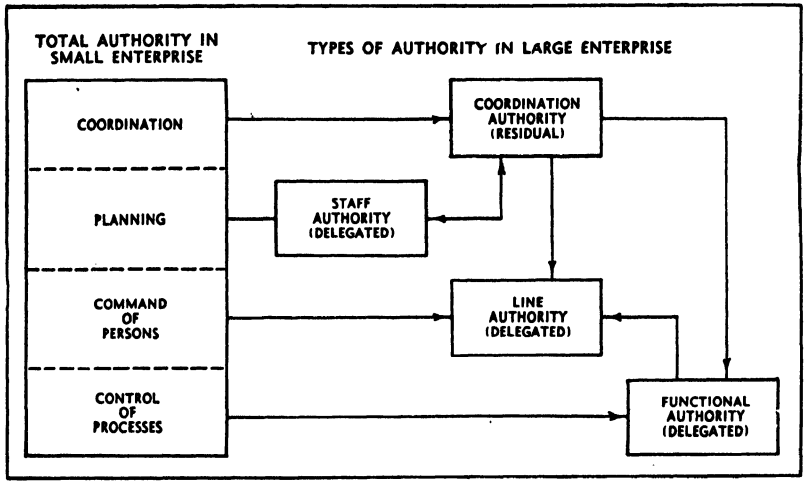


FIG. 41.—Diagrammatic representation of the evolution of types of authority.

agement, diminished only to the extent that coordinative considerations permeate and diffuse the whole organization. The significant point is that the position of the top executive, and often that of the major executive, is strengthened by delegating authority to subordinates, since the residuum which remains when the delegation of tasks has reached its farthest practical point is the task of coordination.

It has been repeatedly emphasized, and it may be reiterated, that delegation of authority and the assignment of responsibility do not and cannot mean the relinquishment of either. Final authority and responsibility remain as the obligation of the properly constituted head of the institution, whatever its size or character may be. It is necessary that this situation be recognized. In the course of the actual management of an enterprise, problems constantly arise which cannot be solved by the workers or executives to whom they are presented. Just as orders flow down,

so there must be provision for appeal of difficult problems upward within the management pyramid to the executive who can take action. Problems may be appealed because of some general decision to reserve such matters for the higher management. Emergencies which present problems outside the knowledge and ability of lower executives often arise. Viewed in another sense, as Frederick W. Taylor pointed out, the exception principle develops management efficiency since all matters are handled at the properly delegated management level with minimum effort and maximum skill.

QUESTIONS

1. By definitions, describe each of the following types of executives in sufficient detail to identify and to distinguish between them:
   a) Coordination executive.
   b) Staff executive.
   c) Functional executive.
   d) Line executive.
2. Describe and illustrate with examples each of the following types of staff executives:
   a) Personal assistant to an executive.
   b) Investigative or research staff executive.
   c) Advisory staff executive.
3. Assume that the president of a company retains the services of an attorney that he may undertake the necessary legal steps incidental to the purchase of certain real estate, including the drawing of a contract and the preparation of deeds and the necessary filings and recordings. On the basis of such an arrangement, answer fully the following questions:
   a) Is the attorney in this example serving in the capacity of a staff executive, even though his only remuneration for legal services is a single fee for this particular transaction?
   b) Would your answer be the same if the terms of the contract provided that the seller instead of the purchaser of the real estate would pay the attorney's fees?
   c) Suppose this attorney accepted employment as a salaried company executive in charge of investments in real estate, and as such he actually purchased the property in question for his concern and performed all the necessary legal steps as outlined above. In such circumstances, what would his executive status be? Would it differ from that ascribed to him in the first example?
   d) Can an executive, under suitably varied conditions, perform the same executive task as a "staff" activity in one set of circumstances, and as a "functional" activity in other circumstances?

4. Restate the criticism of the Taylor plan of functional foremanship as given in the text in Chapter VIII. How is it possible for an executive whose rank is at a relatively higher management level than that of supervisor to experience the same problem in a complex line, staff, and functional organization? What do you suggest as a practical remedy for this difficulty?

5. In foregoing chapters territorial, commodity, and functional departmentation have been clearly differentiated and their application to typical business organizations has been illustrated with numerous examples. Figure 36, showing recent organization of the United States Army, illustrates a fourth type of departmentation. It provides for the subdivision of the executive organization at each lower level into an increasing number of absolutely identical units identified as corps, divisions, brigades, regiments, battalions, companies, platoons, sections, and squads. Each regiment throughout the army is organized like every other regiment, and the personnel of all regiments receives identical training.

   a) Explain why the army method of departmentation is inapplicable to business organization in all but very exceptional cases.

   b) Show why the severe discipline and inflexible rule of obedience to the decisions and orders of a superior whose judgment must be accepted—which is typical of army management—requires more strict adherence to line organization than is necessary or desirable in business organization.

6. The statement is made in the text of this chapter that in business organization there is a tendency for line authority to concentrate at lower management levels, while the authority to coordinate remains at higher levels. Elaborate on this concept by contrasting military and business organization. Bring into your discussion the significance of the "combat team," illustrated in Figure 37, as having affected the level at which certain coordination activities within the army tend to take place.

7. It has been emphasized that functional executives do not extend their delegated authority below the first level of line executives to which their authority flows. On the basis of this principle, answer fully the following questions:

   a) What organizational problems would result if the sales manager of a large concern disregarded this rule and, by personal visits to the factory, undertook to give orders to production foremen and employees concerning such matters as quality, scheduling, and delivery of product?

   b) Would the sales manager's functional authority, as it affects production, be more effective if it could flow directly to a production order and schedule department, which, in turn, would issue orders to the factory?

   c) What complications would prevent expeditious management if the sales manager's status were exclusively that of staff executive, with no functional authority whatever over production?

8. Summarize the advantages of functional organization as indicated in the text material in this chapter together with others that may have come under your own observation. Explain why the principle of paramount necessity operates to extend functional departmentation. Give examples of this tendency.

9. Explain why the application of the principle of paramount necessity may result in the overfunctionalization of a business organization. Point out and illustrate with examples how this danger may be avoided.

10. Explain in fuller detail what is meant by each of the following statements:
    a) Lines of jurisdiction of different executives are the channels through which authority flows from inception to execution.
    b) In line and staff organization, authority may be delegated but not relinquished; responsibility may be assigned but not avoided.
    c) The exception principle of appealing executive problems upward until they reach the proper level for decision plays an important role in segregating the different types of authority into the various levels of the management pyramid.

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Chapter XI

CENTRALIZATION AND DECENTRALIZATION OF MANAGEMENT

THE CONCEPTS OF CENTRALIZATION AND DECENTRALIZATION

CENTRALIZATION is an expression that occurs frequently in discussions of organization and management. "Centralization" means concentration. It may be thought of as a force, directed inward, drawing those things which come within the orbit of its influence toward a common center.

Strong authority exercised by a forceful leader acts as a centralizing influence in management. It tends to draw the executive personnel closer to its leader, or top executive, and to hold it there in a closely knit and highly unified organization. The use of authority as a centralizing force may be a conscious effort on the part of a dominant leader; or it may be an unconscious influence, growing out of tradition, inheritance, loyalty, or character considerations. But whenever this centralizing force ceases to be effective, whether it be relaxed by accident or design, the opposite situation of decentralization tends to develop.

Decentralization should likewise be thought of as a force, centrifugal in character, causing movement or distribution away from rather than toward the common center. "Decentralization" is the natural correlative term, the opposite of "centralization." When one of the terms is used, the other is implied.

Centralization and decentralization are not principles of organization, but rather form a scale of practical values from the one extreme to the other. Every actual business organization must decide for itself, not only in general but in each individual executive situation, to what extent it will centralize or decentralize its organization.

Three Phases of Centralization and Decentralization

There are three different aspects of this practical problem of centralization and decentralization in organization: First there is the question of how far to go in concentrating authority in the hands of the top executive. Another aspect of the problem is the extent to which activities or functions should be assembled or centralized in a particular department. And, third, there is the question of the geographical location of activities

of a particular business, that is, whether they should be dispersed or centralized.

In government, the question of the degree of centralization or decentralization of organization is a political even more than a practical issue. When kings, princes, and other potentates were the customary heads of states, monarchical governments were classified as "absolute" or "limited" in character. The absolute monarch was one whose word was law and whose personal will was paramount. The limited monarch was one from whom certain powers were withheld or decentralized. Clearly, the modern republic or democracy is a government in which authority is even more widely decentralized.

Fortunately for business, the question of how far to go in centralization of organization is primarily a practical problem as to what is best for the particular business. True, business does not entirely escape political regulation with respect to the degree of concentration and dispersion that prevails. For example, chain stores are subject to this influence, caused in part at least by the political struggle between the proponents of "autocracy" and "democracy." Some of the numerous independent store owners, in other words, campaign for regulation of their chain store competitors by pointing out the "democracy" aspect of continued existence of their independent type of enterprise. However, this political aspect of centralization versus decentralization is of minor importance in business organization and will not be further considered.

The practical problem of development and maintenance of the best possible organization is ever present. Each business enterprise must constantly make decisions with respect to individual executives and employees, decisions which not only determine their individual place within the organization but in turn determine the organization itself.

There is no such thing as a perfect organization, since such an ideal presupposes ability to create perfection out of the imperfections and natural differences between the many executives and employees, who, collectively, constitute the particular organization. The practical aim of the top executive of an enterprise must be, therefore, to have the best possible organization, at any given time, and to be developing and improving his organization constantly.

Organization is not a cold-blooded, mechanical process from which consideration of the human factor may be safely omitted. Good organization, in large part, consists in the adjustment of the tasks of management to the human resources available to perform these tasks. On the material side, the best test of good organization is the measure of results in terms of profitability and competitive success of the enterprise. It is more important for an organization to operate and maintain a profitable business concern than it is for it to conform to any theoretical pattern or criteria.

Theoretical Approaches to the Problem

There are three different theoretical approaches to the problem of business organization. Each is a different aspect, or view, of the same business enterprise. These three are summarized below:

1. The organization of a particular business, from its stockholders and board of directors down to its employees, may be thought of as a hierarchy or system of levels, each management level being developed and maintained by the human limits upon personal ability of any one executive, particularly the spans of control, knowledge, time, energy, attention, and personality. The practical problem of centralization versus decentralization is inherent in this "levels theory." To say that a *new management level*, for example, must be inserted within an expanding business organization because its present executive group had become overburdened and overextended is another way of saying that authority, now *centralized*, must be further delegated or *decentralized*.

2. The organization of this same particular business may also be thought of as a subdivided structure or framework of specialized units or groups, usually called "departments," each department or group within the business having certain functions or activities. This "departmentation theory" of organization can also be stated in terms of the "scale of values" between centralization and decentralization. To say that a *new functional department*, for example, must be organized in a particular business in order to allocate to one responsible executive all the authority for a certain type of activity previously scattered among several departments, and hence *decentralized*, is another way of saying that such work must be "*recentralized*" under the new functional executive or department head.

3. A third theoretical approach to proper organization of this same enterprise is to think of organization as a logical system of allocating authority, responsibility, and accountability within every part of the group. This is done by subdividing and allocating the several kinds of authority, that is, line, staff, functional, and residual or coordinative authority. This "authority allocation theory" is likewise a phase of the practical problem of centralization versus decentralization. To say that executives exercising only *staff authority*, for example, can improve organization by relieving the top executive of part of his burden is the same as saying that *overcentralization* can be corrected by *decentralization* of the staff authority, while yet retaining its original *centralized* location in relation to the top executive.

The "levels theory," the "departmentation theory," and the "authority allocation theory" each look at the problem of organization in a different light or aspect. Clearly, therefore, proper organization of an actual business must be accomplished in terms of all three of these fundamental

theories. The centralization versus decentralization approach serves as a "common denominator," and permits discussion of the problem of organization, viewed as a whole.

The Practical Approach to the Problem

An actual business enterprise may be termed a "going concern," and this implies correctly that organization is much more than a passive composite of management levels, departmental groups, and authority allocations. An effective organization is also a dynamic and living thing. It is the rallying ground for sentiment, loyalty, morale, and tradition, sharing, therefore, with leadership the task of motivating the individual executives and employees. It is the complex fabric of interrelated policies, standing orders, and current instructions that flow downward, and of the equally numerous appeals, requests for interpretations, and reports by which accountability flows upward. Finally, it is made up of groups of executives and employees, each group a specialized, harmonious, and efficient unit of the "organization." In this dynamic sense, too, centralization versus decentralization is the common denominator, in terms of which all these practical situations and problems can be stated and discussed.

The degree to which centralization or decentralization shall prevail in management can be determined by the application of the principle of paramount necessity. This principle, if rightly understood and used, can be the dominating factor in the creation of the organization structure in every business concern. As has been observed previously, when management decisions are made on the basis of highest usefulness, unnecessary and uneconomical undertakings are avoided. So also with respect to the extent of centralization or decentralization. Paramount necessity may determine the degree of either procedure, or it may result in a combination of both of them. When the latter happens, the result may be described as *centralized decentralization.*

Centralized Decentralization Defined

The concept of centralization and decentralization furnishes a means, therefore, of stating the combined effect of all the aspects of organization, theoretical and practical, upon a particular position or type of position. It forms a scale of values, permitting measurement from the one extreme of centralization of organization, through the combination situation of centralized decentralization, to the opposite extreme of decentralization of organization.

In such a scale of values, it follows that at all points except the two extremes there will be varying proportions of both factors, that is, centralized decentralization. Such a combination of both organization factors would result, for example, if a business decided to decentralize its activities

by owning and operating a branch factory in a distant city, but at the same time was determined to centralize the entire management of the branch operation by appointing a branch manager in full charge but independent of the factory manager in the home city. Clearly, this combined situation of centralized decentralization will occur more frequently, in actual practice, than either extreme of centralization or decentralization.

CENTRALIZATION OF AUTHORITY

Centralization of authority refers primarily to the authority relationships that exist between the various management levels of the executive organization. It includes the allocation of types of authority, that is, line, staff, and functional authority, since the assignment of authority is obviously related to the determination of management levels.

Taken by itself, the development of additional management levels is a trend toward decentralization of organization. The only way centralization could be accomplished would be by shrinking or contracting the executive organization by deleting one of the management levels. In practice, however, the addition of managerial levels to a growing organization is accompanied by the evolutionary development of various types of authority which tend toward decentralization. The existence of these opposing forces in a growing organization results in a dilution of concentrated power.

Centralization and Despotism

The traditional industrial despot, labeled variously as "big boss," "captain of industry," "magnate," and, more modernly, "tycoon," has acquired his slang title because of his public reputation of extreme concentration of managerial power. To him is attributed complete control down to the smallest details of organization and management. His subordinates are reputed to be mere puppets and "yes-men," frustrated in individual initiative and motivated mostly by the fear or favor of the master at the top.

At the lower management levels the same type of executive is identified by such slang expressions as "taskmaster," "driver," or "hard-boiled boss." In the eyes of his employees he is a disciplinarian, an overbearing manager, or an executive who is too exacting.

These slang expressions, whether referring to the top executive or to those lower down in the management scale, often have to do with the quality of management rather than with the question of centralization of authority. It is true that a person must exercise a great deal of personal power in order to merit such a nickname, and it may be that he is doing so because excessive authority in the organization has been delegated to

him, or presumptuously arrogated by him. However, an executive as often merits and receives the title of "tyrant" from the manner and quality of his executive actions as from the amount or the degree of centralization of authority vested in him.

Power feeds on power in business management as it does in other human institutions. When authority is so exercised by an executive that it is unrestrained and results in personal domination, tyranny commonly ensues. "Megalomania" is a mental disorder that afflicts those who have become tyrants with grandiose delusions of their own wisdom and strength. Its inevitable outcome is disastrous both to the deluded individuals themselves and to the groups whom they may presume to dominate.

Influence of the Legal Form of Enterprise

The legal form of a business enterprise, whether individual ownership, partnership, or corporation, does not necessarily determine the degree of centralization of authority within the organization. Any legal type of organization may be tightly centralized or loosely decentralized. The condition that will prevail will depend upon the policies that are adopted with respect to the allocation of authority and to the managerial structure that is set up to enforce such policies.

The principal stockholder of a corporation may own much more than a majority of the outstanding shares of stock and thus have much the same relationship to the business as an individual owner of an unincorporated enterprise. It does not follow that there will be great centralization of authority within the organization, though often there is a tendency in that direction, especially in small business concerns. Ownership is a legal question, whereas centralization is a matter of policy and practice. Because of the limitations of the human span of control, wise top executives avoid overcentralization of authority, no matter what form of legal ownership a business concern may have, or whatever its size.

CONCENTRATIONS OF THE ELEMENTS OF AUTHORITY

The various elements into which executive authority may be subdivided were analyzed in Chapter III. These subdivisions may again be considered, this time from the standpoint of the degree of concentration which may be applied to them under different circumstances of managerial organization.

The Authority to Plan

In a very small business, with only one executive and a small number of employees, the simplicity of the organization automatically centralizes the *authority to plan.* It is one of the many activities of the single execu-

tive. At the opposite extreme, in a very large business, it is natural for the top executive to develop a group of "staff executives," who report directly to him. This process effects a recentralization of the authority to plan. The planning activity has been decentralized by being assigned to several executives, but the location of all these executives has been concentrated, or centralized, into a staff group directly under the top executive.

As the size of a business increases, the number of management levels and the number of executives also increase. The result is a decentralization of the authority to plan, since each of the additional executives—in the absence of limitations to the contrary—will assume and exercise the authority to plan with respect to their own portion of the business. For example, if the top executive reduces the strain upon his own span of control by specializing his own activities chiefly in the financial phases of the business, it follows that he must allow other executives subordinate to him to do the planning for production, sales, office operations, and other activities. Similarly, if the top executive takes a keen interest in the details of planning for the largest of a concern's factories, warehouses, stores, or sales departments, it follows that the detailed planning for the smaller units will be undertaken and performed by minor executives. Again, if the top executive is an expert sales manager, he will be inclined to leave to others the detailed planning for other specialties with which he has less familiarity.

If this tendency for authority to plan to become decentralized is not counteracted, the result will be chaos within the organization, since many different minds with different plans will inevitably cause conflicts and confusion. Unity and harmony in the organization will be destroyed.

Perfect line organization centralizes the authority to plan at the top. No one other than the chief executive can plan, since all orders, under such conditions, must be originated by him.

Perfect functional organization completely decentralizes the authority to plan, since each of the several functional executives is absolute master over his own line of authority. In the case of the typical business enterprise, authority to plan tends to become more and more decentralized as the size of that business increases because more functional experts are added to the organization. Even the subordinate executives who are related to those above themselves in an apparent line relationship tend to become specialized experts in their separate departments, and hence they acquire a substantial degree of the power to plan.

When a perfect line organization, such as exists in an army, becomes very large, the mass of complicated problems which is thrust upon the commander in chief exceeds his effective span of control. In order to discharge his responsibilities adequately, he must, therefore, develop a

staff of other officers whose principal activity is to do the planning for him. It is upon the basis of their suggestions and advice that the commanding officer issues his orders.

The main activity of the staff of assistant executives, research experts, and consultants developed by the top executive of a large business is to exercise the authority to plan. However, the business executive's staff is not exactly the same as the staff developed to assist the army general. The army staff exists to relieve the general of a planning task which he must perform, if it is to be performed at all. The business executive's staff exists for the purpose of recentralizing the authority to plan which would otherwise become diluted and weakened, owing to unrestrained decentralization.

The Authority to Decide

Creation of an organization of executives and employees, with its various management levels and differing allocations of line, staff, and functional authority, and with its trained and specialized employees, automatically decentralizes the right or authority to decide. The authority to make the necessary decisions is inherent in the performance of assigned tasks or activities. The foreman must make decisions with respect to machine operation and employee assignment and performance, else he would not be able to get the required work done. The accountant must make decisions concerning the posting of the books of the concern if they are to be posted and kept current. The top executive must make the necessary decisions if he wishes to carry his plans into execution. Even the individual employee must decide how to operate his machine, and must start it, feed material into it, remove completed work and waste products, and then decide when and how to stop his machine.

In accordance with the principle of paramount necessity, every executive and every employee of an organization owes his employment to the fact that his type of services are necessary to the business. This means that each member of an organization has his assigned task to perform, and the authority to make the necessary decisions is inherent in each individual's assignment.

This system of completely decentralized authority to make decisions would break down in utter chaos if each executive and employee decided, for himself alone, just what this grant of authority consisted of. A famous legend of the early days of railroading, a century ago, illustrates the point. When trains first began to operate in the United States about 1840, there was no fixed rule as to whether the conductor or the engineer was in charge of the train. Finally, according to the story, a conductor lost his patience when the engineer disregarded his signaled instructions to stop the train at the next station to let off passengers. When the engi-

neer did stop, the conductor is said to have proceeded to thrash the engineer and thus established the precedence of his right to decide over the similar right of decision possessed by the engineer.

The system of decentralized authority to decide remains efficient and harmonious in an organization by imposing limits on each individual's right of decision, together with the system of appeal of exceptions by an executive in one level to his superior in another.

Limitations on Executive Discretion

Standard management practices provide several ways of limiting executive discretion. The very existence of managerial levels automatically limits the areas within which executive decisions may be properly made. The reason is that an individual's control extends only to those parts of an organization which lie beneath his own level in the management structure. Also, the type of authority allocated to an executive limits his right of decision. In general, a line executive is limited to authority over persons, a staff executive to the authority to plan, and a functional executive to authority over processes.

In all instances, decisions of executives are limited to subjects which are consistent with company policies, procedures, and objectives. Even then discretion may be limited by specific reservations. For example, an executive may instruct a subordinate or an employee not to make decisions of a certain character but to refer such questions to some higher authority for final answer. A common limitation of this kind has to do with the expenditure of funds. Executives in many levels of management are usually authorized to make routine expenditures of small sums of money; but above certain amounts, authorization must be secured from higher authority before commitments are permitted.

Finally, the discretion of both executives and employees is determined, to a large extent, by an individual's title and status or by the nature of the position he occupies. Traditions and customs in an organization set bounds to the matter of free decision. Certain decisions are to be expected, for example, from a locomotive engineer, a manager of a shipping department, or a corporation president—each according to the peculiar occupation or position of the individual concerned.

The Appeal of Exceptions

When a problem develops that is "exceptional," or beyond the scope of the usual right or authority of decision of a particular executive or employee or that has been specifically reserved by instruction of a higher executive, the appeal system comes into use. The problem is appealed upward from employee to executive and from one executive to a higher executive, until it reaches the one within whose scope of authority the decision on this particular problem rests. The "appeal system," in other

words, is simply a channel, or channels, of communication within the organization for carrying problems to the executives who are supposed to decide them.

The system of decentralized authority to decide operates successfully and harmoniously when each executive and employee understands clearly just what are the limits of his own right of decision, and when there is a smoothly operating appeal system for transmitting exceptional problems to the proper executives who can and will decide them.

The Authority to Organize

As a business develops and grows larger, authority to organize tends to become concentrated at certain points within the organization. This is due to the fact that the top executive, in whom all authority for organization is naturally centralized, has neither the time for or the interest in detailed organization problems. He therefore delegates his own detailed authority to organize to certain selected subordinate executives, thus creating the condition of centralized decentralization.

In a small business, the top executive naturally centralizes complete authority for determining his organization. He usually does this by selecting his subordinate executives and employees and by assigning duties to them.

In a very large business, the top executive may restrict his activity in the field of organization to the selection of his major executives and his staff executives. He may delegate every other phase of his authority for organization.

In the business of moderate size, the top executive may be expected to restrict his interest in organization to determination of the departmentation and to selection of major executives, staff executives, and department heads. His interest in selection of executives is just as important as his interest in departmentation. By his action in selecting a strong or weak executive, a well-trained or poorly trained person, a low-salaried or high-paid individual, the top executive emphasizes and tends to determine the relative importance of the particular departmental position within his organization.

After the top executive has determined the departmentation and has selected his major executives, staff executives, and department heads, there still remain the organization problems of subdepartmentation and of employee assignment to duty. The task of determining the subdepartmental organization is usually delegated by the top executive to the particular department head. Assignment of employees to particular duties is usually delegated by the department head, in turn, to the foreman or supervisor who is in direct charge of the particular employees. In this way, the total task of determining the organization is performed at three different management levels.

In order to create a sound organization for management, the authority to organize must be both centralized and decentralized. It would be absurd to require the top executive to burden himself with organization details. Also, it would result in confusion if every executive dealt with the problem of organization in his own way. Therefore, as an enterprise increases in size, the tendencies of excessive decentralization must be counteracted by a staff and functional department which will, in a sense, recentralize top executive authority to organize. This unit of management is the usual personnel department.

The Authorities to Command and Enforce

Decentralization is characteristic of the allocation of the authority to command and its concomitant, the authority to enforce. Leadership in a group, whether it consists of few or many persons, is impotent without the authority to give directions and the power to enforce them. Therefore, at any level in an organization where an individual is responsible for an activity that requires the performance of a group of persons working as a unit, there must be delegated to him sufficient authority for command and enforcement. This principle extends not only to executives but to employees who are required to have assistants. Such authority is an obvious necessity for persons charged with the duty of inspection and the maintenance of standards.

Hence, every leader of a group in an organization, executive or otherwise, must be able to issue orders which he can enforce with respect to the activities that have been assigned to him. These two elements of total authority do not necessarily have to be equated in the individual executive. In other words, it is not necessary for an executive to have the same degree of power in each case. The equating of authority is accomplished through the management structure as a whole. For example, if a factory organization must reduce the number of hours in a working day, the top executive will make the decision; the factory manager will frame and promulgate the necessary orders; and the individual subdepartmental superintendents and foremen will institute enforcement—thus each of them joins in determining how best to secure the desired reduction in time.

The Authority to Coordinate

Coordination is the residual of total authority that remains after line, staff, and functional authority have been delegated to various executives. It follows that authority to coordinate is an activity of the top executive, and will continue to be his responsibility even after he has delegated all of his line, staff, and functional authority to the subordinate executives of his organization.

Every executive has the problem of coordinating that portion of the business within his own direct purview. However, he can only volunteer his willingness to coordinate his activities with those of other executives. The top executive alone is able to enforce coordination between departments and executives. This element of authority is automatically centralized at the level of the top executive.

TRENDS IN MANAGERIAL CONCENTRATION

As a business develops in size and complexity, there tends to emerge a distinctive major executive level below the top executive or leader of the enterprise. This level often consists of a group composed of three or more major executives, such as those in charge of sales, production, and finance, respectively.

Combined Major Executive Group

The force which drives a typical business enterprise to develop this managerial pattern is the necessity for recentralization. The management pyramid must have but one leader or top executive. However, as a particular business develops in size, the span of control of the head of the business tends to become increasingly strained. He finds physical and mental limitations on his ability to comprehend and manage all aspects of his far-flung enterprise. Hence, he must reduce his span of control either by delegating more authority to his subordinates or by appointing a limited number of major executives to serve as a combined managerial unit with broad powers.

There is also a decentralizing force that retards or inhibits the development of this level of major executive assistants. Examination of the actual organization of many business enterprises, large and small, leads to the conclusion that the trend toward concentration of management in the hands of about three major executives, who often are the vice-presidents of the company, is always present and can be readily identified. However, this trend is rarely, if ever, completely carried out in practice. As a business grows, the need for functional decentralization of business management is so great as to make the assumption of a perfect major executive level of organization unrealistic and improbable.

Restraints upon Concentration

Under modern conditions of business management, an adequate legal department is a necessity. Such a department will be required to handle legal problems which come from every section of the enterprise. Many of these questions are of such a nature as to claim the personal attention of the chief executive. Therefore the counsel usually is immediately subordinate to the top executive, and a unit of management is added to the

broadening managerial level next below the top over which the president or general manager must spread his span of control. Such a procedure is, of course, an aspect of decentralization. If the alternative method were adopted, namely, placing the legal department under one of the major executives, there would arise at least three complications more serious in character than the obvious strain upon the span of control of the top executive.

In the first place, if the legal department is placed under one of the major executives, the task of coordination will be increased in complexity, since both the head of the legal department and the selected major executive will become involved whenever legal problems arise in another part of the business. Secondly, because the top executive must personally decide and dispose of many questions arising in the legal department, it is an unnecessary complication to interpose another level of management by requiring the corporation's counsel to report to the president through one of the vice-presidents. Finally, the work of the legal department is so highly specialized that the detailed contribution which could be made to it by a major executive, who is not a lawyer, is so slight as to be unimportant or even harmful because it is time-consuming. These considerations are so obvious and so important in the case of a typical legal department as to assure its independent organization and establishment, in most instances, directly under the top executive.

Accounting, advertising, traffic, purchasing, public relations, research, personnel, and methods engineering are other functional fields frequently organized as separate departments directly under the president. In fact, businesses generally confer independent status on all of their so-called "service departments." The heads of these departments are not major executives. However, they are relatively independent of the major executives and rank as their equals within their limited fields of specialization. These specialized functional experts, serving the entire business in accordance with its problems and its needs, have come into being because of the need for recentralization of the activities that otherwise are dispersed within the entire organization.

If often happens that the top executive of a large business enterprise, even after delegating the broad fields of production, sales, and finance to appropriate major executives, or vice-presidents, will still have to exercise more or less authority over fifteen or more executives, all independent and accountable directly to him. This is an apparent violation of the principle of the span of control. It is one of the most potent sources of the overload which the top executive of a business must frequently bear.

Dynamic and Voluntary Coordination

Under well-developed organization and management, this large number of executives, spreading out horizontally just beneath the top execu-

tive at the major executive level, need not be a violation of the span of control or an overload on the leader of the business. Of greatest importance is recognition, by all concerned, of the necessity for dynamic and voluntary coordination. If each of the many higher executives will coordinate his own responsibility and the work of his assistants with the needs of the enterprise and the temperament and needs of his fellow executives, the potential overload of uncoordinated issues and problems will not fall on the head of the business for handling and settlement. If the expert heads of specialized functional service departments serve the major executives who are responsible for successful production and sales results, without straying into the alleys of interference and annoyance, the problems of coordination demanding the time and attention of the head of the business will so diminish in number and frequency as to come well within his optimum span of control.

If the foregoing experience of modern large-scale business is reduced to a diagrammatic representation, the result will not be an exact conventional pyramid. Instead, as shown in Figure 42, it will be more nearly a pinnacle rising from a plateau, the prominence representing the chief executive or top management who is supported by a wide base made up of functional experts. Below this mesa-like level there is, of course, the remainder of the management structure.

Figure 42 shows two of the six vice-presidents as major executives, while the other four rank with the twelve functional department heads who also report directly to the president. This is a correct portrayal of an actual organization, but it must not be thought that there is any differentiation in status between the two unspecialized or senior vice-presidents and the four vice-presidents who have been assigned functional authority. All six are of equal rank within the business, although the two senior vice-presidents do form the major executive level beneath the president, since these two are unspecialized and are therefore participants in management of the entire business enterprise.

This illustration also shows that the president of the company has twenty-three other executives reporting directly to him. Such a scheme would seriously overburden the span of control of the president were it not for the presence in the organization of the two senior or executive vice-presidents. At any time he desires, the president can retreat behind his major executives, leaving them in direct contact with his other vice-presidents and his functional departmental executives. They relieve him as he sees fit and thus keep his personal span of control always within reasonable bounds.

As a business grows, the different executive activities required in its management will increase in number, variety, and complexity, thereby rendering centralization of authority, viewed as a whole, more difficult. Decentralization will be the easy road to follow and will develop to the

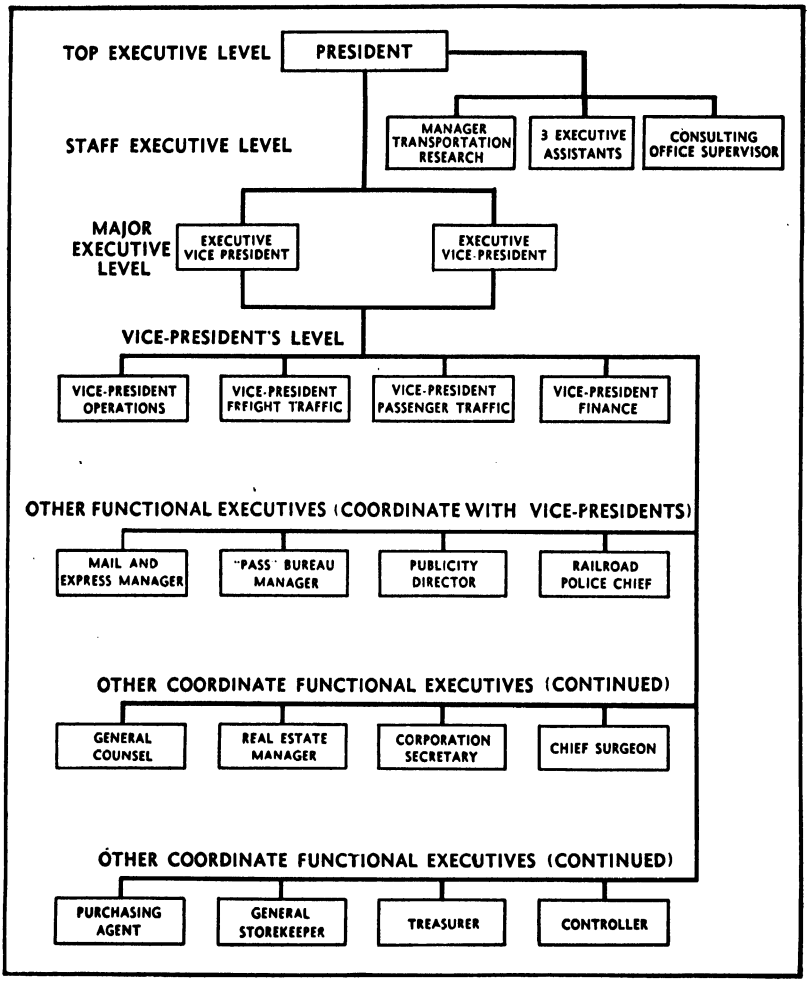


FIG. 42.—Voluntary dynamic coordination of executive management in a large railroad company.

point of necessitating at least partial recentralization. Such recentralization will be accomplished by retaining the authority to plan and the authority to organize at the top executive level. In this way the authority to coordinate, which is inherent in the function of the top executive, will be further strengthened. In so complex a task as the successful management of a business enterprise, planning and organizing are obviously indispensable tools for the establishment of harmony and balance. Only the authorities to decide, to command, and to enforce will remain fully decentralized throughout the organization.

Under such conditions the need for a major executive level and a staff

level of management, both immediately beneath the top executive, is evident. Both levels represent a necessary increase in the number of minds required to encompass the full span of control of the top executive and thus to permit him to bring about the desired degree of recentralization.

Effective Decentralization Illustrated

How effective decentralization can be realized in a large enterprise without removing the basic elements of policy-forming and coordination from the top level of management is illustrated in the organization of the General Motors Corporation. The salient features of this organization are described in the following excerpts from a definitive study of this corporation by Peter F. Drucker entitled *Concept of the Corporation*:

> These manufacturing properties are organized in about thirty divisions. . . . . The three largest are Chevrolet, Fisher Body and Buick, represented in top management by their own divisional managers. The other divisions are organized in groups according to their products, each under an executive who, as a vice president of General Motors, acts as representative of his group in the central management, and as adviser and representative of central management for the divisional managers of his group. . . . . Side by side with this organization according to products there is, as a part of central management, a set of functional staffs which deal with manufacturing, engineering, sales, research, personnel, finance, public relations, law, etc., each under its own vice president.
>
> The manufacturing divisions are headed by the president and his two executive vice presidents; the staff work is headed by the chairman of the board of directors who is also the chief executive officer of General Motors, and by the vice chairman of the board. These five officials form a team. They work through and with two closely coordinated committees, one on policy and one on administration. . . . . These two committees are the central organ of coordination, decision and control, and may well be called the government of General Motors. They pass on all major decisions in the fields of policy and administration. They hear periodic reports on conditions, problems and achievements in all branches of the business. And they are the court of last appeal should there be serious disagreements on policy within the organization.
>
> General Motors could not function as a centralized organization in which all decisions are made at the top, and in which the divisional managers are but little more than plant superintendents. . . . . Hence, General Motors attempts to combine the greatest corporate unity with the greatest divisional autonomy and responsibility; and like every true federation, it aims at realizing unity through local self-government and *vice versa*. This is the aim of General Motors' policy of decentralization.
>
> Decentralization . . . . is not considered to be confined to top management, but it is a principle for the organization of all managerial relationships. It was developed, however, out of the problems of coordinating central and divisional management into one whole.
>
> Central management has twofold functions under a system of decentraliza-

tion. It is at the same time the servant of the divisional managers, helping them to be more efficient and more successful in their autonomy, and the boss of the corporation. And in this role it has to weld several hundred aggressive, highly individual and very independent divisional executives into one team. These two jobs are apparently contradictory but actually interdependent. Their accomplishment is attempted in various ways. . . . :

a) The manufacturing programs of the various divisions have to be approved by central management. . . . . Central management sets the price range. . . . . Central management not only delimits the divisions against each other, but it fits them into a general pattern as part of the unified corporation. It establishes the general over-all aim. . . . . It establishes a total production goal. . . . . It determines how much capital to allot to each division. . . . . Above all, central management thinks ahead for the whole corporation. It is thus differentiated from divisional management not only in power and function but in time.

b) Central management determines the limits within which a divisional manager operates. . . . . It determines both the areas of decision for the divisional manager, and the general rules to which his decisions have to adhere. . . . . Policy decisions of a divisional manager must rest on an explicit or implicit delegation of policy-making power, and must conform to implicit or explicit commands. . . . . And behind this, as an ultimate recourse, there is the absolute power of central management to remove a divisional manager and to appoint a new man in his stead.

c) More in evidence in everyday business conduct is the control through contact which central management exercises over divisional managers. . . . . The vice president in charge of a group of divisions, for instance, has a very real power, but it is rarely, if ever, exercised in the form of orders. Rather, it makes itself felt through suggestions. . . . . However, there is a formal safeguard of central management control, a formal veto on all capital investments beyond a certain limit, and on the hiring of executive personnel beyond a certain salary. This veto power is rarely exercised. . . . . But it has the important result that practically every major policy decision of the divisions has to be discussed extensively with central management.

d) Equally important is central management's role in helping the divisional manager to be as effective as possible. To this end the divisional manager is relieved of all worry over financial matters. . . . . It is the job of central management to obtain the capital for him for any program that has been decided upon as desirable. The same holds for legal matters. Also, General Motors has a uniform accounting system supervised and managed centrally. Finally, most union contracts . . . . . are handled centrally.

e) Finally, the divisional managers are served through the service staffs of central management. Their first function is to advise the divisional manager whenever he feels in need of such advice. . . . . Another important function of the staff agencies is to act as liaison between the various divisions, and particularly as centers of information on new or improved methods. . . . . It should be emphasized that the staff agencies have no direct authority whatsoever over a divisional manager and his policies. . . . . Yet the relationship be-

tween service staffs and divisional managers is on the whole quite frictionless. . . . . To the service staffs—though not exclusively to them—central management owes its knowledge of the details of production, engineering, distribution, and personnel management throughout the business. . . . . Finally, it is the job of the service staff to formulate future policies in closest collaboration with both divisional managers and central management. The staff agencies themselves cannot lay down policies; they can only recommend.

. . . . Within the limits of policy and decision set for him by central management, the divisional manager operates on his own as the boss of the outfit. He is in complete charge of production and sales. He hires, fires, and promotes. . . . . He decides the factory layout, the technical methods and equipment used. . . . He is in charge of advertising and public relations for his division. . . . . He buys his supplies independently from suppliers of his own choice. . . . . In everything pertaining to operations he is as much the real head as if his division were indeed an independent business. According to the estimate of several divisional managers—corroborated by members of the central management—ninety-five per cent of all decisions fall within his jurisdiction.

Division of powers and of functions, unity in action—this definition of a federal union would be a fairly accurate description of the aim of General Motors' policy of decentralization. Such a union cannot rest on blind obedience to orders. It must be based on an understanding of each other's problems, policies, approaches, mutually between central management and divisional managers.

The impression that emerges from an analysis of the aims of General Motors' policy of organization is one of great individual liberty in which every man—at least among the three to five hundred first- and second-line executives —is to be allowed as much responsibility as he is willing to assume. There is little emphasis on title, rank, or formal procedure.

Our conclusion would thus be that in decentralization General Motors possesses a concept adequate to the solution of its own chief institutional problems. . . . . However, it is highly questionable whether decentralization would be used successfully even for relations such as those between the divisional managers and central management in General Motors, were the present trend towards governmental centralization to continue. . . . . Decentralization could not operate were consumption, credit, raw materials and labor organized on a centralized basis, whether the controls be governmental, a cartel, or "one big union." [1]

CENTRALIZATION OF FUNCTIONS

There is a close connection between the degree of centralization of authority prevailing in an organization and the extent to which its various functions are centralized into departments. By "functional centralization" is meant the concentration of activities of a particular type within one

[1] Peter F. Drucker, *Concept of the Corporation* (New York: John Day Co., 1946), pp. 42–97.

specialized department instead of dispersing them throughout the organization. The function of accident prevention, for example, is often left decentralized, or scattered, through all the other departments of the business. If desired, it may be partially centralized, for example, by appointing a safety supervisor to teach the foremen and supervisors the principles of "safe operation." It may be completely centralized, by giving the safety supervisor and his assistants full responsibility and by granting them full authority to decide, command, and enforce all safety rules and measures.

Centralization and decentralization of functions should not be confused with the criteria of association. The criteria of association are the bases for the distribution of the functions to the various departments of the business. They may be thought of as the tests of proper departmentation. Centralization and decentralization are not criteria of good departmentation, but measures of the degree of concentration or dispersion achieved in practice. The degree of centralization is the practical measure of the results of the application of the criteria of departmentation.

Influence of Size upon Concentration

In a very small business, the many varied executive tasks will be assigned to a limited number of persons who constitute the small executive organization. As a result, many more or less unrelated functions will be assigned to a particular executive. When a business has outgrown small-scale operations and has become medium-sized, its organization will have evolved through a process of specialization into a structure composed of many departments and subdepartments.

The principal functions of the business will have been determined with definiteness and clarity and set apart under the jurisdiction of departmental heads charged with the authority and responsibility of efficient operation. Whenever the details of the responsibility involved exceed the span of control of a department executive, his department should be subdivided into smaller groups of functions. Some of these are facilitative in character and therefore organically a part of the task to be performed by this particular division of the business. Others may be purely advisory.

If facilitative, the subdepartments may differ in method, in process, and even in personnel requirements. For example, in a highly organized industrial establishment, it may be necessary for the production department, whose main task is manufacturing, to be serviced by many other activities which are quite unlike the manufacturing processes themselves. Subdepartments of this kind, within the production department, may include a wide range of services, such as designing, personnel, traffic, clerical, accounting, and research.

Each of these subdepartments is a management unit. It possesses in-

dividuality, it has authority, its procedures are characteristic of the specialized field it represents, but its purpose is not an end in itself. Its one reason for being is that it helps to facilitate a major service upon which the entire business depends—in this instance, the manufacture of goods.

What has been said of the evolution of the production department can be matched with descriptions of the other principal departmental divisions of the typical business. Each in its own way and for its own requirements is facilitated by subdepartmentation in a similar manner. As a result, it is not unusual to find units of one particular kind of work attached to different departments and dispersed throughout an organization. A very common example of such decentralization is the clerical staff composed of stenographers, typists, bookkeepers, file clerks, messengers, and other employees of this type. But dispersion often goes further. It may result in the decentralization of research, accounting, personnel, purchasing, and other similar activities of a highly specialized nature which the management has not unified within the particular organization.

The Practical Limits to Dispersion

Complete differentiation of the principal functions, with all of the facilitating services which such an organization policy may require, tends toward increased decentralization as a business grows larger. This tendency, if unchecked, encounters the law of diminishing returns in the sense that the benefits to be derived from the facilitating services are in inverse ratio to the expense involved and to the losses in control and efficiency. It is conceivable, for example, that every executive would like to have his own secretary and his own stenographic staff; that several major department heads would like to have separate personnel departments to manage their particular work force; and that separate sets of accounts would be looked upon with favor in each of several divisions of the business. The possibilities for duplication of facilitating functional groups of this kind are almost endless in a large concern, and they are not without their advocates in smaller ones as well.

Recentralizing Facilitating Functions

When a business organization becomes highly specialized in the manner indicated, thereby broadening the base of its structure as well as increasing the number of its levels, a final stage in its evolution appears, namely, a tendency toward recentralization. This recentralization, however, is not with the original organic functions. It is rather by concentration of the scattered facilitating activities into new departmental units which have not existed before.

As this stage is approached, numerous units or groups of activities,

born of expediency, are attached to dissimilar departments. At some period in the development of the organization, they become so numerous and ubiquitous that a question of policy arises as to whether such decentralization of work should be continued. It is a question of recentralization of these scattered functions—whether activities of a particular type should be concentrated in a new, specialized department instead of being dispersed widely among various major divisions of the enterprise. The facilitating purpose of the function would not be disturbed; but, in the interest of economy, regularity, and efficiency, unified recentralized control would be substituted for the convenience of decentralized attachment.

CENTRALIZATION AND DECENTRALIZATION OF FUNCTIONS ILLUSTRATED

When the term "recentralization" is used, it implies that there has been, first, a dispersion of facilitating activities followed by a concentration of them as the concern has grown in size. It is true that this is a correct description of an evolutionary process. But such a transition does not necessarily have to take place in an organization. It is quite reasonable that a policy of organization should require centralization of these functions from the beginning, or, conversely, a decentralization of them as considerations of efficiency and economy might dictate. Numerous examples could be given to illustrate this problem of management. A few typical ones are offered.

Handling of Cash in Stores

In the routine operations of large retail department stores the handling of cash from floor sales may be undertaken in one of two ways. One method is for each merchandise division to have its own cash register in which every salesperson will place all money received during the course of customer transactions. At certain intervals during the day these cash receipts will be collected for the sake of safety, but each division head is responsible for the reconciliation of the cash on hand with the sales tickets which represent the cash transactions for each period of time between collections. Thus the function of the cashier is dispersed throughout the store.

The other method is to centralize the cashier's function in one office. Cash received from sales is sent to this office by mechanical carriers of various kinds or by pneumatic tubes. In whatever way this detail is handled, the important difference between the two methods of handling cash is that in the latter case a single department assumes the complete responsibility for the reconciliation of cash transactions, whereas by the former method this responsibility is decentralized. The first method doubtless

tends to speed up customer service. At the same time, the chances of theft or error are greater.

The Clerical Office Force

Another example has to do with the clerical and stenographic office force. It is common practice to decentralize the work of correspondence and filing. However, in some large concerns, a central stenographic, typing, and filing department is provided upon whose personnel executives may call when service of this type is required. Such a central office is managed by one person, who sees to it that the number of employees in the office balances as nearly as possible with the work required. Idleness and useless activities are thereby reduced to a minimum. Where dictating machines are used, it is common practice to establish a central transcribing department.

Purchasing

The function of purchasing also frequently presents this problem. Normally, the procurement function in a business is a broad one. If the business is an industrial establishment, it involves the purchase of raw materials for use in manufacture as well as supplies and equipment of all kinds. It is but a natural inclination to split this activity into several parts according to the special needs of the various divisions of the business. Yet purchasing is a highly technical matter. It must take into account such varied factors as price, sources of supply, quality, price trends—and therefore inventory—transportation, and many others. Some of these factors, in principle, are common to all institutional buying. The items may be different, but their timeliness and the method of securing them may be substantially the same in character but vary in details. Therefore, management has often found it desirable to centralize the facilitating function of purchasing, particularly for reasons of economy and coordination. It should not be assumed that this recentralization of purchasing destroys its facilitative character. But a centralized purchasing department usually allows purchases of small items such as tools and emergency repairs to be made at points in the organization where the need for them arises.

Personnel Management

Personnel management also frequently comes in for consideration and treatment with respect to centralization and decentralization. The hiring and firing of employees is often a delicate problem in which many personal considerations may be involved. If there are to be more or less intimate contacts between a superior and subordinates, it is likely that the former would like to have a voice in the selection of his associates. If the

recruitment, assignment, and training of employees were left exclusively to a centralized personnel department, the effect of personal preference on the part of a given executive might be next to nothing. Therefore, while personnel management is generally a centralized function, its authority is established within more or less narrow limits. Here, then, is an activity or function in which centralization in a personnel department is, by deliberate policy, only partly accomplished.

Educational Organization

By way of contrast and yet by way of illustrating and emphasizing the subject under consideration, this problem may be observed in an entirely different field, namely, higher education. A large university, for example, is generally divided into many schools and colleges according to special fields of learning. Many such divisions accept students for entrance in their freshman year. Further, it is generally required that all beginning students pursue traditional fundamental courses in English, mathematics, the sciences, economics, and other subjects, including physical education. A question of policy often arises in these circumstances. It is the problem of providing special instruction in these basic fields by colleges rather than on a basis of unified departments for the institution as a whole. Owing to administrative jealousies, false pride, or the lack of cooperation or confidence, it is not unusual to find separate departments in identical subjects for students in liberal arts, engineering, business, pharmacy, music, teacher-training, and other major divisions of the university. Here, again, from an administrative point of view—in the interest of economy at least—the problem is one of the relative merits of concentration and dispersion.

Alternative Effective Plans

The solution of the problem as to whether there should be a dispersion or a concentration of functions in an enterprise is not one-sided. In theory, it might seem that a centralization of all facilitating functions unquestionably has the better of the argument. But the deciding factor is the practical test of effective performance. This effectiveness must comprehend values to the enterprise as a whole and to the particular phase of the organization which a given function serves. Often the decision in the matter hinges on the personnel factor. Sometimes it is a question of organization flexibility because centralization tends in the opposite direction toward inflexibility. Then again, it may be a problem of divided responsibility. It is obviously less difficult to exercise effective authority over unifunctional departments than those in which activities are mixed. Where unrelated activities are combined in a department, executive supervision must, consequently, be divided.

Proper departmentation is one of the most important aspects of "the art of management." It requires high executive ability to strike the best possible balance between basic functional departmentation and their facilitating agencies. There are three alternatives. The basic departments may be completely unifunctional, thereby having incorporated within their structures all necessary facilitating services. This plan may be described as decentralization of functions. An exactly opposite plan is to concentrate facilitating services in specialized departments available to the operating divisions of a concern according to need, but separated from them in matters of organization and jurisdiction. This method can be said to be a centralization of functions. In between lies a middle ground: facilitating functions may be centralized in some particulars and decentralized with respect to others. Just what system shall prevail in an organization will depend not so much on a ready-made pattern as upon considerations of efficiency, economy, and coordinated effort in each individual instance.

CENTRALIZATION OF PERFORMANCE

Thus far, "centralization" and "decentralization" of authority have been used as definitive terms to describe degrees of concentration in executive power, and "centralization" and "decentralization" of functions have served to express the degree of concentration and dispersion of particular managerial activities. There remains to be considered a third phase of this practical index of business organization, namely, "centralization" and "decentralization" of performance.

When the operations of a business are concentrated at a single place, there is said to be "centralized performance." Since this is a spatial concept, the reference to place may deal with both intra- and extraplant locations. That is, this problem of organization includes within its scope questions and decisions with regard to the positions and places of processes —whether they shall be in one building, in one section of a building, in one plant composed of more than one building, or in one center or locality. It is not difficult to understand the various forms in which this problem may appear. Several typical examples will serve to illustrate it and its opposite alternative, namely, decentralization of performance.

Retail Department Store Operations

The typical retail department store is a good example of the centralization of performance. It is, in reality, simply a collection of specialty shops under one roof. This principle of variety in offerings has merely been expanded until the modern department store not only carries stocks of goods of almost every conceivable character but also provides its customers with services of various kinds equally diverse and extensive. In fact,

it is the boast of many such stores that, with a few exceptions, all of the material wants of household and family, from necessities to rare luxuries, are available to purchasers within their walls.

Chain Grocery Store Operations

The extreme opposite of the department store, of course, is the typical chain grocery store. Not only is its merchandise limited to articles of food and household supplies essential to kitchen and laundry, but, by its very nature, its customer convenience depends upon its dispersion in location. Instead of being situated in one place, it is scattered widely. The development of so-called "supermarkets" in recent years is in reality a recentralization of performance with respect to the merchandising of groceries and allied commodities. But in its broadest aspects, the department store represents centralization of performance, and the chain grocery store decentralization of performance in the sale of merchandise at retail.

Gasoline Filling Stations

Among the best examples of decentralization of location are the ubiquitous gasoline filling stations, of which there are nearly as many as there are miles of paved highways in this country. And yet, even there a tendency toward a kind of centralization of performance has appeared in recent years in the one-stop service station where all the needs of the motorist may be supplied.

Processes of Manufacturing

Centralization of performance is a common characteristic of many types of manufacturing plants. In continuous manufacturing, for example, continuity in processing requires a steady flow, for product sequence, from the intake of raw materials through the various stages of production to the final output of the finished product. Centralized performance facilitates this flow; hence each stage in production is unified, and all the operations are performed in one place. In many factories a sequence of processes determines the entire factory layout, even at the expense of complete "product sequence." For example, if the product is a machine or similar article in which iron, steel, and other metals are basic elements, usually there is but one foundry, one central shop for turning and milling machines, another shop for draw presses, one assembly line, and one finishing and inspection department.

In very large-scale, continuous manufacturing concerns, such as in the automobile industry, decentralization of performance is also an established policy. That is, in a corporation which owns and operates many plants, there may be, in addition to a centralized assembly plant, one plant given over exclusively to the manufacture of bodies, another to the build-

ing of frames for chassis, and others to the making of wheels, motors, radiators, and other parts. Yet, in the River Rouge plant of the Ford Motor Company, except for minor and special parts purchased in their finished state, the manufacture of motor cars proceeds from the reduction of iron ore to the completed automobile serviced with fuel and oil ready for the customer's use at the end of the assembly line. This is an illustration of centralized performance on a large scale within a single plant.

Optimum Limits of Centralization

The managerial problem as to whether centralization or decentralization of the tangible operations of a particular business best serves all interests concerned, is evident.

Centralization of location of the operations of a company doubtless makes possible a greater specialization of labor; it reduces duplication in effort and equipment; it tends to constrict the area of control over which supervision must be exercised; it diminishes the cost of communication and, in many instances, of transportation; it saves time otherwise required to move from one unit to another; and it often eliminates confusion in conflicting orders which are issued at long range to many persons of similar status. All of these advantages are important, but they are sometimes gained only by the sacrifice of other values which cannot be realized except through decentralization. Among these are the ability to serve a clientele quickly and in conformity with varying needs of different sections, to alleviate congestion, and to lessen the risks which are increased by congestion. Some enterprises have taken the view that decentralization contributes to better standards of living for employees—certainly an important consideration in the development of sound personnel policy.

There is no single formula which can be applied to the solution of this problem, but the fact remains that many conditions which made a high degree of concentration economical and necessary no longer prevail. In the further development of individual companies, and of the country as a whole, consideration must be given to the relative merits and the ultimate effects of both centralization and decentralization of the location of performance.

Centralization and decentralization are counterforces that shape and reshape the organization of an enterprise. The need for appropriate concentration, dispersion, and recentralization is the necessity of adjustment of the actual organization to its own unique problems of size, executive personnel, life history, and trends. Centralization and decentralization are, in part, indexes or measures of the degree of concentration of authority, functions, and performance in an enterprise. But they are more than that, since the skill with which the balance between the two extremes of too much concentration and too much dispersion is accomplished has a dy-

namic effect upon the personnel of the entire organization. Good organization, in other words, makes possible good morale and efficient output.

TESTS OF PROPER ORGANIZATION

Awareness of the importance of the proper degree and kind of centralization and decentralization of the activities of management does not necessarily mean that an executive will prove himself a master of the art of management. His problem is one of balancing opposite trends and influences so that the best possible organization may be achieved at any given moment. Visual aids, such as organization charts and diagrams, can be of material assistance in comprehending trends, relationships, and form in the management structure. An understanding and application of the principle of paramount necessity will also help an executive to solve organization problems, particularly when adjustments seem to require additional managerial personnel. In an instance of this kind, if the business can be carried on satisfactorily without a new executive level or a new functional executive, a change in the degree of centralization is neither necessary nor desirable.

Another important test of proper organization is whether or not the allocation of authority together with commensurate responsibility and accountability is clear-cut and understood by all concerned. The sense of confusion, frustration, and injustice, and the wastefulness resulting from lack of clear understanding by an executive of his powers, duties, and opportunities are obstacles to good business management. They are serious handicaps to the development of high executive morale, and they overburden the top executive with unnecessary coordination problems. This lack of clear definition and statement of executive authority, responsibility, and accountability is easily recognized as an error of organization, although its correction may take long planning and patient work by the head of the business. It is one of the most important tests of proper organization.

The most important test of all in evaluating the actual merit or lack of merit of a particular organization is to determine whether the organization serves in its proper place as an efficient managerial tool or technique or whether it overshadows the management. This is an easily identified virtue or fault because it can be measured in terms of leadership. If the top executive of any enterprise stands out as the leader of his concern as well as its coordinator, and if its individual department heads are known as forceful and progressive executives, then organization bears its proper relationship to management. If, on the other hand, the top executive is obliged to spend an excessive amount of time in attempting to coordinate and harmonize executive activity, and if his department heads avoid exertion because they do not feel they have the right to push forward to new

gains, then the organization is defective and is strangling management instead of facilitating its tasks.

QUESTIONS

1. Write out definitions of the verbs "centralize," "decentralize," and "recentralize." On the basis of your understanding of these terms, perform the following exercises:
   a) Draw a diagram of a square with a line diagonally bisecting it into two equal triangles. Label one triangle with the word "centralize" and the other triangle with the word "decentralize." Explain how this diagram can be used to illustrate the reference in the text to "a scale of values ranging from complete centralization to complete decentralization."
   b) Choose an intermediate point on the diagonal line and draw another line through it parallel to the base of the square. If either of the rectangles thus formed represents organization in whole or in part, point out how each of them is necessarily composed of varying proportions of centralized and decentralized management.
   c) Show by means of the diagram you have made that decentralization simply means less centralization in management. Now define "centralized decentralization," remembering that this coined expression is simply a convenient way to point out any combination of the two concepts.
   d) Show by your diagram that recentralization in management simply means a greater degree of centralization than does decentralization.

2. There is evidence that modern complex business organization and management have evolved from the simplest form of small business enterprise. In this simple form, there is complete centralization of authority because there are no management levels between the sole owner-manager and his employees; there are no departments or subdepartments, and there is no delegation of authority. On the assumption that this development from the simple to the complex can be substantiated, fully discuss the following:
   a) Show that, as the size of a particular business enterprise grows, the first trend is toward decentralization. Indicate this tendency, separately, in terms of the "levels theory," the "departmentation theory," and the "theory of the allocation of authority."
   b) Show that, as the size of a particular business enterprise continues to increase, there necessarily develops a trend toward recentralization. Indicate this tendency, separately, in terms of the "levels theory," the "departmentation theory," and the "theory of the allocation of authority."
   c) Show that, at any given point in the evolution of a business enterprise after it has begun to grow in size, there develops a combination of centralization and decentralization which has been described in the text of this chapter as "centralized decentralization."

3. Explain in greater detail the following quotations taken from the text of this chapter:
   a) Wise policy avoids overcentralization of authority no matter what form of legal ownership a business concern may have.
   b) Decentralization will be the easy road to follow and will develop to the point of necessitating at least partial recentralization. (Note that this statement is, in fact, not a contradiction of item *d* below.)
   c) General Motors could not function as a centralized organization in which all decisions are made at the top.
   d) To combine the greatest corporate unity with the greatest divisional autonomy and responsibility is the aim of the policy of decentralization of the General Motors Corporation.

4. Present convincing arguments favoring the desirability of the recentralization of the authority to plan, with particular reference to the following:
   a) It would not be necessary to consider this problem if a business enterprise were organized on the basis of perfect line organization; but this is impossible.
   b) In the organization illustrated in Figure 42 this problem might have been solved by permitting each of the twenty-three executives shown in the diagram to make his own plans. However, it would appear from the diagram itself that in this particular company the authority to plan has been at least partially recentralized.
   c) In the example of the General Motors Corporation there are two specific statements that indicate that most of the authority to plan has been recentralized.

5. Present convincing arguments favoring the desirability to permit and even to encourage maximum delegation, and hence decentralization, of the authority to decide, with particular reference to the following:
   a) The "principle of paramount necessity" exacts such decentralization, and the imposition of limits upon executive discretion, together with the "appeal of exceptions" upward, make such decentralization practicable.
   b) Explain how the problem of decentralization of the authority to decide has been solved in the organization illustrated in Figure 42, especially the manner in which limitations have been imposed on executive discretion.
   c) In the example of the General Motors Corporation, show how the decentralization of the authority to decide has been handled, pointing out particularly its system of appeal of exceptions.

6. Discuss the "authority to organize" from the following standpoints:
   a) Explain why the authority to organize in its major aspects must remain centralized in the top executive levels, while with respect to details it becomes decentralized at certain points within the organization.
   b) By means of examples, distinguish between staff and functional activities

of a typical personnel department with respect to its authority to organize.

c) Explain how Figure 42 illustrates the decentralization of the authority to organize in a business enterprise that has no central personnel department.

d) Show how centralization and decentralization of the authority to organize are achieved in the management of the General Motors Corporation.

7. It is generally conceived that the "authority to command" and the "authority to enforce" should be fully decentralized throughout an executive organization. Discuss this concept as follows:

a) Assume that a factory superintendent has exercised the full authority that has been delegated to him to command that certain production work be undertaken by designated employees, and, further, that his authority to enforce these commands is curtailed by the safety inspector who orders the work suspended for reasons of safety. Explain how this apparent conflict in authority is resolved by being "equated through the management structure as a whole."

b) Point out what the example of the General Motors Corporation shows with respect to the allocation and exercise of the "authority to command" and the "authority to enforce" in the management of that company.

8. Discuss the "authority to coordinate" from the following standpoints:

a) Show that there is a valid difference between the willingness to coordinate on the part of executives and the authority to enforce coordination between executives and departments.

b) Analyze the major executive level in management, indicating especially its place and importance with respect to centralization of the authority to coordinate.

c) Select one of the functional executives specified in Figure 42 and point out why his existence in this organization enhances coordination by the recentralization of activities that would otherwise be scattered throughout the enterprise.

d) Summarize the coordination organization and procedures that are described in the General Motors Corporation example.

9. Distinguish clearly between "centralization," "decentralization," and "recentralization" of functions in relation to the criteria of functional departmentation with particular reference to the following:

a) The influence of size of an enterprise upon the grouping of functions into departments taking into account the limiting factor of the "clean-break" criterion.

b) The desirability of recentralizing facilitating functions taking into account the criterion of coordination.

c) The three alternative methods of organizing facilitating functions as explained on page 301 in relation to basic functional departmentation.

10. Outline the tests of good organization in so far as the proper degree of centralization, decentralization, and recentralization of performance is concerned. Draw upon the illustration of the General Motors Corporation for examples and proof of tests.

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Chapter XII

THE FORMULATION OF POLICY

EVERY decision made by the board of directors and by the higher executives, together with each original decision of department heads and supervisors, is either itself a policy or is derived directly from some established policy. A "policy" may be defined as a "guide to action." Obviously, every command or order from an executive to his subordinate leads to action, that is, operation. Therefore, every command must be guided properly, and this is the role of policy. Since commands or orders lead to action, it follows that there must be a policy basis for every order and for every resulting action.

CHARACTERISTICS OF POLICY EXPLAINED

The word "policy" is generally used in an all-inclusive sense. As such it covers all guides to action. It forms the basis upon which decisions, whether major or minor, are made throughout management. It is customary, however, to distinguish the various aspects or characteristics of policy by other terms. It is even possible and desirable to state them in an order of a descending scale of importance.

Underlying all policies of management are the objectives or goals of a particular business or institution. There may be several such objectives, depending upon the nature of the enterprise itself, its purpose, and the contribution it can make to society. For a business enterprise, however, there are generally three main objectives: First of all, there is the objective of profit. The statement that a business institution cannot exist as a private enterprise without realizing a profit on its operations, needs no further elaboration. In the second place, there is the occupational objective or kind of business that is to be carried on. Both of these objectives are tangible in the sense that they can be readily identified. The third objective is more intangible but none the less important. It may be described as "reputation," "standing," or "personality." It consists of traits that identify or characterize a business in the community and in the industry of which it is a representative. This objective is as much the result of conscious effort on the part of management as is the realization of profit and the production of particular goods and services. It includes such matters as "square-dealing" with customers, quality of goods and services, courtesy, and even the personal characters of executives and employees.

"Policy" itself is the term used to describe the most important and

most carefully formulated guides to action, other than basic objectives. From the standpoint of frequency in use, policy may be classified into three types.

Policies That Are Established Precedents

The actual number of managerial policies which prevail at a given time is always less than the number of directives, orders, and commands that result from them. The reason is that some policies become precedents. A precedent is something that is said or done that serves as an example or guide to authorize and justify subsequent acts of the same or an analogous kind. Precedent-type policies may develop by being used over and over again as bases for decisions in the exercise of executive authority. A policy becomes a precedent in management in the same way that a legal decision becomes a precedent in jurisprudence. In law, it is a judicial decision, proceeding, or course of action which serves as a rule for future determination in similar cases. In both instances, such a precedent usually originates at a level of authority higher than that at which it is applied through orders or commands. For example, a decision of the Supreme Court is precedent for decisions of lower courts. So also in management, a policy promulgated by the board of directors becomes precedent for orders issued by the executives in an organization. A precedent also becomes established through repetition, especially when such repeated acts take place at the same level of authority. Such repetition is fundamental to the common law which is the unwritten law that receives its binding force from long traditional usage and universal acceptance. This process may also be observed in management where a "certain way of doing things," long an established and unvarying practice, eventually becomes an unbroken policy.

Formulated Nonrecurring Policies

Many policies never become precedents simply because after the initial instructions based upon them have been issued and subsequent action has taken place, they are never used again. They are formulated as policies, but they serve only once as a guide to action. For example, the board of directors may decide upon the policy of expansion by merger with other concerns; but after the first merger of this type has been decided upon and accomplished, there may never be another practical opportunity for such a merger.

Unformulated Nonrecurring Policies

As shown in the merger illustration above, a policy is not a command any more than it is an action. Performance, or action, is the last step in a chain consisting of policy, command, and action. The term "unformulated" means that the policy portion of the chain has been omitted. Orders

are issued, and action takes place without the preliminary guiding benefit of policy. In such case, the order itself becomes an unformulated policy. Because of the lack of managerial foresight, an unformulated policy may be necessary on occasion or imperative in instances of breakdowns or emergencies. For example, if a fire should break out in a place of business, orders will be issued to control it whether or not there exists a previous policy respecting procedure in case of fire. In such a case the instructions issued on the spot by persons in authority become an unformulated and nonrecurring policy.

Terms Related to Policy

In the terminology of management there are other words that are used to explain policy and its execution. Such a word is "strategy," which means a plan for the employment of resources and the strength to improve a competitive position and to secure advantageous objectives. Most commonly it is a military expression; but since it involves planning, it also may be appropriately applied to business management to describe a formulated policy designed to emphasize or interpret other more general policies. "Tactics" is another military term that is usually associated with strategy. It denotes the detailed steps that are employed to accomplish the ends sought by predetermined plans or strategy. Therefore, it is fair to say that tactics is also formulated policy, but detailed as to method and procedure.

Terms that are more common in the language of business management are "standing orders" and "routines." Standing orders are minor or less important policies always expressed in the form of directives, instructions, or commands. Signs bearing such notices as "No Smoking," "One Way Traffic," and "No Admittance," are samples of a type of standing orders. Routines, techniques, and routing sequences are operational policies which prescribe the manner in which standardized tasks are to be performed.

Policy is a vital phase of the management process, controlled by the higher management but of importance to everyone down to the employees and their immediate supervisors. Organization is the skeleton framework of a business. The lines of authority which hold this framework together are, at the same time, channels through which flow the elements or currents of authority, responsibility, and accountability. Policies, like lanterns, signals, or warning flags, are placed in position at numerous points along these channels of intercommunication in order to guide the management to the goal of efficient operation.

THE TECHNIQUE OF POLICY FORMULATION

The three steps of policy, command, and action tend to be taken by different management levels. Policy is most naturally and properly decided and formulated by the board of directors or by the top executive

and his major executive assistants. Commands or orders are issued by the department heads and the supervisors, and action or performance is accomplished by the employees. However, this scale is descriptive only of the general situation. When the company president signs his name to bond certificates several thousand times, he is taking action or working. On the other hand, in an emergency, the humblest employee may make a decision which is actually an unformulated policy.

The Role of the Executive in Policy-Forming

The importance of the role of any particular executive in policy-making depends upon the authority vested in him by virtue of his office. In a typical large-scale business organization, an executive with exclusive line authority has the least to do with the formulation of policies. His very status suggests that he is preoccupied with enforcing policies rather than with making them. Next in importance in an ascending scale is the functional executive, the staff executive, the chief executive, and finally the board of directors. Since the duty of coordination falls chiefly upon the top executive, much of his time and energy are necessarily devoted to policy-making. As has been pointed out previously in the chapter devoted to the board of directors, its chief function is "to formulate basic policies for the business either upon its own initiative or by approval and sanction of recommendations brought to its attention." Thus the board stands as the "court of last appeal" in policy-forming; its interest and action in the detailed problems of management will be as little or as great as circumstances may require.

The appeal system of determining which executive has jurisdiction over an exceptional problem is an important device for determining who is to formulate policy. Some policies originate at the top of the management hierarchy. More often policy is formulated because some problem has been appealed upward to the executive empowered to determine the policy of the business in that particular respect. Note that, since a policy is usually determined at a higher management level than that at which commands are issued, an appealed problem will normally travel to a higher executive if no established policy can be found to serve as precedent. If a policy precedent exists, one of the lower executives will usually concede the problem to be within his jurisdiction and will issue the required instructions.

The more important the policy, the more likely it is to be stated in general terms, rather than in the form of a command. This emphasizes the separate and distinct steps of policy and command, the one naturally preceding the other. When a policy is of routine or unimportant character, it is often convenient to state it in the form of a commonly derived or standing order. The "No Smoking" sign in an office or other place of

work obviously is notice of a policy to reduce the hazard of fire rather than to control the habits of people. So it is convenient to use the naturally derived and commonly understood command that simply prohibits smoking in certain places.

A frequent comment on the work of some higher executives is that they "devote too much attention to detail." This criticism is more correctly stated as spending too little time in formulating policy and too much time in issuing orders with respect to individual problems. The skilled higher executive delegates, as completely as possible, the issuance of commands and devotes his time and energy to formulating policies.

Classification of Formulated Policies

In Figure 1, Chapter II, it was shown that it is sometimes useful to divide the management of a business into two parts—an upper executive group called "administrative management" and a lower group called "operative management." This distinction is made on the assumption that the managerial activities of the board of directors and top executives—set apart as the administrative group—can be clearly recognized as differing from the activities of a subordinate executive group classified as operative management. The difficulty encountered in such a classification is that it disregards the fact that similar duties, though in varying proportions, are required of executives at all levels of management.

In spite of this difficulty, however, the term "administration" does have a connotation that is more particularly applicable to the duties of the higher levels of management. As generally accepted, "administrative management" refers to executive duties that are mainly concerned with the formulation of basic policies and with the major problems of coordination. In contrast, "operative management" refers to similar duties at departmental levels. Hence, from the standpoint of policy-making, administrative policies are formulated in the higher levels of management, and departmental policies are made at lower executive levels.

In the process of the formulation of policies, management is confronted with varying situations out of which there emerge three types of policies—imposed, appealed, and originated. Imposed policies are exclusively administrative in character. Both appealed and originated policies are primarily administrative; but when they are of minor importance, they are typically departmental.

Policy Imposed by Law

Anything that is "imposed" implies conformity to pressure or force which cannot be avoided. Administrative formulation of imposed policy becomes necessary when government, through legislative enactment or court action, passes a law, issues a directive, or makes a decision which

must be accepted by the management of a business enterprise. Because conformance is required, such action is imposed, and it becomes an executive responsibility to formulate the directive or order in question as one of the policies of the concern.

The business executive constantly faces the problem of legality of his commands and instructions. It often happens that he does not know exactly what the law is. Indeed, he may not even know that there is a law on the particular subject, so complex is the law itself.

When executive action or inaction results in violation of the law as it apparently exists, there are several subsequent alternatives from which one must be chosen. If improper action has been taken, the board of directors or top executive may frankly admit that the management was ignorant of the particular law or ruling and then modify company policy and derived instructions to comply with the law. This, of course, is the usual procedure.

The board of directors or top executive may decide to take no action because the law seems to be inapplicable or for some other reason is unenforceable. This is not to be construed as meaning that business executives are not law abiding. Many of the provisions of modern business law, especially those derived from regulations issued by commissions and boards established by general statutes, are actually in the nature of governmental recommendations to business. They often contain inconsistencies or uncertainties as to meaning that require further clarification before obedience to their mandate can be enforced.

The board of directors or top executive may decide that a particular federal, state, or local law is unenforceable because it seems to be unconstitutional. Executives know that refusal to obey a law is a legal offense that will cause the government, sooner or later, to bring court action against the violator. In such a lawsuit, the constitutionality of the statute in question will be tested as the primary issue. Test cases are often appealed to the Supreme Courts of the various states and for final decision to the Supreme Court of the United States. If the law is declared constitutional, executive action must then be taken by management to adjust policy and orders to comply with it.

The federal, state, and local governments have enacted many laws and created numerous agencies for the purpose of regulating business policy. Such regulation seems to be increasing. In fact, the point may eventually be reached where all major policies of each individual enterprise are subject to government review and modification. In other words, the imposition of governmental policy upon business is of increasing importance.

Policy Suggested by Trade Associations

Closely related to policy imposed by law is policy suggested to management through the institution of the trade association. A trade associa-

tion is a nonprofit organization formed by independent business competitors to promote their common interests and advantages. While trade associations are found in most or all industrial countries, they are especially characteristic of the United States. It has been estimated that there are about 15,000 of them in this country, all of which influence business policy in some degree. These associations may be classified approximately as follows:

1,500 national and regional trade associations
1,500 state trade associations
5,000 local trade associations
5,400 local chambers of commerce
1,600 specialized local associations, such as credit bureaus[1]

Among these 15,000 different associations dealing with management problems, the most important are the 1,500 national and regional trade associations that devote their attention primarily to particular fields of business.

The ways in which trade associations influence business policy vary according to their individual standards and purposes. In general, their aims fall into two broad categories. One of these may be described as a service designed to assist and improve managerial procedures. It includes such activities as research into processes, new uses, and markets for products; legislative, statistical, and technical aid; cost accounting and credit information; standardization of product, sales promotion and joint purchasing; and many other services of similar character.

The other broad activity of trade associations has been an energetic attempt to stamp out competitive trade abuses. By definition, "competition" means rivalry. "Business competition" is the effort of two or more sellers in a market to dispose of the same or similar products or services to buyers by offering inducements to them in terms of price, service, quality, and other considerations. Or competitors may vie with one another with dissimilar products or services, contending for a share of the purchaser's dollar. In any case, competition is the essence of the free enterprise system and, to that extent, has had the support of competitors themselves as well as the general public. Furthermore, the latter has sought to enforce competition by means of public law.

While businessmen have striven to preserve private enterprise, including its competitive aspects, they have at the same time often engaged in competitive rivalry so keen as to cause trade abuses. Much of the work of trade associations has been their efforts to prevent the vicious kinds of

[1] Temporary National Economic Committee, *Monograph No. 18* (Washington, D.C., 1941), pp. 465–66.

competitive struggle characterized by such adjectives as "cutthroat" and "destructive."

It can readily be seen, therefore, that the goal of public as well as of business policy has been to find a balance between competition which is wholesome and rivalry which is dishonest, abusive, and destructive. The trade association has played an important role in this undertaking. The well-financed trade or industrial association has accomplished much voluntary improvement in the policies used by individual member businesses. This has been brought about chiefly by means of education of the members in best practices and in ethical conduct.

The type of activity on which trade associations have laid stress in educating their members is illustrated by reference to a few of the organizations and their accomplishments designated by the American Trade Association Executives, the central professional organization in this field, as outstanding achievements:

National Automobile Chamber of Commerce: Cross-licensing agreement under which seventeen hundred patents were pooled without cost.

National Retail Credit Association: Establishment of a system for exchanging credit information on a national scale.

Laundryowners' National Association: Erection of a million dollar proving plant and operation of a vocational training school.

National Board of Fire Underwriters: Expenditure of $300,000 in showing nearly three thousand hospitals how to reduce the fire hazard.

Cotton-Textile Institute: Distribution of statistics, education of the members in cost accounting, advertising of cotton goods, and a campaign against night employment of women and children.

Association of American Soap and Glycerine Producers: Trade promotion campaign conducted in cooperation with health, social service, and educational agencies.

Tanners' Council of America: Improvement of raw material, establishment of a credit bureau, technical research, promotion of uniform cost accounting, publication of monthly statistics, a color and style program, proper labeling of products, and improvement of public relations.

Southwestern Ice Manufacturers' Association: Marketing plan which has increased the sales of ice and improved the service to the public.[2]

Obviously, all of these accomplishments, and scores of others like them, have had the effect of imposed policy on management. To conform to the standards and practices thus developed, the managements of member firms have been urged to modify existing policies and to formulate new ones designed to realize the aims of their trade associations.

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[2] Simon N. Whitney, *Trade Associations and Industrial Control* (New York: Central Book Co., 1934), pp. 35–37.

Legal Restrictions on Trade Associations

During their long history, there have been many instances when trade associations have gone beyond the service functions that have been described. In their attempt to eliminate trade abuses and to protect their members from destructive competition, they have entered the field of industrial control by using methods that emulated the "pools" that existed in the latter decades of the nineteenth century, namely, agreements to fix prices, limit production, or divide the market. To the extent that such agreements could be effectuated by a trade association, they became imposed policy, restrictive in character upon its membership. Because these actions were restrictive, trade associations thus ran afoul of antitrust legislation.

In interpreting the Sherman Antitrust Act of 1890, the courts have held that indirect or educational methods may be enjoined if they result in concerted action to restrain trade. Further, that to destroy competition or to create its opposite, monopoly, is also contrary to law. Trade association activities are therefore unlawful to the extent that they restrain trade. Just what activities are specifically banned are noted in a long line of United States Supreme Court decisions. The most important of them may be summarized as follows: joint selling,[3] price-fixing,[4] division of the market,[5] curtailment of production,[6] and boycotts to enforce desired channels of distribution.[7]

The Sherman Law has been called "the bulwark of compulsory competition."[8] It was designed primarily to guard the public against oppressive monopolies, and it did so by attempting to keep competition open to all concerns who might wish to enter a market. The restraint on combination acted at the same time as a drawback on the activities of trade associations. Free competition has its evils as well as its advantages; and, unless kept under control, it can be suicidal to those taking part in it, and without permanent benefit to the public at large. How to stamp out the

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[3] *Continental Wall Paper Co.* vs. *Voight & Sons Co.*, 212 U.S. 227, in which a contract by wallpaper manufacturers to market this product through a common selling agency was declared illegal.

[4] *U.S.* vs. *Trans-Missouri Freight Association*, 166 U.S. 290, wherein a combination of railroads organized to fix freight rates was condemned.

[5] *Addystone Pipe and Steel Co.* vs. *U.S.*, 175 U.S. 211, wherein an agreement between castiron pipe makers to divide the market was found to be unlawful.

[6] *American Column and Lumber Co. et al.* vs. *U.S.*, 257 U.S. 377, in which it was held that it is illegal for an association to curtail output, even though persuasion and education, rather than direct agreement, were employed.

[7] *Eastern States Retail Lumber Dealers' Association* vs. *U.S.*, 234 U.S. 600, declaring illegal the circulation of lists of wholesalers for the evident purpose of boycotting those who sold directly to consumers.

[8] Edgar L. Heermance, *Can Business Govern Itself?* (New York: Harper & Bros., 1933), p. 218.

evils of competitive trade abuses without stifling initiative and enterprise with the heavy hand of monopoly has been a continuing concern of trade associations.

Trade Practice Conferences

Federal legislation in 1914 recognized the fact that unfair methods of competition are as undesirable and destructive of private enterprise as monopoly had been interpreted to be. In fact, when competition is destructive, it can, in itself, result in a restraint of trade. Recognizing this fact, the Federal Trade Commission was created as a special agency to provide a remedy for unfair methods of competition which were not covered by the Sherman Act or at common law. It was set up as an administrative tribunal authorized to use summary procedure to protect legitimate business.

In 1919 the Commission inaugurated a plan of voluntary legislation known as the Trade Practice Conference. More than two hundred of them have been held since that time. In most cases these conferences are sponsored by some particular trade association and represent, therefore, collaboration of the trade association and the federal agency most concerned with the regulation of business policy. The business representatives present thresh over their differences and come to agreement upon questions of fair and unfair practices with respect to their particular trade.

Out of such an understanding, a tentative code which is considered in detail by the Federal Trade Commission is drafted. Usually there are certain rules in that code which can be affirmatively approved at once as coming within the scope of existing law. These rules are designated as Group I. Group II rules are stipulations in the adopted code which are accepted as expressions of the trade on the standards of practice in question. They are endorsed by the Commission in the sense that they do not violate any law. If rules that border on legal violations are proposed in the conference, they are rejected.

In those industries or trades in which trade practice conferences have taken place, the trade association may attempt to impose policy upon particular business enterprises both by mandatory requirements and by optional requests. "Mandatory requirements" are rules and provisions agreed to by the trade practice conference that are considered by the Federal Trade Commission as constituting "unfair trade practices." Since they are illegal, the Federal Trade Commission joins with the trade association in imposing rules on individual enterprises. For example, the Federal Trade Commission, after a trade practice conference, promulgated Trade Practice Rules for the Rubber Tire Industry.

One of the Group I, or legally enforceable rules, is the following:

RULE 10 (a).—The passing off, selling, or offering for sale of used, rebuilt, recapped, retreaded, or repaired tires as new or unused tires, is an unfair trade practice.[9]

Advisory and optional provisions are the permissive practices and recommended voluntary restriction, which the Federal Trade Commission will not enforce, but which may be promoted and followed on an optional basis. An example of this Group II type of rule, from the Rubber Tire Industry Rules, is as follows:

RULE A.—Where merchandise at wholesale and merchandise at retail are sold in the same establishment, the failure on the part of any member of the industry to correctly differentiate between or identify the two types of transactions, where the result may be to create confusion and deception as to the character of the transaction in the mind of the purchasers, is condemned by the industry.[10]

In addition to policies that have been submitted to the Federal Trade Commission and classified by that government agency as enforceable (Group I) and permissive (Group II), the typical trade association is constantly making legally permissable suggestions respecting their policies to its members and to nonmembers. These suggestions are transmitted by personal contacts, by means of meetings and through written material supplied to members and to the press. To the extent that such suggestions are adopted, they become imposed policies from the viewpoint of the affected business enterprise.

APPEAL AND COMPLIANCE PROCEDURES OF IMPOSED POLICY

As business policy tends to become regulated to an ever increasing extent by governmental agencies and trade associations, it is necessary to develop procedures, sometimes complex and complicated, for rehearings and appeal from decisions that have been made.

The Process of Appeal

The trade practice conference procedure of the Federal Trade Commission is an example of this appeal process. Every member of the particular trade or industry may attend the conference, and may participate in the formation of the proposed rules. The rules are then put forth in tentative form by the Federal Trade Commission, giving another opportunity for protests or suggestions before final promulgation. Even after publication in approved form, the rules can still be appealed to the courts for decision as to their legality. The decision of a lower court can be appealed to the United States Supreme Court.

[9] Temporary National Economic Committee, *Monograph No. 34* (Washington, D.C., 1941), p. 50.

[10] *Ibid.*, p. 51.

This process of appeal, hearing, decision, and appeal to the next higher level is cumbersome and time-consuming. However, since it permits full and fair consideration of all sides of the business policy in question and since it protects minority interests and permits adjustment to meet special situations, it is a vital phase of democracy.

Although varying in form, there is an appeal system, consisting usually of many different levels and agencies, in every procedural device set up by the government to control business policy. These paths usually begin with the trade association, proceed to an administrative governmental agency, and terminate in the courts. This type of appeal process should be distinguished from the appeal of internal problems within one particular business. The former is a series of steps in determining a legal or semi-legal question, namely the exact wording and effect of an imposed business policy. The latter is the machinery for making the exception principle of management effective, that is, the referral of internal problems to the executive best qualified to solve them.

The Process of Compliance

In cases where governmental regulations or laws are imposed on a business, the foregoing discussion points out two different broad situations. In one group of problems the process of formulation of policy consists in refusing to obey the imposed government requirement. Instead, by passive or active methods of fighting, the business seeks to obtain modification, clarification, or even elimination of the law or regulation. The business, in other words, seeks to have the government give it what its executives believe to be a more reasonable basis for policy formulation in the particular instance. When this appeal step is concluded, and in the numerous other cases where the edicts of government have been accepted without question, the next step is administrative formulation of the required policy. This step may be simple or extremely complex, depending on circumstances. Even the smallest business must frequently face and solve this problem.

Sometimes the new requirement of the government is a simple and direct order or prohibition. In such cases it is possible to formulate business policy simply by furnishing appropriate subordinate executives and employees with a copy of the new law or with a brief summary or paraphrase of its new requirements.

More often, the law or regulation can only be converted into usable business policies through much effort. It may be necessary, for example, to ask the appropriate official or board to rule on various questions. Enforcement of the order may make necessary internal reorganization of the business. For example, accounting requirements contained in a tax law may be enforceable in a particular business only after the addition of

employees with specialized skill in certain phases of accounting. A law requiring certain holding companies to go out of business obviously would require an extensive reorganization of the companies affected. This would result in the formulation and reformulation of many of their management policies.

Policy which is imposed on a business, either by a trade association or by the government, always involves a compliance problem. The question faced by the formulators of the required administrative policy or policies is whether to insist upon broad, general obedience, or whether to instruct subordinates to "toe the chalk line" and comply with the letter as well as the spirit of the law. This is determined largely by the language used and the attitude taken in formulating and promulgating the new policy. Subordinate executives and employees usually have a very definite emotional reaction toward imposed policies, that is, they desire to comply or they attempt to evade the specific requirements. This attitude can often be traced to the unconscious revelations of higher executive thought on the particular subject contained in the manner of promulgation of the policy. If, for example, a state law limiting truck-load weights is considered arbitrary and unfair by the higher management of a trucking concern, this attitude is quickly reflected in "lip service" and evasion tactics by the rank and file.

In the case of policy imposed from above by the government, the members of the board of directors and the highest executives responsible for formulating administrative policies are the ones who squirm and fume over the problem of educating the remote government officials or of adjusting sensitive business to a strait jacket of excessively rigid and exacting requirements. When this same group of board members and higher executives pass on problems appealed from lower managerial levels within their own business, the roles are reversed. They become the remotely placed court of last resort, likely to formulate general policies not properly adapted to specific problems and conditions. Their subordinate executives and employees often, under these circumstances, comment on the time and effort required to "educate the front office."

APPEAL AND COMPLIANCE PROCEDURES OF INTERNAL POLICY

The very nature of the internal appeal process within a business unit fosters the use of committees as an important technique in administrative formulation of the necessary policies. For example, if a field salesman is offered a large order, provided a further concession in price is made, he will appeal to his zone manager who will appeal to the sales manager. The appeal from the salesman to his superior (the zone manager) will probably be in written form, that is, a report by telegraph or letter requesting further instructions. The appeal from zone manager to sales manager,

assuming the zone manager considers the proposal worthy of appeal, will probably take the form of a telephone talk, a conference, a meeting with the sales manager and the others he may call in for discussion and consultation, or a report in written or oral form to a committee designated by the sales manager. If the sales manager seeks a policy decision by the higher executives or by the board of directors, he likewise does so by means of telephone talks, informal meetings, or by report to a designated committee.

The Committee Technique

A "committee" is a group of two or more persons qualified to consider or decide some problem. In this broad sense, the telephone talk between the zone manager and his superior sales manager is a committee meeting. It is evident, therefore, that the appeal system of carrying exceptional problems upward to the management level capable of issuing commands or formulating appropriate policy, naturally results in use of the committee technique. Depending on the customs of the particular business and on the importance of the problem, the committees called into being may consist of only two, or of many persons. The committee meetings may be of short duration or long, or may even result in many sessions of the group.

The committee may be purely advisory, serving only to assemble and transmit information concerning the appealed problem to the higher executive who will formulate the required administrative policy. The committee may be called together for the one purpose or for consideration of all similar problems. If organized as a standing committee, it may serve only to exchange information, to give information to a superior, or to decide questions as a group by majority or even by unanimous vote.

Practical Limitations of the Committee System

There is a great temptation to overorganize the natural committee system for handling appealed problems and formulating the necessary administrative policies. Because the board of directors is a committee, it is argued by some there should be a complete system of policy committees within the entire executive organization. When this type of organization of standing committees on policy is tried, it necessarily results in numerous committees, each to consider some one management subject. There will be committees on employee complaints, safety committees, suggestion committees, new product committees, marketing committees, production committees, and finance committees.

At the lower management levels, such standing committees of executives, and often of selected employees, have the great merit of providing

a recognized channel for consideration and transmittal of appealed policy problems. It is common experience that the creation of a standing committee on safety or on suggestions, for example, will result in much more attention being given to the problem by the entire organization.

On the opposite side is the fact that standing committees are wasteful of the time of their members. For instance, the superintendent of maintenance must sit through lengthy discussions of production problems because of his permanent membership. On the other hand, if the personnel of the committee on production problems is left to the needs of the moment, the superintendent of maintenance will naturally be called in only when his work is involved.

At the higher executive levels, the converging of all the various standing committees on policy toward a few major executives creates a serious inroad into the executive's available time and energy. He finds himself devoting many hours each day merely to committee attendance or to study of committee reports.

The natural outcome of this time-consuming situation is the formation of an executive committee under the chairmanship of the top executive, president, or general manager. Such a committee of major executives sometimes becomes a substitute for, or an aid to, the board of directors. In fact, where this evolution progresses to the point of a strong standing committee of executives, the board of directors either tends toward a passive role or else takes over the executive committee by adding its principal members to the board's membership.

There will always be two schools of thought—the one objecting to the organization of complex and time-consuming internal standing committees involving the entire management hierarchy and the other advocating such procedure. As in most things human, the true path of optimum results seems to lie between the two extremes. Some subjects, like safety work, should be organized by means of permanent, active standing committees. Other subjects should be handled as the needs of the moment require.

It is very important to reduce the standing committee duties of major executives to a minimum. These men must carry the burden of formulating all types of administrative policy, and even the permanently constituted committee of major executives may consume more time than it is worth. More important is the fact that any standing committee is bound to hamper an executive's freedom of decision and action. Even though he is certain that no vote will be taken to impose the ideas of other executives on his field of work, yet he will feel obliged to defer to their opinions and thus to postpone policy formulation until a meeting of the committee permits him to explain his problem and his proposed decision to his colleagues. Much valuable coordination takes place in such an executive

committee, but it is sometimes doubtful whether this gain is not more than offset by the hampering effects of committee delays and confusing argument and discussion.

ORIGINATED ADMINISTRATIVE POLICY

The most important of the three types of administrative policy is that which is originated and formulated by the board of directors or one of the higher executives. Originated administrative policy is the rudder of the business, steering it toward its objectives. It is the means by which the higher management adjusts the business of the present so as to insure profitable operation in the future.

Imposed policy, coming down to the business from some government agency or trade association, almost always has a limiting or prohibiting effect upon the particular phase of company activity. Imposed policy is, therefore, essentially negative or regulatory, not dynamic.

Appealed policy, on the other hand, is primarily formulated to meet some exceptional problem, emergency, or potential emergency. Often a subordinate, for example, appeals a policy because he disagrees with the first instructions from his superior and wants to have the problem reviewed and redecided. Appealed policy decisions are made primarily to solve current problems, that is, to coordinate various phases of the present operation of the business.

The point has already been made that there is always present in the upper management levels one leadership or coordinative position, usually called president or general manager. Originated administrative policy always comes, in the last analysis, from the schemes and plans of this central or top executive. He may receive suggestions from the board of directors, from subordinate executives, or even from strangers. He may confer on the problem with one or many persons. This will not change the fact that the new policy, when originated and formulated, will be an act of leadership and therefore the peculiar work and province of the top executive.

If the business is relatively small, the president or general manager may not only originate, but may also personally formulate and promulgate, this type of administrative policy. However, often in small enterprises and almost always in large businesses, it is advantageous for the leader or top executive to give his principal assistants, that is, the major executives, an opportunity to share in the vital task of originating administrative policy. This may be done directly by passing the leader's plan over to a major executive so that the necessary new policy or policies will be formulated by the latter. It may be done indirectly by an adroit suggestive discussion of the problem, so that the particular major executive will believe that he made the original suggestion to his general manager

or leader. In either case, the time required in formulation of the policy is saved to the top executive; the second and closer review by the major executive will reveal details that must be solved or elaborated upon; and the major executive will have a greater personal interest in the new policy and in its successful acceptance by subordinate executives and by employees.

To make clear the broad and important field of originated administrative policy, the following situations are illustrations of certain types of policies to which special top executive consideration may properly be given:

Merger.—Unknown to most of the executive organization, and perhaps even to the board of directors until the final stage of negotiation, the president may undertake personal contacts which will lead to merger of his own and another business.

Expansion.—The president or general manager may plan to build a new factory or to expand his sales force. The fulfillment of his scheme may require new financing, involve plant or product design, or require reorganization of the existing sales force. The top executive has to seek out the needed information and ability, both within and outside the company, in order to perfect his plans and formulate his expansion policy.

Contraction of Facilities or Force.—At times the company leader or coordinator faces the necessity of eliminating activities and personnel in order to reduce expense or to increase efficiency. He has the problem of timing his reduction policy correctly in terms of the business cycle and of convincing his subordinates of the necessity and advantages of the step that is contemplated.

Research.—Encouragement of research is necessarily one of the personal concerns of the highest executive of the business, since research has future value only, never present value.

Executive Personnel.—In every organization such problems must be faced as executive apprenticeship, promotion, demotion, and retirement. Only the president can originate and formulate appropriate administrative policies for management of the executives themselves.

Strategy and Tactics.—To use a military example, a declaration of war is a formulated policy; the decision to carry on war by means of an attack upon certain mountain passes, ports, or oil fields is strategy; and the method of attack which uses a sequence consisting of planes, tanks, and infantry supported by artillery, is an example of tactics. The way in which the president or leader of a business wishes to have a particular policy carried out is a phase of his task of originating policy. In many cases the top executive does not originate a particular policy, but only originates the strategical approach, the tactical methods, or both.

One of the most fundamental tests of the quality of management of

any business is the way the formulation of administrative policy is handled. If appealed problems are considered promptly, yet with full review and investigation of the facts, it is clear that subordinate executives will be able to do their work better. If imposed policy is analyzed and fully understood by executives in the higher level of management, their departmental and supervisory assistants will waste less of their time and make fewer mistakes. If the business leader or top executive formulates the many policies which vitally affect the company and states these policies concisely, then everyone can be coordinated with his established policy. Conversely, consider the confusion which too frequently occurs when the top executive fails to originate policies or expresses himself in confused fashion so that the business is left at the mercy of competitors. A sense of futility or despair grips subordinate executives, making them desert to other companies or play internal politics to achieve their own policies or satisfy their personal, and often selfish, ends.

DEPARTMENTAL POLICIES

In addition to administrative policy, which is formulated by the higher management, many policies are made by the lower management. These may be designated as "departmental policies."

Departmental policies have to do with operations of the business. Each department has its own functional field or zone of activity. Within each departmental field, there will necessarily develop three types of policies: first, executive policies; second, standing orders; and third, operating routines and techniques.

Executive Policies

When top management leaves the formulation of policy to departmental executives, their duties are generally confined to originating and promulgating the strategic and tactical details of the course of contemplated action. First of all, the product of their work becomes executive policies that are formulated in conformity with other strategic and tactical decisions of superior officers of the firm. To illustrate this close relationship between executive policies and administrative strategy and tactics, some typical situations may be cited.

The president of a paper mill in which there had been persistent serious labor trouble decided to bring about better internal understanding of such problems by employing a well-known labor union official to become personnel manager of the company. Obviously, the stratagem of securing a labor leader as personnel manager was the background for all the executive policies that were subsequently formulated by the new official for the guidance of the industrial relations department under his jurisdiction.

In another instance, the purchasing agent of a cotton piece goods mill was encouraged by the board of directors to use a large cash surplus of

the company to speculate in cotton. In doing so, he developed a departmental policy to buy certain cotton futures when they were quoted below a stipulated price on the cotton exchange. However, he did not hedge his purchases with offsetting sales of futures contracts. This departmental policy was clearly predicated on the strategy of speculation approved by the board; and, by inference, since there were no instructions to the contrary, the directors also approved the tactical method of omitting hedging in buying futures on the cotton exchange market.

The veto of a proposed departmental policy may be illustrated by the case of a traffic manager who learned he could reduce the transportation costs on a certain ore by having it shipped by barge from mine to plant in 500-ton lots on an inland waterway. He assumed that the selection of this carrier would conform to an established policy of using the cheapest means of transportation for company shipments. Accordingly, he sought the approval of the general manager to authorize him to handle the traffic in this manner. But the manager vetoed the proposed plan because he felt it was strategically unwise to take so much traffic away from the railroads who were among the firm's best customers; and, tactically, it was not in the best interests of the company to buy such large lots of this raw material at one time.

It is true that the task of the functional department head is to run his portion of the total business. To do this, he must be authorized to formulate and enforce executive policies. However, his policies must also be coordinated with those of his fellow executives at the departmental level. Much of this coordination is accomplished through friendly interchange of views by the various department heads. Some of the coordination is accomplished through the strategic and tactical suggestions of the higher executives. Where compromise and guidance fail, conflicting views are carried upward, and an "appealed" policy which must be followed by even discordant department heads is formulated.

Standing Orders

In addition to the formulation of executive policies, department heads are also charged with the responsibility of setting up standing orders. Such orders are devices for effectuating and facilitating the transmission of information which specifies the manner and conditions of work. The necessity for an order must be made evident to all those to whom it is intended to apply. Therefore, orders are stated in clear and concise language. Their purpose is to stimulate interest and to secure cooperation and coordination in the performance of the work to be done.

Standing orders must have an obvious relation to the requirements of a given situation and be definite in their placement of responsibility. For these reasons, they must be formulated in the lower levels of management; but, like executive policies, they must not run counter to the admin-

istrative policies of the firm. On the contrary, though they may be said to be of minor importance, the significance of standing orders is that they facilitate and expedite the work of an enterprise in an orderly and efficient manner.

Routines, Techniques, and Sequences

Closely related to standing orders are operational routines, techniques, and sequences. They take the form of instructions or commands which prescribe, in some detail, the manner in which assigned tasks are to be performed. Since their purpose is direct application to the work required of employees, instructions of this sort must necessarily originate in the management levels that are in the closest contact with actual productive processes.

Standing orders and instructions dealing with routines, techniques, and sequences are complementary devices of management. They are not identical. "Standing orders" are, in effect, adopted standardized plans, procedures, and regulations basic to performance, while "instructions" govern the details of the operations involved. They are a means of assuring the proper execution of orders and working plans. Since this is true, the information they provide must be supplied by the individuals who are responsible for the particular phase of the work concerned. As with all of the aspects of policy-making, routines, techniques, and sequences must be in harmony with all overlying policies and procedures in order that the functions of an enterprise may be unobstructed in the achievement of its objectives.

THE TREND TOWARD WRITTEN POLICY

The extent to which policy is formulated in writing depends on many factors. In general, the larger the company, the greater the tendency to reduce all policies to writing, to preserve them and to be sure that all concerned in them have a written copy. There is a school of thought among executives who are believers in methodical management, which favors the formulation of policy in writing regardless of its relative importance or of the size of the business. However, just as "red tape" strangles government, so blind adherence to rule hampers business management. There should be room for freedom of action within mentally maintained limits for certain policies, even in the largest enterprises. Otherwise, quick adjustment by department heads to their immediately pressing problems becomes impossible.

The more legal or controversial the problem, the more likely the needed policy will be formulated in writing. Imposed policy and appealed policy both tend to be formulated as written statements, summaries, or agreements, the first for legal, the latter for controversial, reasons.

Administrative and Executive Policy

It is generally true that administrative policies of the originated type and executive policies as well are reduced to writing at the time they are formulated. This usually is done by means of approval or disapproval of the recommendations of a report; by preparing minutes of a conference; by writing a short note, memorandum, or letter on the subject; or by filing correspondence and handwritten notes.

However complete and accurate the file of policies is kept, it has value as a reference or recording system rather than as the actual basis for operation. The higher executives and the department heads of a business rarely refer back to the exact written form in which a policy was originally formulated. There is neither time nor need for such bothersome checking, since the executive's memory of important policies is vividly linked with the experiences or situation that caused the policy to be developed. An important phase of executive skill is his accumulation, through the years, of this memory of decided policy. The better his memory of decided policy and the context or circumstances of its creation, the more likely the executive is going to be able to meet new conditions with new and aggressive policies. The successful executive uses decided policy as a tool, not as the hampering "dead hand of the past."

Even less likely to be written out in detail is the application of strategy and tactics to any particular policy situation. These serve as the delicate shading of emphasis by which the executive adjusts his policies to the situation before him.

Standing Orders in Written Form

In contrast with other types of policy, standing orders are always in written form. This necessarily follows from the fact that such directives must be kept permanently and constantly before the supervisors and employees. This can only be done by issuing them in writing or printing on posted signs, filed notices, or in letters and memoranda.

One of the commonest techniques for handling standing orders is to issue them as memoranda from one executive to another, with the notation or inference that the instructions are to remain in effect until cancelled. Often such a system is organized by the simple device of numbering each order, and of issuing notices of cancellation when any numbered order is withdrawn or redrafted. A more complex system provides for numbering or coding and filing by subject, followed by reissue of all orders in force at regular intervals.

The greatest problem in connection with standing orders is to keep them within usable limits. The story is told of one company which followed to its logical extreme the Frederick W. Taylor precept of getting

all operating facts out of the realm of guesswork and memory. This company, after years of effort, accumulated volume upon volume of standing orders, covering every operating situation and procedure. For example, a standing order was set up for shipping clerks prescribing the exact number of nails to be used in closing the top of a packing box. After this company was reorganized, this entire accumulation of standing orders was discarded without noticeable loss of efficiency and with considerable saving in cost of compilation.

Another problem in connection with standing orders is to make sure their text is available when needed. This is best accomplished by placing the order at the point of use. "No Smoking" or "Keep This Door Closed" signs are examples of such distribution to the place of need. This is not possible, of course, in many cases, and the problem is how to make sure that the appropriate supervisor or employee will keep his file of orders up to date. The best way to insure this is to have the file checked and made current at regular intervals. The field salesman, for example, starts his work with an up-to-the-minute file of the standing orders pertaining to his job. The only way to be sure that it remains up to date is to call the file in every year or two to be checked and made accurate again by a home office clerk.

Written Instructions for Routine Operations

There will always be controversy as to which is the better cook, the one who follows the cookbook exactly or the one who disregards all but the dictates of his skill in the culinary art. Similarly, the compilation of routine instructions may be carried out to minute details or much of actual operations may be left to the skill of supervisors and workers.

With ever increasing technical complexity and with more demand for product uniformity and cost reduction, business operations must be conducted according to predetermined formulas or routines. The prize no longer goes to the skilled employee who disregards prescribed procedure. The question, then, is not whether to use a cookbook, but what kind of a cookbook to use. Obviously, accumulation of a complex file of hundreds of routine directions is wrong because it does not form a usable or practical means of reference, or cookbook.

The best way to handle operation routine is to devise and install mechanical devices that record the key points of operations. Then the supervisor and those who work with him do not feel under formal orders to use an absolutely predetermined routine or technique. They know, however, that failure is brought conspicuously to the attention of the department head, and therefore they are constrained to use uniform and efficient methods. Such a procedure eliminates a mass of standing orders, yet it achieves the same results.

The first locomotives, for example, had neither safety devices nor speed indicators. Modern locomotives, with safety valves to protect against boiler explosion and with speed-recording devices, can be operated by their crews in close conformity with the orders of the management. The engineer follows a prescribed operating routine which is partly a standing order on the observance of signals and track speed limits and partly a technique inherent in the machinery and the safety devices of his locomotive.

Written Manuals

One of the newer management tools is the department operating manual. Examples are sales manuals, accounting manuals, and production manuals. A "manual" is a discussion and compilation of the more important policies, standing orders, and operation procedures of the moment. It is usually written as a guide for new employees, but is always valuable in refreshing the memory of older employees.

The preparation and use of manuals is an educational process within the business. The fact that a manual cannot be kept up to date, but must be revised and reissued from time to time, is proof that it cannot replace other methods of formulating and promulgating executive policies, standing orders, and operation routines.

The Annual Budget

An even more important method of codifying operating policies is the annual budget. The budget is, of course, the annual forecast of income and the planned allocation of expense. Expense is allocated down to individual employees and equipment in properly detailed sections. The budget desires of the subordinate executives are fitted together and then revised by the controller and finally adopted by the president or even by the board of directors.

As finally adopted and made available to executives, the budget reflects and converts current company policy into results of anticipated future operations. Economy is the policy at some points, expansion is provided for at others. Ability to meet expected competition is reflected in the production and sales estimates. The monthly budget reports, comparing actual with planned results, show the trend of operations as compared to the originally formulated policy. At every step and stage, the budget helps the alert department head to coordinate and perfect his actual operations with company and departmental policies.

THE FORMULATION OF POLICY ILLUSTRATED

The nature of policy and its important role in management can be illustrated and clarified by a consideration of pricing problems which con-

cerns all business enterprises. Pricing policy is not only universal, but it is a vital matter in that the price which a business places upon its goods or services is a major governing factor in its ability to operate successfully.

In a large establishment, pricing is usually the responsibility of the board of directors upon the advice and recommendations of the top executive, and, of course, of the sales manager or official that corresponds to that title. Minor deviations from an established pricing policy are usually decided by the sales manager himself. In a small concern the owner-manager or some person designated by him is vested with the authority to set prices. In either case, whether a business is large or small, there are two important justifications for reserving final decision as to the price to be charged as an exclusive function and responsibility of the highest level in the management.

In the first place, all vital decisions affecting the monetary position of a business should be reserved to ownership or to those who represent ownership, such as the board of directors of a corporation. Basic pricing policy and the general strategy and tactics employed to achieve its purposes fundamentally affect both income and expense and therefore have a definite bearing upon the financial condition of a concern. In the second place, the success of a business may depend upon the continuous patronage of a certain group or type of customers. Customers are both favorably and unfavorably responsive to price adjustment. Customers are extremely sensitive to fancied or real signs of discrimination or favoritism. Even the smallest change in price, therefore, is potentially important enough to merit the attention and decision of top management.

Price-Lining

"Price-lining" is a method of establishing prices on goods at different levels on the basis of quality or service, or a combination of both of them. It is also sometimes known as "price range." Within the general price structure, there are many price levels that go to make up the average price that prevails at a given time. For example, prices that are above average are at a level that will attract only the more or less exclusive trade of high income classes of people. At the other extreme are the below average prices which appeal to a class of trade whose incomes are low. In between these two levels are the medium or average prices aimed to fit the pocketbooks of people in moderate financial circumstances. The quality and the price of the goods offered for sale correspond to each other. That is to say, a line of goods of high quality commands high prices, a line of medium quality will carry average prices, and a line of merchandise of low quality will be sold at low and below average prices.

It is therefore apparent that price-lining is a matter of policy. It has long been recognized as such by retailers, especially in the department

store field. Some stores feature only high-priced lines, while in others low-priced goods predominate. Still others price their merchandise at a level that will capture the average or general trade. The automobile field presents a parallel situation among manufacturers. Everyone is familiar with cars offered by that industry in different price ranges calculated to fit the purchasing power of all income groups. It may be said, however, that in the field of distribution as a whole, retail and wholesale merchants usually find it desirable to stock and to sell goods at several different price levels.

The significance of price-lining as a policy is that it tends to standardize the products of manufacturers and the merchandise of trade, and to simplify the markets for them. There is a relatively distinct market for each price group. Therefore, the seller who offers first one line of a particular quality at a corresponding price, will be selling in a limited market. The important decision to make in adopting such a policy is what class of customers is desired. Single price-lining is always restrictive, whether adopted by a merchant or a manufacturer. By introducing additional qualities, a wider range of the buying public can be reached.

Customer Classification

Many businesses classify their customers and offer to some of them prices more attractive than are offered to others. There are several different bases upon which such a classification of customers is justified.

A common practice has been to classify customers on the basis of the quantity of goods purchased at any one time, or during an established period of time, and to allow a discount on the purchase price corresponding to the size of the order. In general, the result has been that the larger the order the greater the discount, and the lower the price per unit. A price policy of this kind obviously classifies buyers on the basis of size. The small buyer with limited purchasing power is discriminated against in favor of one whose requirements and resources are greater.

It was the fear that such discrimination would result in the eventual destruction of the small businessman that led to the enactment of the Robinson-Patman Act of 1936. This law provides, among other things, that it shall be unlawful to discriminate in price, in the course of interstate commerce, between purchasers of commodities "of like grade and quality," regardless of quantity, except that due allowance may be made "for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered."[11]

The purpose of the Robinson-Patman Act is to prohibit discrimination between customers rather than a classification of them. Discrimination is

[11] Clayton Act, as amended, Section 2, Public Law 692, June 19, 1936.

more than distinguishing between persons. It implies that a relationship existing between a seller's customers entitles them to equal treatment. It is discrimination when concessions granted to one party casts some burden or disadvantage upon another.[12] Where no such relationship exists, the law does not apply. Therefore, it does not require a uniform price policy for all of a concern's products or all of its customers. It applies only to commodities of "like grade and quality," and to customers who are served under like circumstances. Hence it is permissible to have price differences between different classes of goods as well as between transactions in identical goods if it can be demonstrated that such differentials are directly due to savings that result from (1) the *methods* of sale and delivery of the goods, or (2) the *quantity* of the goods produced, sold, and delivered.

Another method of classifying customers is according to their status as wholesalers or retailers. This distinction is not made on the basis of the quantity of goods purchased, but on the purpose for which goods are bought. Thus a wholesale merchant is one who buys goods from manufacturers, producers, and wholesalers and sells principally to retailers. A retail merchant is a dealer who buys goods from manufacturers, producers, and wholesalers, but sells to consumers at any time and in any quantity. A supplier who sells to both wholesalers and retailers distinguishes between them because of their different functions, and his price policy is different in each case. Wholesale purchasers are given the largest discount and, therefore, the lowest net price. Customers classified as retailers are offered a different and somewhat higher price.

A third method of classification of customers is by the indirect process of classifying the product. Users of this method offer the best terms only on the product that can be used by those capable of buying large quantities at low production cost to the seller. The highest price is charged on products sold under the higher cost conditions. A corollary of this method develops when a producer, in business because of one product, accumulates a surplus of another associated product. Such so-called "by-products" are offered at whatever price the traffic will bear—no matter how low—since they would otherwise yield nothing to the revenue of the enterprise.

Finally, customers may be classified on the basis of the apparent cost to a particular customer of a similar product offered by a competitor. This is the delivered price method used by business enterprises where the cost of transportation constitutes a large part of the cost to the purchaser. If he absorbs a portion or even all of that cost—assuming, of course, the price discrimination law is not violated—the seller is in a position to meet competitive conditions as he finds them at the point of delivery.

[12] Burton A. Zorn and George J. Feldman, *Business under the New Price Laws* (New York: Prentice-Hall, Inc., 1937), pp. 75–76.

Of course, not all concerns classify customers according to the methods described. But where such classification is deemed desirable, a business enterprise may use each of them to some extent in order to arrive at its price policy. To an increasing degree, however, government regulation imposes the responsibility upon business management to apply a uniform method to all customers who are accepted as potential or satisfactory purchasers.

Variations in Merchandising Policies

"Merchandising" means trade or commerce in goods and services. Price policy is obviously a major factor in this phase of management. Merchandising decisions arise from the interplay of the manipulation of price, quality, or service. By "manipulation" is meant the control of action or response, especially with reference to prices, by deliberate and skillful management. A reduction in price and a simultaneous increase in quality or service amount to the same thing and accomplish the same end. Some businesses emphasize "price manipulation," that is, the movement of prices up or down to meet changes in the market. Others try to stabilize price by manipulating quality. If the price of a type of product tends to rise in the general market, price can be held at a given point by reducing quality or discontinuing some form of service. Conversely, if the price tends to drop, it can be stabilized by increasing quality or service. The following examples taken from actual situations illustrate some characteristic merchandising policies in common use among various types of business concerns:

Meat Packing.—The rate of earnings per dollar of sales is so small that it has no appreciable effect upon the prices of meat or livestock. The price of meat varies with the quantity offered for sale and with consumer buying power. The price of livestock is governed by the price of meat and by-products. Meat packing is an industry which operates in a free market where the price of raw material and the sales price of finished products depend upon the unrestricted operation of the law of supply and demand.

Investment Trust.—One form of this type of business is a voluntary association in which the trustees function as a board of directors. Funds derived from the sale of shares of the concern to the public are invested in other securities. The current market price of its own shares is determined by the net liquidating value of the securities in its portfolio in the free market of the New York Stock Exchange, plus a fixed percentage added to cover selling expenses.

Department Store.—The retailer may be regarded as the purchasing agent for the public. He first sets his retail prices as near the current demand as possible and then goes into the market and purchases at these

prices. Sales analyses show which prices are most popular and where consumer-buying is concentrated. The typical department store buys and sells in the open market, but it also exercises partial control of price-lining by purchasing at several of the most popular price levels.

Automobile Manufacturing.—The first step in bringing out a new model is to determine a competitive selling price. From this price are deducted the dealer's commission and an estimated sum to cover overhead expenses and profits. What remains is the cost of manufacturing. The car must be as perfect as possible, and yet the manufacturing cost must be low enough to result in a retail price which consumers can and will pay. Automobile pricing has sometimes been called "administered pricing" on the assumption that the manufacturer can fix any retail price he chooses. This assumption is obviously erroneous because the factors which must be considered are the costs of manufacturing and selling on the one hand, and the price which will result in consumers' acceptance on the other. Through efficient operation the manufacturer may have partial control of the former, but he has no control of the latter.

Cement Industry.—Cement is commonly sold by manufacturers at "delivered prices" because purchasers of this commodity demand quotations on this basis. Therefore, the cement manufacturer widens his area of distribution by selling at distant points at the price offered by his most favorably located competitor. Any competitive disadvantage resulting from unfavorable freight rate differentials must be absorbed by the manufacturer in the delivered price.

Manufacturer of Gunpowder.—The United States Government is a large consumer of smokeless powder for the use of its armed forces. At the same time, the maximum price to the Government has been set by congressional action on a basis of cost of production plus a margin which insures a reasonable profit to the manufacturer. The selling price of smokeless powder for domestic military purposes is, therefore, not subject to market fluctuations and remains relatively stable.

Electric Utility.—It has been characteristic of electric utilities that supply energy for domestic consumption to reduce the rate charged per unit consumed though prices on other consumers' goods increase. The justification for a price policy of this kind is that as the rate is lowered to the residential user the consumption of electricity increases more rapidly than the proportionate increased cost of generating the current. In other words, in this industry it pays to lower the retail selling price in a market where a marked increased demand results from this policy.

Educational Institution.—Governing boards and administrators of in-situations of higher learning, whether public or private, may attempt to meet increased operating costs by shifting a considerable portion of these costs to students through increased tuition fees. Such a policy is inimical to the ideal of public education and often has the effect of denying the

opportunity of advanced training to highly capable students whose resources are inadequate to cover college expenses. Therefore, it has been urged that scholarship funds be provided in colleges and universities to enable secondary school graduates of real ability to continue their education, irrespective of their parents' financial status. To operate under such a policy, a school must establish a system for classifying student customers and formulate a plan for furnishing complete financial assistance out of endowment income to those least able to continue their studies.

Street Railway.—A street railway system in a large city was bound by its franchise to a five-cent fare. Earnings from this low fare were insufficient to meet the demands for improved equipment and better service or to meet operating expenses. Management of the system was turned over to a board of public trustees who were faced with a large deficit and the threat of ruin. Under this public management, the fare was raised to ten cents and assessments were levied upon the cities and the town in the metropolitan area served by the railroad. The deficit was thereby wiped out, and both the quantity and the quality of the service were improved. A change in price policy was the deciding factor.

Mutual Life Insurance Company.—The report of a mutual life insurance company shows that over a period of more than one hundred years of continuous operation, the amount of money paid in by its policyholders was substantially less than the amount paid back to them plus the value of assets held for their benefit. Since it is a mutual company, it is a cooperative enterprise. Its price policy is that of cost because it returns, as annual dividends to its member policyholders, all income in excess of claims, expenses of operation, and other charges.

Teachers' Insurance and Annuity Association.—The announced attractive feature of this company, also a cooperative organization, is that its premiums are lower than those of leading commercial companies for corresponding contracts. This favorable competitive position is achieved through its marketing policy of employing no soliciting agents and because its income from endowments meets most of its operating expenses.

RELATION OF STRATEGY AND TACTICS TO POLICY

Since a policy is the basic guide that gives direction to the acts of management, it precedes both executive orders or commands and the actual performance of the tasks that lead to the accomplishment of the desired objectives. Assume, for example, that a successful chain store enterprise dealing in clothing and other merchandise decides upon the policy of extending its stores beyond the eastern part of United States to the cities in the western part of the country. This policy results in issuing the necessary order to establish a unit of the chain in Denver, and a new store is opened there.

Naturally, the eastern chain store management wants the new western

units to be successful. This attitude leads to a methodical survey of the western retail situation to serve as a basis for the decision that will control subsequent strategy and tactics. These strategical and tactical shadings of emphasis and interpretation of the policy which has now been established will determine the success or failure of the new western stores, as the chain executives well know.

In military affairs, after the policy to make war has been established by some means such as a formal declaration of war or an overt act, the next step is to draw up an elaborate "estimate of the situation." This estimate of the situation provides the background of information and opinion for determination of the military strategy and tactics to be used in subsequent attack and defense. This military estimate of the situation and the methodical market survey used in business are parallel techniques.

In solving business problems, it very often happens that the methodical survey of the marketing, financial, production, or general economic situation is made before the final policy is determined. The decisions involved in the policy are made tentatively before the general survey has been completed. If the survey indicates that the proposed policy will fail, should be modified, or should not be applied to a particular situation, there is no need to go farther. If, on the other hand, the market survey or other appropriate investigation verifies and corroborates the probable success of the proposed policy, this same methodical assembly of economic data is now available for further use as a basis for the development of strategy and tactics.

The Five Good Marshals

The five words—"why," "what," "when," where," and "how"—have sometimes been called the "five good marshals" for clear thinking. They sum up the procedure of the formulation of policy and the use of that policy as a guide to action. As soon as a proposed policy has indicated tentatively "what" to do, the general survey of the problems indicates "why" it should or should not be done. If it should be done, then the tentative policy becomes the established "what" to do. The general survey now serves as basis for the translation of the "what" policy into strategical orders and instructions as to "when," "where," and "how."

In the chain store example, the formulated policy is to extend the chain from the eastern United States, where it is now operating, to include stores in the larger western cities, such as Denver and Los Angeles.

The first step of methodical market survey, it may be assumed, gives the necessary answers as to "why" the proposed policy will be successful, and thus establishes the new policy as to "what" to do.

This same market survey is now used by the chain store management to determine its general procedure, or strategy, in carrying out the new

policy. For the sake of illustration, it may be assumed that the following interpretative decisions are made:

1. That establishment of the new chain units should begin at once and progress at the rate of not more than one every twelve months in order to use the existing executive organization of the chain store business without interfering unduly with the operation of its existing stores. This determines, in general, "when" the new stores will be opened.

2. That the first of the new stores be established in Denver's downtown retail shopping district, because Denver is the easternmost large city of the west and the method of progressing from the east toward the Pacific Coast obviously will be the most economical use of executive time in the absence of any other strong consideration. Location within the downtown shopping district of Denver is a natural strategical requirement based on Denver's size and the nature of the proposed store. This answers the question as to "where" the new stores are to be established in broad rather than specific terms.

3. That the new Denver store be established in its own building within the downtown shopping district and be completely remodeled and re-equipped according to the standards of the chain store company, but that every effort be made to impress the Denver shopping public with the local character of the new establishment. This is the determination of "how" strategy, still in general terms.

Policy and Strategy

It is difficult to draw an exact dividing line between policy and strategy. In many instances, an already established policy tends to modify or interpret a newly formulated policy. In such a case, the established policy has a strategical effect on the new policy.

Some policies are established as a guide to some specific action, such as the purchase of new machinery or the expansion of the business by the addition of another store. Other policies are established as strategical guides and modify all other policies. When depression hits, for example, the business may adopt the policy of cutting all expenses. Such a policy has a strategic or interpretative effect on all of the existing policies of the enterprise.

It is clear from this discussion that the term "strategy" may be used interchangeably with the term "interpretative policy." Strategy, in other words, is a policy which is formulated or is being used for the purpose of interpreting, or shading the emphasis and meaning, of other policies. The top management often gives full authority for formulation of operating policies to its departmental executives, limiting itself to originating the necessary strategic policies which guide and influence all actual operational decisions.

The strategical policies of the top executive leadership of a company determine such factors as the speed, quantity, and quality of accomplishment of specific operating policies. The inability or unwillingness of the top management to decide such questions of strategic policy as to how much money will be available for some new purpose leads inevitably to indecision and wavering in carrying out the formulated policy. The strategic attitude of the board of directors, the president, and the major executives toward a company's competitors will strongly influence all sales policies. If the top management is afraid of its competitors, for example, it is difficult for the sales department to formulate departmental sales policies designed to overcome strong competition.

Policy and Tactics

The term "tactics" in military parlance denotes the method of carrying out strategy and thus accomplishing the formulated policy or campaign. However, like strategy, tactical decisions are themselves policies, since they are guides to action or performance. In military affairs, the three terms, "policy," "strategy," and "tactics," form a sequence from basic decision to broad interpretation to detailed procedure or methods. In business situations, the use of the three terms, "policy," "strategical policy," or "strategy," and "tactical policy" or "tactics," has the same significance in separating and identifying the three steps required for the accomplishment of some goal determined by policy.

The application of tactics, or tactical policies, to the actual operation of a business is best illustrated by reference to competition between businesses for a share of a particular market or kind of business. By definition, "competition" is rivalry or struggle for supremacy. The following illustrations are examples of different kinds of tactics sometimes employed by business concerns to gain advantageous competitive positions.

Concerted or Massed Effort.—Tactics sometimes may take the form of a concerted effort of large proportions, undertaken at one time, whereby a business concern attempts to establish itself in a favorable position among its competitors. For example, a company may risk a large investment in plant and facilities to increase production, lower costs, and extend its market simultaneously rather than gradually. Or by research and technical invention, it may plan ahead to enter its field with a superior product at a lower cost, with the intention of securing for itself a major portion of the potential business in a given line. A concern may seek to achieve a similar competitive position by a brief but vigorous and extensive advertising campaign designed to force its way into the consciousness of the public in spite of competitors who presently may seem to control the field. All these tactics are massed or concentrated efforts which, by force of strength, are designed to successfully overcome existing competition.

Persistent or Continuing Effort.—Massed or concerted efforts to overcome competitive hazards are tactics applicable only to enterprises that have extensive resources which can be drawn upon and risked in a contest in which the outcome is not assured. Therefore, the most common tactics employed by business firms to obtain a satisfactory position among competitors may be described as persistent and continuing effort. Every aggressive concern is constantly campaigning for a greater volume of business, increased customer acceptance, and broader, more favorable, public recognition. Since such tactics are a common practice and widespread among competitors, the rivalry which ensues is often heated to the point of bitterness. However, disparagement of one another by competitors is not to be countenanced in playing the game, nor is misrepresentation tolerated under the law. Therefore, tactics of this kind tend to keep executives alert and aggressive and cause them to sense the demand of the public promptly and accurately and, accordingly, to render an acceptable service which merits increased market participation.

Consolidating Gains.—When, as a result of a single, concentrated campaign or a continuing one, a business finds itself in a favorable competitive position, other tactics must be employed to consolidate all the gains that have been made. To achieve victory in a contest where competition is keen is exciting and sometimes dramatic. The contest itself, therefore, often appeals strongly to certain executives for that reason. On the other hand, the work of consolidating gains is routine and rather humdrum. There is a saying that after a new process or machine is invented it is necessary to "take the bugs out of it." That is to say, it must be strengthened here, adjusted there, or even be redesigned in whole or in part in order that its potential purposes may be fully realized. So, also, when a campaign has been successful in opening up a new sales territory, for example, it is necessary that steps be taken to follow up the first success with methodical canvassing and exploitation of the new market. In many businesses it is the function of the advertising department to open the way to new markets, but it becomes the task of the sales and credit departments to consolidate initial gains into a permanent sales volume.

Maintaining an Established Competitive Position.—When an enterprise has reached its optimum competitive position in a market, or because of its technical advancement it is firmly established in its particular class of industry or business, aggressiveness is still a requisite to success. Tactics must be employed to hold what it has gained, for unless an active campaign is carried forward to protect the goals already achieved, retrogression will soon develop.

Many businesses are keenly aware of this fact, and special tactics are evolved to cope with the situation. For example, certain trade-marked brands of staple household goods like packaged soap are distributed

through retail store channels. When the products are first introduced, these outlets are found by an aggressive sales campaign carried on by salesmen in the field. When this plan of distribution has been established, the salesmen are withdrawn and the retailers are supplied by selected wholesalers in their respective territories. Should subsequent sales fall off—which is not an uncommon experience—field salesmen are again sent out by the manufacturer of the product to re-establish the trade that has been lost. Such recurring direct selling tactics have been deemed desirable and necessary in situations of this kind because of the small annual volume of purchases that are realized from individual, independent, retail stores.

This is not the only method that is used to protect established gains from drifting away. Institutional advertising through trade journals, popular magazines, newspapers, radio, other media, are means to this end. Publishers of textbooks maintain field representatives who call upon the members of the faculties of schools, not for the purpose of making direct sales, but rather to retain adoptions already made and to be instrumental in securing new ones when such opportunities arise. Life insurance companies have developed various tactics employed through their agencies and agents to encourage and help policyholders to keep their insurance policies in force. Within the management of business itself, executives seek to maintain efficiency in their departments against the influence of depreciation, obsolescence, and sometimes tradition, and thus guard against retrogression from gains that have been made.

Tactics of Retreat.—There are times when tactics of retreat are necessary. Ground may have been gained in a competitive position from which, for strategic, economic, or other reasons, it is wise to withdraw. Examples of this kind are unsuccessful ventures, the outcome of which could not be forseen when they were undertaken. Then, too, it sometimes happens that shifts in population, the incidence of war and the return to peace, the migration of industry, and changes in the general political situation may create conditions to which business must adjust itself. In any one of many situations, therefore, tactics of retraction, rather than of aggression, can have a strengthening effect upon an enterprise.

The psychological aspects of aggression are very different from those of consolidation or defense. An executive who shows aptitude in programs of development and growth may not display efficient ability in maintaining a position that has once been established. Also, there is even a greater psychological difference between aggression and withdrawal. Ground once won is hard to give up. It is easy to understand that an executive who has been accustomed to press forward does not readily turn back, even though hard facts and logic point the way. Therefore, the development and use of various types of tactics to implement and enforce policy are not simple executive functions. Hence it follows that tactical decisions

can best be made, not by one officer in a company, but by as many authoritative executives as the application of particular tactics to specific situations may warrant.

The Tactics of Diplomacy

The historical record of business rivalry for competitive advantage contains sordid stories of bitter trade wars. At the same time, it has been an established public policy in this country to foster and protect competition and to declare by law that efforts to stifle it by agreements, contracts, conspiracies, or other means are contrary to the public welfare. Therefore, in order to retain the benefits of competitive enterprise and yet to curb competitive activities that are detrimental to the public as well as to competitors themselves, certain tactics are no longer tolerated. They are legally banned as unfair trade practices. Business directors and executives who authorize or countenance such methods are running the risk of public condemnation, and as violators of the law they are subject to severe fines and imprisonment. As a result, the tactics of diplomacy are supplanting the strife of the arena.

An example of the lethal competitive struggles that once prevailed, is the patent war. A "patent" is a certificate issued by the federal government, securing to an inventor for a term of years, the exclusive legal right to make, use, or sell his invention. When a business enterprise devises new processes, creates new products, or finds ways to improve old ones, such developments may be patented. The effect is a monopoly for a guaranteed period of years, as far as a particular patent is concerned. A patent war ensues when one firm appropriates for its own uses the patented inventions of another, or, more commonly, develops much the same idea but loses the race to the patent office. Patent wars result in legal battles between patent owners until a court decree extinguishes one patent claim, or the costs involved lead to the financial exhaustion of one of the contestants. Because tactics of this sort are now considered to be unfair trade practices, conflicting patent claims more and more tend to be settled by peaceful diplomatic negotiations. Often the result of such negotiations is cross-licensing, a procedure which permits both parties in the controversy to use the new invention in its most advantageous form.

An extension of cross-licensing of patents is the patent pool. It is a device which enables one firm to use a great many patents of others in exchange for the use of certain patents which it owns. A pool can be accomplished in different ways. One way is cross-licensing between patent owners, already mentioned. Another is to transfer the titles to patents (since a patent is property) to a trustee who is authorized to distribute them to members of the pool according to stipulated terms. A somewhat similar method is to transfer patent titles to a corporation empowered to

issue licenses for the use of the patents or to grant powers of attorney to a common agency authorized by the owners of the patents to distribute licenses for their use. In any event, the patent pool saves the loss of time and money involved in litigation, but more important, it makes a new invention available for useful purposes with the least delay.

However, the tactics of diplomacy illustrated by the patent pool may not lose sight of the ethical group considerations involved. The patent pool has forged a weapon of potential monopoly control, but it may use it for purposes of market stabilization and the establishment of peaceful competitive conditions. If such tactics result in monopoly, or if they are designed to produce monopoly profits, the actions taken will be contrary to law and will also encounter adverse public opinion.

Other examples of the movement toward the tactics of diplomacy are to be found in labor relations. The strike and lockout are both illustrations of aggression in which the objective is to win by force or exhaustion. To the extent that labor disputes can be settled by negotiation and arbitration, diplomacy replaces strife. As a further illustration of this change, it will be recalled that prior to the turn of the twentieth century, certain railroads are said to have been operated on a policy of "the public be damned," and in conformance with it, set their charges for transportation on a basis of all the traffic could be made to bear. The policy of the railroads in this country today is based on a philosophy of "the public be served." They tend to carry on their struggle for existence and for profits through complex diplomatic negotiations between shippers' committees, railroad committees, and the Interstate Commerce Commission.

PUBLIC OPINION AND POLICY

Under conditions of diplomatic negotiation the public expresses itself partly through law, but chiefly through public opinion. "Public opinion" consists of a mass of more or less vague individual impressions that crystallize in a unified attitude for which the support of common acceptance by the people can be definitely discerned.

Like an individual, the public obviously has opinions on many subjects. With respect to business, there are two types of public opinion. One type is based on fundamental ideas and ideals, like the belief in, and devotion to, a system of private enterprise in a capitalistic society. The other is based on countless routine contacts of the general public with individual business concerns. These contacts are derived chiefly from customer transactions, advertisements, and news stories in newspapers. The reactions of people to them leave impressions that find expression in opinions. The attitude thus expressed can be favorable or unfavorable to business as a whole, even though the sources upon which it is based may be inadequate

and inconclusive. The fact remains that the business community, by its own actions and attitudes toward the public, can influence if not control public opinion of this kind.

When public opinion is apparent, how it should be dealt with depends upon the view that is held with respect to its importance. A natural and simple attitude is to disregard public opinion as to be of little or no consequence. In circumstances where social control of business seems to be accelerating, this view is untenable and dangerous. A better plan is to analyze public opinion, to evaluate its errors and truths, and, by means of formulated procedures and policies, to take steps to make whatever improvements are indicated in the relations with the public.

Public relations work is coming to be recognized more and more as an indispensable function of management. It is a planned activity that has for its purpose the creation of public good will through news releases, advertising, lectures and exhibits, and other means that can be used to exert a favorable influence on the public. Since public opinion represents an average situation, there is no such thing as completely favorable or completely unfavorable public relations. What can be achieved by management, however, is a coordination of all contacts with the public so as to obtain some desired improvement in public opinion.

Sincerity is the necessary basis of any substantial improvement in public opinion toward any particular business. Trustworthiness and sincerity depend upon policy, strategy, tactics, and diplomacy. It follows, therefore, that the way to obtain favorable public opinion and win the respect and cooperation of those charged with law enforcement is to use policy—in all its various forms and shadings of emphasis—in such a way as to merit public confidence and win governmental approval.

THE DEPENDENCE OF POLICY UPON INTERNAL AND EXTERNAL CONDITIONS

In this chapter, an attempt has been made to outline the several aspects of policy and policy-forming and to emphasize the importance of them in the management process. Since business is an activity which depends upon human beings and the ability to serve their needs, it is conditioned by the ever moving and ever changing stream of social evolution. Business must necessarily move along with that current. Whenever any business enterprise, or any part or policy of it, fails to do that, it is discarded by society and disappears.

Management is the helmsman on the craft of business. To steer an even course, to realize stability and profit, and to avoid disaster requires of management ceaseless vigilance manifested by a continuous flow of decisions and commands. As has been pointed out, commands and orders

lead to action, but unless such action is to be other than haphazard and wishful, the decisions which give rise to commands must be based on policy for which the responsibility rests in executive authority.

Policies are of many kinds depending upon their various purposes. Their classification, formulation, and use have been discussed in considerable detail in order to leave with the student a clear comprehension of the range and indispensability of this type of executive activity. Judgment, knowledge, and imagination gained through experience, research, analysis, and perception have been emphasized—directly and by inference—as prerequisites in establishing guides to action. Hence, the point was made that the higher the concentration of the responsibility of policy-forming in a level of management, the less numerous will be the duties of performance on the part of the executives which constitute that level.

Nor can rigidity be tolerated in successful policies and in their formulation. The importance of adjustment to conditions, internal or external, physical, social, and legal, has been shown. Conformity to regulations enacted by law, sometimes called "social control," is often a major consideration in successful management. Likewise, to be able to set up internal guides which will assure coordination between the distinctive functions of a business, and direct them all toward a common objective, requires both flexibility and diplomacy.

It has been shown that the achievement of the objectives of a business enterprise necessitates the determination and development of satisfactory means to gain such ends. Such means were described in military terms, namely, "strategy" and "tactics." Strategy is a matter of interpretation of policy in the light of a given situation, and tactics denotes the details of effectuating the strategy evolved after recognizing the steps involved in accomplishing a formulated policy. It is commonplace to say that every business has problems which must be "attacked" before they can be solved. Yet trite or not, it is precisely in the method and manner of such attack that managerial tactics come into play. Just what they shall be, their nature, force, and direction, depend not only upon the wisdom and judgment of the members of a business organization to whom they may be assigned, but to the impact of public opinion as well.

Thus, invariably and inescapably, management in its role of policy determination and execution, must look both inward and outward. Obviously, sound decisions cannot be made without an understanding of the internal problems and conditions of the business itself. Nor can it be overemphasized that since business deals primarily with human beings, neither may the implications and effect of social control, directly or indirectly, be neglected when policies are made and promulgated.

The formulation of policies and their issuance in commands, orders, and other forms of directives are therefore, one of the most important,

as well as one of the most critical, tasks with which the executive group in any business enterprise is charged. This task is so pervasive and far-reaching in its effect upon the affairs of a going concern that it challenges the finest qualities of managerial talent.

QUESTIONS

1. Define the following terms in sufficient detail so that each of them may be easily identified and clearly distinguished:
   a) Profit objective.
   b) Occupational objective.
   c) Reputational objective.
   d) Precedent-type policy.
   e) Formulated but nonrecurring policy.
   f) Strategic policy.
   g) Tactical policy.
   h) Unformulated and nonrecurring emergency instructions.
   i) Standing orders.
   j) Operational standardization of task performance.
2. Explain how the appeal system works in determining which executive has jurisdiction in the following situations:
   a) The exception principle has been referred to as a means of classifying problems at each higher level of management, thereby permitting only those of suitable importance to be appealed upward. Show how this technique necessarily results in the handling of the more important problems of policy by higher management.
   b) In previous analyses of the elements of authority it was pointed out that the authority to decide is inherent in every executive position, subject, however, to limits upon executive discretion and to the appeal of exceptions to superiors. Show how this phase of management distinguishes the task of policy formulation from the authority to issue and enforce commands.
   c) In the text of this chapter it has been stated that, if a policy precedent exists, one of the lower executives will usually accept the problem as within his jurisdiction and will issue the required instructions. Explain and illustrate some circumstances in which a lower executive may fail to assume jurisdiction, as, for example, ignorance of precedent, uncertainty as to its applicability, or a desire to shift the responsibility for decision to his superior.
3. Use the technical terminology employed in the text of this chapter to identify and explain the following policies:
   a) A decision by the federal government to reduce "retained profits of business enterprises" during World War II by imposing excess profits

taxes and by the renegotiation of wartime contracts that have been unduly profitable.

b) A decision on the part of downtown department and specialty stores not to be open to customers on Saturday afternoons during the summer months.

c) During a drought, a local city government passes an ordinance intended to cut consumption and use of water supplied by the municipally owned water utility. A local industrial establishment refuses to comply with the ordinance on the ground that its water supply is pumped from its own wells on its own premises.

d) An association of railroads petitions the Interstate Commerce Commission for a postponement of an order requiring all freight cars to be equipped with certain safety devices. The association asserts that the new devices cannot be properly installed on old cars presently in service; that such cars should be allowed to wear out without modification, and then should be replaced with new rolling stock fully equipped according to the Commission's specifications.

4. A small business concern has purchased a large truck for the purpose of using it to transport a part of its product to a market about fifty miles away. Trace the operation of the appeal process and the development of policy in the company under the following conditions:

a) Assuming the absence of legal restrictions, trace the probable channel through which appeal will flow in the organization when the truck driver asks for instructions as to how heavily to load his vehicle.

b) Assuming the existence of numerous state laws and regulations governing the loading and operation of trucks, trace the probable channel through which appeal will flow in determining the imposed policy as to how heavily the truck may be loaded. Assume also that a state traffic officer has indicated that a permit can be obtained from the state highway department for very heavy loading.

5. A "committee" is a group of persons qualified to investigate, consider, and take action upon some problem. State which of the following groups may be rightly considered to be committees according to the foregoing definition, and give reasons for your answer:

a) A foreman and one or more workmen who have reported to him for work instructions.

b) A bus driver and a traffic policeman engaged in a discussion while the latter is writing out a "ticket" covering a traffic violation incurred by the bus driver.

c) A salesman and his sales manager engaged in a telephone conversation concerning the best solution of a sales problem.

d) Several attorneys arguing a case involving the Sherman Antitrust Law before the Supreme Court of the United States.

e) The stockholders of a concern in a meeting legally called for the purpose of voting to dissolve the corporation and to go out of business.

6. Define and illustrate with examples each of the following types of policies:
   a) Policy imposed by government.
   b) Policy imposed by trade associations because such imposition is backed by government.
   c) Policy suggested by trade associations.
   d) Imposed appealed policy.
   e) Internal appealed policy.
   f) Originated policy formulated at the top executive level.
   g) Originated policy formulated below the top executive level.
   h) Departmental policy.
7. A sales manager of a certain firm adopted and formulated in writing a policy which provided for price concessions to a selected class of customers of the company. Although he believed he was merely carrying out a clear-cut administrative policy in attempting to secure this class of business, the sales manager requested the president of the company to give specific approval to the policy he had advanced. Discuss this development of departmental executive policy with special reference to the following circumstances:
   a) Among other things, the sales manager requested the president to secure legal opinion as to whether this departmental policy could be construed to be in violation of a law which prohibits discrimination between customers.
   b) The sales manager also asked the president to approve the tactics whereby he proposed to capture a certain class of business through the medium of price concessions to selected customers.
   c) In support of the policy he had formulated, the sales manager submitted estimates showing large increases in sales volume and net profits, despite the proposed reduction in price to certain customers.
8. In this chapter, it has been implied that the larger the business enterprise, the greater the necessity and tendency to reduce all policies to writing. Take a somewhat different view, that is, that even a small company should formulate, compile, and preserve its numerous policies in written form, and that such action will not only avoid confusion and misunderstanding but it will tend to increase efficiency and the ability of the company to compete with other enterprises, regardless of size. Expand on this idea and illustrate your exposition with examples of your own selection.
9. Explain in some detail the following statements selected from the text of this chapter:
   a) Determination of policy, even in detailed form, should be the exclusive function and responsibility of the top management of a company.

b) Strategy may be defined as "interpretative policy."

c) Tactics may be defined as "detailed procedural policy."

10. Give your own interpretation of the following statements selected from the text of this chapter:

a) Trustworthiness and sincerity depend upon policy, strategy, tactics and diplomacy.

b) The way to obtain favorable public opinion is to use policy in such a way as to merit public confidence and win governmental approval.

c) Public opinion consists of a mass of more or less vague individual impressions that can be definitely discerned.

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Chapter XIII

EFFICIENCY IN MANAGEMENT

THERE is widespread misunderstanding concerning the meaning of the term "efficiency" as used in business management. It is often assumed that efficiency merely denotes a reduction in cost. Such an interpretation of the word is too limited. Efficiency is the quality of effectiveness, competence, and capability in productivity. Efficient operation of a business means effectual management and adequate performance of work. Efficiency is a fundamental concept in the whole management process. A business is operating at its highest efficiency when it can produce goods or services of a desired quality in a required quantity within permissible limits of time, at the lowest cost consistent with its financial situation and obligations. Not only is this test the measure of efficiency with respect to productive processes, but it applies to every task that needs to be performed.

The Elements of Efficiency

The concept of efficiency is complex. In addition to cost, it includes the elements of quality, quantity, time, and method. Clearly, an undue emphasis upon the reduction in cost as the one measure of efficiency is fallacious. The false notion that efficient management can be measured alone by minimum cost probably stems in large part from the prominence that was some years ago accorded to so-called "scientific wage systems" promoted by self-styled "efficiency engineers" or experts.

Efficiency cannot be achieved by cutting costs and neglecting all other considerations. It can only be obtained by establishing a proper balance between the five elements of quality, quantity, time, method, and cost. Essentially, the acts of management issue from human effort in three ways. At one extreme there is maximum performance to which a person's strength and ability set limits beyond which he cannot go. At the other extreme is minimum performance, which is the least a person can do if he does anything at all. In between is the optimum or most desirable worker performance. It is balanced performance in the sense that waste and loss are avoided whether in overdoing or underdoing. So when we speak of attaining or striving toward efficiency, it contemplates an optimum condition of cost as well as of each of its other elements.

The Measure of Efficiency

Even though minimum cost is not the sole measure of efficiency, monetary cost is the common denominator of all business effort. It is the commonly accepted standard by which the results of human performance in a business organization are weighed and tested. Therefore, it is entirely consistent to consider relative cost, and even a reduction in cost, as an approximate measure of efficiency when applied to any or all of its elements.

It is customary to assume—and it is generally true—that increased operational efficiency results in savings to the business. These savings may be in time, effort, materials, and many other things—all of which usually can be reduced to measurement and comparison as a saving of money. These savings can be classified into three types. The first type is the direct and apparent one which can be readily traced to its source. It may be the result of a new idea, procedure, or process which has produced an immediate result that can be identified, measured, and expressed as a definite monetary saving. The second is the indirect type of saving. It may be an improvement in the rate of production, or the quality of the product, or an ultimate saving at some future time. While this type of saving is less tangible than the first type, it, too, can usually be definitely appraised and expressed in terms of money. There is a third type of saving that results from increased efficiency which is so intangible that it cannot be estimated in advance in dollars and cents, even though it does result in measurable material advantage in the long run. It is illustrated by the saving of executive time and energy, better public and labor relations, style or quality appeal in a product, or an improvement in morale and attitude throughout an organization from workers to president.

EXECUTIVE RESPONSIBILITY FOR EFFICIENCY

The better the executive organization, the greater the opportunity for increased efficiency. Highly skilled executives know how to develop efficiency. Furthermore, a soundly developed organization gives each executive the best possible opportunity to do his own work well. Particularly important is avoidance of violation of the spans of control and knowledge, since such violation cuts down the personal efficiency of the executive himself. The chief executive or leader of the business organizes and coordinates his subordinate executives so that they can be efficient. They can, in turn, increase and develop the efficiency of their supervisors and employees.

The dynamic aspect of managerial efficiency consists of creating balance among the elements of quality, quantity, time, method, and cost. That is to say, it is the ever present executive task of departmental heads to see to it that anyone of these elements is not out of proportion to the

others. Higher management assigns this detailed task to its departmental subordinate executives. However, supervisors in the lowest levels of management rarely have control over all of the factors; hence it is their duty to secure efficient performance of the work to be done within already established limits.

The terms "direction" and "control" are often used to describe the executive activities of department heads. One phase of the activity of direction is planning; it is the foundation of all efficiency in operation. Control is the executive activity of requiring and obtaining efficient operation from supervisors and employees. Planning and control are the two steps taken by the department heads of a business to obtain and improve efficiency. When specialization in management results in staff, line, and functional departments, some departmental executives tend to concentrate on planning and others on control.

Scientific management as developed by Frederick W. Taylor, and as especially applied to an industry in which machine operations are involved, separates efficiency of operation into two parts: planning and performance. (See Fig. 24, Chap. VIII.) According to Taylor, planning involves finding out and writing down exactly how the work should be done for best results; deciding the route the work should take; and determining when the work should be done and how much it would cost. These requirements include the same fundamental elements that have been mentioned above. In other words, management could not be scientific, and therefore not efficient in Taylor's opinion, without taking into account the factors of quality, quantity, time, method, and cost.

At the level of performance, Taylor placed control for efficient operation in the hands of persons with titles that are now becoming obsolete. They were the gang boss, speed boss, inspector, repair boss, and disciplinarian. Comparable present-day designations would be supervisor or foreman, time-study or methods engineer, inspector, maintenance supervisor, and director of personnel. The task of these persons, whatever their actual titles may be, is to supervise the work that is being performed, and each within the limits of his particular authority, controls operations for the purpose of maintaining and, if possible, increasing efficiency. In other words, these executives (or their representatives) are the center of control at the point of production; but, at the same time, they are also subject to the direction and control of their respective department heads who are charged with the over-all responsibility of efficient planning without which the desired efficient performance cannot be realized.

APPRAISAL OF EFFICIENCY

"Appraisal" is the act of setting a value upon something. In the terminology of accounting, it refers to the estimated value rather than the

actual value of land, buildings, equipment, and other property. In nonaccounting aspects of management, appraisal includes an estimation of the worthiness of proposed and existing plans, methods, and operations. The implications of appraisal go beyond those of inspection, investigation, and research. These latter activities may be necessary as preliminary to sound appraisal; but appraisal itself, as a device of management, denotes measurement of value in terms of money. Therefore, this appraisal process is indispensable in determining the degree of efficiency which prevails at a given time, and in forming a judgment as to what the outcome of a contemplated plan or policy may be. In a word, the purpose of appraisal as a function of management is to facilitate skilled judgment when decisions have to be made as to the worth of present performance or future plans.

Although it is not always apparent because its effect is indirect, every decision of management must finally depend upon executive judgment as to its profitableness. Appraisal is the process of deciding just how profitable or valuable to a business any one of a multitude of things may be. Such decisions may have to do with plant, product, equipment, employees, executives, policies, campaigns, or even the utilization of a new idea or new invention, to mention but a few. It is obvious that considerable experience and close association with managerial problems are requisites of effectiveness in the ability of an operating executive to judge or appraise with fair accuracy the financial results of a present decision upon future performance.

METHODS OF EXECUTIVE APPRAISAL

Present decisions are of two kinds: (1) to continue existing operations without change; and (2) to modify them by expansion, retraction, or complete elimination. Appraisal of prevailing situations is the first step in planning. Only in this way can a department head decide whether present methods should be continued, improved, or abandoned. In making such decisions, various methods of appraisal can be used:

The Comparison Method

The "deadly parallel" or comparison of one particular operation or situation with another is probably the most common form of appraisal. It is constantly used as a means of appraising particular workers and particular machines. For example, some street railways have installed devices that record the coasting time, with power shut off, of each car. If one motorman can operate his car day after day on a particular route with a given percentage of coasting time and without undue delay, it follows, in accordance with the principle of the deadly parallel, that other motormen operating similar cars over the same route should be able to match his economy record.

A basic scientific principle is that experimental evidence is not valid

unless all the factors except the one being studied are held constant. The "deadly parallel" is valid, therefore, in appraising different workers only if all the conditions under which they work are, in fact, alike. In the foregoing example, for instance, the parallel might be invalidated by the fact that the motorman making the most favorable coasting record did not work during the rush-hour periods of heavy traffic.

A common and important example of appraisal based on the "deadly parallel" arises when the executive in some manner discovers that in another business a machine is being operated more efficiently than in his own department. The problem he must face is whether the conditions in the other business and in his own department are actually alike, so that the apparent savings of the former should likewise obtain in the latter. Since a business, to be successful, must keep from being the highest-cost producer in its particular industry, such comparisons are constantly being made by department heads as a means of appraising whether to retain or improve existing operating methods.

The Survey Method

Frequently the "deadly parallel" can be created only on a sample basis because it is impossible to make a comparative study. This is the "survey" or sampling method of appraisal. The buyer for a restaurant can only ascertain by reference to experience and by experiment how many portions will be produced from a given purchase of meat or ice cream. He cannot arrive at exact information, but must compare one actual situation with another.

Under such circumstances, the department executive must judge not only the scientific validity of the parallel but also the adequacy of the sample. In accordance with the principles of statistical theory, a sample is likely to be invalid or worthless if the number of situations sampled is very small. Since, in business, it is often necessary to make a decision based on a single sample, there is frequently very little opportunity for comparison with other similar situations. An electric public utility may induce a business to establish itself within its service area because of desirable non-peak power consumption by the new enterprise. After a short period of operation, the new business may demand a substantial reduction in the rate charged for its current, claiming that a similar business located in another city has a lower rate. The public utility must then decide, on the basis of these meager facts, whether it will force this desirable customer out of business or into use of some other source of power if it refuses to cut the rate.

The Yardstick Method

The "yardstick" method is another common technique for appraisal of operating problems. In every phase of business operation there are

yardsticks, varying in validity from scientifically proved principles and theorems to pure rules of thumb derived from executive or worker experience. These yardsticks do not find their way into actual use in the appraisal of management problems directly from the so-called "pure sciences" and the fundamental philosophical studies. Yardsticks are brought into business from the applied sciences, such as engineering and chemistry, accounting and business statistics, business law and business management, and from work itself. When carefully studied out and accurately formulated, these yardsticks may be properly called "standards."

Yardsticks develop first as the observations and conclusions of an experienced executive derived from long personal contact with the problem. Yardsticks are often based in part on the traditional knowledge handed down by generations of employees. Merely because the executive can offer no proof or valid justification for his conclusions does not mean they lack accuracy. The human mind is a remarkably accurate device for storing up observations over the years and thus building up conclusions whose accuracy is felt by the executive rather than thought through logically. It has been observed, for example, that individuals, such as Indians, farmers, or fishermen, who have spent their lives out-of-doors, display accuracy in forecasting tomorrow's weather equal to or greater than the reliability of desk-made forecasts derived by the trained government observer from scientifically collected and analyzed data.

When observations of the experience type can be summarized and expressed in statistical form, a step has been taken toward their formulation into laws and principles. Individual personnel managers, for instance, observe the constant stream of new employees hired to replace those resigning or discharged, and conclude that employee turnover is excessive. This conclusion may then be refined and improved into the statistically expressed decision that employee turnover exceeding about 20 per cent annually is excessive.

The credit reporting agency of Dun and Bradstreet has worked out many such principles or financial ratios, one of which they state as follows:

> When a commercial or industrial business enterprise has a tangible net worth between $50,000 and $250,000, its operations should be carefully analyzed if the depreciated value of its fixed assets is greater than two-thirds of the tangible net worth, or if the current debt is greater than two-thirds of the tangible worth. When the net investment exceeds $250,000, its affairs should be watched closely if the depreciated value of its fixed assets totals more than three-quarters of the tangible net worth, or if the current debt is greater than three-quarters of the tangible net worth. In no case should the funded debt be larger than the net working capital. These three comparisons of balance sheet

items are outstanding sign-posts of financial strength, credit stability, and business health.[1]

Forms of Appraisal Terminology

The term "appraisal" is used in this text to describe the first step toward efficiency in management. Appraisal itself is an important element in a decision of management. It is the process of evaluating the possible merit of some new idea, method or investment. It is certainly true that a problem thoroughly understood is more easily solved. Hence, if an appraisal by a department head indicates that substantial savings can be obtained through modification of an existing method of operation, the first step toward greater efficiency has been taken. It should be followed by an executive decision that would bring about the desired change.

Even though theoretically, appraisal precedes planning in striving for efficiency, the two steps are so closely related and associated that it has been difficult to separate them in actual practice. The result has been that business executives use other terms to include both appraisal and planning. Common among them are such expressions as "estimates," "findings," "conclusions" (of research), and even "design" and "system."

In large businesses, particularly in railroads and public utilities, there is in common use a form by which executives make requests for permission to make expenditure of funds. This form is often called an "authority for expenditure." When properly filled out by a department head, it is, in effect, an appraisal of certain efficiencies in operation whether proposed or maintained. The term "estimate," and a form by that title, as used by other businesses, amounts to the same thing. Sales, production, repair or construction, inventory, and financial estimates are combinations of appraisal and planning. They are used by most concerns with varying degrees of care and effectiveness.

In government management, the term that is generally accepted is "justification." It is a written request for funds supported by an argument which sets forth the purpose and the need for a particular appropriation. In cases where the justification for the expenditure is to maintain or increase efficiency, it is an appraisal or evaluation of cost compared with the results that can be achieved.

PLANNING FOR EFFICIENT OPERATION

If an executive decides in favor of some new method, he must then plan the new process or action. The planned or proposed action of the future must be related to the objectives, policies, and strategies of the company and the tactics of the department itself.

[1] Roy A. Foulke, *Behind the Scenes of Business* (rev. ed.; New York: Dun & Bradstreet, Inc., 1937), p. 34.

This second step of planning, after appraisal has indicated that improvement in efficiency is possible by the proposed action, is the determination of the limits of good practice in connection with the change. These limits are much the same as the tolerances permitted by inspectors in factory operations. Less than a century ago, machinery made of metal was finished by hand, with accuracy or tolerance of one-sixteenth of an inch. An engine cylinder might have been considered round if it was not out of true more than about one-sixteenth of an inch.

Today tolerances used in the manufacture of moving parts of machinery have narrowed down to thousandths of an inch or less. Interexchangeability of parts is obviously dependent on extreme accuracy of manufacture, which means minimum tolerance. Because management is not yet an exact science, the tolerances that can be applied to planning a new building—machine, process, or procedure—of course, still fall far short of the fine exactness that can be achieved with mechanical devices.

If the executive's appraisal has caused him to decide to erect a new building that would permit continuous flow and mechanical conveyance of the product at lower cost, the new structure must be planned in terms of the entire business. It must be so located as to fit in with the construction plans of other departments and not clash with them. It must be constructed in such a manner that it may be readily extended as the needs of the department may require. It must be arranged for possible joint occupancy with other departments. Its cost must find its proper place in the general budget of the business. In order to realize the economies contemplated, it should not be necessary to operate the new plant at a production rate in excess of the ability of the rest of the business to absorb the output. Thus, proper planning turns a sound, well-reasoned appraisal into efficient production.

Evolutionary and Revolutionary Planning

In planning a change in operation, the department head must decide whether its effect will be evolutionary or revolutionary. Where such procedure is practicable, it is usually best for a change to take place by slow degrees and as opportunity affords. In fact, many managerial decisions can be carried out in no other way than by gradual stages of evolution.

A plan that contemplates radical or revolutionary changes in a business is more likely to be successful in its application to the physical plant and equipment than to the redesign of routines or system. It is often more economical to erect a new building than to try to reconstruct an old one to meet changed conditions. Similarly, it is often impossible to obtain desired operating economies without the purchase and installation of new machinery Progress in departmental operation has also emphasized

the importance of improvement in routines and systems. This emphasis has been due partly to the application of the technique of time and motion study and partly to the efforts of manufacturers of special machinery to sell their products. Office equipment, for example, cannot be sold unless office workers are willing and able to use it. They must be skilled in the operations of the new equipment or experienced in the use of a system which is imposed upon them by it. For nearly a century, American manufacturers have been selling machinery, both to industry and to the general public, by teaching users how to operate new devices.

Because revolution in an operating system tends to arouse resistance rather than cooperation among employees, it is usually wiser, and often possible, to accomplish change in system and routine by gradual evolutionary stages.

THE TECHNIQUES OF APPRAISAL AND PLANNING

While appraisal and planning for efficiency in management is one of the chief tasks of departmental executives in an organization, it is a more specialized and centralized function in some instances than in others. For example, for designers and methods engineers, it is a primary and highly centralized activity. For others, like sales and office managers, their supervisors and employees, to secure and maintain efficiency in their respective departments is a constant obligation that is combined with their other duties. Whether this functional activity is highly centralized or not, the techniques that are used to accomplish it are several which can be identified as more or less distinctive methods and procedures.

Research

Research may be said to be the first step toward efficiency. "Research" is the endeavor to discover, to develop, and to verify knowledge. It is a consciously planned effort to solve problems which are suggested in terms of the unknown.

In large business enterprises, there are so many unknown things that are worth finding out that separate research departments are maintained at great cost. These departments are staffed with trained experts and technicians whose investigations include applied as well as pure research. Applied research has to do with the study of problems that have a definite bearing upon existing situations. For example, in the field of electrical power, applied research has discovered how more electricity can be generated per pound of coal used for fuel in steam plants. In other words, research has increased the efficiency of steam boilers and turbines. Pure research is, in a sense, research for its own sake. That is to say, pure research is motivated by scientific curiosity aroused by the observation of an unexplained phenomenon, the contemplation of a theoretical mathe-

matical formula, or some other abstruse stimulus. The outcome of such research may or may not have practical significance. When scientists delve into the mysteries of sunspots, cosmic rays, electronics, and atomic fission, they are engaged in pure research in the first instance. Industry has often been willing to provide resources for studies of this kind because there are numerous examples that indicate clearly how the results of pure research have turned out to be extremely practical.

One aspect of applied research may be described as production research. Its purpose is to eliminate waste in the use of materials and productive effort. If applied to mechanical equipment, for example, it will attempt to find out what part of a machine wears out first in order that its durability and useful life may be lengthened by strengthening that particular unit. For a physical plant as a whole, production research helps management to distinguish between depreciation and obsolescence in order to affect the former with proper maintenance, and the latter with replacement or redesign, thus both restoring and increasing production efficiency.

Another common type of research of great importance to efficiency in management is market research. "Market research" is the study of all problems which relate to the transfer and sale of goods and services from producer to consumer. From this definition the scope of research of this character is obviously very broad. It may be used to discover which type of customers or what trade territory has been served adequately and which has been neglected; it may evolve new methods of selling, new advertising plans, or new channels of distribution for goods and services; and it can reveal what new products or improvements in old ones should be developed. The solution to problems of this kind, and many more like them, suggest how market research is an effective managerial instrument both for maintaining and increasing efficiency in the important function of sales.

These various research problems may be suggested by operating executives, supervisors, and other sources within the management group. They may also arise within a research department itself. It is a common experience to find that intensive study of one problem frequently reveals entirely new ones which may turn out to be as important as the original project.

Time and Motion Study

In the appraisal and planning of production in a business enterprise—whether the product be goods or services—standards are necessary because they provide measures of optimum performance. One such standard or yardstick has to do with the determination of a fair rate of work. In order to discover what output may be reasonably required of a worker,

the technique of time and motion study has been developed. Fundamentally, by means of it an attempt is made to arrive at a sound basis for integrating the interests of employees from the standpoint of fairness, with those of the concern itself as the latter relate to economy and efficiency in operation and effectiveness in serving the public.

Time study consists of the accurate observation, record, and analysis of the time required to perform a given task. Motion study is that phase of time study having to do with the investigation and analysis of the movements that are made by a person in doing a particular piece of work. Owing to the limitations of the human eye and the chance for error in judgment based on inexact data, precision instruments like the stop watch and motion-picture camera, as well as electrical and other devices, are used to insure accuracy in time and motion studies.

Thus a particular time study attempts to discover all available facts that have a bearing on efficiency in the performance of work. The several different steps involved in the investigational phase of such a time study are illustrated in Figure 43. This illustration describes the technique as applied to a machine shop in a manufacturing plant. The method is equally applicable, however, to time study of typing in an office, wrapping parcels in a retail store, assembling folios in a print shop, or any activity in which the conservation and wisest use of time and human effort will result in greater efficiency. Indeed, it is difficult to imagine any type of work that requires routine and system in which time and motion study, with its results properly applied, could not effect important improvements and economies.

Figure 43 shows that after the preliminary survey has been made of work that is performed in the particular machine shop to be studied, the method of study is divided into four parts. These are investigation of the mechanical equipment, observance of quality, description of product, and study of the employee at his work. The results of these four descriptive and analytical steps are shown in the lower portion of the figure in the panels labeled "method," "control," "standards," and "performance." Motion study is a phase of the time study of employee performance. Collectively, these results constitute the time study of any particular operation or task; and from such a time study is derived the task standard which is a determination of the amount of work that may be reasonably required of an employee under certain conditions.

Since this method is fundamental in time and motion study no matter what the particular job to be investigated may be, a brief elaboration of each part of it, as illustrated in Figure 43, will further emphasize its purpose and importance.

Method.—Investigation of the mechanical equipment includes a determination of the tools that are needed; what dies or jigs and fixtures or

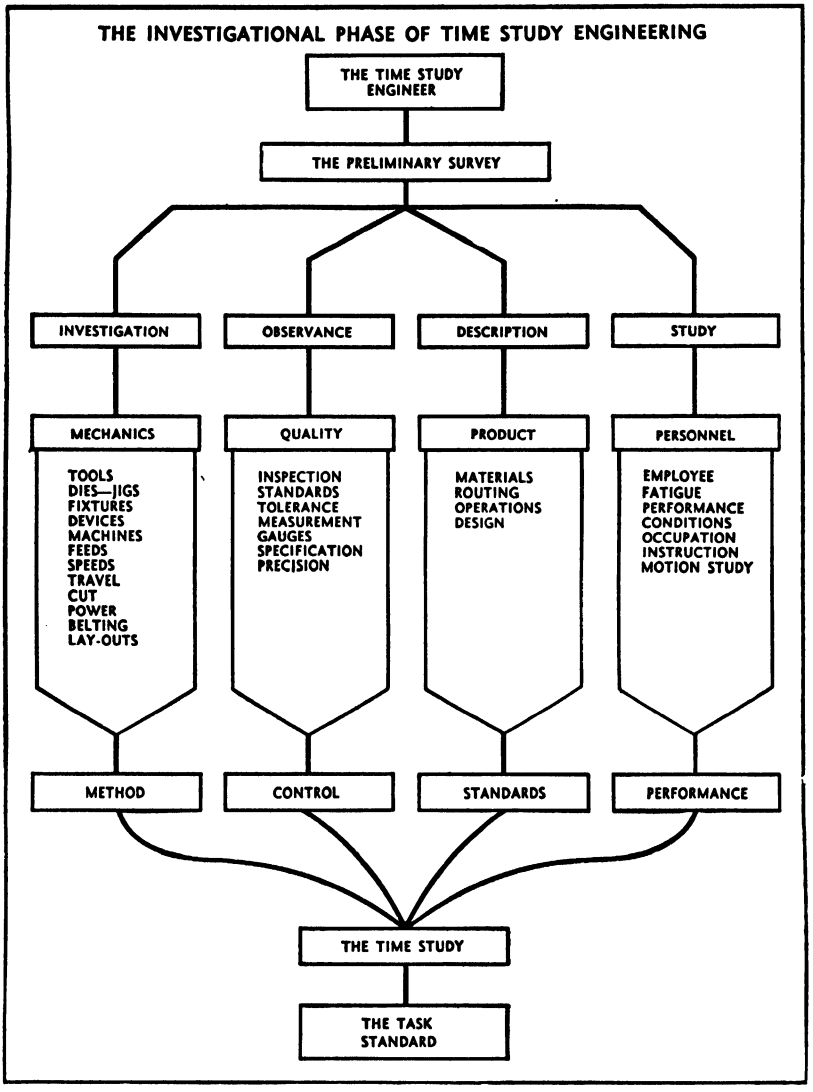


FIG. 43.—Time study engineering illustrated. Adapted from George H. Kuhl, *Proceedings of Time Study Engineering Conference, Society of Industrial Engineers* (Chicago, Illinois, February 1928), p. 18.

other devices must be used to hold the materials while the work is being done; what machines are required, and what feeds, speeds, travel, and cut adjustments must be made; what power is to be used and how it is to be transmitted; and how the work and machinery are to be arranged or laid out. This detailed investigation results in a complete statement of

the method used in production of the particular product or performance of the particular operation.

Control.—The second step is to observe all factors which affect the quality of the product or output. It includes the method of inspection, the standards of quality or of materials, the tolerances permitted, the method of measurement or gauging, the product specifications, and the precision or interchangeability of production. This detailed checkup results in a complete statement of the policies, standing orders, and supervisory methods employed by management to provide quality control.

Standards.—The third step is a description of the product itself, its method of production, including routing and processes, the materials that go into it, and its design, style, or other characteristics of form. This part of the study results in a detailed summary of the standards or specifications according to which this particular article is manufactured.

Performance.—The final step is the study of the worker and his performance. This includes the assembling of personal facts concerning a particular employee or type of employee; a study of the elements of fatigue involved in his job; a description of the operation required; an account of the conditions surrounding the job, such as heat, light, noise, and ventilation; a classification of the work; the nature of the instructions provided to the worker; and, finally, a time and motion study of the employee while he is actually engaged in the operations required of him. This detailed investigation of the employee—how and under what condition he performs his task—results in a report on personnel as contrasted with the results of the other three steps which have to do with the physical aspects of the work that is done.

Design

In its abstract sense, "design" means to sketch, pattern, or model according to a plan. As an activity of management, designing is one of the most important methods of appraisal and planning. Correct design is a contributing factor to efficiency, while the lack of it may defeat efficiency altogether.

Efficiency through correct design may be achieved in various ways. It may pertain to the proper design of a building in order that it may be constructed to provide the greatest usefulness in the purpose for which it is intended. It may have to do with machines, tools, and other equipment with the same objective in view. Design is also a factor of major importance in such matters as style, fashion, quality, and utility of products.

In most manufacturing concerns, departments of design or their equivalent are recognized as regularly established units of organization. Sometimes such a department is a subdivision of the engineering department. In other instances it is allocated to tool-making, die-making, or

pattern-making departments. Less frequently the design of a new product or the improvement of an old one may be undertaken by maintenance mechanics or by specialists employed for the particular purpose. Often consulting designers are called upon to solve difficult or unusual problems.

The range of design as a technique of appraisal and planning extends from the area of original research to competitive rivalry. In its accomplishment, therefore, design may be entirely new or it may be a matter of redesigning something already in existence. Redesigning, in turn, may be a methodical and continuous activity, or it may be spasmodic and intermittent.

Original Research in Design.—When the first airplane was built and flown by the Wright brothers, they had thereby solved a problem of original research in design. When the first skyscraper, with its steel frame and lightly constructed outer walls had been completed, its architect and builders had thereby proved the correctness of their theory of design. The new type of one story, windowless, air-conditioned and noise-proofed factory building is another example of design research.

Sometimes the purpose of design is to devise a new style or model. The automobile industry is characteristic of such designing. Its designers seek to create motor cars of new appearance and usefulness and to base their conclusions on the results of consumer research that reveals public preferences.

It also is proper to speak of "design of layout or arrangement." This kind of design is almost always derived from a study of a particular proposed layout which requires an original approach, since it will almost certainly differ from other previously designed arrangements. The designer prepares plans for the arrangement of fixtures, equipment, aisles, and stock space, to eliminate congestion and to provide for the free flow of work or customers throughout a factory, store, or office. An excellent illustration is the design of the internal layout of a cash-and-carry grocery store.

Competitive Designing.—Design is also an important factor in maintaining or improving a competitive position. A great deal of time, money, and energy is expended on design by business concerns of all types in their effort to outstrip or even keep abreast of their competitors. Examples of such rivalry are legion, but they are fundamental to both technical and aesthetic progress. If one manufacturer succeeds in producing a better automobile, radio, refrigerator, or electric razor—manifested by a wide public acceptance—it is imperative that producers of similar articles design their products in keeping with, or in advance of, those that have become popular in the channels of trade. Or if a retailer finds that he can attract customers to his store because of its arrangement and facilities designed for their comfort and convenience, other stores will be im-

pelled to follow suit or lose out in competition. Even in the field of production efficiency, this factor of competitive rivalry is a motivation for design. If one railroad, for example, is able to obtain better operating results by virtue of improved design in equipment, other railroads must redesign their rolling stock, motive power, or shop facilities in order to realize comparable economies.

Redesigning.—Business and industry are continually confronted with the necessity for redesign of plant and product. Some of this work is methodical and proceeds item by item. In other instances, it is spasmodic and undertaken only as special need for it arises. The methodical redesign of details is unspectacular; but it may contribute much more to efficiency than the design of a complete new product, new factory, or a new layout. Methodical redesign takes up each detail in turn and considers whether greater efficiency can be obtained by a redesign of the individual part. The use of improved alloy steel in making cutting tools, for example, may result in only a small reduction in the cost of production. However, if the improvement in design can make a saving every time the particular cutting tools are used, the economies realized may accumulate into a substantial sum over a period of time.

The automobile has been improved far more through methodical item-by-item redesign than through drastic or basic changes. Many of the extra accessories of former years are now standard equipment. Likewise, the simplification of the operation of an automobile has been accomplished by gradual, methodical, year-by-year improvements effected by methodical redesign of its parts.

Irregular redesigning occurs when it becomes necessary to make abrupt changes in a product or machine due to failures that come to light only through use. These failures are caused by faulty original design. The style, shape, or some other characteristic of a new product may not meet with customer acceptance even though its inherent usefulness is good. Redesigning of substantially the same article may remedy such a condition. In mechanical devices, it is not uncommon to find that the redesignment of a single part may make all the difference between a machine that is unusable and one that is entirely satisfactory. Again, an example may be cited from the automobile industry. At one time, a new model of a certain make of car included a newly developed assembly of the rear axle. This assembly was held together by means of keys or wedges. Unfortunately, these keys were not strong enough to stand the strain put upon them under severe driving conditions. When the keys, which were of soft metal, sheared through, the assembly would fail and one of the rear wheels of the car would fall off to the annoyance if not danger of the driver. A redesign of the assembly of the rear axle in subsequent models of this automobile, eliminated its faulty construction.

Standards and Specifications

A "standard" is an authoritative rule or model established for the measure of quantity, quality, weight, extent, or value. As a device of management in the achievement of efficiency, a standard, therefore, is a reliable guide to and yardstick of accomplishment. When a task performed or an article produced conforms to the specifications of the standard which controls its particular measurement, it is said to be "up to standard" and acceptable. If it does not meet such requirements, it is "below standard," and subject to revision, improvement, or rejection.

Standards are of two sorts—those that are fixed and those that are subject to change. Certain standards obviously must remain stable or the use of them would result in confusion and chaos. For example, as a standard of measurement a foot is always exactly twelve inches in length; and similarly, a pound, avoirdupois weight, invariably contains sixteen ounces. Everyone is familiar with these standards, and many others in everyday use; they need no further elaboration. But in business and industry, there are other standards which change under the impact of new inventions, new designs, and improved procedures. With these more flexible measures or tests of excellence and tolerance, the quest for efficiency is particularly concerned.

Standardization as a technique of appraisal and planning, therefore, involves the development of specifications which cover those phases of business operation in which efficiency would be difficult to achieve without tangible guides against which results can be measured. "Specifications" are statements which contain detailed descriptions or enumerations of particulars that apply to designated operations, products, equipment, or other facilities.

Standardization and Simplification of Design

After the general design of an article or product has been developed, it is necessary to define its details by preparing specifications which will control the selection and use of the materials that go into it and its characteristics when completed. These specifications, together with the design itself, then become production standards. Their purpose may be one or more of several things, such as control of quality, cost, and intended purpose. For example, if a new building is to be constructed after its general design has been worked out, it will be necessary to plan and design each of its many details. Take the item of doors. Specifications may be required for hundreds of them. These specifications will indicate the size of each of the doors, their construction, location in the building, and the quality of materials required. If it becomes possible to use one type and size of door throughout the new building, complete standardization of design will have been achieved.

As the foregoing illustration shows, specifications or standards may be developed for each separate element in design. However, it often happens that many parts can be made alike or that the same part may be used in several different products. This broader process of standardization has been called "simplification." The United States Department of Commerce, cooperating with many trade associations and research agencies, has promoted simplification campaigns in order to facilitate mass production. If every one of the millions of passenger automobiles, for example, could use the same sized tire, the mass production of tires would reach its theoretical maximum. In practice automobile and tire manufacturers have reduced tire sizes to a small number. Mass production may still approach its theoretical maximum if the number of tires required in each size is large enough to permit tire-making machinery to operate in the most efficient manner. Of course, theoretically perfect efficiency in mass production cannot be achieved, but a reduction in the variety of output through simplification in design is a step in that direction.

Similar advances have been made in the use of standards, specifications, and simplification in the field of purchasing. Purchasing agents generally buy supplies and equipment that must conform to standards and specifications that have been developed in their own concerns or, in some instances, that have been worked out by the purchasing agents themselves or by producers in their state and national organizations. By knowing exactly what is needed, unsatisfactory materials can be avoided, excessive costs prevented, and dependable sources of supply can be established.

Testing

Closely related to standards and specifications of design is the use of actual tests to determine the degree of efficiency that is realized. Design and specifications may be adequate, but construction faulty. Tests will reveal faults that may exist, or they will prove the soundness of design. The best proof that an airplane motor has been built according to specifications is its performance in an actual flight. If it develops the expected horsepower and responds to controls as anticipated, the presumption is strong that it has been properly constructed. Or if a merchant offers for sale a fabric or a paint as sunproof, the best guaranty of such a claim is that an actual test of a sample has proved resistant to the direct rays of the sun.

Standardized Forms and Reports

The purpose of establishing standards is to increase efficiency. There is nothing to be gained from standards unless some contribution can thereby be made to one of the five basic elements of efficiency—quality, quantity, time, method, or cost. This prerequisite is all too often overlooked in the appraisal and planning of forms.

A "form," when filled out properly, is a standardized internal report or record. It is always designed because some record, summary, or analysis is desired by some executive for some purpose. Unfortunately in many businesses, forms are never reviewed after having been once established as part of the office routine. Information continues to be collected and recorded long after it has served its purpose.

One of the characteristics of business development has been the increased cost of office operations as compared to the principal or functional operations of a business. One of the chief sources of such increases in cost has been the steady accumulation of reports and records required of the office.

To counteract increasing office expenses, one successful organizational device is the establishment of an office methods committee. Through careful study and analysis of needs and purposes, such a committee can restrict the addition of new forms or the data requested on existing forms. It can discontinue unnecessary records and combine those that are closely related to one another. The committee can give consideration to other savings by redesigning forms, reducing the number of copies required of them, and the selection of inexpensive paper. Finally, it can coordinate forms and office system or procedure so as to secure maximum efficiency.

Standard Costs

In most large businesses the development of standard costs is a required responsibility of their respective accounting departments. These costs may apply to individual items or specific operations. They are estimated costs derived from a normal rate of operation under normal conditions of production. Standard costs provide a basis for the control of actual costs even though the latter may be greater or less according to prevailing conditions.

Since standard costs reflect normal operating conditions, in a business where production and sales are both major factors, actual costs that are below standard tend to be caused by a sales volume that is above normal; and costs that are above standard will be due to a sales volume that is below normal. Management can often use this comparison to great advantage in securing a closer balance between supply, operation, output, and sales.

Task Standards

The purpose of the establishment of task standards is twofold, namely, to determine a fair rate of work and to promote efficiency in that work. Consequently, such standards are significant to both the employer and the employee. If, by means of time and motion study, it has been found

that a certain job can and should be performed in a given way in a specified length of time, the standard thus devised is valuable only if the results are profitable to the business and, at the same time, favorably affect the morale of the workers involved.

Task standards can also be evolved without a formal time study. For example, if the results of market research show that a certain sales territory, with reasonable sales effort, can and should produce a certain volume of business, this sales volume becomes a standard called a "quota." The quota is valuable only if its establishment produces more profitable sales for the business and, at the same time, provides a stimulus to the sales force through increased returns to its members. The use of quotas in this manner is a common practice in insurance companies.

Therefore, task standards have their significance for reasons of both efficiency and incentive. It is doubtful whether these two objectives can be separated under any circumstances in the long run. The most efficient worker at any level of an organization is the one who does what he likes to do; who takes satisfaction in the product of his labor because the efficiency of his performance is recognized both by himself and his employer; and who is motivated by the promise of reward or advancement either in his present task or in some other. The basic purpose of task standards is to discover, prepare, and teach better methods of doing a job to the end that all may profit who are concerned with it.

METHODS ENGINEERING

An outgrowth of scientific management of which Frederick W. Taylor was the founder has been the creation of a new and distinct functional division of management called "methods engineering." Methods engineering undertakes to provide standards, systems, methods, and plans of routing for work in process. The point of view of the methods engineer is that there is a "best way" to perform any particular task. This best way is constantly changing because it depends upon many conditions. Hence, the principal activity of methods engineering is concerned with the discovery of the one best way to do a job in a given environment under prevailing conditions and to teach the method of performing it when that method has been determined.

In the early years of the scientific management movement, many methods engineers sought for perfection, that is, the one best way under ideal conditions. This approach to the achievement of highest efficiency was unrealistic, since perfection may not be realized in an imperfect world. No business can hope to have perfectly trained employees who perform their tasks with perfect equipment under ideal circumstances. In actual practice, therefore, the methods engineer seeks to achieve the one best way with attainable qualities of human skill, equipment design, and

the conditions of work. It follows that methods engineering is constantly evolving in its attempt to realize the highest degree of efficiency in processes and methods.

There are three fundamental objectives of successful methods engineering: they are to discover ways and means of making constant improvements in employee skill, machine productivity, and the movement of material.

Employee Skill

Methods engineering is concerned with continued improvement of human skill. No matter how automatic the machines and other equipment may be, the human element cannot be entirely eliminated from productive processes. Indeed, there is much work to be performed in all occupations in which efficiency is dependent upon the essential skill of the worker. Time and motion study is the standard tool of the methods engineer as he seeks to improve the proficiency of employees. The best use of time and energy is his goal. How time is consumed in performing a given task is revealed by means of a trained observer equipped with scientific timing devices whereby an accurate record and analysis can be made of the time required to perform given operations under certain conditions. High speed is not necessarily the ultimate goal of such study, for haste can also make waste. The objective is again the "best time," an optimum or balance between speed that results in errors, breakage, and undue fatigue and dilatory movements that consume time without compensating results.

Motion study is a refinement of a phase of time study. The passing of time cannot be controlled; it is inexorable, but how human energy shall be utilized in a segment of time is subject to direction and regulation. So the methods engineer uses motion study, combined with, and as a part of, time study, to find the "best way" to perform an operation. Slow-motion pictures have been used successfully to reveal lost motion, which is unproductive effort; and unnecessary motion, which results in the same thing. Again rapidity is not the crucial test. It is rather the conservation and wisest use of human effort. The most efficient way of doing a thing is usually the easiest as well as the most profitable way.

Psychological tests are becoming a further refinement, beyond and supplementary to time and motion study. Physical skill is often conditioned by mental aptitude. Some skills require constant concentration, while others can become automatic. It is obvious that the same person may be incapable of becoming efficient in both types of activity. Therefore, when other analyses have shown by time and motion studies what movements, and at what speed, are required for optimum efficiency in a given task, well-chosen psychological tests can assist in the selection of employees who should be assigned to perform it.

Machine Productivity

Machine productivity is determined in part by the skill of operators and in part by such factors as the speed at which equipment can be run with safety and the idle time due to breakdowns, repairs, adjustments, and change of materials. It is the function of the methods engineer to increase machine productivity by all the means that are available. One of the marked improvements that has been made in this connection has been a change in the transmission of power in factories. Once this was done almost entirely by means of overhead shafting from which moving belts transmitted power to separate machines. Modern methods have substituted the electric cable for shafts, pulleys, and belts. Individual machines are equipped with separate electric motors. This improvement not only saves power, but it also increases productivity because each machine can now be operated at its own best rate of speed.

Another great improvement, likewise made possible in large part by the use of electricity, is the reduction in time required to change material and to make adjustments. Mechanical devices for feeding the machine and for performing several operations simultaneously, all cut down the amount of time the machine has to be idle.

Movement of Material

One of the greatest contributions of methods engineering has been in planning efficient movement of material. The story is told of the evolution of the modern tag-making machine, beginning as a series of machines—one to cut the cardboard, another to print the shipping tag, another to punch and reinforce the hole in the tag, and another to insert the string. Each machine had to be fed and its production removed and carried to the next machine. Today all the machines are combined and produce from cardboard, string, and ink printed shipping tags, boxed and ready for sale.

As this tag-making illustration shows, the ideal method of moving material is within and by the machine itself. Material movement is then perfectly coordinated with production and takes place at minimum cost. This concept of completely self-contained machines, each encompassing one entire process or article, is carried to its logical conclusion when an entire factory is constructed to house one such machine or mechanism.

Development of mechanical conveyance of work-in-process has come about in order to approximate perfect movement of material, as within a machine itself. The production lines of an automobile plant are an example. All production flows toward the assembly line, there to be combined into finished automobiles ready to be driven away to the delivery area.

Methods engineering has to do with every aspect of the business. In

the field of selling, for example, there is growing attention to the problem of teaching the salesman the "one best way" to sell his prospective customers. By means of movies, diagrams, or oral discussion, the salesman is taught the best way to make his presentation, to answer arguments, to demonstrate his product, and to close the sale.

Standardizing Office Work

Methods engineering employs the techniques of appraisal and planning to standardize, systemize, and route work of every character. Such methods are as important to office work as to the operations of a store or factory. In the case of the work in an office, methods engineering seeks to increase efficiency by making a detailed study and analysis of the activities of all clerical employees. Particular stress is laid upon elimination of waste of time. To that end, the contributions to office efficiency may be illustrated by the following improvements for which methods engineering has been largely responsible.

By grouping activities that are similar in character, increased skill has been developed and loss of time has been avoided. An example of this accomplishment is the establishment of the central stenographic pool where all typing is done by skilled specialists. When dictating and transcribing machines are used in connection with such a pool, much time is saved by omitting the services of stenographers to take dictation in shorthand.

Like a factory, an office also has its main route of production. By properly routing the flow of work, time has been saved that otherwise would be unproductive as employees have been required to wait upon one another for tasks to be completed. Therefore, methods engineering has sought to develop an efficient office arrangement to make it possible for successive stages in the work to be performed at desks or other facilities located next to each other. By this simple and logical plan, time is saved in the movement of both persons and materials.

Much of the work in an office is repetitive. To save time, machines have been introduced to perform such processes. Duplicators, machines for addressing, sealing, applying postage, and opening envelopes are examples. Other standard mechanical office equipment in wide use are calculators of many kinds, posting and billing machines, automatic punch-card sorters, tabulators, and printing machines. All of these devices have been developed not only to speed up the volume of work that increasingly must be handled by office employees but to increase accuracy and to remove much of the drudgery and strain to which the personnel is subjected.

A minor improvement in office methods, but none the less important, has to do with the preparation and use of forms. In redesigning forms to increase efficiency, spaces for unnecessary or extraneous data are left out.

Also, the lines to be filled in by typewriting are spaced to conform to the roller-spacing intervals of a standard typewriter. By so doing the movement of the paper from one line to the next can be accomplished by the typist without the necessity of extra hand adjustment. Another improved detail is the interleaving of rolls of forms with carbon paper so that each new set of forms may pass automatically into a typewriter or posting machine, ready for manifolding.

Systems and Methods

An attempt is sometimes made to draw a distinction between systems and methods in achieving efficiency. Too often this effort results in a mere play on words, and is, therefore, of no importance. In general, where a difference can be discerned, system implies an orderly sequence in accomplishing work. Thus the steps involved in keeping a record of accounts may be properly called an "accounting system." "Method" is a synonym of system; it can mean both process and arrangement. In a mechanical process such as an assembly line or a materials elevator in a factory, it is customary to say that the conveyor belt "method" is used. However, as technical advancements increase the mechanization of operations, the distinction between system and method becomes pointless.

The methods engineer, by that or similar title, has come to be recognized as an important member of the management group in modern business. His designation is accurately descriptive of his function. It is broad enough to cover the techniques of standardization of design and specifications, the improvement of systems and methods, and the planning and routing of the flow of work. As such, the modern methods engineer has supplanted the speed boss, efficiency expert, and other so-called "scientific management engineers" who, in the past, have often been looked upon with disapproval.

THE CONTROL OF EFFICIENCY

Control is a function of management that has both positive and negative characteristics. In its positive aspects, it is the purpose of control to secure and maintain acceptable productivity from all the resources of an enterprise. In a negative sense, it is the purpose of control to prevent and reduce inacceptable and incorrect performance. Control may be likened to steering an automobile, ship, or airplane. Such vehicles are worthless, if not dangerous, conveyances when steering fails or is absent. Steering gear is designed not only to keep a vehicle on a chosen and purposeful course but also to permit avoidance of hazards and obstacles in the way.

Control through Leadership

The orders, directions, and instructions prepared by the several departmental heads of a business exert positive control over supervisors and

employees. There can be no doubt that the proper preparation of detailed instructions and the elimination of all possible conflict between orders issued by several superiors to one subordinate result in effective control, and, therefore, in efficient operation. But there is another phase of leadership that is also a positive method of control. It is the psychological influence of the personality and behavior of a superior upon his subordinates.

Personal leadership by the top executive is difficult, if not impossible, in many organizations, especially in large concerns. It is important to retain such leadership as much as possible, but the size of a business may require that management at the top give its primary attention to such other matters as policy and coordination. It then becomes necessary to exert personal leadership at the departmental level of management in order to retain to the fullest possible extent its salutory effect upon morale.

Personal leadership for efficiency in operation can be exercised by both precept and example. If office hours begin at nine o'clock and the department head habitually arrives at eight-thirty, his example of this detail of leadership will result in a favorable influence upon the punctuality of his subordinates. If the department head "pitches in" when an emergency arises and demonstrates not only his own skill but also his loyalty to the interests of his company and his willingness to work overtime or to endure unpleasant conditions and even hardships, other employees will take notice of him and tend to follow his example.

Leadership means more than exerting influence over employees. It also means having dominance over them. When a leader controls a group of human beings, as a departmental executive controls his subordinate supervisors and employees, that means he has imposed discipline on them and can exact obedience. Discipline is impossible unless the subordinate accepts the dominance of his superior.

Control through Inspection

The negative aspect of control is to prevent, restrain, and minimize carelessness and mistakes in the performance of work. This duty is the function of inspection in all its various aspects. Inspection, to be worthy of recognition as a technique of management, must have for its purpose something more significant than mere snooping, spying, or invidious criticism of employees and their work. Instead of creating embarrassment and ill will, it should be helpful and stimulating, stressing its main objective, namely, better productivity for the benefit of all concerned.

So far as any single department in an organization is concerned, there are two types of inspection—external and internal. This distinction is based on the principle that a person vested with the authority to inspect must not be subject to the control of one whose department is to be inspected. In other words, activities that check each other must be sepa-

rated departmentally. This is the external aspect of inspection. Its internal side is the unquestioned right and duty of the top executive and his major executive assistants to inspect the work of any subordinate department. By so doing, they are, in a sense, inspecting themselves because they are responsible for all the activities of the concern. Honest critical self-examination is to be desired; it is seldom overdone. The fault, if any, is rather its neglect.

An important skill which must be developed by the departmental executive is ability to sense the need for internal check-up or inspection within his own department. Executives of long experience develop an almost uncanny sixth sense. They seem to know that something is about to go wrong. To the astonishment of their subordinates, they turn up and begin to ask questions about this or that mistake or difficulty. The executive who has this type of ability to sense trouble has no difficulty in gaining the support of his subordinates who look up to him as their leader in fair weather as well as in foul.

The following examples may serve to further clarify the distinction between external and internal inspection. When the board of directors or top executive employs an outside firm of certified public accountants to audit the books of account, the result is an external inspection of methods and results of the work done by the accounting department of the business. When the inspection department of a factory is set up independently of the production department, both reporting to the major executive in charge of production, the result is external control of the quality of production. Such control restrains the production department from accepting a poor quality of work; or by evidences of approval, it may verify satisfactory production. On the other hand, when a particular department checks up its own performance or output, it establishes methods of internal inspection.

Control through Forms and Records

Forms and records are important devices of control. They contain data by which significant comparisons may be made for purposes of appraisal. An analysis of recorded information also aids in the formulation of standards, or it may serve to check performance against the past or against standards already set up. Comparisons and standard measures of proficiency are indispensable in the proper evaluation of actual performance in terms of attainable quality, rate of output, and methods of production.

THE CONTROL OF EFFICIENCY ILLUSTRATED

The many problems encountered that require solution in the control of efficient operation may be illustrated by using field selling as an example. By "field selling" is meant the sale of goods by traveling repre-

sentatives of a concern who call upon customers in designated sales territories.

The difficulties involved are many in exercising effective control over the work done by the traveling representative. Studies that have been made of the distribution of his time show that only a small fraction of each working day is spent by the salesman in productive solicitation of customers and personal interviews with them. Nevertheless, fieldmen average much longer hours of work, including the time spent in travel, than is considered reasonable for office and plant employees.

There are practical obstacles that make impossible complete control over the daily routine of work done by the field salesman. It is not possible to specify exactly the individuals he should see each day, nor the time of each call, nor the length of time allotted for each call. To give the traveler each morning such an outline of his current day's work would require ability to foresee chance events. If train or bus transportation is to be used, one day's work will begin at 8:30 A.M., the next at 11:00 A.M., and the next will necessitate an overnight Pullman ride. If the salesman is to use his own car, the delays due to tire and motor trouble or to weather conditions are equally variable. Similarly, the number of customer calls that can be crowded into a day can be averaged, but it cannot be laid out in advance for any one day.

Control of the Day's Work

The smallest unit of time that can be controlled is the day. Control of the day's work is sometimes accomplished by means of a fixed or predetermined route. The salesman, acting under general instructions from his superior sales executive, outlines in advance the route for each day of the coming week. This outline consists principally in the names of the towns and cities proposed to be covered on particular days, and the name and location of the hotel where the salesman plans to spend each night and to which mail and telegrams should be addressed. Once agreed upon by the salesman and his executive, the fixed route must be followed unless some emergency arises, which must be reported promptly to the home office. To be off a prearranged route without permission is similar to unauthorized absence of factory or office workers from their places of work.

To aid in bringing about effective control, detailed information may be prepared by the sales department and forwarded to the salesman in time for use. Such information includes the latest revised classification of all customers and prospects within the geographical area to be covered during an ensuing week.

Suppose, for example, that the salesman is to spend Wednesday night at the Acme Hotel in Smithville and that he is to call on customers and

prospects within subterritory 102 during Thursday, driving on to Jamestown to remain that night. Subterritory 102, prior to the salesman's calls, might show the following situation:

Known prospects with good credit rating	12
Prospects never called on by salesman	1
Called on last trip	7
Called on during year, but not on last trip	4
Customers considered active	10
Customers called on last trip	5
Called on previous trip, but not on last one	4
Called on during the year, but not recently	1
Customers considered delinquent	2
Total possible calls on prospects and customers	24

With this current classification of each of his twenty-four customers and prospects before him, the salesman will presumably plan his day's work on a balanced basis. His best customers must receive preferred attention and must be called on every trip through the territory. Delinquent customers must be contacted in an effort to obtain payments and to restore accounts. Important prospects must be interviewed. At the same time, no prospect or customer may be overlooked for too many months.

Control by Reports

In addition to reports from the sales department to the field salesman, there must be reports from the territorial representative to the home office concerning his activities. These usually take the form of a single sheet or form for each call on each prospect or customer, and give the name and address, the date of the call, and the results in terms of orders, quotations requested, or invitation to call again.

This regular flow of reports from the sales department to the salesman and from him back to headquarters, built around the prearranged route being followed through the territory, tends to control the quantity of work. If the salesman fails to keep up his average number of calls, or if he disappears for a day, the zone manager or sales correspondent assigned to his territory is quickly aware of the change in efficiency and output of work.

The most important measure or yardstick of the work done by the salesman is the volume of sales produced by his territory. This information must be interpreted, however, in terms of the stage of development of the territory. A relatively unexploited territory can only be developed to full production through prolonged solicitation. A second measure or yard-

stick of the work done is the volume of probable annual sales added by the salesman through solicitation of initial orders from prospects.

Records furnished to the salesman and required from him must be kept simple and not voluminous. Most salesmen must use an hour or more each evening in studying the instructions and records from headquarters and in preparing reports and writing up orders to mail to the office. It is easy to make the so-called "paper work" overshadow in volume and in apparent importance the real task of the salesman, which is skilled solicitation of business.

The most valuable special reports commonly required of salesmen have to do with lost customers and with prospects. Somewhat detailed statements by the field representative of the reasons why a former customer now refuses to buy are of great value to the sales department. Such reports reveal product weaknesses, unnecessary price differentials, and measure the efficiency of advertising and of the work of the salesman himself. If the turnover of customers is high so that new purchasers must constantly be discovered to take the place of former ones who are no longer willing to buy, sales cost is likely to become excessive.

The records of the sales department as to who are the potential customers of the future are never absolutely accurate. Concerns come into existence, and others go out of business. Marketing channels shift, opening up sales opportunities with new groups of buyers. To keep the prospect list up to date, the traveling salesmen are commonly asked at intervals to take censuses of their territories. Such a census of a given trade area becomes the basis of an appraisal of a salesman's productivity, and hence aids in control of his efficiency. When compared with existing sales records, it will show how well the territory is covered. It also supplies accurate lists of names and addresses to which advertising material can be sent by the sales department in order to keep in touch with the entire market, prospects and active customers alike.

APPRAISAL OF EXECUTIVE PERFORMANCE

While stress has been laid on the importance of efficiency at the level of operations, and of the methods for measuring it, efficiency cannot be taken for granted among top and major executives of management. Failure to be efficient there is just as prevalent as anywhere in an organization, and generally more disastrous. It was pointed out in Chapter II that the largest percentage of business failures is generally attributed to poor management.[2] This condition can only mean a lack of ability, negligence, or some other aspect of inefficiency on the part of those who are charged with the responsibility of making managerial decisions and directing and supervising personnel. These weaknesses need to be detected and corrected with as great vigor as do those that prevail in the work of employees.

[2] See p. 38.

Business Longevity

The seriousness of inefficient, and therefore ineffective, executive management of business is reflected in the findings of studies of business mortality. Twelve years was the average age of a retail outlet operating in the United States in 1939. Moreover, it was found that there is a close correlation between age and sales volume. That is, older stores generally enjoy

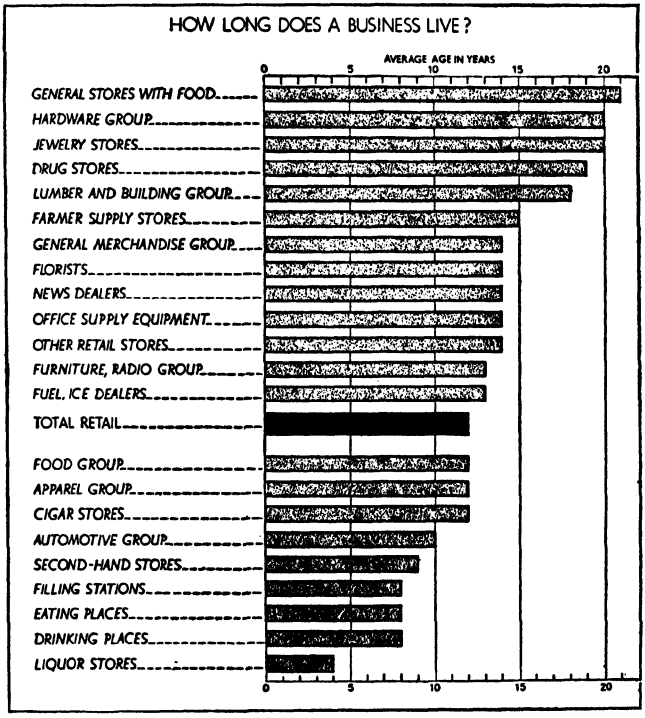


FIG. 44.—Average age in years (horizontal scale) of retail business establishments, 1939. From Dun & Bradstreet, January, 1947.

larger total sales than do younger establishments. These tendencies are graphically illustrated in Figures 44 and 45.[3] To which may be added: "The concern under sound aggressive management weathers the storm, but the one under weak, unskillful management joins the daily obituary list of business enterprises."[4]

[3] From a graphical publication entitled *Business Longevity in the United States* (New York, January 6, 1947), prepared by Dun & Bradstreet from figures made available by the U.S. Department of Commerce from the censuses of business of 1929 and 1939.

[4] Foulke, *The Sinews of American Commerce* (New York: Dun & Bradstreet, Inc., 1941), p. 379.

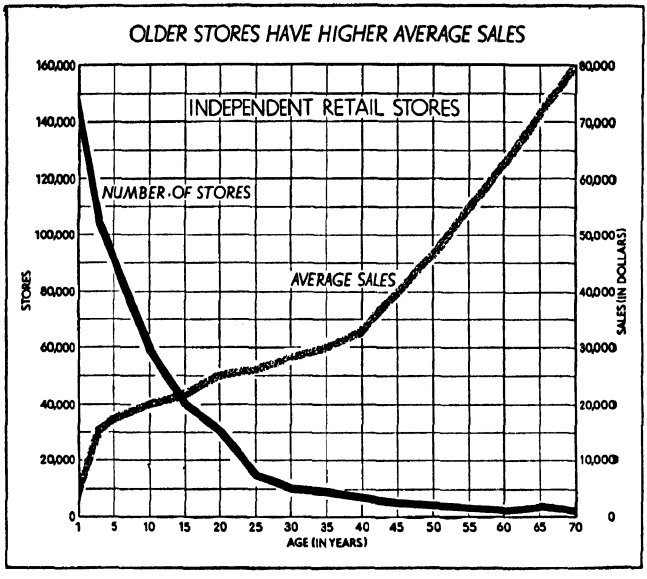


FIG. 45.—Correlation between age and sales volume in retail business establishments, 1939. From Dun & Bradstreet, January, 1947.

Appraisal of Executive Proficiency

In order to be healthy and to operate at maximum efficiency, it is necessary for an organization of any considerable size to provide for the appraisal of executives in the upper levels of management as well as supervisors and employees at the levels of production. The training and appraisal of foremen and workers has long been an established practice. Such programs present no great difficulties because the training offered has specific application to the tasks involved. It can be put to use and absorbed by the individuals while they are actually working at their jobs. Furthermore, as we have seen, the performance required of them is subject to tangible measurements, and their efficiency can be rated according to standards and, in most instances, material output. An appraisal of executives whose time is consumed with the formulation of policies, coordination, and other forms of decisions is more difficult. Neither the procedures nor the productivity of such executive acts lend themselves to quantitative measurements, as far as individual performance is concerned. Also, the effectiveness and value to the business of a particular executive act may not become apparent immediately but may take time. These are some of the obstacles to the systematic appraisal of executive performance.

Since the measures of executive proficiency are more or less intangible, they must of necessity be couched in terms of the "manifest qualities of leadership." That is, they are "qualities" that are observable and that can

be evaluated by their presence or absence in an individual as they find expression in daily conduct. There are well-defined ways in which high quality of executive accomplishment shows itself. One analyst of executive appraisal has listed five such characteristics.[5]

Tests of Executive Proficiency

The first quality is described as a "quiet swiftness," which is characteristic of the executive who gets his work done with dispatch and promptness, but without noise or fuss. It is a mark of mastery of careful planning, painstaking coordination, and efficient utilization of available resources.

The next quality is "smoothness of operation." In this respect the proficient executive may be compared to an efficient machine that operates without friction, vibration, or breakdowns. It performs its work smoothly because it is built of materials that can stand the strain put upon them. It is set on a firm foundation, and its bearings are properly designed and lubricated. Such a machine carries its load with apparent ease. So also, the able executive carries on evenly and steadily without crises in his department because he is completely aware of departmental happenings and has command of every detail under his jurisdiction.

Another characteristic is "ready responsiveness." It is not a pose but rather a temperamental quality that precludes hesitation in tackling any task, however difficult or baffling, that may be properly assigned to him. He is not disconcerted because the going may be hard.

The latter spirit is reflected in another quality, the "habit of advancement" in all departmental affairs. It is a manifestation of an executive's concern with the "best way" of doing things, to use the terminology of the methods engineer. He considers an improvement in efficiency which is already high a normal rather than an exceptional accompaniment of his job.

Finally, a characteristic of the proficient executive is "discipline in personal relationships." This quality is reflected in three ways: first, in the mastery of his relationships with his subordinates; second, in his attitude toward coordinate executives or persons of equal rank; and third, in his ability to take orders from superior authority.

All these traits are conducive to confidence, understanding, and reliance. Self-discipline is a prerequisite to the discipline of others. A department head must be the symbol of authority to his employees; but until they have sufficient confidence in him to go to him for advice on personal matters as well as those that have a direct bearing on their work, the executive has not achieved full strength as a leader. Personal discipline

[5] E. H. Schell, *The Technique of Executive Control* (New York: McGraw-Hill Book Co., 1934), pp. 218–21.

is, likewise, an important factor in the relationships between executives of similar status. Loyalty to the firm and pride in performance tend to draw such persons together into a common understanding that saves time in conferences and avoids internal politics. Mutual praise, openly expressed, is not to be expected; but when mistakes are made and differences in opinion appear, they are accepted as such as long as motives remain unquestioned. When an executive is recognized for his proficiency, the relationship between him and his superior becomes one of respect and reliance. Formality and austerity tend to disappear to be replaced by a feeling of mutual trust and friendliness.

Criteria for Executive Promotion

The tests of executive proficiency are also the criteria for promotion. Executive ranks are continually depleted because of disability, retirement, and other causes. Such vacancies call for replacements. Since the selection of those persons best qualified for advancement obviously depends upon the appraisals of other executives, many companies have attempted to remove guesswork, prejudice, and favoritism by establishing training programs and other such criteria as the bases for promotion.

An example of a plan for executive development is one that has been adopted by a large electric utility.[6] A study of the major executive positions in that company showed that they were occupied by officials who were men of wide knowledge and experience in all phases of the business. Obviously, it would be necessary to find men of comparable qualities to succeed them. Furthermore, it was an accepted policy that advancement in the company should follow a plan of internal upgrading. But junior executives, however proficient in jobs limited by the function of specialized departments of a large concern, would have little chance of being qualified for managerial authority and responsibility in advanced positions that required a well-rounded background of knowledge and experience. To correct this condition and to insure the presence within the organization of a body of executives who would be adequately equipped to assume higher ranks when occasions demanded, an executive training program was adopted and put into effect.

The plan is simple. It consists of a systematic rotation of executives and high-ranking supervisors among the various departments of the organization for suitable periods of time. No formal rating is required on the men who are involved in the program, but written statements are submitted at the end of each assignment by the vice-presidents or department heads to whom the men have been sent. These statements review

[6] This plan is described in detail by D. S. Sargent, Senior Assistant Personnel Director, Consolidated Edison Co. of New York, Inc., in American Management Association, *General Management Series No. 133* (New York, 1945), pp. 16–25.

and evaluate the work of each so-called "executive trainee." The written reports are supplemented by discussions in executive conferences. As a consequence, officials who have the authority to recommend or make promotions have a personal knowledge of the qualifications of executives in subordinate positions who are available for advancement.

The results of this plan are reported to have been successful in achieving the objectives contemplated. The joint appraisal of the rotating executives has been fair. Opportunity has been afforded to scrutinize men in action as they have been given the chance to gain an understanding of the problems of departments other than their own. As they have shared in these many diverse problems, they have tended to find solutions that have been in the best interests of the company as a whole rather than to make decisions that have been favorable to single departments alone. Men who could be identified by their versatility, capability, and executive competence have been automatically sifted from those who have lacked these qualities, which is the process of appraisal in the plan. They have emerged from obscurity to a place of recognition, which is the first step in promotion.

Criteria for Promotion in Higher Education

A counterpart of appraisal and criteria for promotion in industry is to be found in institutions of higher learning. Members of college and university faculties by long tradition have been classified by ranks which have generally determined status, salary, and tenure. Characteristically these ranks have borne the titles of instructor, assistant professor, associate professor, and professor, in that ascending scale. For those who have chosen the profession of academic teaching as careers, the advancement from one rank to another is obviously a matter of serious concern. Likewise, for administrators who have the authority and responsibility of confirming such promotions, these decisions are of grave importance if individual injustices and errors in judgment are to be avoided. Therefore, leading institutions have studied the establishment of sound and fair criteria for promotion as thoroughly as any aspect of college and university management. They know that the absence of such standards is likely to lead to favoritism, snap judgment, and mere expediency.

As an illustration of the type of appraisal made, the following criteria have been taken from a statement of policy of a western university. Of first importance are two tests, namely, effective teaching and research or creative work. It is stated that these factors are of equivalent significance in a first-class university. Then follows a consideration of academic degrees which, though not entirely adequate, serve to indicate a certain mastery of a field of specialization. Next are publications and similar works which are recognized as objective evidence of proficiency. It is

added that "in considering the individual for promotion, evidence of capacity for future usefulness is of prime importance."[7]

In addition to the character and quality of the professional activities of a faculty member, his contributions to the administrative work and welfare of the university and his services as a citizen of the community, state, and nation, are also taken into account. Length of service is also recognized as significant, although secondary in importance. Promotion is mainly contingent upon a satisfactory record according to the other criteria.

THE SIGNIFICANCE OF EFFICIENCY

Although each is clothed with its own individuality, all enterprises are alike in that they are concerned with the primary purpose of efficiency in operation. Since efficiency in operation is essential to successful management, the basic principles and techniques of planning and appraisal may be applied to any organization. Naturally, the emphasis upon the different aspects of efficiency varies with different concerns and institutions and the departments within them because their objectives are not identical. Likewise, there is a difference in policy, supervision, motivation, and leadership. Yet, while policies, objectives, and procedures may vary, the fundamental processes of efficient management remain the same.

QUESTIONS

1. Distinguish clearly between each of the following terms:
   a) "Efficiency" and "parsimony."
   b) "Efficiency" and "economizing."
   c) "Appraisal of efficiency" and "inspection of production."
   d) "Appraisal of efficiency" and "authority for expenditure."
   e) "Appraisal of efficiency" and "planning for efficiency."
2. Assume the case of an automobile mechanic who has little knowledge or experience in the theory and practice of business management, who, nevertheless, as owner-manager as well as mechanic, decides to open a repair shop. Consider the following somewhat typical problems which confront a man in his situation and suggest solutions to them:
   a) This owner-mechanic soon finds that he is unable to perform a certain type of motor repair on what he regards a profitable basis unless he charges much more than the price suggested by a well-known automobile company for such work. Explain how the "deadly parallel" system of appraisal by comparison might help him to reduce his own costs, and hence his charges, for this kind of work.

[7] University of Colorado, *General Criteria for Faculty Promotion.*

b) As a dealer in a few products related to his automobile repair business, this shop owner buys a barrel or drum of radiator antifreeze solution which he offers for sale at the manufacturer's price per gallon. When his supply of the liquid has been completely sold out, he discovers that he has not sold as many gallons as the purchase invoice stated the drum contained upon delivery to him. Upon further investigation, he also finds that this discrepancy probably has been due to his having used improper and wasteful measuring devices in selling this article to customers. Explain how this experience illustrates the survey method of appraisal of efficiency. How should this dealer solve this problem in the future?

c) After some years of modest but profitable operations, this owner-manager is called upon by a traveling salesman who attempts to sell him a stock of automobile tires. He resists the salesman's urgent selling arguments on the ground that such expansion of his small business would deplete his cash resources and leave less than $2,500 in his bank account. He states that he has never allowed his bank account to fall below $2,500 and that he attributes his business success to this policy. Show that the owner of this shop is applying the yardstick method of appraisal of efficiency to his operations; that he may be in error in his conclusions because he has not taken into account the effect of expansion upon inventory turnover, and hence the validity of the measure of the yardstick is doubtful.

3. The term "yardstick" may be considered to be general in its meaning and to include the concept of "standard." It is also possible, and perhaps more valid, to consider that the terms used by management in referring to appraisal and planning techniques form a scale of values ranging from the application of judgment at one extreme to the application of highly scientific procedures and devices at the other. On the basis of such a scale of values, arrange the following sets of terms in a descending order and include enough explanatory discussion to make your reasoning clear:

a) Applied product research.

b) Pure (theoretical) research.

c) Time study.

d) Motion study.

e) Original research in design.

f) Competitive designing.

g) Office forms.

h) Psychological tests of aptitude.

4. Rewrite the following sentences and show by your choice of words and composition that you have discerned the correct and proper shading of meaning that distinguishes "evolutionary" from "revolutionary" methods of planning when applied to changes in policy or procedure:

a) A three-story building housing a small business burns down. The presi-

dent of the company decides to use the insurance money to build a modern one-story, windowless building in which a new type of machinery will be installed because he believes in the slow and orderly evolution of his concern.

b) In announcing to all concerned the establishment of a central filing room and stenographic pool whereby one group of office workers will supply the entire correspondence requirements of all the executives in the company, the office manager calls this change a revolutionary step forward toward greater office efficiency.

5. Include the terms "centralize," "decentralize," and "recentralize" in an explanation of the effect of executive authority to plan upon a business organization in each of the following situations which involve changes in departmentation:

a) The establishment of a new department of market research.

b) Instructing salesmen to "go out and get the orders," but leaving them to perform market research in their own way.

c) The establishment of a system of job classifications, i.e., based on an analysis of job specifications, all jobs are grouped into a small number of classes, each class requiring much the same degree of skill and training, and each one carrying the same levels of compensation from starting to maximum pay.

d) Authorizing each foreman to determine the compensation of each employee assigned to his particular supervision.

6. The formation of the characteristic shape of pretzels before baking is a process that must be performed by human hands because no machine has yet been devised that can bend a strip of dough properly. Hence, pretzels are shaped by women who work beside a moving table upon which dough is carried in front of them. A skilled worker is said to be able to twist a "stick" of dough into a raw pretzel, ready for salting and baking, in two seconds. Such a worker will attain an average production of five thousand raw pretzels per working day. Assuming a study were to be made of this process in the interest of increased efficiency, show how time study with respect to method, control, standards, and performance as illustrated in Figure 43 and explained in the sections of the text related to that diagram, can be applied to the operation of a pretzel-bending production line.

7. Distinguish clearly between the following techniques of appraisal and planning:

a) "Standardization of design" and "simplification of design."

b) Testing by wearing out to destruction in order to reveal faults and testing at the beginning or during use in order to prove proper assembly and operational soundness.

c) Standardized forms and standard costs.

d) Rule-of-thumb task standards and the "one best way" of methods engineering.

8. In the production of shipping tags, the one best way of manufacture seems to be to combine all mechanical processes in one machine into which are fed ink, string, and cardboard, and from which cartons of finished shipping tags emerge. On the basis of this illustration of methods engineering, answer in some detail the following questions:
   a) Why does the elimination of the operations of lifting, carrying, refeeding, and assembly otherwise necessitated by adjacent machines, usually result in greater efficiency?
   b) Would increased efficiency result if there were a marked difference in the rate at which successive operations are performed, which difference cannot be overcome without slowing down the continuous machine operation?
   c) Why do psychological tests offer possible ways to improve selection methods for repetitive machine operations?
9. Explain how the control of efficiency may be realized through each of the following means:
   a) Leadership.
   b) Inspection.
   c) Forms and records.
   d) Methods engineering.
10. In the text material of this chapter, emphasis has been given to the importance of efficiency at the executive as well as at the operational level of organization. With this fact in mind, answer the following questions and give specific examples to illustrate and support your answers:
   a) What, in your opinion, are the most obvious evidences of managerial inefficiency at the executive level?
   b) Why can it be said that managerial inefficiency is generally more disastrous than inefficiency at the level of operations?
   c) Why are the criteria of sound appraisal of executive proficiency also requisite tests for executive promotion?

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Chapter XIV

THE PRINCIPLE OF INCENTIVE

EVEN though the techniques of planning, procedure, and production may have attained a high degree of perfection in the processes of an enterprise, it may still be inefficient because a further principle of management has been neglected, misapplied, or its full significance unrealized. It is the principle of incentive. When efficiency has been achieved in the material aspects of quality, quantity, and the cost of the goods or services produced, there still remain to be directed certain less tangible and psychological forces inherent in all of the human beings that go to make up an organization. They are the influences that prompt executives and workers alike to a willingness to work and to cooperate toward a common goal.

It has been said that "a business organization is a static affair, full of potency to be sure, but inert until management breathes into it the breath of life."[1] This observation may not be literally exact, since the principal elements of an organization are animate beings; yet its true implication is apparent. For an organization to become something more than a collection of persons—robots in a mechanism devoid of initiative and self-motivation—a vitalizing impulse is necessary. This life-giving quality in the structure of an organization is manifested by morale, a community spirit described by the French term, *esprit de corps.* Morale issues from the mental habits of individuals which induce them, singly and collectively, to subordinate willingly their own purposes to a common end.

Willing submission to reasonable discipline, unreluctant response to cooperative and coordinated effort, and a devotion to duty are all requisites of good morale. But they can be realized only temporarily and intermittently unless management is successful in developing an attitude of respect for and an interest in the policies and objectives of a concern on the part of the members of its organization. There must be an integration of interests as well as a willingness to assume responsibilities if this desirable condition is to be attained. It can only be done through the provision of proper incentives.

THE NATURE OF INCENTIVE

By definition, an "incentive" is a stimulus or an inducement which incites to action. In its broad meaning, the term may be applied to any

[1] Willis Wissler, *Business Administration* (New York: McGraw-Hill Book Co., 1931), p. 83.

factor, material or nonmaterial, which will impel, urge, or encourage a person to perform tasks and to strive for achievement. The primary effect of an incentive is a psychological reaction. By nature, or because of experience and training, an individual responds in certain ways to stimuli to which he is subjected. His reactions to such impulses may be both mental and physical. An "incentive" may therefore be said to be a force which acts upon the mind of a person, the response to which is revealed in physical and mental behavior.

Motive and Incentive

Behind every human action there is a motive. A "motive" determines the choice of action, while an "incentive" incites to its realization. Some motives are instinctive and elemental; others are the result of reflection and reasoning. Motives, in turn, stem from desires or longings which are characteristic of normal human beings. These desires may be roughly classified into four groups: (1) the desire to live; (2) the desire for possession; (3) the desire for power; and (4) the desire for recognition.

The Desire to Live

It is a maxim that self-preservation is the first law of nature. So strong is the desire to live that not only do animals and human beings alike guard against and flee from danger, but their first instinctive concern is to find and to consume food that life might be sustained. This simple fact needs no elaboration; yet it is the fundamental basis of the greatest of all economic activities, namely, that of making a living. As man has triumphed in the struggle for existence and has risen in his scale and standard of living, the bare necessities of food and shelter have not been deemed sufficient to satisfy this desire. Therefore he has been motivated to add comforts and even luxuries as his resources have permitted him to do so. Nevertheless, the stimulus to which he has responded has been a development of the desire for life and living.

Closely associated with the effort of an individual to sustain his own life has been his desire to rear and to provide for a family. Again, this longing is instinctive in all life. To reproduce and preserve the race is so strong a natural impulse that parents willingly sacrifice themselves in the interest of their offspring. Because of it, the welfare of the family has become so impelling a motive that it is reflected in the multitude of things that surround and influence personal life and mode of living. The urge for family betterment is complex and intimately personal, but it is at the same time one of the mainsprings of national pride and patriotism.

The concern for economic security is another aspect of the desire to live. The right and the opportunity to make a living, whatever the scale

and the standard of that living may be, is a matter of paramount importance. To realize the necessary resources to maintain a given status temporarily is obviously not enough. A corollary to the desire to live is the desire of longevity. People generally wish to live as long as possible; but they are conscious of the hazards of accident, sickness, old age, and other incapacities to which all are subject. Hence it is a matter of concern to an individual that his productivity be maintained as steadily and as fruitfully as possible not only to sustain him, his family, and his place in society from day to day, but to make provision for retirement, old age, and even for those who may be dependent upon him when death takes him away. The latter motive is far from being incidental or insignificant in the desire for economic security. It is the basis of the institution of life insurance and the establishment of inheritable estates.

The Desire for Possession

Man is an acquisitive being. "Acquisitiveness," the instinct to possess for one's self, lies at the roots of the right to ownership, which is property. It has been said that "property is to man what the nest is to the bird, the honeycomb to the bee, the burrow to the fox, and the shell to the hermit crab; without it man is a fugitive and a vagabond on the earth, or else a slave to someone else." In recognition of the fact that the chief seat of authority in society rests immediately upon private property, it has been guaranteed by the Constitution of the United States. Where one man obeys another because the law of the land says he must, a hundred men obey others because of the authority that resides inherently in the control over valuable things.

The desire to own private property has been a strong inducement to work, to save, and to invest such savings in homes, businesses, and other tangible evidences of ownership. It has spurred men to improve, invent, and create things because they have regarded the products of their genius and skill as something that belonged to them. Progress and civilization could hardly exist in a propertyless world, for people in a state of primitive savagery are notoriously poor.

The opposites of poverty and riches are usually measured in terms of wealth. To be poor is to own little or no property—a condition which most people try to escape and probably none really enjoy. Hence the motive that determines the choice of action by an individual is often the natural desire for material possessions. To deny him the opportunity of satisfying this desire, to interfere with it, or to attempt to take it away is like stealing a bone from a dog or disturbing a hornet where he lives. But to encourage it and to cause its realization is to provide a strong incentive for effective achievement.

The Desire for Power

It is but a step from the desire for possession to the desire for power. Just as in primitive society the man with a weapon or tool was stronger than he whose strength consisted solely of his wits and bare hands, so in modern civilization the individual with extensive possessions is more powerful than one who has few or none. That is to say, the former can do more things. He can more readily adapt himself to his environment; and to a greater degree, he can create the conditions under which he chooses to live.

The desire for power goes further; it is an element of leadership. There is an instinctive ego in man which impels him to be self-assertive within the limits of his experience. It is the desire to be put in charge of someone or something—a challenge to his vanity, perhaps, but nevertheless an eagerness to test his strength. Advancement and promotion are ends sought because of the desire for power. In management, it is the ambition to be moved "up the ladder" in the scalar levels of an organization by the allurement of authority to make decisions and to give orders rather than to be subjected to them.

Another aspect of the desire for power is the desire for knowledge. It is an old saying that "in knowledge there is strength." Power is not necessarily limited to the domination or rule over persons or the control over things. It is equally proper to consider an understanding of men and events as power because thereby comes the strength of judgment and the validity of conclusions as bases for personal action. It is said that "who knows only his own generation remains always a child."[2] The implication is obvious: as a child one is weak, but as education is acquired, one grows in mental stature and power. The instinct of curiosity is a manifestation of the desire for knowledge. As it is developed and nurtured, the desire for knowledge is transmuted to a desire for power. The desire for power is frequently one of the strongest motives that shapes men's deeds.

The Desire for Recognition

Man has often been characterized as a gregarious animal. That is, from their primitive state in the dim past, human beings have lived together in groups that can be described by such terms as "family," "tribe," "race," and "nationality." This social habit has differed from the gregariousness of animals in that human rationality has made it possible for a member of a group to retain his own individuality. He has had an awareness of self along with his consciousness of kinship or attachment to the entire body

[2] Graven inscription, conceived by the late President George Norlin, on the façade of the library building of the University of Colorado.

of persons of which he is a part. This awareness may be called the "identity of personality." It is the basis for the desire for recognition. It is a natural tendency for the normal person to wish to belong to an organization. To be a "joiner" is instinctive with him. At the same time, he resists losing his identity but craves to be recognized as an individual who can be distinguished from another not as a mere fraction of a unit.

It is said that in animal life the first manifestation of a growing brain is the special faculty of imitation. Man has inherited this faculty, and in his desire for recognition he has attempted to do what others whom he admired or envied were doing. On some occasions, such imitation has been for the purpose of ostentation or show; on others the motivation has been caution, social standing, or simply an attempt to "keep up with the Joneses." In any event, the human propensity to imitate is one way of satisfying the desire for recognition.

Another example of the desire for recognition is the faculty of invention. It is the next step after imitation in the assertion of individuality. To be the originator and creator of something new or different obviously distinguishes a person from his fellows. Besides, like all motives, it is egoistic. That is to say, it is an expression of self-interest, satisfaction, and pride in one's own creative ability. It is the impelling motive of craftsmanship, so characteristic of the pioneer and the artisan. When stimulated and encouraged, it is an urge to excellence in performance and achievement.

The will to produce by hand or brain not only is stimulated by a sense of self-satisfaction, but also is satisfied by the desire for recognition because its tangible manifestation attracts attention to its creator. To be observed and to receive consideration by others is a strong motive that spurs on an individual to greater productivity. But to be lasting and most effective, the desire for consideration must be motivated still further by appreciation and praise. It is a natural human characteristic to desire credit and commendation for work well done. If good work is disregarded or goes unrecognized by expressed approbation, the inducement to further effort often disappears and interest is lost because frustration produces an attitude of "what's the use." Deserved praise is generally more productive than any amount of coercion as a means of motivation. A compliment is a response to the desire for recognition, while compulsion almost instinctively meets with resistance.

Finally, the culminating satisfaction to the desire for recognition is the achievement of status. "Status" has been defined as rank or position among one's associates or in society. It is closely related to the desire for power, but often a title or similar designation is more sought after and coveted than increased authority. Again, it is a matter of recognition.

Often the element of fairness enters into the consideration of status. To be overlooked or to be the victim of discrimination when appointments and advancements are in order in an organization clearly does violence to the desire for recognition. When many persons are involved, comparisons are unavoidable, and the question as to why one person was not advanced may be as serious a question as why some other one received promotion. The hope and promise of improvement in status is a powerful motive. It is not only the expectation of greater financial reward that makes it so, though that, too, is an important consideration; but to be distinguished for merit when merit is due develops incentive whose impulse is as strong as any other influence.

TYPES OF INCENTIVE

In the foregoing discussion of the nature of incentive, three terms have been used that are related, but the clear meaning of which should be distinguished. They are "desire," "motive," and "incentive." A "desire" is a longing, craving, or aspiration for something, the lack of which in one's life leaves a want unfulfilled. Desires create motives. A "motive" is a force or emotion within a person which determines choice or induces action. Putting the two together, desire identifies that which is wanted and motive determines the choice of the way to achieve it. But accomplishment is not attained without "incentive," which is the stimulus or inducement which brings about action that leads to the realization of desire.

An analysis of the fundamental human desires shows that incentives designed to fulfill them fall in three classes or types: financial, nonfinancial, and social.

FINANCIAL INCENTIVES

There have been those who have held that there is only one really significant incentive, the financial one. This attitude is obviously fallacious. It can be admitted that the hope and promise of material gain is *one* of the strongest inducements that motivates an individual to do his best, but it is only one. To disregard all other incentives or to say there are no others is to assume that the satisfaction of all human aspirations can be calculated in material values. Facts prove that this is not so. The doctrine that man does not live by bread alone has been amply proved. Yet, because man must work to live and the elemental requirements of life are physical, it is proper to give first consideration to the incentive of financial reward. Moreover, being material, the incidence of such reward at its source and its immediate realization by the recipient are both easily measured. Perhaps that is why this form of incentive has been given more attention and prominence than any other.

Incentive Wage Payments

There has been a tendency to classify all financial incentives under the general heading of some type of wage payments. As applied to the employed group in an organization commonly called the "workers" in productive processes, the incentive of monetary gain has been regarded as compensation for better than average productivity. As a result, many systems of wage payments have been developed—some of them simple in their application, and some of them complicated. The purposes involved have always been two: first, fairness, that is, a fair day's pay for a fair day's work; and second, to provide every employee with the maximum possible incentive to do his best work. Some of these systems will be described in greater detail later in this chapter.

Wage plans that are derived from exact or "scientific" classification and standardization of job tasks and skills are also important as financial incentives. They are financial in character because such plans assure worker "A" his wages compared with those of worker "B" are based on factually determined similarities or differences in the respective jobs of the employees.

In addition to specialized wage systems, other types of financial incentives have been adopted more or less widely. These include profit-sharing and bonuses apart from, and in addition to, the going wages paid to employees. Another type, used less frequently, consists of two closely related plans—namely, stabilized employment and the guaranteed annual wage. The first of these latter plans assures the worker that he will have a steady job, and the other attempts to determine in advance what his income will be for a given yearly period.

The employee is interested in security not only during his productive years but even more during old age or at the time when some other eventuality removes him from a payroll. Adequate provision for such a contingency is clearly a financial incentive. Hence retirement plans have been widely adopted along with other forms of financial reward for satisfactory service. All of these plans are illustrated in the last section of this chapter.

All the foregoing examples of financial incentives are related to earnings on the job. There is another group of incentives which have less direct financial implications but which nevertheless are material in their consequences. They have to do with programs of health and accident insurance, savings, investment, credit unions, hospitalization, and housing. In some instances, certain aspects of these programs are made available to employees outright without extra cost; and in others the members of an organization contribute a share toward their maintenance. Some of these plans are merely facilitated by an enterprise, rather than supported

financially, by such means as quarters, clerical help, or some other convenience that would not otherwise be readily available.

Incentives for Indirect Workers

There has been a tendency to stress the importance of financial incentives in their application to the so-called "working force" of employees to the exclusion of those who have erroneously been called "nonproductive workers" as well as executives of all grades and levels. This one-sided attack upon the problem is obviously wrong. All of the members of an organization are human beings whose desires and aspirations, on the whole, are the same, varying only in degree and circumstances. Therefore, more and more attention is being given to wage and salary incentives for so-called "indirect workers."

In addition to those who are engaged directly in processing operations, there are three general classifications of employees: service workers, facilitating workers, and salaried personnel, including executives from the supervisory level to the top. Service workers are the persons who provide direct assistance to those who actually turn out the products of a concern. Transportation workers, crane operators, truckers, and tool and maintenance men in factories are examples. The predominant factor in any financial incentive plan for such employees necessarily is the performance of the particular production group served, whether with respect to quantity, quality, schedules, or costs—separately or in combination. A sound procedure is achieved by establishing ratios of indirect labor usage to that of direct labor. The incentive pay received by the service workers is, therefore, based upon the performance of the direct workers served, modified by the degree of utilization of the service workers themselves.

The second group of indirect workers are the facilitating employees whose functions, while essential to the operations of an enterprise, do not closely or directly influence the performance of the production workers. Included in this category are construction and installation men, general maintenance and repair groups, employees in receiving and shipping departments, and others assigned to various facilitating tasks. The predominant, and perhaps the only sound, factor upon which their incentive pay can be based is their own performance. It is therefore necessary to provide a measure of their work by individuals, by groups, or by departments in the same way that an appraisal is made of the performance of direct workers. This is merely the application of the tests of efficiency as explained in Chapter XIII.

Incentives for Salaried Personnel

Financial incentives are as important to the third group, the salaried personnel, as they are to other employees; but they are generally provided for this group in a manner different from that used for wage earners. The

inducement that is held out to salaried personnel is usually advancement in salary and status contingent upon satisfactory service and seniority in tenure. Accordingly, definite salary scales are prepared so an individual may determine what continued employment in the organization will mean to him if he can "make the grade." Figure 46 is an example of such a schedule for clerical and other office workers. The principle upon which it is based is the one in common use for civil service employees in various units of government including the federal government. There is this difference, however, between civil service employment and appointments to similar positions in private concerns in that in the former, tenure is continuous, while in the latter it is usually on an annual or some other term

Year of Service	Grade or Rank				
	A	B	C	D	E
1	$1,440	$1,560	$1,740	$1,980	$2,280
2	1,500†	1,620	1,800	2,040	2,340
3	1,560‡	1,680†	1,860	2,100	2,400
4	....	1,740	1,920†	2,160	2,460
5	....	1,800‡	1,980	2,220†	2,520
6	....	....	2,040‡	2,280	2,580
7	....	....	....	2,340	2,640
8	....	....	....	2,400‡	2,700
9	....	....	....	....	2,760
10	....	....	....	....	2,820‡

† Eligible for promotion to next rank at end of this year.
‡ Terminal salary for this rank.

Fig. 46.—Example of a salary scale for clerical and other office workers.

basis. In a government position a civil service employee can hold his job continuously and realize increases in salary automatically within the limits set for a particular classification as long as money is appropriated for the department or function involved. One can be discharged only "for cause," which is generally interpreted to mean insubordination, immorality, dishonesty, or some other like personal offense. Security of this kind often leads to indifference and inefficiency. On the other hand, permanence of tenure and advancement in a private concern depend upon quality of service and such intangibles as loyalty, dependability, and cooperation.

Incentives for Executives

Financial incentives for executives in the lower and intermediate levels of management often follow similar plans for salary increases. Figure 47 illustrates this method. It shows four levels or ranks. The beginning executive in this scheme is employed on an annual basis. If his work is satisfactory, he is advanced each year up to the fourth year, when he is eligible for promotion to the next level. If he is not deemed eligible, he may get

the final salary indicated in the scale for that rank, which is terminal as far as he is concerned. He will possibly not go beyond it. If, however, he is promoted to the next rank, his tenure goes to three years. The chances for future advancement or terminal salary at this rank are indicated in the scale. Permanent tenure is afforded only in levels three and four. Of course, under such a scheme, an individual may also be discharged for cause; the illustration has been used simply to show the possibilities of financial incentives for salaried persons whose performance is acceptable.

With respect to executives in the uppermost brackets of management, including the chief executive, formal salary scales, such as those that have

Year of Service	Rank or Position*			
	A	B	C	D
1	$3,000	$3,300	$4,300	$5,300
2	3,100	3,450	4,450	5,450
3	3,200†	3,600	4,600	5,600
4	3,300‡	3,750	4,750	5,750
5	....	3,900	4,900	5,900
6	....	4,050	5,050	6,050
7	....	4,200†	5,200†	6,200
8	....	4,350‡	5,350‡	6,350
9	....	....	....	6,500‡

* Tenure: A, Annual appointment. B, First appointment, 1 year; thereafter 3-year terms. C, First appointment, 2 years; thereafter permanent. D, First appointment, 2 years; thereafter permanent.
† Eligible for promotion to next rank at end of this year.
‡ Terminal salary for this rank.

Fig 47.—Example of a salary scale for personnel in middle and lower executive ranks.

been indicated, hardly apply. Such salaries are usually determined by the board of directors or by some other governing body in amounts sufficiently attractive in themselves to be incentives for persons to aspire to realize them. Often such salaries are related to persons rather than ranks. Hence they are variable. This does not mean that top officials are insensible to financial incentives. Position cannot change inherent human qualities. They are subject to the same impelling motives as other persons, but the realization of them may be different. Perquisites of various kinds, such as bonuses, opportunities for investment, and, in some types of institutions or business locations, residences, are afforded them. In short, their incentives obviously are other than annual salary increments or a percentage of base pay. Indeed, it may be safe to say that, while financial incentives are not absent, they may be quite secondary or incidental.

NONFINANCIAL INCENTIVES

It is unrealistic and inadequate if a consideration of nonfinancial incentives is confined solely to wage earners or as supplementary to wage

systems. Such incentives are important in all ranks of employees, whatever their material benefits or positions may be. In the ascending scale of management levels it can probably be defended that nonfinancial incentives gain in importance with each succeeding rank.

In order to determine what nonfinancial incentives are effective and important, it is only necessary to consider the human desires which cannot be satisfied in whole or in part by material considerations alone. These incentives have been broadly classified as the desire for power and the desire for recognition. It must be reiterated that mere satisfaction in, or with, a job is not an adequate incentive. It is true that irritations, grievances, and dissensions frustrate incentive and should be eliminated as far as possible, but their removal or avoidance will not generate incentive unless other conditions are created to take their places. Such other conditions consist of stimulating influences that prompt individuals to qualify themselves for betterment for their own advantage and for the good of their organizations.

A carefully considered summary of nonfinancial incentives has been stated by Austin S. Igleheart as follows:

> What are the ingredients of job satisfaction? The employee has his own ideas about that. Here are the factors which he lists in the order of their importance to him: (1) interesting work; (2) job security; (3) the interest the company takes in the individual; (4) chances for advancement; (5) working conditions; (6) handling of workers' complaints; (7)—and a rather poor seventh at that—pay; (8) the immediate supervisor; (9) the other people on the job; (10) vacation policy; and (11) working hours.[3]

Consideration of the Individual

The purpose of incentive is to bridge the gulf between management and men, and between men *in* management. It has been emphasized that, while it is instinctive for an individual to associate himself with a group, yet he is jealous of his own identity. Therefore it is essential to avoid barriers that tend to separate the members of an organization, and, at the same time, preserve the dignity of individual personalities. To do so is to humanize an organization, to transform it from a cold-blooded mechanism to an alliance of persons working together.

Incentives that result from a consideration of the individual take several forms. Of primary importance is the environment within which an employee or executive performs his duties. It includes conditions of health, comfort, decency, and convenience. It is obvious that pleasant and satisfactory surroundings are more conducive to high productivity than

[3] Austin S. Igleheart, President, General Foods Corporation, "A Challenge to American Management;" excerpt from address delivered before the Traffic Club of New York, February 21, 1948.

those that are forbidding or repulsive. Enterprises that have attempted to provide wholesome working conditions through methods of so-called "employee welfare work" have often been considered paternalistic. Where such criticism has been justified, it has been because the attitude, rather than the purpose prompting such action, has been wrong. Paternalism is generally obnoxious because it has the flavor of charity, implying that the donor is entitled to special gratitude. To be truly an incentive, the one to whom it is available must feel that he is entitled to its realization because of his own efforts and because he is recognized as a rational being, a valuable employee who performs worth-while work.

In addition to physical environment, an individual is also sensitive to his psychological environment. That is, the personal relationships and attitudes that exist between the members of an organization. In this respect, an important factor is courteous treatment. Regardless of the necessary differences in rank and authority possessed by the various employees of a concern, each should be accorded considerate attention. It is natural for a person to respond favorably to friendly, courteous treatment; but his reaction is antagonistic to an overbearing manner on the part of an executive superior in rank or to any associate who is impudent, rude, and ill-tempered.

Another factor of personal relationships that has an important bearing on incentive is cooperation. "Cooperation" means joint action toward a common end, and most people will join their efforts with others if they are assured of reciprocal treatment. This is particularly true between superior and subordinate; if a person in a subordinate position can feel assured at all times of the help and support of his chief, a powerful incentive is generated within him to discharge his own duties faithfully and well.

This cooperative spirit is closely related to confidence which grows out of a consciousness of fair treatment and the certainty that promises once made will be kept. Disillusionment destroys incentive, whereas reliance based on confidence is a powerful stimulus. As an incentive, confidence extends beyond routine performance on the job and includes a recognition of personal interests as well. The concern that is able to create a bond between itself and all of its employees beyond the formal employer-employee relationship is making the highest possible bid for loyalty and morale. A friendly interest in personal affairs, providing it is not intrusive and paternalistic, makes a person feel he is an individual who is recognized for what he is as well as for what he does. Unfortunately, in the development of this wholesome spirit of association, envy and false pride on the part of certain members of a group cause them to charge those who accept friendly advances with "apple polishing," and those who extend them with "favoritism." If the friendly attitude here described is

honest and sincere, both accusations are unjust and malicious because they tend to prevent the full utilization of an incentive that can serve an extremely useful purpose.

One of the most forceful of all nonfinancial incentives in this category is expressed appreciation and praise for achievement because it satisfies a fundamental desire for recognition. To be unnoticed and disregarded when one knows he is entitled to a "good word" is not only deeply disappointing but leads to indifference and indolence as far as subsequent performance is concerned.

Opportunity for Self-Assertion

The incentive of self-assertion is an essential complement to any incentive plan if it is to be as effective as possible. It is an established tradition in this country that an individual may rise to any height to which his own capabilities and energy may lead him. It follows that incentives should be such that the members of an organization are made to feel that they are intimately associated with it because by their contribution they can strengthen the position of the concern and improve themselves. An atmosphere of this kind incites interest—a prerequisite to initiative. It aids the development of individual capacity, it stimulates inventive and constructive thinking, and it cultivates an attitude of joint responsibility.

Opportunities for self-assertion can be provided by utilizing the instinct of personal pride. An expression of the creative urge which is latent in every individual develops self-respect and the esteem of craftsmanship, which are intangible rewards in themselves. The ambition of the artisan to be proud of the work of his own brain and hands tends to be stultified or lost entirely when an individual loses his identity and mechanical processes relieve him of the necessity for highly developed skill. His attention instead becomes centered upon his pay check and the hours of work required of him to hold his job. His talents remain undeveloped because there is neither the desire nor the challenge to exercise and give expression to them.

The pioneer of the early days was essentially a free agent. He was artisan, craftsman, and dictator of his own destiny. Modern society and business are so highly organized that interdependence of persons has tended to supplant the conception of free agent in a literal sense. Yet it is still desirable to preserve the virtues of initiative and self-assertion by providing incentives that will retain them or restore them when they have been lost. This objective should be one of the aims of training programs, for example. If the establishment of company schools, the rotation of executives, or any other plan of training is limited in its purpose to the immediate benefits which may accrue to the concern, it falls short of its full significance. A training program should also provide an incentive to

the person who takes part in it to improve himself for his own sake and to supply a medium through which his talents and genius will have a chance to find expression.

Research is another aspect of the opportunity for self-assertion. The incentive behind investigation is the instinct of curiosity. The incentive behind the application of the findings of research is the instinct of creation. When these two forces are given the chance to exert themselves, inventions, new concepts, new processes, and the extension and wider application of existing knowledge result. In educational institutions the failure to provide facilities for research for scholars or the failure of the latter to take advantage of the opportunities that may be afforded are regarded as indications of inefficiency. It is generally recognized that the productivity of a scholar can only be measured by the quality of his research. In business and industry much the same attitude has developed. But again, research, like training, must furnish the incentive for self-assertion to be fully effective.

Opportunity for Leadership

Every person does his best in his productive years while he is still striving toward a goal. To feel that one has reached a dead end or that the future holds no promise of advancement deprives one of the most quickening incentives possible. On the contrary, the hope or, better, the assurance that meritorious service will result in progress is a constant urge that impels an individual to put forth his best effort. Everyone wants a "raise" and is encouraged when he receives it, but a "raise" in pay is oftentimes not sufficient to satisfy the craving for advancement. Status is frequently as highly prized as material remuneration; and when these two factors can be combined, the result is a peerless incentive.

The first step in supplying an incentive for advancement is executive goodwill. Goodwill begins at the top of management and extends down through all executive levels to the employees at the bottom of the pyramid. It is characterized by such qualities as sympathy, understanding, and interest. Above all, goodwill is established on sincerity. Duplicity is easily detected, and selfish motives breed discontent and antagonism. Goodwill does not happen spontaneously. It has to be planted and nurtured by means of personal contacts between superiors and subordinates. In such contacts, however, an impression that subordination and inferiority are essentially the same should be avoided. Between the members of an organization, there must necessarily be a difference in rank and position. One can occupy a subordinate position and, at the same time, not be inferior to his superior either in performance or in personal qualities. The inference is plain. A man can be just as fine a person and do just as good a job within the limitations of his assignment as the one to whom he is directly ac-

countable. To recognize this fine distinction and to let it be known is to build goodwill.

The next step is the critical one of proper placement. A person's incentive may be dulled because he has been assigned to a duty which does not challenge his best efforts nor utilize all of his talents. Therefore his qualifications for leadership remain undiscovered. The individual himself may be conscious of them, but he finds himself in a cage the bounds of which he cannot break. Unless he is assisted by higher management, he eventually loses interest, and, with incentive gone, he becomes another automaton who follows a routine without concern for the present or hope of the future.

Assuming that a person possesses the qualities and talents of leadership, he finds the incentive to achieve when given a share in authority and responsibility. There are several ways of accomplishing this end. He may be called upon to represent the group of which he is a member; he may be asked to sit in on conferences; or he may be assigned committee service. It is in the spirit of democracy that everyone wishes to have a voice in affairs to which he contributes and in circumstances to which he is subject. As a citizen of his community, he may share in government at least to the extent of being able to vote—a right guaranteed and held sacred whether exercised or not. It is only natural that he should incline toward a similar privilege in his job, even though he distinguishes between that which is private and that which is public. Self-interest is obviously involved, but the motives of self-determination and self-assertion are also present. When these motives can be channeled and directed to the common benefit of all interests in an enterprise, they provide a forceful incentive for employees and supervisors who have found some recognition for their own leadership talents.

Fruitful response to the incentive of leadership culminates in the recognition of personal qualifications and commendable performance coupled with appropriate advancement. The realization that worth will be compensated and that promotion in status depends upon merit rather than "pull" or favoritism, is a dynamic force that generates enthusiasm, loyalty, cooperation, and a spirit of "willingness-to-do." As has been shown throughout this study, leadership is an indispensable element in management. Because of its salutary effect upon incentive, the opportunity for its development in the rank and file of an organization should not be disregarded.

The Social Incentive

There remains one other nonfinancial incentive to be considered. It is called the "social" or group incentive. Even though a person is subject to incentives that impel him to individual action, it is evident that as a mem-

ber of any organization he is far from being isolated in his employment. He is in constant association with fellow workers and with his superiors in rank. In effect, he is a member of a social organization. As such, he is subject to the influences of formal and informal codes of behavior, of group feelings and attitudes, of friendships and antagonisms, and of mutual dependence upon a system or group of sentiments that characterizes the particular social unit of which he is a part.

It has been pointed out by Roethlisberger and Dickson that the members of the social organization of an enterprise interact daily upon one another, "and from their association certain patterns of relations are formed among them. These patterns of relations, together with the objects that symbolize them, constitute the social organization of the enterprise. Most of the individuals who live among these patterns come to accept them as obvious and necessary truths and to react as they dictate. Both the kind of behavior that is expected of a person and the kind of behavior he can expect from others are prescribed by these patterns."[4]

In applying this observation to an exhaustive study of the employees in the Hawthorne, Illinois, plant of the Western Electric Company, these authors have concluded that none of the results of their investigations have given "the slightest substantiation to the theory that the worker is primarily motivated by economic interest. The evidence indicated that the efficacy of a wage incentive is so dependent on its relation to other factors that it is impossible to separate it out as a thing in itself having independent effect."[5]

The Complex of Influences

It has been customary to consider the realization of material benefits to be the principal incentive to which an individual is responsive. Man has been often characterized as essentially an economic being whose choices are made on a basis of financial gain and whose nonfinancial incentives are incidental appendages of no real significance. The foregoing analysis has attempted to show that such a view is not valid. The economic incentive is important, but it must be taken into account in conjunction with other noneconomic influences and interests.

Incentives are the expression of the whole man; and man is not motivated exclusively by factors that are tangible, logical, or factual. He is a creature of feeling and sentiment, and of complex desires which he carries with him to work as well as elsewhere. His behavior is colored and modified by them whether he is the chairman of the board or the most humble

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[4] F. J. Roethlisberger and William J. Dickson, *Management and the Worker* (Cambridge, Mass.: Harvard University Press, 1941), pp. 554–55.

[5] *Ibid.*, pp. 575–76.

laborer in a corporation. These psychological aspects of his nature are not accidental, nor do they exist in isolation. They are the products of one another and of the fact that man lives his life associating with other people in groups of various kinds. Motivation, therefore, and the incentives that prompt him to action are determined not only by his own reasoning but by the impact of the attitudes of a social group upon him. Furthermore, the incentives that incite him to action will be rated in importance by him, consciously and unconsciously, in relation to the effect of their results upon him both as an individual and as a member of his social group.

THE PURPOSE AND PRODUCT OF INCENTIVES

As we have seen, the whole purpose of incentive as a principle of management is an integration of the interests of an enterprise and the interests of the individuals and the groups of individuals who constitute its organization. Integration is a unifying force, a process not only of bringing together but of binding together essential elements which complete the whole. Incentives, then, properly established, understood, and applied, have the effect of establishing a bond between the constituent parts and interests of the human elements in an organization.

The analogy between the structure of a modern skyscraper building and the organization of a typical enterprise is helpful in distinguishing incentive from other components of management. A skyscraper is constructed of an interior framework or skeleton of steel incased by an outer wall of masonry. The steel structure, with its setbacks at the upper stories and the surmounting tower, is analogous to the hierarchy or pyramid of management. The separate bricks—thousands of them—that compose the masonry correspond to the individual workers and executives, the living human beings who clothe the organization with life and directed activity.

In the case of the building, two factors hold the bricks together and retain them in their proper places in relation to the entire structure. One factor is the cement or mortar which is laid between the bricks as a binder, which joins them with each other and with the other building materials, including the steel framework. The other factor is the affinity of the bricks for the cement, which results in cohesiveness so that the whole wall becomes an integrated unit. In other words, the bricks are not slippery when in contact with the cement but instead establish a bond with it and adhere to the cementing substance.

In a business organization, it is essential that similar conditions prevail to bind its component parts together. There must be a cementing agency to form a bond or union, and there must be cohesiveness in order that the bond may be effective and strong. Leadership manifested by the complex function of coordination is the cement. Coordination permeates the whole

structure from the highest level of management down to each individual person within the organization and binds him into the structure and substance of the enterprise.

However powerful the cement, it would be ineffective if it could not adhere to the elements it is intended to bind together. To it must be added the cohesive agency of individual incentive. It is personal incentive that causes the individual employee and executive to respond to the molding influence of coordination. As the cement of organization, coordination could not adhere to the individual without the cohesive force of personal incentive. Together, coordination and incentive hold the human building blocks together in the desired relationship to each other and to the framework of the organization.

Hindrances to Incentive

Incentives, to be most effective, must be as carefully planned as any other management procedure. There are objectives to be sought and hindrances to be avoided. As has been stated previously, incentive plans must, first of all, abstain from paternalism. Paternalism denotes a relationship similar in character to that existing between a father and his dependent children. Specifically applied to the organization of an enterprise, the term is used to describe the practice of an employer to undertake to supply the needs and regulate the conduct of employees in matters affecting their own interests on the assumption that the employer can best determine and secure their highest welfare. Obviously, such a policy is repulsive to mature men and women. They resist being treated like children without discretion regarding their own best interests. Employees naturally resist the implications of charity. Paternalism is contrary to self-assertion, and hence deadening to initiative and incentive.

Any incentive plan, to be sound, must also avoid exploitation. "Exploitation" means taking advantage of someone whether by force or by cunning. Under such a system a superior at first encourages and subsequently compels an employee to produce more than a normal quota of work; and in return forces him to accept a smaller compensation than he should reasonably expect. Exploitation of this character has been more common in connection with incentive wage payments than with other types of incentives. Instead of integrating the interests of employees with those of the employer, the reverse has resulted, and workers have finally become antagonistic instead of cooperative.

Workers have frequently resisted incentive wage payment plans branding them as nothing more than the establishment of the hateful "speed-up" system—an attempt to take advantage of the natural cupidity of an individual by holding out the promise that he will be paid more if he produces more. But the "joker in the deck" shows up when workers

discover that the employer has meant one thing and they have interpreted the "deal" to mean something else. For example, assume that a piece-rate plan was involved whereby the normal rate was ten cents per piece for ten pieces per hour, or a wage rate of $1.00 per hour. The incentive would be based on that rate, so that if twelve pieces were produced in an hour, the return to the worker would be $1.20. At some point, when by virtue of the financial incentive, production had been markedly accelerated and fifteen pieces per hour had become a new normal rate of output instead of the previous ten, the employer would then drop the piece rate from ten cents to seven cents. Unless there was a justifying offset in mechanical improvement, the worker would then find that he was being expected to do 50 per cent more work for 5 per cent more pay.

Other forms of exploitation may not be as glaring, but they are serious hindrances to incentive whenever they are permitted to exist. On this point an industrialist, discussing the incentive system he has adopted for his own enterprise, has this to say: "The only way to increase the pride of the worker in himself and his job is by putting him in a position in which his skill and application will be rewarded in accordance with his production. His reward must be commensurate to his skill and application. Only so is a spur given to his development and his ambition to develop."[6] And in the term "worker" he "includes all men who work with hands, head or spirit."[7]

Finally, an incentive system must avoid ambiguity. It must be easy to understand and simple to apply. Involved language, complicated formulas, and numerous exceptions and provisos lead to confusion and distrust. It is only natural for an individual to wish to know as nearly as possible what the products of an incentive plan will mean to him and how he can best realize them. If questions of promotion are at issue, then the employee should be able to determine for himself how to qualify for such advancement. If the incentive system is purely financial, he should be able to calculate his own earnings easily and accurately and to determine when and under what circumstances the benefits may be received. If a firm provides, for the good of its personnel such facilities as insurance, hospitalization, sick benefits, and retirement plans and considers these to be incentives, then the eligibility to share these benefits and the circumstances under which they can be realized should be made so clear as to leave nothing to the imagination of any person concerned. Incentive plans that might be suitable for one group in an organization might be inapplicable to another. In the interest of thorough understanding it is often desirable to precede the installation of incentives with a program of education.

[6] James F. Lincoln, *Lincoln's Incentive System* (New York: McGraw-Hill Book Co., 1946), p. 43.

[7] *Ibid.*, p. 2.

Outcomes to Be Realized

The outcomes to be realized from the response to incentives are of two principal orders—those that bear directly upon the interests of the employed personnel and those that are of prime importance to the concern itself. It is significant to observe, however, that benefits cannot accrue to the one without advantage to the other. They are mutually dependent upon each other. Indeed, the aim of incentives is the integration of interests; yet for purposes of analysis, it is possible to view these interests independently.

Briefly stated, incentives spur an individual to strive for four goals. First of all, he wishes to hold his job: that is economic security. Next, he hopes to get ahead: he aspires to earn successively more and more money. Then he craves to be somebody: he seeks advancement in status as well as in income because he yearns for recognition and leadership whereby he may be distinguished from other members of a group, or attain a higher position among his associates. Finally, he wishes to lay up something for a rainy day: he is concerned about possible incapacitation, retirement, and the creation of an estate. Incentives are designed and intended to assist a person to reach all of these goals as far as his talents, skill, and effort will permit him to do so.

On the side of an enterprise the material objectives of an incentive program are greater efficiency in operation, increased production, lower costs, and better profits. Unless these gains are realized, it is obvious that the benefits to employees cannot long be sustained. There are, however, employers who are enthusiastic about incentive plans who take a somewhat different view. They insist that, if profit is the sole objective of an incentive system, the plan is doomed to failure in the long run. On the other hand, if its purpose is to make an increasingly useful product that can be sold at a price that tends to become increasingly lower, along with which profit is merely a by-product, an incentive plan applied under proper management can be eminently successful. It is pointed out that there is a difference in emphasis between these two goals. One centers its attention on profit and pays too little heed to other values, while the other seeks to make enterprise and all its parts more useful to mankind, thereby relegating the emphasis upon profit to a position of secondary importance. Profit will still be realized; and, it is confidently asserted, in no less yield, but it will be a by-product instead of a motive.[8]

Whatever the differences of opinion may be with respect to the realization of a financial gain from incentive, there is agreement that there are other important outcomes for an enterprise. They are the development

[8] *Ibid.*, pp. 161–62.

of loyalty, morale, and cooperation throughout the entire organization. When these qualities are present in the members of the personnel of an institution, the indispensable element of coordinated effort is most likely to be achieved. And there is one more goal that is cherished. It is a good name or reputation. Like an individual, a business concern also takes pride in its standing and the characteristics for which it is recognized. If it can avoid internal friction, labor troubles, strikes, and other ills of similar character, management is not only relieved of many "headaches"; it also receives favorable notice from other organizations and from the public.

FINANCIAL INCENTIVE PLANS ILLUSTRATED

While it is recognized that financial considerations are not the only important incentives that incite individuals to make the best use of their talents and skills, nevertheless the concluding section of this discussion will be confined to a presentation of selected plans that illustrate their application in various forms. Financial incentives have received more attention and have been described more fully than nonfinancial ones because they are regarded by many persons—employers and employees alike—to be the most significant. Yet, when the methods which follow are critically analyzed and all of their implications are considered, it is obvious that in many instances material benefits are not the only ones involved.

Primary importance has been attached to financial incentives because it has been recognized, and properly so, that the satisfaction of material wants is basic to all other human aspirations. There is truth in the saying that "soul-saving cannot be separated from bread-winning." But in addition to their appeal to fundamental instincts, financial incentives have been given prominence because they are tangible and can be measured with respect to both incidence and outcomes. What is involved in them can be calculated in advance of their application by an employer, and the advantages that will accrue from them are immediately realizable and easily understood by the employee.

The factor of fairness is another reason why material rewards have been given first place in incentive plans. This factor has two elements: greater reward for greater output, and equitable distribution of the total income of an enterprise. The first of these elements based on the theory of a "fair day's pay for a fair day's work" concerns individuals and the wages and salaries they receive. The second element is a recognition of the fact that all members of a concern contribute to its prosperity. It is maintained that a successful incentive system must be tied in with the net profits of the enterprise. Profit is the measure of the success of a business. As such it is also the measure of the ability of those who participate in it. Participation in the prosperity of a successful concern is both a material and a nonmaterial incentive. To inform all employers in an organization of

the result of their skillful operation and to afford them an opportunity to share in such gains is to provide a challenging incentive that cannot be fully measured in dollars and cents. Its application has been called "incentive management, a philosophy of industry and life which starts with the needs of society and depends primarily for its success on the development in the individual of his latent abilities."[9]

Time Payment Methods

Compensation paid to an individual for the time consumed by application to his task is probably the oldest form of remuneration for services rendered. It is still the most prevalent method when all occupations are taken into account. The time payment method has been unfairly criticized on the ground that it provides little or no incentive. It is pointed out that individual members of a group of employees may be paid the same per unit of time for varying amounts and qualities of work. That such persons will arrange themselves around an average which represents a mean between the output of the best and the poorest producers. Therefore, the capabilities of the most efficient persons remain unchallenged, and the least efficient receive undeserved rewards.

There are two answers to this criticism. If a situation like the one cited in the previous paragraph prevails, it is merely an admission of the lack of proper standards and appraisal. It is an evidence of poor management when it is admitted that salaries and wages are unrelated to competence manifested by productivity. Furthermore, the charge that time payments provide no incentive falls to the ground when it is realized that its alternative, piecework, is inapplicable in a great many occupations. Discussions and considerations of incentive plans have too often left the impression that incentive systems have to do merely with workers in factories and especially in large-scale industries, where the mass production of material objects is the rule rather than the exception. Obviously, if incentive is a principle of management, which most assuredly it is, then it has its place in the stimulation of every "worker with hand and brain and spirit."

Financial incentives are just as necessary in a bank, an office, a hospital, an educational institution, or any other place where the product of talent and effort cannot be measured as objectively as in a factory. Yet standards can be set up and maintained that have a definite relationship to the time payments involved. It would be naïve to fail to recognize the inequities that have occurred in time payments as a system of remuneration. There is no doubt but what abuses in this method have been the underlying cause for public legislation designed to regulate hours and wages. Labor unions,

[9] *Ibid.*, Preface, p. vii.

too, have sought in some cases to correct injustices in the ancient system by contractual agreements. But compulsion, whether by force of law or the pressure of organized labor, does not necessarily create fairness to all concerned. It may remedy underpayment to a degree, but it will not prevent "soldiering on the job" or "feather bedding" in employment, two colloquial terms which describe a pretense of working and a "slowdown" in production, respectively.

Straight-Line Compensation

By definition, "straight-line compensation" is a principle according to which remuneration is directly proportional to output. It is commonly known as the "piecework system" of wage payments. In its simplest form, the employee is paid for his work at a stipulated rate per piece produced in a given unit of time. It is a method that has been widely adopted because it is simple, inexpensive, and easily understood. The worker can compute his own pay, and it can be entered directly into the calculations of cost accounting without the necessity of an intricate formula in arriving at the cost of labor in quantity production and under varying and nonstandard conditions.

Unless the straight piecework system is qualified in its application, it may become subject to inequities and abuses. Originally under this plan, the employee was paid only for the actual amount of work he produced. If production was halted through no fault of his own, that was his misfortune. Also, piecework has led to price-cutting because of inaccurate standards or sharp practices on the part of management. In recent years, however, the piece rate is generally based on assured and accurately determined standards, and the employee is guaranteed base earnings to protect him against loss from interruptions to production.

Piecework wage payments can be applied either to individual or group output. The advocates of group piecework take the position that it is more equitable than straight piecework because an individual will suffer less from differences in rates between jobs in the same department. If straight piecework is paid to individual workers, some will feel they are discriminated against if they are assigned to tasks that turn out to be less remunerative than some other jobs performed by their associates in the group. To avoid grievances on this score, group piecework is preferred on the ground that each member of a department participates in total group earnings. In that way, if differences in piece rates between tasks prevail, no one employee is affected more than any other.

Modifications in Piece-Rate Systems

Since this textbook is not concerned exclusively with industrial management, and since piecework is not an incentive in all types of business,

no attempt will be made to provide an exhaustive and detailed analysis of all the modified piece-rate systems that have been developed over the years. Whatever their character, the aim has been to find a formula that would be fair, acceptable, and attractive as an incentive. Five such plans will be described briefly:

The Taylor Differential Piece-Rate System.—This system was developed by Frederick W. Taylor. Two rates are set up for each job according to a standard determined by time and motion study. A high rate is paid to those whose productivity is equal to or higher than the standard, and a low rate is paid to those who fail to reach it. The incentive is obviously not only to turn out more pieces but, by so doing, to realize a higher rate of pay per hour.

The Gantt Task and Bonus Plan.—This plan was devised by H. L. Gantt, an early associate of Taylor. In its modern application it provides that an employee be paid a bonus plus standard time for standard production or better. The bonus is a percentage of his hourly rate, which simply means that if he turns out as many or more pieces than required by the standard in an hour, he will have a higher piece rate. The incentive is obvious.

The Bedeaux Plan.—Another type of task and bonus plan was worked out by Charles E. Bedeaux, an industrial consultant. It is more complicated than the Gantt system in that it involves a point system. Each minute of allowed time is called a point. The number of points (that is, minutes) allowed for a particular job is shown on the employee's work ticket. The value of each point is his hourly rate divided by sixty. The basic hourly rate is guaranteed so that when a worker produces more "points" than there are minutes in an hour, he will have earned a bonus to the extent of the excess points.

The Halsey Gain-Sharing Plan.—This plan is named for its author, F. A. Halsey, a mechanical engineer. Under its provisions it is optional with the workman whether he elects to work on a premium basis or not. He is assured of his basic time payment, assuming he is competent in his job. But a standard time for a given task is determined. For every hour he can shorten this time he is given a proportional fraction of his hourly wage as a premium.

The Lincoln Plan.—This plan takes its name from its originator, James F. Lincoln, president of the Lincoln Electric Company, Cleveland, Ohio.[10] It is based on the theory that the piecework wage system is the most accurate means of measuring production. In the application of this system, fair and equitable standards of performance are set up. A rate of pay is then determined for standard performance, which rate is regarded as a

[10] For detailed description of plan, see James F. Lincoln, *Lincoln's Incentive System.* (New York: McGraw-Hill Book Co., 1946).

contract that may not be changed by management no matter what the earnings under it may be. Cutting piecework rates is not tolerated.

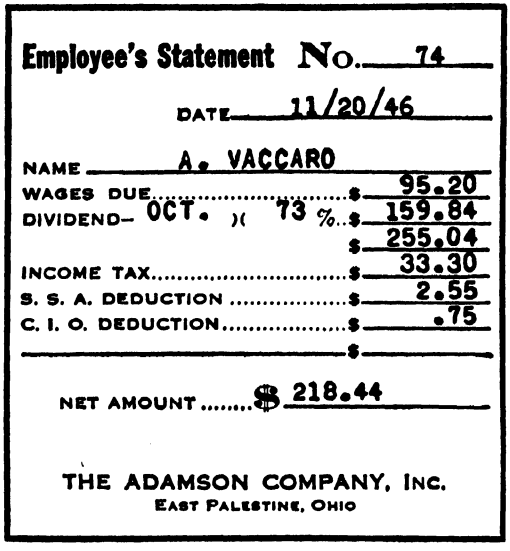
Profit-Sharing

It has been emphasized that the most significant contribution that incentives can make as devices of management is to bring about a stable integration of interests between employer and employees. To achieve this goal, good wages and an assurance of economic security are not enough because these considerations too often by-pass nonmaterial impulses. To integrate interests as fully as possible, a sense of participating must be engendered by promoting the incentives that incite ownership, as well as employees, to efficient performance. One of these incentives is the realization of profit; and another, closely related to it, is an awareness of authority and responsibility. Profit-sharing schemes are designed to make use of both of these incentives. Rarely successful for more than short periods of time, they must nevertheless be regarded as a highly desirable field for further and courageous experiment.

The Lincoln Electric Company, referred to above, also has an interesting profit-sharing plan. Increased savings that accrue to the company because of increased quantity, quality, and lower costs are considered to be gains that result from "incentive," and are called a bonus rather than profits. This bonus is shared, first, by the workers, engineers, and executives in accordance with their contribution to the success of the enterprise, and, second, by customers through lower prices. Profits are calculated as a fair return on investment and are counted as part of the costs of operation for the purposes of this plan.

As a further illustration of such a plan, one small company uses a 50–50 profit-sharing method.[11] All employees—office personnel, sales force, and production workers—participate in it. The gradation of each worker's share in half the profits of the company is worked out according to established wage or salary scales. Profits are determined and distributed as regularly as wages on the theory that the reward from profits must be tangible and immediately realizable to be most effective. Figure 48 shows how this system works out in practice. All inferences of paternalism or generosity are scrupulously avoided. It is emphasized that the stipulated share in profits is a right of partnership and not a liberal gift of management. To stress this policy and to implement it, the employees are also accorded both authority and responsibility for decision-making through representation in a production committee which has a voice in management to the extent implied by its name.

[11] John Chamberlain, "Every Man a Capitalist," a description of the profit-sharing plan of the Adamson Co., Inc., East Palestine, Ohio, in *Life Magazine*, December 23, 1946.



Employee's Statement No. 74

DATE 11/20/46

NAME A. VACCARO

WAGES DUE	$ 95.20
DIVIDEND– OCT.)(73 %	$ 159.84
	$ 255.04
INCOME TAX	$ 33.30
S. S. A. DEDUCTION	$ 2.55
C. I. O. DEDUCTION	$ .75
	$

NET AMOUNT $ 218.44

THE ADAMSON COMPANY, INC.
EAST PALESTINE, OHIO

FIG. 48.—Pay statement of the Adamson worker which shows that his wages were $95.20 for half of November and that he received $159.84 as his share of the October profits, or 73 per cent of his net pay for October.

Share-the-Production Plan

A modification of profit-sharing, but stressing the same incentive of partnership, is the share-the-production plan as adopted by a shoe manufacturing company.[12] It is also based on the conception that the traditional weekly wage system contradicts the idea of the integration of the interests of employer and employees. This plan attempts to keep workers enthusiastic and devoted to their employer by lessening the possibility of layoff when unfavorable business conditions come along.

The main feature of this plan is that employees share in a specified proportion of the value of the product of the company. The total annual payroll of all classes of workers is determined jointly by management and the labor union to be a percentage of the wholesale value of production. The amount thus allocated to wages becomes a part of the yearly union contract. Participation in the plan is limited to a fixed number of employees for whom eligibility is based on two years employment with the company. Once an employee has been designated, he cannot be laid off except for misdemeanor.

[12] The Nunn-Bush Shoe Company, Milwaukee, Wis., described by Joseph L. Snider, *The Guarantee of Work and Wages* (Boston: Graduate School of Business Administration, Harvard University, 1947), pp. 30–41.

Participants receive regular pay checks fifty-two times per year regardless of the number of hours the factory operates. Such payments represent drawing accounts the total of which, for each individual is his yearly differential rate which is calculated on his contribution to production. This differential is a flexible figure which is revised upward if the group wages fund accumulates a large balance at the end of the accounting period and reduced if it seems likely that drawings will exceed earnings. At the end of each four-week-period, the actual value of production in terms of wholesale sales is ascertained and the predetermined percentage of it is allocated to the wages fund. Each participating employee regularly receives a complete statement which shows exactly how his payments have been determined.

Guaranteed Annual Wage

From an employee's point of view, a guaranteed annual wage is an incentive because to some degree it promises economic security. From the employer's standpoint, it assures stability in employment and fulfills the social responsibility of furnishing steady jobs to workers. A further effect is to stimulate management to plan new work and to undertake new ventures when it is realized that the payroll stays in force whether employees work or not. All three of these considerations have been the basis for a guaranteed annual wage plan of George A. Hormel & Company, a meat packing concern of Austin, Minnesota, which will be used as an illustration of this system.[13]

The plan used by this company offers employment to nearly 6,000 employees on a year-round basis. There is no length of service required for eligibility, and it covers all employees except a few part-time workers. In its main features the plan is simple. It establishes the weekly wage of an employee by paying him in each of the 52 weeks in the year an amount equal to thirty-eight times his hourly rate whether he works more or less than 38 hours per week. If at the end of the year an employee has worked more than an average of 38 hours per week, he is paid for his extra hours.

Exceptional productivity is compensated by means of a group bonus system. This involves the application of standards to the work performed. The additional remuneration of the bonus will accrue to an individual as payment in any week for the number of hours by which the actual clock hours he works are less than the time set up by the standard for the volume produced. Since production in a meat packing plant is a departmental rather than an individual matter, the group bonus method is used. Thus, if the workers in a department achieve an output in 20 hours that

[13] *Ibid.*, pp. 19–29.

is considered to be standard at 30 hours, they receive their basic weekly rate plus pay for 10 extra hours at that rate. Production workers, mechanics, maintenance men, and so-called "white collar" employees who are not eligible for a bonus or extras because of the nature of their tasks are not discriminated against. Similar benefits are provided for them by other means in addition to their guaranteed annual wages.

Guaranteed Employment

Guaranteed employment is often confused with a guaranteed annual wage. The two plans are not the same, although the latter implies the former. It would be contradictory to envision a yearly salary without employment for the same period. Firms have hesitated to inaugurate guaranteed annual wage systems because they have feared that they would thereby be putting themselves into the uncomfortable and ethically questionable position of promising more than they could reasonably deliver. It is less difficult to guarantee a job for a definite period than it is to promise an assured income.

The Procter and Gamble Company of Cincinnati, Ohio, is a pioneer in venturing upon stabilized employment. Its long experience has become an important example of experiments aiming to turn to advantage the incentive of job security. The plan it uses was introduced in August, 1923, and with substantially no change, it has been in effect ever since.

The Procter and Gamble plan is very simple. It involves no formulas for calculating the amount of the annual guarantee or the amount of weekly compensation. The plan is a simple statement of guaranteed employment for a certain number of weeks, or the equivalent in hours, during the year. A summary of its provisions by an executive of the company is as follows:

> We guarantee a worker 48 weeks' work in the calendar year, provided he wants to work and will take any job we can give him. We don't guarantee an annual wage,—we guarantee a job.
>
> The employee's pay is controlled by the rate which covers the specific job he is working on.
>
> We don't guarantee every factory employee; a man has to be with us two years, by which time we both can feel that his association with us is more or less permanent; so we have the two-year period of probation.
>
> We don't guarantee 52 weeks' work. We guarantee 48 weeks' work in a given year, based upon the standard work week at the plant where the man is employed.
>
> The management retains the right to redetermine from time to time the number of hours which will constitute the standard work week.
>
> The directors retain the power, without changing the established work week, to guarantee only up to 75% of the established work week. (This 75%

reduction was invoked only once. During the dark days of the early 30's for a short time it was applied to three plants.)[14]

The Annual Bonus Plan

Bonuses, as we have seen, are generally premiums that are paid to workers for production above standard. Furthermore, a bonus is usually an appendage tacked on to some other incentive system as an added inducement. It is a common device attached to methods of payment for piecework. In the illustration which follows, the annual bonus is the main incentive. It is entirely apart from wages and salaries, and is never used as a consideration in hiring personnel. As evidence that an incentive plan is as applicable to a small concern as to a large one, the company selected is a highly specialized manufacturing concern that employs fewer than two hundred persons. Although shopwork is its principal technical production process, in no instance is piecework a basis for wage payments.[15]

In its employment policy, the company pays the going salaries and wages which prevail in the region for comparable services. To participate in its incentive plan, eligibility begins at the end of one year of service. Except for this provision, every person on the payroll is eligible, and no special distinction is made between factory workers, office personnel, or junior and senior executives. This mutual participation is based on the proposition that differences in productive capacity are compensated by differences in salaries and wages, and that the bonus available to all categories of employees should be in direct proportion to their established income based on their contribution to the yearly activity of the company.

A significant feature of the plan is the basis of the determination of the fund from which participation in the bonus is paid. The gross income of the business is regarded as consisting of three parts. First, there is the major fraction, which must be used to pay for going wages and salaries, materials and supplies, utilities and power, and all the other usual and necessary costs of operation. The second fraction is called a "bogey." It is reserved by the company for interest on invested capital, repairs, replacement reserves, and general maintenance. It is the minimum net income on which the business can be sustained and thrive. The third part is net income over and above both federal taxes and the bogey requirements of the business. This is the part that can be used for the annual bonus. This concept is roughly illustrated in Figure 49. Individual participation in the

[14] Excerpts from an address by William C. Werner, Manager, Division of Public Relations, Procter & Gamble Co., before the Employers' Association of Chicago, November 15, 1946.

[15] The C. A. Norgren Co., Denver, Colorado, manufacturers of lubrication and pneumatic appliances for heavy tools and other equipment.

bonus is figured pro rata on the basis of the relationship of the total earnings of the individual to the total earnings of all eligible employees. The plan is set up on a voluntary basis for one year at a time. The accrued bonus is paid in cash annually on December 15. In order that enthusiasm may not wane in the interim, prominent notice is posted each month showing the amount of the bonus credit for the month just closed and the total accumulation in the bonus fund to date. In order to avoid discrimination and

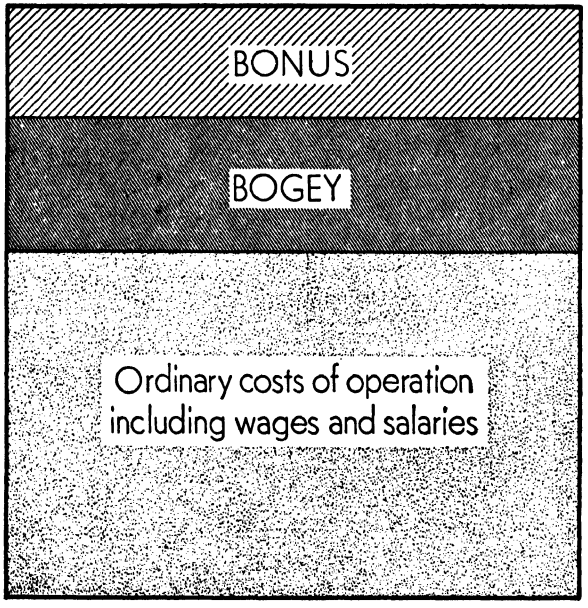


FIG. 49.—Graphic representation of the gross income for determination of the bonus fund in the C. A. Norgren Co.

dissatisfaction in the event an eligible employee should leave the company for any reason, all such former employees receive their full participation in the bonus for the interval in which they were qualified up to the time of their separation.

The Brookings Study of Annual Wages

The Brookings Institution study by A. D. H. Kaplan on the problem of the guarantee of annual wages furnishes a valuable and objective review of this subject. As shown in the foregoing discussion, it is closely related to the profit and bonus sharing plans, on the one hand, and to the employment guarantee and share-the-production plans, on the other. The

following excerpts give the point of view and significant conclusions of Dr. Kaplan:[16]

When it has been said that workers under the stabilization plans now operative are in general well satisfied with them, the personal element in the labor-management relationship seems as important as the formula in determining its success.

A plan like that at Nunn-Bush obviously calls for a high degree of mutual confidence between employers and employees. That confidence is reflected in the independent audit of the firm's books, the expense of which is borne jointly by the management and the labor force. On the basis of the annual audit, the workers at Nunn-Bush have on three occasions accepted a reduction in their base rates in order to prevent an excessive deficit in the reserve for wages. In similar spirit, the employees have agreed to price reductions which meant a smaller amount to labor in the interest of maintaining total volume, and hence the total amount of sales.

Procter and Gamble knew that soap was used the year round, but orders came in seasonal spasms in accordance with traditions established by the wholesalers. The manufacturer therefore had first to educate the retail trade to regularly spaced purchases throughout the year before a schedule of regularized production could be sustained. Hormel had to educate the labor force to the necessity of transfers from one job to another if slack time in one department were to be offset by productive work where it was available.

In contrast to the success of the annual-wage plan at Austin was the experience of the Hormel (Spam) plant in Chicago. There the annual-wage plan inaugurated in 1939 was abandoned after three years because of resistance by the employees.

It may even be that management, aware of the importance of income security to the maintenance of labor efficiency and industrial peace, will be inclined to go along with labor in enlarging the area of annual-wage commitments.

It is conceivable that a large percentage of the body politic would prefer a slowing down of material progress or a contraction of individual choice for consumer, worker, or investor; and even a levelling off at something less than our present standard of living, provided the standard upon which we do settle can be made more secure.

If, however, a generalized guarantee of annual wages is successfully promoted with the thought that the guarantee can be progressively expanded without contracting and radically modifying our present system of competitive private enterprise—then we are confronted with a dream that is destined to end only in disillusionment.

There is no inconsistency . . . . with the belief that . . . . firms could, by more effective utilization of their machines and man power, or more astute cultivation of their markets, come out with a sounder relationship between

[16] A. D. H. Kaplan, *The Guarantee of Annual Wages* (Washington, D.C.: Brookings Institution, 1947), pp. 44, 56–57, 76, 82, 209–11.

management and labor without sacrificing the profitability of the total operation.

The conclusion . . . . however, remains that if a system of generalized guarantees across industry . . . . is to be made effective, with sustained production to match the guarantees, the economy must be placed under a new discipline. An authoritative role would have to be created for a government agency as the arbiter of the flow of commodities, manpower, machinery, investments, and funds to keep pace with the stride of pay-roll commitments in the affected areas of the economy.

Noncontributing Retirement Plan

Retirement plans are generally recognized as financial incentives. Many such systems have been devised. Most of them require that employees contribute jointly with the employer in establishing the principal which yields the annuities upon retirement. A deviation from this customary method is the noncontributing retirement plan, so designated because no deductions are made from wages and salaries in order that employees may participate in it. All funds are supplied by the employer and are usually deposited in escrow with a prominent bank or other financial institution.

An example of this plan is the one established by the Western Auto Supply Company of Kansas City, Missouri. In addition to the foregoing provisions, it sets the normal retirement age at sixty-five. Three years previous service with the company is the only qualification for participation. Upon retirement, the annual income realized by the employee is computed by multiplying the years of participation in the program by a percentage of the annual pay received each year during that period. An employee may elect to retire any time after reaching fifty-five years of age, in which case the annuity income is the actuarial equivalent of his normal annuity benefit. In the event of death, options are provided for survivor benefits, but only one beneficiary may be designated.[17]

Annuities that can be realized under noncontributing retirement plans appear to be relatively modest at best. There are two reasons why this is so. In the first place, the annual increments to the retirement fund are not so great as they are when employees themselves contribute a share to them. In the second place, the establishment of federal social security retirement benefits, to which the employee is also eligible, has tended to reduce the urgent need for substantial annuities from private sources.

Conclusion

The foregoing examples of nonfinancial and of financial incentive plans are by no means exhaustive of all the methods that have been devised and

[17] The retirement plan of the Western Auto Supply Co., Kansas City, Mo., 1946.

adopted in various places. Nor are they general patterns that fit all situations. They have been presented merely as illustrative of what has been done to discover incentives that can be applied to the solution of many vexing problems of the relations between employers and employees.

No particular incentive plan is a ready-made appliance that can be installed on the mechanism of management without adaptation to a special situation. Nevertheless, the illustrations which have been presented demonstrate certain principles and procedures in the field of incentive management that may be turned to account in enterprises of all kinds and sizes. There are many companies throughout the land that could achieve greater regularity of business and employment and could enjoy improved morale in personnel relations, by wise improvements in their incentive plans.

QUESTIONS

1. After referring to a standard dictionary for definitions of the terms involved, explain and defend the following statements:
   a) Motivated action and impulsive action are opposites. The former type is a foundation of organized management; the latter type is only of accidental value, and may even be harmful to effective management.
   b) "Goad," "stimulus," "incitement," "provocation," "encouragement," "inducement," and "influence" are all synonyms of incentive. Yet "incentive" is the best word to use as a managerial expression. Of its synonyms, "stimulus" and "inducement" come closest to "incentive" in meaning.
   c) *Esprit de corps* is an important phase of morale, but it is not exclusively definitive of this term because other factors in the mental habits of individuals are included in morale.

2. Name and describe briefly the four types of desire that underlie motivation, and explain how and to what extent desire may play a significant role in each of the following situations:
   a) The awarding of lapel buttons or pins at suitable ceremonies in recognition of the services of particular employees, according to some such plan as a bronze pin for 10 years, a silver pin for 20 years, and a gold pin for 30 years continuous service.
   b) An incentive pay plan based upon a reasonably accurate measurement of performance which provides a bonus in excess of customary earnings for production in excess of the normal or customary task standard.
   c) Being assigned to a foreman who is recognized for the following personal qualities: he is honest and fair; he assumes full responsibility for mistakes and does not shift blame from himself; he is progressive in his attitude toward methods, procedures, and products; and he always strives to solve and to settle employee grievances at the supervisory level, if possible.

3. Explain fully why and how each of the following considerations must be recognized as having the characteristics of a financial incentive plan. Note especially the proper relationship between measured performance and extra pay:
   a) Contracts with American employees whose work location is in certain foreign countries, in which provision is made for long vacations, such as six months, with full pay, and transportation to and from the United States after a certain period of foreign service, such as five years.
   b) Payment of a year-end bonus consisting of a week's pay to each employed person.
   c) Payment of a year-end bonus consisting of $50 in cash to each employed person.
   d) Payment of higher than regular rates for all work done between midnight and 8:00 A.M.

4. Analyze and explain fully the "nonfinancial" incentives that are inherent in the system of classification of salaries by ascending amounts as the title and skill involved in a particular position increase in importance as illustrated in Figures 46 and 47. Distinguish between these "automatic" salary promotion plans and classification and standardization as applied to "production" employment in a factory.

5. From the standpoint of the stimulating influences of a nonfinancial character involved in them, discuss each of the following incentive situations:
   a) A competent supervisor has a friendly attitude toward his workers, speaks cheerfully to them as they work, mingles with them during rest periods, makes inquiries concerning the welfare of their families, and tries, wherever possible, to help them solve their personal as well as their employment problems.
   b) Loyalty, *esprit de corps*, and morale—all tend to reflect the degree of sincere belief in the serious importance of their work on the part of employees, and in their ability to think about their work. Management must convince workers that thoughtful attention to their work is really worth while.
   c) Every employee should understand his job so well that he will be able to think through his daily problems and get his work done, even though he may be obliged to improvise and to deviate from fixed written instructions. The very achievement of successfully completing a job will raise his morale.

6. Discuss fully, with particular reference to the significant points involved in the time payment method of employee compensation, the following statements:
   a) When employees are paid at the rate of so many cents per hour or so many dollars per week because this policy is the agreed or customary rate for their type of work, proper incentive is possible only by putting

effectively into practice the basic principle that each employee is entitled to a fair day's pay in return for which the employer is entitled to a fair day's work.

b) Suppose a skilled worker is being paid 40 cents per hour more than his helper or apprentice who assists him in his work. It may be assumed that improvement in machinery makes the skilled worker's task more difficult and the duties of the helper less important. Thus a wage rate inequity develops. Such inequities must be settled or disputes will arise and incentive will vanish. This adjustment can be accomplished by detailed study of jobs and methodical classification of jobs into groups, each group being entitled to the same time payment.

7. Discuss the following statements fully with particular reference to the significant points involved in the straight piecework method of employee compensation:

a) When employees are paid at the rate of so many cents per piece produced, or when a group of employees is paid at the rate of so many dollars per unit of product assembled, proper incentive is possible only by putting effectively into practice the basic principle that each piece-rate worker is entitled to total compensation proportionately higher than a fair day's pay, in return for which the employer is entitled to proportionately more than a fair day's work.

b) If the standard or fair hourly wage for a fair day's work on a particular task is $1.00 per hour, and a piecework employee produces 25 per cent more work per average hour than is contemplated for a fair day's work, then the straight piecework plan is inequitable as compared to straight time payment for the same class of work, unless the time worker is able to earn an average of $1.25 per hour when he is on piecework. In other words, the basis for measurement of the fairness of a straight piecework plan is its relation to the principle of fairness in a time payment plan, namely, "a fair day's pay for a fair day's work."

8. List six or more plans of wage payments described in this chapter, arranging them in categories according to each of the following schemes:

a) In the order of the importance of the factor of accuracy of underlying time and motion study. (Note that the Taylor plan would contain little incentive if the "high task" were easily accomplished; also that straight time payment could be applied without any measurement of a fair day's work.)

b) In the order of the ease and accuracy with which each employee can compute his accumulated pay at any time. Indicate your appraisal of the factor of ease of computation as a nonfinancial incentive.

9. Distinguish fully between the following types of incentives, (1) profit-sharing, (2) share-the-production, (3) guaranteed annual wage, (4) guaranteed employment, and (5) the annual bonus, from the following standpoints:

a) List for each plan the different types of financial and nonfinancial incentives, giving reasons for your classification. Follow the Igleheart classification of the "ingredients of job satisfaction" in your analysis of each plan. Do not overlook the Roethlisberger and Dickson comments on the social incentive.

b) Even if it were true that these plans result in passing on to the employees the income of an enterprise that would otherwise be paid out as taxes, the incentive aspects of such plans make them desirable in concerns that are not earning large incomes above expenses. (Comment on the accuracy of this statement, rewriting it so that it expresses your own views.)

10. Write a brief commentary expressing your own views on the subject of the guarantee of annual wages as set forth in the excerpts quoted from the study of this subject by A. D. H. Kaplan.

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Chapter XV

THE MANAGEMENT OF BUSINESS ASSOCIATIONS

ONE OF the striking phenomena of the social economy of the United States is the development of thousands of voluntary associations. Each of these associations has a purpose and an organization. Prominent among them is a large group designated as business associations. They are the voluntary associations that have been formed by businessmen for business reasons. Although organically they are separate and distinct from individual business concerns and companies, yet from the standpoint of purpose, motivation, and influence, they are actually a part of private business management. For this reason, consideration will be given to the organization and management of the business association in the light of its close relationship to private business itself.

In Chapter XII it was pointed out that there are more than 15,000 business associations in the United States today.[1] Of this number 80 per cent are local organizations and consist chiefly of the town, city, and county chambers of commerce. The remaining 20 per cent are national, regional, and state trade associations that have to do with manufacturing, wholesaling, retailing, and such service types of business as finance, real estate, construction, insurance, transportation, recreation, and many others. In fact, it is difficult to name any occupation, profession, or trade that is not represented by an association of this character.

Not only is the number of business associations large, but their variety seems endless. Each new association is slightly different from all others. Each one is founded by a nucleus of enthusiastic members and proceeds through long years of evolution. Some business associations achieve worth-while ends. Many fall far short of initial hopes and expectations. However, most of them struggle along somehow. Few business associations, once organized, go out of existence no matter how unnecessary or worthless they seem to have become.

VARIATIONS IN ASSOCIATION ORGANIZATION

Figure 50 summarizes the wide variety of business associations, indicating the possible range of variation of certain major characteristics, that is, membership, purpose, scope, staff, and organization. The figure is ar-

[1] See p. 315.

ranged to be read both vertically and horizontally. It should not be regarded as more than a guide or indicator of the typical business association. Every conceivable arrangement of the factors of membership, purpose, scope, and organization can and probably does exist in some voluntary association. Nevertheless, Figure 50 does indicate the usual or typical situation. Reading across the diagram, each of the variables is self-

Variable	Approximate Degree of Variation			
A. Type of member:	Qualified persons	Persons and businesses	Qualified businesses	Qualified associations
B. Typical degree of qualification for membership:	Open to all qualified persons	Regionally restricted, ex., chamber of commerce	Qualified along horizontal or vertical trade lines	Open to all qualified associations
C. Usual purpose of typical association:	Collection and dissemination of information; conferring status	Collection and dissemination of information; forming and enforcing community policy	Typical trade association purposes	Leadership and coordination of member associations
D. Scope of association activities:	Local, state, regional, national, or international	Local, state, or regional	Local, state, regional, or national	Regional, national, or international
E. Typical organization of association's staff:	Local chapter secretary and limited national headquarters staff	Extensive local staff and limited state or regional staff	Limited local staff and extensive national headquarters staff	Limited regional, national, or international staff
F. Common type of association:	Professional association	Chamber of commerce	Trade association	Council

Fig. 50.—Variation in association characteristics.

explanatory. Each of the horizontal lines does not form an exact scale of values, but rather indicates the typical or normal degree of variation between different association types.

The Professional Association

The first vertical column of Figure 50 indicates the general characteristics of the association of businessmen whose membership consists entirely of persons. This type of association is given the general title of "professional association" at the bottom of the column. Such an association is

open to all properly qualified persons. Its usual purpose is to collect information from or for its members and to disseminate information among its members. The professional association very often becomes a device for conferring status upon its members, since they must possess certain ability in order to become members. The professional association may be local, state, regional, national, or even international in scope. It is usually organized into local chapters headed by a national headquarters organization.

An example of a professional association of businessmen of general character is the service club, a good example of which is the Rotary Club. Officers of this club—including a president and a secretary—are generally unpaid members except in the larger organizations where a full-time professional secretary is employed. Weekly luncheon meetings are held, the purposes of which are the fellowship of the members and programs intellectual, informative, and entertaining in character. Above the local club is the Rotary regional district and International Rotary, both being associations of associations. The local clubs are the members of the district organization, and the Rotary districts in the United States and other countries are the members of Rotary International. Rotary International determines the qualifications for individual membership, issues charters to acceptable new clubs, publishes a magazine for its members, and conducts the annual meeting.

A professional association of businessmen of limited character is exemplified by the National Association of Cost Accountants. As the name implies, this association is open to members who are at work in some branch of accounting. The local, or regional, chapter holds monthly dinner meetings, addressed by a speaker on some business subject. The national headquarters supervises the local chapter activities, publishes a magazine for its members, and conducts the annual meeting.

Chambers of Commerce

The second vertical column of Figure 50 indicates the general characteristics of the association of businessmen whose membership is composed partly of persons and partly of businesses. This type of association is given the general title "chamber of commerce" at the bottom of the column, since there is a chamber of commerce organized in this manner in every important city and town. The chamber of commerce is usually organized to cover some definite place, such as a town or city. Its major purpose is to collect information from and for its members, and to disseminate information to its members. However, the chamber of commerce is also developing great importance as an organ for formulation and enforcement of community policy in such matters as public improvements, governmental budgetary control, and solicitation of new industries.

The chamber of commerce is primarily a local agency and develops as extensive a local staff as its budget will permit. The state or regional chamber of commerce is rarely organized on more than a limited staff basis.

The Boston Chamber of Commerce, for example, is a large institution of this sort, having hundreds of personal and corporate members throughout the Boston metropolitan area. Its staff organization is divided into departments covering such activities as membership, industrial development, and harbor and port development. A magazine is published for the members and many different meetings are held each year. Some meetings are arranged for the entire membership. Others are restricted to a selected portion of the membership. The staff devotes an important part of its efforts in representing its interpretation of the point of view of its members to government officials and agencies. In other words, the staff takes community policy, as formulated by its membership, and attempts to enforce it.

Steps above the typical city chamber of commerce are the state chamber of commerce, the regional council, the United States Chamber of Commerce, and the International Chamber of Commerce. Each of these is a membership organization, the latter two being primarily associations of associations. The United States Chamber of Commerce is, in large part, an association of the local chambers of commerce of the entire country. The International Chamber of Commerce is an association of national chambers of commerce like the United States Chamber of Commerce.

Around the local chamber of commerce there usually develops a group of smaller local associations, linked both with the chamber of commerce and with some national association of specialized character. For example, a Better Business Bureau is a local association of merchants organized to encourage and enforce truthful advertising. The Better Business Bureau does work which would otherwise fall to the chamber of commerce to perform. It may itself be a member of the National Better Business Bureau.

Another example is the retail trade board, which replaces or serves as the otherwise necessary retailers department of the chamber of commerce. A retail trade board, or merchants association, is an association of retail business. Such questions as opening and closing hours are agreed upon and promulgated. Store employees are offered centralized educational opportunities, for example, in the art of selling. A buying pool on such material as string and boxboard may be operated for the members. In addition to its relation to the local chamber of commerce, the retail trade board is usually also affiliated with the National Retail Dry Goods Association, which is a trade association among whose members are most of the larger retailers of the country.

Trade Associations

The third vertical column of Figure 50 indicates the general characteristics of the associations of businesses, or "trade associations." The trade association differs from the chamber of commerce in having little or no membership of individuals as distinct from corporations; and in having most of its activities and staff organization concentrated at the national, or headquarters, level. There are hundreds of trade associations in the United States, each with somewhat different organization and purposes. From the standpoint of membership, trade associations may be of the vertical or horizontal type. These types and their interrelation result in four different kinds of trade associations as follows:

1. The National Stationers Association may be considered an example of general vertical organization, since its membership is open to all retail stationers, to all wholesale stationers, and to all manufacturers selling either to wholesale or retail stationers. It vertically covers the whole field of the stationery industry—manufacturing, wholesaling, and selling.

2. A national association of manufacturers of business forms exemplifies a possible affiliate of the National Stationers Association. This would be an example of limited vertical organization because its membership would not be open to wholesalers or retailers, but consists solely of manufacturers of record books, forms, and related products.

3. The Associated Industries of Massachusetts may be taken as an example of general horizontal organization of a trade association, since its membership is open to any and all manufacturers within the borders of the state of Massachusetts. A similar national organization, the National Association of Manufacturers, is likewise open to all manufacturers as members. The National Retail Dry Goods Association, mentioned above, is another example of general horizontal organization.

4. A manufacturers research association would be an example of limited horizontal organization. Its membership would be open to various kinds of manufacturers but limited to a small number of members, in order to permit effective pooling of research work done by the executives and specialists of the member companies and by those paid by the association.

Councils

The fourth vertical column of Figure 50 indicates the general characteristics of the association of associations, or "council." The term "council" is a convenient name, but usually the name of the association does not reflect its organization. Rotary International and the United States Chamber of Commerce have been mentioned above as being associations of associations. The National Industrial Council is another ex-

ample, this being an affiliate of the National Association of Manufacturers. The National Industrial Council has as its members the state associations of manufacturers, such as the Associated Industries of Massachusetts.

The association of associations is somewhat like the holding company of private business. The council type of organization may have great importance because it tends to become responsible for the coordination of its members, thus giving it quasi-managerial influence over its member associations.

CHARACTERISTICS OF ASSOCIATION MANAGEMENT

Associations, for the most part, are corporations. They are incorporated under special state statutes that govern the creation of "corporations not for profit." Therein they differ from business corporations; but like them, associations have charters issued to them which give them corporate existence and authorize them to carry on their affairs as legal entities. Therefore an association, like any other corporation, is an artificial person created by law. As such, and within the limitations of its charter, it has all the rights and privileges of a business corporation.

In addition to its charter, an association is usually self-regulated under a constitution and a set of bylaws. The constitution provides for the establishment of the organization and contains the name and location of the principal office of the association, its objectives, and a brief statement of its government and powers. The bylaws are formulated to provide for the operation of the association. Among other things, they ordinarily contain sections that deal with membership, dues, directors and officers, meetings and elections, committees and procedures of amendment.

The Membership Level

One marked difference between a business corporation and an association is the fact that the latter needs no capitalization and no shareholders. Yet, from the standpoint of management, the members of an association occupy a position similar to that of the stockholders in a corporation. In the case of the private business corporation, the real owners of the business are the more or less numerous stockholders. The stockholders, however, commonly delegate practically all of their ownership authority to their elected committee, the board of directors. Aside from the power to vote once a year for the directors, the reserved powers of the stockholders are small in number and are rarely used.

In the case of an association the ultimate authority and control of management rest with the members in good standing, collectively. However, instead of voting shares of stock, each member has only one vote, so that a voice in the affairs of the organization is an individual matter rather

than one of financial interest. Also, should the assets of an association be liquidated for any reason, all members in good standing at the time of such liquidation would share alike in the equity of the organization unless stipulations in the constitution and bylaws provide otherwise. By a "member in good standing" is meant one who has met the specified conditions of membership, such as the payment of dues.

It is customary for the members to delegate their authority to one of several committees of which the main committee is usually called the "board of directors." However, the degree of delegation of authority is never so complete as it is in a private business corporation. The board of directors and other committees generally act for and in the name of the basic group, that is, the entire membership. Usually the constitution and bylaws of the association reserve many subjects for final decision by the entire membership at regularly called meetings. Some associations go so far as to provide for a referendum or mail vote of their membership on all vital questions of policy. The referendum or poll taken by the Chamber of Commerce of the United States of its individual members, each of which is a local chamber of commerce, is an example of this method of policy formation. Even where no provision for compulsory reference to the entire membership exists, the fact is that a committee of members such as a board of directors cannot disregard majority opinion since individual members can always express their negative vote merely by resigning.

Top Management Level

In the business association, there tends to be dual top management. The president is the unpaid chief executive, usually elected by the members voting at their annual meeting. Because he has been elected by the members, he has a mandate to manage the association independent of, though linked with, the board of directors.

In addition to the president, the association membership elects, or more often the board of directors selects, the salaried top executive of their paid staff of employees. This salaried chief executive reports to the president, to the board of directors, and to the entire membership. As illustrated in Figure 51, this results in dual top management, the exact division of authority between president and secretary (or otherwise titled salaried executive) depending on such factors as personal tact, forcefulness, and determination, and particularly on the extent to which the paid executive voluntarily subordinates himself to the unpaid association president.

When an association attempts to do something, its procedure is to refer the matter to a committee, with or without "power to act." If it has "power to act," the committee can consider the matter and then can state the conclusions or decision of the association without obtaining other approval. Otherwise the committee reports back to the board of directors

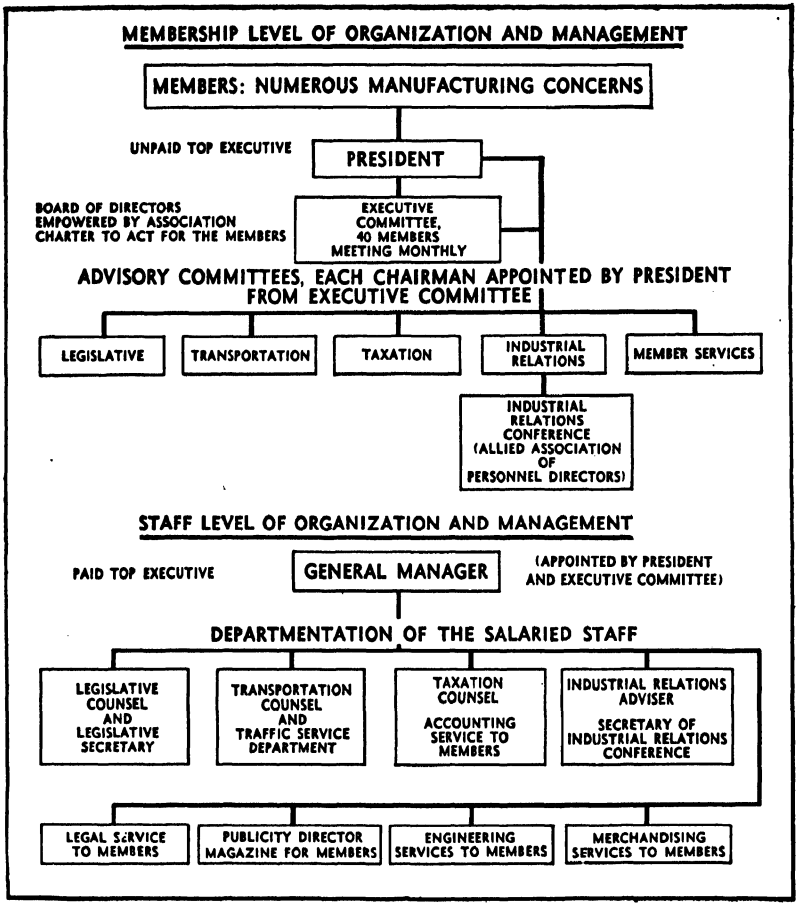


FIG. 51.—Organization of a typical state manufacturers association.

with findings and conclusions. If the committee is the board of directors, it must ask the president to seek approval of the entire membership at the next meeting unless it has "power to act."

Sometimes the association organizers, to avoid such cumbersome machinery, create a self-perpetuating board of directors and even continuing key committees by authorizing the particular committee to fill its own vacancies. This device is in most common use in institutional management, which occupies the border zone between association management and business management. An endowed hospital, college, or university, for example, is usually organized with a board of trustees which maintains its own existence by filling its own vacancies. Since it is thereby freed of responsibility to any higher group, the board clearly has full power to make decisions.

Although "power to act" rarely goes to the point of self-perpetuating committees, the typical association usually gives its directors and committees rather wide leeway in making other types of decisions for its members. For example, an association may take a position for or against pending state or national legislation. This decision is made by the association's board of directors; and the public, as well as the members, are thereupon notified that this is the attitude and position of the membership. It must be remembered that this use of "power to act" is constantly tempered by the silent veto of threatened or actual membership resignation.

Organization Illustrated

Figure 52 is an unusually complete presentation of the complex organization of a large national trade association. The chart, prepared by the National Lumber Manufacturers Association as an exhibit for a book on its organization and growth, brings out very clearly the upper, or membership, level of management, and the lower, or staff level, of management.[2] It also shows in the same compartment, linked together, the dual top management consisting of unpaid president and salaried manager. The chart names ten advisory committees in addition to the executive committee and the board of directors. These advisory committees cover a wide range of activities, briefly tabulated below:

1. The forestry committee and related staff activities are concerned with national and state forestry policy and forestry legislation and with research into improved forestry practice.

2. The committee on lumber economics and related staff activities are concerned with collection and dissemination of statistical and economic facts concerning lumber. This includes analysis of prices to the extent permitted by law. This department is a member of the National Industrial Conference Board, a national association of associations for study and distribution of economic facts.

3. The Credit Corporation Committee supervises the National Lumber Manufacturers Credit Corporation. This is an example of an association owning and managing a private business enterprise, namely, a credit-rating and collection service.

4. The committee on governmental relations and its related staff provide the legislative service, not only for the National Lumber Manufacturers Association but also for other affiliated lumber associations which subscribe to this special service.

5. The advisory committee on interinsurance has charge of the

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[2] John W. Blodgett and W. M. Ritter, *Highlights of a Decade of Achievement by the National Lumber Manufacturers Association* (Washington, D.C., March 5, 1929).

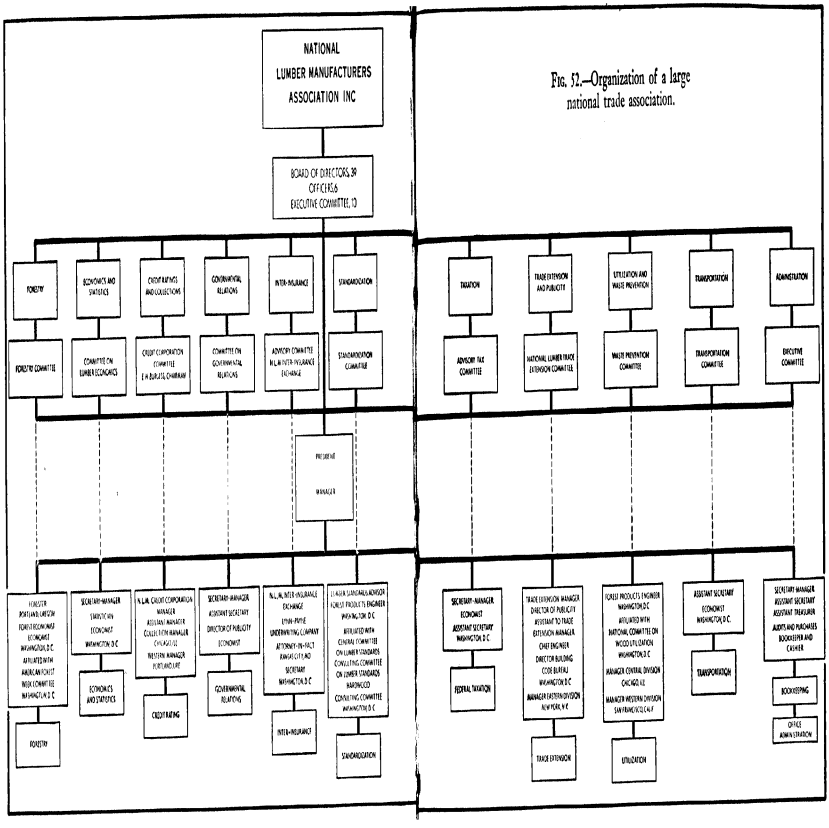


Fig. 52.—Organization of a large national trade association.

National Lumber Manufacturers Inter-Insurance Exchange. This is another private business enterprise, providing reciprocal insurance together with inspection and fire prevention services to members.

6. The standardization committee and related staff are a research agency to develop and promulgate specifications, grades, and standards for lumber.

7. The advisory tax committee and related staff provide a member service on federal taxation problems.

8. The National Lumber Trade Extension Committee and related staff are an extensive organization doing research and promotion work to increase the use of wood. An important part of this work is in connection with municipal building codes, revision of which in many cases permits much greater use of wood in building construction.

9. The Waste Prevention Committee and related staff are a research and publicity agency aiming to reduce waste in the preparation and use of lumber.

10. The Transportation Committee and related staff provide transportation counsel and traffic service for the National Lumber Manufacturers Association, and also for the other lumber associations which subscribe to this specialized member service.

THE TRADE ASSOCIATION STAFF

The word "staff" is used in this chapter to designate the entire group of paid employees of any particular association, including the salaried secretary or manager. This use of the term "staff" is in accord with general usage and does not conflict with other applications of the term, since the voluntary business association is an agency created by certain businesses to help them attain their own business purposes. The association em-

ployees, in other words, form a part of the organization of each of their member firms. From the standpoint of member companies, association employees are part of their staff to whom have been delegated certain staff duties, as determined by the membership management level of the association. Most of the work done by an association for its members is staff work, involving the exercise of staff authority only. It is the rare association which performs any work of functional or line type for its members. The National Lumber Manufacturers Association, of Figure 52, is one of these exceptions since it operates both a credit and collection business and an insurance business for its members.

The Salaried Trade Executive

Associations with a long history may be observed to have gone through stages of expansion and contraction. Sometimes they display great activity; at other times they are obviously in the doldrums. A potent cause of this variable rate of progress is the dual chief executive level of unpaid president and salaried manager, director, or secretary. Obviously there will be times when a new president and his salaried manager fail to agree; yet the disagreement does not bring about appointment of a new manager or election of a new president. The disagreement, however, may injure or retard the progress of the association. Here is another great difference between private business management and association management. In a private business the single chief executive, the president for example, must retain the confidence of the board of directors above him and has full power to force coordination beneath his own position. In an association, the coordination of the salaried manager with the president and board of directors above him and with his staff of employees beneath him is much less automatic and often falls far short of desirable and efficient interrelations.

One of the common criticisms made by business executives of some particular one among their numerous associations is that it is being run for the benefit of the paid staff of employees rather than for its members. Another angle of this same criticism is the caustic comment one sometimes hears that the association's paid manager is not trying to do what the members wish done, but instead is trying to make the members do what he, the paid manager, wants them to do. Of course this is another angle of the question of how far an association should go in trying to enforce its policy decisions on its members. The paid association manager often is the victim of circumstances, trying to carry out the instructions of some policy committee or of the board of directors.

Granting that such criticism of the paid association manager is often unfair and groundless, it is, nevertheless, sometimes true that the manager attempts to play the role of independent executive and tries to disregard,

weaken, or detour around the membership level of association management. The sharp criticism of such tactics as "dictatorship" proves that the concept of dual top management is natural and inherent in association organization. The successful association executive keeps his position and accomplishes desired results through skilled coordination. He cannot become a strong or outstanding leader without having the unpaid president and the general membership cry "tyrant" and set about to unseat the dictator or else destroy his association through key member resignations.

Functional Staff Organization

Viewed from the standpoint of the entire association, the staff is organized into functional departments. Each department, in general, consists of a committee of members and the "staff" executive who serves as expert for the committee. The output of each of these functional departments of an association is member service. The committee on prevention of industrial accidents, for example, will have associated with it an appropriate functional executive, namely, the safety engineer. The output of this combined functional department of the association is specialized member service, that is, safety engineering.

There is no well-defined line of authority within an association staff. Instead there are several lines, each extending from the salaried manager to a functional executive and through him to the several levels of assistants and clerks constituting his organization. The most important of these lines of authority runs from the manager to and through the office work departments. Since an association produces nothing but member service, it follows that such clerical activities as mailing, multigraphing, and stenography are of importance because they do the manual labor incidental to member service.

However necessary it may seem to the individual member, much of the member service work done by any association is routine and relatively inconsequential. Members will ask for minor assistance in locating a new source of supply, in checking credit, in translating from a foreign language into English, in finding an applicant for a job, or in seeking a job for a friend. Nonmembers write or call with their requests and problems each of which requires tact and time to handle properly.

To sum up, the paid employees of a business association are usually grouped in functional departments under appropriate functional executives. These functional executives, viewed collectively, form the staff of the association. They produce an output called "member service" which is part of the necessary staff work that otherwise would have to be done by individual members. This is again a dual relationship from the standpoint of organization. Within the association, the salaried departmental execu-

tive is in charge of a function as exemplified in Figure 51. In relation to member users of such departmental service, these association executives are performing staff activities of staff type value to particular association members.

POLICY-FORMING ACTIVITIES

The relation of the association staff to policy divides itself naturally into two phases: activities before policy has been decided and formulated, and follow-up activities. The first activities lead up to formulation of policy, and the latter activities lead toward enforcement of policy.

Preformulation activities of association staff executives may be characterized as a process of collective fact-finding. For example, assume that a local association of retailers receives a suggestion from one member that the association undertake to develop a centralized or pooled delivery service for all of the downtown stores. Its first problem is to ascertain the facts. The association staff gets at the facts by collecting them by an appropriate technique. It may send out a questionnaire to its members. It may send an investigator to each store. It asks the related associations in other cities about their experience and practice.

Where it is practical to do so, one of the best ways to make an investigation is to call a general meeting, conference, or even committee meeting of members. Skillful direction of the discussion of such a meeting will result in each member telling his fellow members, as well as the association executive, just what the problem is, as he sees it, and how it should be solved.

A vital by-product of the staff efforts to collect the facts with respect to the policy problem is that the members themselves find out much more about the problem. This may result in solutions being adopted by the individual members, so that it ceases to be a collective or group policy problem. More often the great gain is in making the members more conversant with the situation and, therefore, more able to vote wisely when called upon, and in committee or informal contact to express opinion and thus to participate in formulating policy.

As associations develop in size and in financial strength, they become more willing to put this preformulation type of work on a sound basis. Larger associations may make a thorough canvass with trained investigators before reporting to one of their committees as to the actual facts. They use the questionnaire technique sparingly, but accurately, testing their returns and developing an adequate sample. They develop an extensive library and data file. They do not hesitate to employ laboratory and statistical experts to check their data and analysis methods.

After the results of the collective fact-finding done by the staff have been laid before the appropriate committee, the subject is discussed, and

the policy of the association is formulated. After further discussion, if required by the president and board of directors or by the entire membership assembled in annual meeting, the formulated policy, as revised, is promulgated as the policy of the association's members. In the example of delivery service of downtown stores, used above, the association might decide that such service should be pooled and that some private trucker should be found who would undertake the service for all the stores. This decision is the first step in enforcement of policy, which now becomes the duty of the staff. The association executive is now expected to do something about the decision of the association, often with no weapon except tact and no tools except an occasional letter or personal call.

The best means of securing enforcement of an association decision on policy is education of all concerned—members and nonmembers alike. Every means of education is used by associations, such as meetings, conferences, moving pictures, form letters, personal letters, magazine articles in the association's publication, reports of progress, and personal contacts between approving members and disapproving members or nonmembers.

As already pointed out above, a new enforcement factor is developing, namely, promulgation of the association policy as a regulation or law. To an increasing extent, the legal principles of public safety, public health, and interstate commerce are being used for enforcement of business policy upon one and all—association member and nonmember alike. Much of the demand for this type of enforcement of policy comes from the general public, but it is also true that certain business associations have sought to solve their enforcement problems by encouraging legislation and regulation of this sort.[3]

Types of Policy Considerations

Disregarding their burdensome errand-running and courtesy work, the real member service of the typical business association is in the field of policy. Of course this does not mean association policy, but rather member policy. To make this clear, the following examples of various association activities in the field of policy are given:

1. In dealing with broad national issues, an association, for example, may decide to oppose a new tax measure on the ground that it would place an unfair and unreasonable burden on its members.

2. In the case of local political issues, an association may decide to favor a new underpass on the ground that it will promote public safety and provide a market for the products of member companies.

3. In the field of industrial relations, an association may decide to institute an educational system, so that the salesmen of its members may attend and develop greater selling skill.

[3] See pages 314–16.

4. In production, an association may urge use of certain standards or specifications of grade, size, or quality, in order to increase the mass production possibilities.

5. In marketing, an association may publish lawful open price data which will help the individual member to solve his pricing problems.

6. In the field of finance, an association may urge that credit should not be extended to certain categories of customers of member companies.

7. In purchasing, an association may become a buying pool for its members by offering to place a collective order for any or all of its members with one source of supply.

8. In research, an association may establish fellowships at universities, or may establish its own laboratory, to attempt to solve various problems encountered by the members.

This brief review of the various policy activities indicates that associations have as varied an interest in policy as do their members. There is no policy problem an association is unwilling to tackle if instructed to do so by its members.

Securing Policy Compliance

This discussion of actual association organization shows clearly that the central activity of the upper, or membership, management level is to determine policy. The central board of directors and the standing and temporary committees drawn from the membership, all concern themselves chiefly with policy formulation and enforcement. If the association is adequately financed and properly organized, the work of the association, whether research, publicity, or managerial in character, will be performed primarily by the paid staff.

As has been pointed out, the methods used by committees to sound out membership sentiment with respect to policy differ greatly from committee to committee. The common assumption is that the committee members can speak for the entire association because they would not serve on the committee if they did not have some special skill or interest. The silent vote expressed by resignation of a member is the best test of this assumption.

In attempting to secure compliance with established policy, the committee which has made the decision faces the most difficult aspect of association management.

The most common method of obtaining enforcement of policy is to authorize the staff to undertake a campaign of education. Such a campaign usually brings good results. If the policy is easy to understand and is fair to the average member, its adoption by most of the members and even by some of the nonmembers is not difficult to accomplish. For example, a policy to eliminate Saturday morning work may be adopted by

a majority of the retail stores as a result of educational work by the local chamber of commerce staff, acting on instructions of their board of directors.

Naturally, most policy decisions made by an association produce the best results only if adopted by all, or nearly all, of the affected businesses, whether members or nonmembers. Consider the confusion if one of the railroad companies refused to accept the standard specifications of the Railway Engineering Association and constructed equipment or used track dimensions that made interchange with other railroads impossible.

Since education alone will rarely cause all the affected businesses to adopt the promulgated policy, associations resort to one of two methods to secure compliance. One method is to reward compliance and penalize noncompliance. The other method is to ask some governmental agency to step in and require compliance.

The reward and penalty method can be used in many cases. Railroad equipment specifications or track standards, for example, are not difficult to enforce because every railroad knows the advantage of uniformity and the loss of traffic from connecting lines in event of nonuniformity, that is, noncompliance. Automobile manufacturers readily conform with tire manufacturers on standard rim sizes and tire specifications, lest their product earn public disfavor because of lack of readily available, local stocks of replacement tires.

With the growth in number and activity of business associations, policies are being developed and their enforcement attempted in instances where the automatic economic reward and penalty is less clear to the backsliding member or recalcitrant nonmember. Under such circumstances, associations are sometimes tempted to provide cartel-type fines and punishments. Since such methods of enforcement are illegal in the United States, they need not be discussed further.

A technique of increasing importance is to encourage an appropriate government agency to enforce the policy which has been decided upon. The trade practice conference device sponsored by the Federal Trade Commission tends in this direction, since quasi-government approval is derived from the mere relation of the Commission to the conference. State legislation which permits price-fixing of trade-marked articles accomplishes an enforcement purpose. Licensing laws calculated to limit certain types of business, for example, gasoline filling stations or house-to-house selling, have similar purpose and effect.

CRITICISM OF THE TRADE ASSOCIATION

It is desirable to consider the criticisms of the American type of trade association. The following excerpts from the Trade Association Survey made for the Temporary National Economic Committee help to sum-

marize and explain the statements and discussion of this chapter. These quotations also emphasize the transitional situation of the trade association, in its relation to government control and regulation.

A trade association may serve as a means of restraining competition in two ways: (1) By fostering mutual restraints of competition among the members of the industry; and (2) by furthering actions designed to suppress the competition of enterprises outside the group. . . . . Of the two types of restraint the second is much less frequently found among the activities of trade associations than the first. Group action to eliminate competition from enterprises outside the group, unless backed by legislation ordinarily requires coercion. Group coercion in turn encounters definite legal obstacles, which is not necessarily true of mutual efforts of association members to minimize competition among themselves. . . . . Mutual restraints of competition, or, to avoid any invidious connotation which the term "restraint" may have, cooperative efforts that are designed or have the capacity in some degree to temper the force of competitive circumstances, are found among the activities of a large proportion of national and regional trade associations. . . . .

That unmitigated rivalry for the available business of an industry through price competition is shortsighted economics and a potentially destructive business policy is characteristic of the thinking encountered in trade association circles. It is deemed to be within the best interests of the participants in the market that rivalry be moderated—restrained in some degree. This principle of business conduct is urged in most instances, not as a means to an unlimited exploitation of the market, but as a means of achieving "market stability," or "price stability"—as a way of avoiding "destructive" or "cut-throat" competition, "price demoralization," or "chaotic competition." Trade associations differ, of course, in the explicitness with which they define and in the emphasis which they place on this objective. . . . .

In their endeavor to promote the stability of the industry the staff and leaders of the trade association may actively attempt to indoctrinate the members with the principle of voluntary self-restraint in the market. Or, accepting as sufficient the individual members' belief in its desirability, the association may endeavor to implement this policy by recommendations concerning specific trade practices or by collecting and disseminating trade information that will enable the members to act intelligently in accordance with a farsighted attitude toward the market. Or, in the event of intense competition among the members or chronic "chiseling" by competitors outside the association, the association may attempt through collusion to attain the market stability that could not be achieved by less direct means. . . . . Although trade associations from time to time are implicated in charges of collusive restraints on competition, there appears to be ground for the often-repeated contention of trade association leaders that a large majority of trade associations, at least those of national and regional scope, avoid sponsoring or participating in this type of concerted action. . . . .

Noncollusive efforts by trade associations to achieve "market stability" are principally of three types: (1) The fostering of trade practice standards; (2)

the dissemination of trade statistics and price information; and (3) the promulgation of uniform cost accounting principles and guides and the dissemination of cost statistics. . . . .

In support of their efforts to achieve price stability, trade association leaders contend that unrestrained competition, particularly under conditions of excess capacity and depressed demand, has a tendency to drive prices to levels that are destructive of the interests of the enterprises, their investors, workers in the industry, and in the long run of the interests of consumers as well. . . . . To deny or disregard these claims as lacking in essential truth or wide application is to argue for the enforcement of really free competition. Such a position would point to a policy of forbidding not only the collusive restraints of trade but all trade association activities that may result in a lessening of competition. . . . . It might forbid trade associations altogether, on the ground that people who are to compete fiercely should never be allowed to be convivial together.

As to the basic issues, it appears that two paths are open. The first is to sharpen and strengthen the antitrust laws in the effort to approach more closely to the ideal of perfect competition. In such a program the functions of trade associations would be further limited and restricted. The second path is to relax the antitrust laws, opening the way for industries to endeavor to deal with specific problems by group action, under the supervision of some appropriate Government agency. Many individuals have urged the desirability of some agency whose duties would not be overwhelmingly those of prosecution and law enforcement but which could contribute toward the operation of a more flexible policy with respect to business practice and performance. In such a program trade associations would be the natural vehicles . . . . and their present activity would undoubtedly be further extended. . . . .[4]

THE MANAGEMENT OF BORDERLINE CORPORATIONS

In comparing one form of corporate business organization with another from the standpoint of management, three types are generally recognized—namely, the private business corporation, the business association, and the government proprietary corporation. Yet there are some enterprises and institutions which do not lie within any one of these classifications. They have some of the organization characteristics of all three of them. Therefore they are borderline concerns.

Institutional Management

In addition to the business association, there are many other corporations organized under statutes that provide they must operate on a "not for profit" basis. Typical among them are schools, colleges, universities, hospitals, sanatoriums, penal and charitable institutions, and others of a public or quasi-public character. Whether they are supported by endowments, gifts, or public revenue, or whatever their purposes and objectives may be, the problems of business management are common to all of them.

[4] Temporary National Economic Committee, *Monograph No. 18* (Washington, D.C., 1941), pp. 345–49, 352–53, 358.

The authority for the formulation of policy in an institution of this kind is usually vested in an appointed, elected, or self-perpetuating board of directors, or, more commonly, a board of trustees, together with an unpaid chairman or president. This plan of organization is essentially identical with that of the business association. Furthermore, dual paid and unpaid top executives tend to prevail. In the management of an institution as in a typical association, the salaried executive, be he president, chancellor, director, or manager, cannot function independently of the unpaid chairman of the board or president of the organization.

Clearly, such an institution is not an association; it is more nearly a business in that its organization must be such as to permit effective and efficient operation. At the same time, such an institution also resembles a government-owned business, or even a government bureau, since it is organized to perform some public service on a "not-for-profit" basis. In these circumstances, the organization and operation of the institution, under its salaried top executive, contains many compromises between considerations of private business and considerations of public welfare which are apparent to the student and need not be further elaborated.

Mutual Companies

There is another type of business organization that resembles in part the business association and in part the private business corporation. It is known as the "mutual company." The term "mutual" implies a reciprocal relationship between persons, that is, giving in return for having received. Hence, a mutual company is one which ordinarily possesses no capital stock but in which members assume the role of stockholders and share both risks and profits. The relationship of the members to one another is one of interchange and interdependence. This form of mutualized business is perhaps most common in mutual insurance companies, in which the members, as policyholders, assume the peculiar double relation of being insurers and parties insured. It is the whole membership of a mutual insurance company which contracts to indemnify each of the members with respect to the loss against which a policyholder may be insured.

There are thousands of mutualized businesses. They include not only insurance companies but savings and loan associations, mutual savings banks, cooperative societies, and many others. In its normal business affairs, a mutual company performs its operations like a private concern. It is an individual establishment vested with the same rights and powers as any other lawful enterprise. In general, it has similar business objectives and the same concern for efficiency and profitableness. From its members and its clients, it obtains its capital which it invests in its business, and its management is subject to the authority, responsibility, and accountability of a salaried executive group quite like any other business firm.

On the other hand, the mutualized businesses all have an association of appropriate character at their ownership level. This association may consist of the depositors in the bank or the insurance policyholders, each of whom becomes a member automatically when he enters into the financial relationship. The association may be a trade association or trade union which has gone into business for the benefit of its members. It may be a group of consumers, like the Harvard Cooperative Society, which operates a large retail store; or a group of producers, such as the California Orange Growers Cooperative, which grades, packs, and markets Sunkist oranges around the world.

Since the ownership level of the mutualized business is an association, the question arises as to the role of the membership level of management and as to the presence or absence of dual top management, paid and unpaid. The answer is that the imperative need for effective business management automatically relegates the association members to a role akin to that of stockholders, expressing themselves only through election of the board of directors which, in turn, hires a top executive to run the business. Nevertheless, the second or unpaid top executive is usually present and is always a potential factor in mutual management.

The Value of Comparisons

In other fields, such as economics, the value of comparative studies has long been recognized. Entirely aside from the growing importance of the trade association as a phase of business management, comparison of the association type with the business type of management is important and valuable.

In private business corporations the ideal situation is to have a board of directors and a president, or top executive, sharing the highest management in balanced fashion. In the trade association, there tends to develop dual management, partly performed by the unpaid board of directors and president and partly performed by the salaried association secretary. This duality of management and resulting destruction of unity is a tendency to be guarded against in private business. However necessary and useful this type of association management is, it represents an undesirable possibility in private business enterprises.

In associations, committees are an absolute necessity. This is not true of business management, which can learn and profit from association experience, and thus develop within the particular business enterprise, efficient but not burdensome use of the committee device.

QUESTIONS

1. Business executives and business concerns commonly justify membership in particular associations on the grounds of "group solidarity" or "all are exposed to the same problems and therefore all should support a common

agency that is attempting to study and solve them." Discuss these arguments from the following standpoints:

a) The number of ways such reasoning could be justified by two concerns dissimilar in every respect except that both are located in the same city.

b) The number of ways such reasoning could be justified by two concerns, one located in New York and the other in Los Angeles, who are identical as to product and size.

2. Review the brief discussion in Chapter I of the disparaging attitudes toward business in ancient times. Against this background, discuss the view held by some persons that various types of business associations in the United States can and do lessen criticisms of modern business enterprises. If you take a negative position in this argument, be sure to support your reasoning with defensible evidence.

3. Correct the following partially incorrect statements, giving reasons for your revisions:

a) It is easy for the unpaid president or chairman of an association to exert effective leadership because of the assistance given him in preparation of his speeches by the salaried secretary who is always ready to take full responsibility.

b) The reason why salaried secretaries of associations have banded themselves together into professional groups with high standards of ethics and of training requirements, is because such standards and training make it easier for them to dominate their associations and overshadow their unpaid presidents.

c) Figure 32 in Chapter VIII, which illustrates in some detail the organization of a large business enterprise, shows clearly that private concerns never make use of the dual system of top management organization common to associations. The same policy is also demonstrated in the references to the top management of another large company described in Chapter XI.

4. Assume the existence of an active and effective association of owners of apartment houses in a large city. Indicate, with adequate reasons, the extent to which you believe this association will exercise the following types of authority:

a) Authority to plan, including investigation and research.

b) Authority to decide.

c) Authority to organize.

d) Authority to enforce.

e) Authority to coordinate.

5. By means of pertinent illustrations, point out how the concepts of the spans of control, time, energy, attention, and personality apply inherently in the dual management system of organization of the typical association.

6. Assume the existence of a national association of lumber manufacturers such as outlined in Figure 52. Indicate, with adequate reasons, the extent

to which you believe the board of directors of this association will undertake the following types of procedures as discussed in Chapter V:

a) Acts of decision.

b) Acts of confirmation.

c) Acts of counseling.

d) Acts of review.

7. Assume the existence of a large trade association such as the one illustrated in Figure 52. From the standpoint of effective management, explain the importance of the following:

   a) The role of trusteeship of—

      (1) The directors.

      (2) The unpaid president.

      (3) The salaried secretary or manager.

   b) The comparative importance of and emphasis upon the profit objective and the occupational objective insofar as the association itself is concerned.

8. In Chapter VI review the topics that deal with executive activities, tools, and procedures. Prepare a statement that will present your own views as to the extent of the applicability of each of them to the work of a salaried association executive.

9. Elaborate upon the following statements and explain more fully what is meant by each of them:

   a) There are more rigid and narrower limits to the discretion of an association executive than normally apply to a business executive, yet within these limits the freedom of the association executive to act in the interests of his organization is very great.

   b) The channels for appeal of exceptions reach up through member businesses to the association. Likewise, the association forms a natural and important channel for the transmission downward of imposed governmental policies and the interpretation of such imposed policies.

10. Explain and illustrate the place and importance of strategy, tactics, and diplomacy in association executive activities, both at the unpaid and salaried management levels.

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Chapter XVI

THE MANAGEMENT OF GOVERNMENTAL PROPRIETARY ENTERPRISES

THE FIELD OF GOVERNMENT PROPRIETARY MANAGEMENT

THE field of government proprietary management is important both from the standpoint of its nature and the type of business units which are embraced in its scope. Such units include water systems, toll bridges and tunnels, railroads, electric power plants, irrigation systems, housing projects, insurance concerns, and banks. Indeed, it is probably true that among the governments of the world, in their proprietary management of varied enterprises, there is to be found at least one example of every type of business organization.

The term "captive mine" has been used as a colorful description of a coal mine owned and managed by a large industry. This chapter is concerned with the management of business enterprises which are "captive" in somewhat the same sense within our own structure of government. As will be developed through close analysis of one of the most common types of captured enterprises, the municipal water utility, government proprietary management is a distinct and unique field of management and organization because of this "captive" relationship to government. Government proprietary management of these "captured" enterprises is quite different from the management of coal mines owned and operated by private enterprise.

Government Proprietary Management Defined

The dividing line between government itself and a government proprietary enterprise is factual, not theoretical. The test is whether the particular unit of government collects a charge from each customer or user, which charge is related to the quantity or cost of the product or service taken or received by that particular customer. If such a charge is universally and uniformly levied against all customers, then the government unit is acting as a proprietor and the result is, not government, but government proprietary management.

It is not necessary for the income from charges to equal the cost of operation of the business. The government may, of course, insist that its proprietary business be self-supporting, a normal and healthy policy much to be desired. It may make up a deficit through general taxation. It may

capture all surplus or profit above annual expenses as an addition to its tax-derived income, thus imposing a sales tax upon the customers of the proprietary business. A government very often does not relate income and expense, mingling tax revenues and business income in one general fund and appropriating from such total income for all expenses, including the cost of operation of the proprietary business. When a government, merging all income and expense in this manner, likewise follows a much too common practice by failing to keep books on capital investment, depreciation, maintenance, and replacement, it becomes impossible to tell whether the "captive" proprietary business is being operated on a deficit, a self-supporting, or a profitable basis.

The term "government ownership" is commonly used to describe government proprietary management, because of its frequent use in political campaigns concerning acquisition by the public of some existing business enterprise, such as an electric power utility. However, ownership is not an essential test. The government may manage a business, as proprietor, even though it does not own it. This is true, for example, of the Boston Elevated Railway, which continues to be privately owned, although it has been operated for many years by a board of trustees appointed by the governor of Massachusetts. On the other hand, publicly owned enterprises may be privately operated. This is true of the interstate railroad owned by the city of Cincinnati and the gas works owned by the city of Philadelphia. Both of these ventures have been leased by their government owners and have been managed by private lessees for several decades.

Types of Government Proprietary Enterprises

Government proprietary management includes sharply defined businesses such as the various municipal utilities; and it also includes borderline types of enterprises which form a boundary zone between itself and government as well as between itself and the association type of management.

Some government proprietary businesses are limited to governmental units as their only customers. This is true of the military arsenal and the navy yard, which produce and maintain specialized military products and munitions for their government owner. Another example is the prison factory, which is commonly required to confine sales of its products to other governmental agencies, thus minimizing the competitive effect of its enforced labor.

Many government proprietary businesses are required by law to provide some of their services free or at far less than cost, the resulting deficit being borne by taxation. The municipal hospital, for example, must admit patients without regard to their ability to pay. The state university is partly supported by taxation, thus reducing very materially its necessary

tuition and fee charges collected from the individual student. Despite these exceptions, the normal type of government proprietary business offers its product or service to all available customers, and obtains most or all of its income from its resulting sales revenue.

Historically, government enterprises of this type are of comparatively recent origin. Although the federal government has operated the postal service for more than a century, most of its other business enterprises, such as the Federal Reserve Banks, and the Tennessee Valley Authority (public utility operations), the Panama Railroad and its associated steamship line from New York to Panama, the Panama Canal, the Alaska Railroad, the Inland Waterways Corporation (barge line), the federal reclamation and power projects such as Hoover and Bonneville Dams, the Export-Import Bank, the Reconstruction Finance Corporation, the United States Housing Authority, and many other government proprietary business enterprises are all of comparatively recent origin, that is, since about 1910.

In the case of the states and municipalities, much the same history may be noted. Beginning more than a century ago, states and cities have been building and operating canals, railroads, water systems, banks, and other businesses. However, there were few such enterprises created prior to 1850. Since 1850, and particularly since about 1910, there has been a rapid increase in the number and the relative importance of government proprietary businesses managed by state and local agencies.

Management by Trusteeship

The moment a proprietary activity or business enterprise is purchased or taken over by the government, some sort of trusteeship level of highest management must be created. It is impossible for the thousands, perhaps millions, of citizens to manage the business personally. Nor can any single person or group of persons, no matter how elected or appointed, be said to be the owners of the business and therefore entitled to the rights and subject to the responsibilities of the private board of directors. The elected or appointed top management level in the case of the public business is necessarily a sort of trusteeship level. Whether one executive or a commission, he or they have in some manner been legally clothed with power to manage a business which is not and cannot be owned in any personal sense. Trusteeship is used here in a broad sense to indicate accountability to the public rather than to imply any uniform legal responsibility.

PROPRIETARY MANAGEMENT IN CITY GOVERNMENT

In order to give specific point to the various aspects and problems of government proprietary management, its establishment and operation as a part of municipal government will be used as typifying its chief char-

acteristics. Cities, both large and small, are commonly concerned with the management of one or more utilities that have been developed to serve the needs of the population within and often adjacent to their corporate limits. By "utility" is meant a service essential to the public welfare, but for which users are charged specified rates apart from the levies of public taxation. Well-known examples of such utilities are those that supply water, electricity, gas, and street transportation.

The Prerequisites of Efficient Management

Many cities have tried for decades to pour the new wine of proprietary business enterprises into the old bottle of traditional city departmental organization. In other localities there have been experiments with various degrees of independence and separate organization, even to continued operation of the utility system by means of the purchased private corporation.

This experimentation has often been expensive and wasteful. The public has been forced to learn that the economic laws of supply and demand and price continue to operate even under public management. The public has typically expected more capacity and more of certain types of service than were expected of predecessor private utilities. Organization has become, in most cases, more complex, and efficient management more difficult to obtain than under private conditions. In addition, the utility has sometimes discovered that its municipal government is often impulsive or even irresponsible, inclined to raid personnel and treasury and to disregard the plain words of contracts and agreements.

Out of all this confused experimenting there is evolving a trial-and-error proof of the necessity for strong central management and integrated organization of the municipal utility. How can the proprietary enterprise live within its income unless its income is permanently appropriated, by whatever device, to its use? How can the public be served courteously and quickly unless all contacts with the public are under the same management, not scattered among various city departments? How can extensions and betterments be planned and constructed efficiently and serviceably unless the agency that operates the utility also has a part in planning, or at least in approving, the new work? Hard facts such as these force all government proprietary enterprises toward better organization and efficient management.

The City Manager, Council, and Board Plan of Organization

As has been stated above, the ultimate authority for proprietary management by a unit of government resides in an established trusteeship rather than in ownership. This trusteeship, in theory, may be vested with authority and responsibility as broad as the powers and obligations in-

herent in the board of directors of a private business corporation. In practice, however, there are important limitations to the authority of the board of trustees of a municipal utility. These restrictions are due to considerations of length of service of individual trustees, the internal organization of the board itself, and the difficulties encountered in bridging the gap between the functions of trusteeship and those of the actual operation of the utility.

In a city government which consists of a council and a city manager, or in which there is a specialized district utility board, involved problems of management have been solved by making a sharp distinction between the higher management level of trusteeship and the next lower level of executive activity. This executive level corresponds approximately to the president or general manager of a private corporation. It is usually a single salaried executive, directly responsible to the trustees, the city manager, or the utility secretary or manager. Thus the trustees, without breaking down the legal concept of their group authority and responsibility, delegate operating management to a paid, personal representative, who derives his executive authority from the trusteeship group and is accountable to them.

The Mayor Plan of Organization

The mayor, having derived his own mandate directly from the people, can, and often does, exercise his executive authority without any thought of accountability to the city council. In a sense, therefore, this method of organization provides for separation of duties within each management level and cannot be represented as a true pyramid of executives heading up to the highest or trusteeship level. The mayor, by virtue of the veto powers of his office, is a member of the trusteeship group, exercising a restricted legislative responsibility over council decisions. This dual role of the mayor often breaks the top management of the city into two parts. Under such circumstances, the city council, instead of being the trusteeship head of the city government—comparable to the private board of directors—either becomes an annoying dissenter and heckler of the mayor or is controlled through party machinery and made subservient to the mayor and his political party.

Beyond doubt, the combination of the powers of trusteeship and powers of the executive in the person of a forceful mayor does get things done. But such a combination is not without its difficulties. Any change in the person of the mayor, by reason of elections, causes breaks in policy, or even the undoing of the work of predecessors. Control of a municipal utility by the mayor causes such effects to be felt both in major policies and in operation matters such as forced turnover to make room for the supporters of the new mayor.

Because the mayor of a city has his own elected status, separate from the city council management committee, he can drift toward dictatorial control over all city employees and city departments. The city manager, on the other hand, is more like the secretary of an association. He is the creature of the management committee that appointed him. He derives much of his power as top executive from the management committee, in whose name he speaks. To get things done, he must "sell" his ideas to the management committee. This does not keep him from being a leader and a forceful executive. However, he cannot assume the prerogatives of the general manager in a private business, nor those of a general in command of an army, without running the risk of losing the support of his management committee and of the community.

Cities which operate their municipal utilities as part of the general city government, under the city council-mayor plan of city organization, tend to scatter their government enterprise among the older departments of the city government, in "built-in" style. This system introduces many operating complications for the utility. It causes public annoyance and criticism because of divided responsibility and lack of coordination below the level of the mayor, and it fails to give weight to the basic legal and psychological differences between the utility, a proprietary undertaking, and the regular city activities or governmental undertakings. Finally, mayors, because of their political interest in controlling policy and personnel throughout the city government, are notoriously poor in delegating authority to subordinates. The system of mayor-trusteeship and mayor-management thus produces a flood of problems beyond the capacity and time of the mayor—all pressing for attention.

THE MUNICIPAL WATER SUPPLY UTILITY

From the standpoint of definitive study, one of the best examples of government proprietary management is the municipal utility which supplies water, and sometimes other services such as electricity, to the public for domestic and industrial consumption. The remaining portion of this chapter will therefore consist primarily of an analysis of this important type of public enterprise.

The modern municipal water system became possible in 1664, when French government engineers brought about development of cast-iron pipe. Their first installation was for the fountains at Versailles. So excellent was this installation that it is still in use today. About 1815, the first modern plumbing fixture, the water closet, came into use in the better-class houses of London. The quickly increased demand for domestic water supply developed the water utility type of enterprise.

In 1800, Philadelphia's municipal water utility started operation. It was

the only government-operated water utility in America at that time, and its use of cast-iron mains and its large steam-pumping plant made it one of the mechanical wonders of the age—the showpiece and pride of all Philadelphians.

By 1900, there were about 3,000 water utilities in operation in the United States, half of them privately and half municipally owned and operated. By 1935, there were about 6,000 water utilities in this country. There were 5,400 municipal water utilities, but the 1,500 private water utilities of 1900 had dwindled to about 600. The largest remaining private water utilities, in 1935, were the Hackensack Water Company, serving about 400,000 residents of 50 suburban communities of Greater New York—all in New Jersey; and the Indianapolis Water Company, serving about 360,000 residents of Indianapolis, Indiana, and vicinity.

THE BOARD OF TRUSTEES OF A CITY WATER UTILITY

By definition, a "board of trustees" is a committee to which has been committed, in the interest of others, the legal right and power of disposition and use of property and the management of the necessary business affairs of an enterprise. "Trusteeship" implies the powers and responsibilities of superior management plus the central objective that the decisions made and the actions taken shall result in impersonal rather than personal benefits.

The board of trustees of a city water utility occupies this position of top management of a business enterprise concerned with one or more vital public needs. The enterprise itself is most generally a specific function of the city government, with the result that the board of trustees constitutes a unit of government. In a managerial sense, it is often accountable through the mayor or city manager to the city council which is the governing body of the municipality, but in a broader sense, it is always accountable directly to the public for whom it has assumed its major utility service responsibility. Where there is no separate board, its trusteeship responsibilities as discussed above, are undertaken by the city council and the elected mayor, if any.

Composition of the Board

A study of various water boards and utility district boards leads to the conclusion that, as a class, government enterprise trustees are high-type citizens who take a sincere interest in their duties and who work long hours at little or no pay. With management and policy power divided equally among the board members, the opportunity for personal profit or "graft" is small and seems to be very rare. Board members do exact from their utility petty favors, such as patronage rights to place friends in

employment, and rather often welcome promotion from honorary pay to one of the higher-salaried positions with the enterprise. Rarely could it be said, however, that such perquisites as are exacted exceed what the directors of a comparable private corporation would probably consider reasonable.

Boards tend to be composed of older men. It is a mistake to think of public trustees as being unimportant men. It is more correct to think of them as being "safe" men, whose attitude on various problems important to the appointing power has been tested by years.

An outstanding reason why younger men will not ordinarily serve on utility boards is the usual charter or state prohibition against personal profit from a governmental position. The government enterprise, in the course of the ordinary year, buys from, or uses the services of, a considerable portion of the more important businesses of the community. The younger man, active in business, must not only sacrifice the time needed for his own work, therefore, but must also sacrifice business profits that might otherwise come his way.

Many older men refuse to serve when tentatively canvassed because of the rigidity and the implications of the provisions intended to prevent fraud and graft. Board members must commonly give bond, and older men know that the surety bond is sometimes collectible when no fraud has occurred, as for example, in a bank failure where deposits of government funds are involved. Viewed in this light, board membership is not an honor to be coveted, but a responsibility to be dreaded.

Tenure of Board Members

Once a board member has been appointed or elected, the employees of the government proprietary enterprise desire the longest possible service by this board member. This is because the board member learns slowly, as the problems of the business are turned up at the monthly meetings. The board member tends to rely, in his early career on the board, too much upon outside experience—however valuable—and too little upon actual knowledge of the utility's particular problems. The board, with power spread evenly among the members, naturally listens to the "authoritative" statements of its members. Length of service is the only possible remedy for what might be called the "amateur experting" within the board of one member upon his fellows.

Powers and Duties of the President

A question of importance is the relative power and duties of the board's president, usually elected by the board members from their own ranks. In Louisville, Kentucky, for example, the president is paid a typical though modest executive's salary. He has actual presidential duties, be-

cause the private water supply corporation is still kept alive by its municipal owner. The East Bay Municipal Utility District (Oakland, California) on the other hand, re-elected the same member president year after year. Although not paid more than his associates, the annual reports comment on the fact that he has spent part of every business day in his office. Evidently, by common consent and his own willingness, his duties are broader than those of the individual member.

Powers of Committees and Members

In general, the power of standing committees within the government enterprise board is sharply limited by the legal responsibility resting on the full board to pass all binding motions and make all final acts. Standing committees tend to be contact and research devices which recommend final actions to the board.

The device of "power to act" by which an individual board member is given the power to fill in the blanks left in a motion already passed by the board is an interesting technique for delegating power of the board for reasons of speed or efficiency. Many an internal controversy rages when the manner in which the "blank check" was filled out by the delegated member is spread on the minutes as an accomplished fact.

The right of the individual member of the trusteeship group to give direct personal instructions to any executive or employee is, in theory, limited, unless specific management authority has been delegated by law or by the board to the member. This is a recurring problem. When one trustee "orders" patronage employment favors or other perquisites, he is approaching an ever present potential source of organizational uncertainty and disruption.

This brief survey of trustees of government proprietary enterprises—especially as found in water boards and utility district boards—indicates that they are, in general, well qualified for the work of highest management. Use of the trustee group as a complete "management committee," as used in private business, is hampered by the following problems:

1. The length of service of board members is an uncertainty.
2. The power of the president of the board is limited. He is not the president of the enterprise, only of the board.
3. Similarly, standing committees of the board cannot in practice acquire power and stability.
4. There is a legal inability to delegate the authority of the board, even to one of its own members, which makes the device of passing a motion in blank, conferring "power to act" upon one of the board's own members in a particular case, difficult to use.
5. Board members, attempting to cut across red tape by giving personal instructions to executives or employees, create confusion or raise ethical ques-

tions, both tending to prevent the board member from exercising any executive authority.

THE EXECUTIVE LEVEL OF MANAGEMENT

Students of government generally distinguish between "amateur" and "professional" executives. The "amateur" is usually thought of as one who is elected or appointed to represent the voting public, whereas the professional is one who is retained or employed. Clearly, the proper role of the elected or appointed "amateur" is trusteeship as defined above. The "professional" or "career" executive should derive authority from, and be accountable to the trusteeship group which employs him. Most business enterprises operated by the government, such as municipal water utilities, suffer complications and inefficiencies of management due to their disregard of this basic principle. There are two reasons for such defects. First, every government proprietary business unit comes into being as a result of some legislative act, such as an ordinance, a law, a charter, or a constitutional amendment. Usually neither lawmakers nor lawyers who draft legislation understand the importance of the proper separation of management levels. In the second place, the public mistrusts high-salaried professional executives. This emotional attitude makes all too easy the selection of weak, and all too difficult the selection of strong, subordinate executives by the "amateur" members of the trusteeship group.

Since the trusteeship group cannot be familiar with all phases of the utility, it is necessary for the top executive, on the one hand, to serve as a filter through which problems are sorted, analyzed, and classified, and then transmitted to the trustees for decision. On the other hand, current decisions of the trustees must be converted into appropriate instructions. Although the top executive has narrow personal limits of discretion, he has broad powers of conversion of trusteeship decisions into instructions and orders, issued "in the name of the trustees." Thus from the standpoint of the trusteeship group, the top executive is its eyes and ears; and from the standpoint of the operating organization, he is the mouthpiece of the trustees. This two-way coordination between the trustees and the operating organization is the essence of top level management activities in a government proprietary enterprise.

The weaker the trusteeship activity, the less able it is to perform effectively, and the more the top executive resembles a general of an army or the strong leader of a well-organized business. Conversely, strong activity at the trusteeship level shifts the responsibility of the top executive toward two-way coordination activities described above.

Status of the Public Enterprise Executive

The chance of the municipal utility executive for relatively high pay would be greater if his duties more closely resembled those of the general

manager or president of its antecedent, the private water utility. As has been pointed out, the application of the term "manager," even in cities with strong water and utility boards, does not make the top executive of the utility a "manager" in the private business sense. The public enterprise executive is almost entirely a coordinator. It may well be that this type of authority should customarily command a lower salary than is paid for the broader kind of leadership, characteristic of general management in private business. The difference is the degree of delegation of authority by the management committee. The board of directors of a private business will commonly delegate to its general manager the maximum possible authority and exact from him maximum possible personal responsibility and accountability for success or failure. The board of trustees of a government proprietary business, on the other hand, is apt to delegate minimum personal authority to its top executive. Everything, as far as possible, is determined on the basis of custom, law, regulation, or motion passed by the board to meet a specific case.

Another reason for the relatively lower salary of the top executive in municipally owned, as compared to private utilities is the practice of promotion from within. Like other municipal undertakings, management is usually recruited either from within the organization or from within the city. The latter method also produces executives of local experience, and, therefore, of local earning power. The typical top executive of the municipal utility may be described as an engineer, usually with university training, whose knowledge of his utility approaches perfection but who has had little or no outside experience. Even though his ability as an executive might justify much higher pay, he has no bargaining power.

It must not be forgotten that the municipal executive sometimes is in a favored position from the standpoint of having life-employment under civil service rules. He can and does place a high value on such security in comparison with the relatively greater insecurity of executive employment in private business.

Restrictive Legal Functionalization

Legal functionalization is a characteristic of most government proprietary business enterprises. This term designates the practice of defining in exact legal language certain functional duties to be performed by such executives as the attorney, the auditor, the treasurer, the purchasing agent, and the civil service commissioners. Often these functional assignments are overlapping and conflicting. Under its charter a municipal utility may be fully responsible for management, but, at the same time, its authority is limited since all purchases must be made through the city purchasing agent and all legal counsel must be obtained from the city attorney. Such fixed functionalization leads inevitably to duplication of work. For instance, the utility organization and the office of the city

auditor may both be held responsible for accounting. The result is more or less perfectly coordinated parallel books. Duplication is present not only in the books themselves, both sets of which must be posted from original records; but also in the time spent in reconciling the two sets of books and adding explanations of minor differences resulting from slight variations in posting.

Again, legal functionalization creates a consciousness and a habit of divided responsibility on the part of the employees in an organization. The practice of divided responsibility is accepted both because the theory of government under our Constitution generally sets up checks and balances and because the principle of double control is commonly used throughout the field of accounting. In practice, the latter reason is more important than the former, though attorneys who draft the particular enabling legislation doubtless have the former in mind. In some cities, a check drawn by the municipal utility in payment for services must be "audited" by another office of the city government before payment. This means that the proposed payment must look reasonable and honest and must have its proper accounting classification so that it may be posted against the proper item of the budget. The check, having run this gantlet, may then be deposited for payment, but it is still only a warrant until redeemed out of utility funds by the city treasurer, a third arm of the city government.

Legal functionalization automatically shifts management emphasis from leadership to coordination. Thus when a question arises between an accounting employee in the municipal utility and his "paired" accounting associate in the city auditor's office, the result is an appeal to the utility top executive on the one side and to the city auditor on the other side. The consequence of this appeal is either a "jurisdictional dispute" concerning the final decision or a solution arrived at by agreement or compromise. Frequently there is no machinery for final settlement. The city auditor has his mandate direct from the people by one route. The top executive of the government proprietary enterprise also has his mandate direct from the people by another route. There is no management agency competent to direct the two independent arms of the city government in such a way as to arrive at a solution.

Legal functionalization of government enterprises results in a "line of decisions" concerning jurisdictional questions which arise from time to time. The solution to each such problem must always result in giving one of the two agencies the authority and responsibility for making the final decision in the particular case, in which circumstance the other of the two agencies becomes a mere rubber stamp. The municipal utility, for example, may have to "rubber-stamp" either the treasurer's investment of its earnings in sinking fund reserves or his deposits in banks of his own

choice. The city treasurer, on the other hand, may be forced to "rubber-stamp" the municipal utility's expenditure of its own funds for construction, even though resulting diversion from debt service will present financial difficulties at a later date.

The Executive Committee

An outstanding defect, inherent in many, if not most, government proprietary enterprises is the lack of clear-cut lines of demarcation between the management activities of the trustees or highest management committee and the salaried top executive or coordinator. The trustees have broad powers of administration, but their ability to manage is confined to the trustee committee as a whole. Individual trustees cannot function as executives without confusion and interference. On the other hand, the top executive often cannot be a real leader because he does not have the power to issue instructions and commands that must be followed. The top executive is primarily a coordinator who derives his power from his position as representative of the trusteeship committee, and he spends much of his time in coordinating his trustees and the activities of the government enterprise.

The problem of the successful conduct of meetings of the trusteeship group is a matter of constant concern to the top executive. If meetings are not successfully conducted, the resulting confusion will add to the burden of the top executive and be charged to his neglect. The essentials of successful conduct of water board meetings are a planned agenda, a system of presentation of problems in sufficient detail and of suggestions concerning the proper action to be taken on each problem in a manner to permit formation of judgment by the trustee members; and a legal record of the formal actions taken.

This problem of proper handling of trustee meetings is well solved by the device of the committee of executives, consisting of the top executive plus the major departmental executives who head the operating departments of the government enterprise. A typical plan of procedure is as follows:

1. The committee of executives holds a lengthy session four or five days in advance of the regularly scheduled meeting of the trustees. The purpose of this meeting is to prepare the agenda for the coming meeting. This means that each executive presents to the committee those problems which he wishes to have passed on. Some of these problems need not be progressed, since the committee and the top executive are often able to solve the particular problem, especially if it involves internal coordination between different departments. The work of the executive committee, therefore, sorts out the problems of the current time period, and solves those which can be solved without higher

authority, with the result that agenda are produced less likely to be unnecessarily loaded with minor and inconsequential matters.

2. Each of the items proposed for the agenda, having been scrutinized and accepted for presentation, is then assigned to one or more of the committee members, and, through them to their subordinates, for preparation of a written résumé of the problem, recommendations for action, and justification of recommendation. The length of such a written statement varies with the importance of the problem, the familiarity of the trusteeship members with it, and the adequacy of available data concerning the matter.

3. Twenty-four hours before the scheduled meeting of the trustees, each member receives a folder containing a copy of the proposed agenda, plus copies of all of the written statements that will be presented at the meeting. Experience has shown that the trustees do go to the trouble of becoming familiar with the contents of this folder before the meeting. This procedure saves time, forces the executive to defend his position with facts presented in writing, and permits reflection by the voting trustee before the meeting.

4. In the meeting itself, each item of the agenda is taken up. The members of the executive committee are present to answer questions. In practice, the trustees rarely take time to reread the entire written statement. Instead, the time of the meeting is devoted to asking questions which lead to action, to dropping the matter as not requiring action, or to returning the problem for further study and subsequent report. Often, in the latter case, a committee of trustees is appointed to determine the next steps to be taken, or, through power to act, to make the necessary final decision.

From the standpoint of the top executive of a government proprietary business, the executive committee is an indispensable part of the machinery of coordination. Through it and through its contacts with the trusteeship group, considerable coordination simply happens in natural fashion. The more difficult problems are properly identified, and they can be segregated for the purpose of more complete study and transmittal to the trustees. In this way, the "amateur" representatives of the public, or trustees, who are finally responsible can become thoroughly conversant with the problems of the business, thus lessening the chances for irresponsible decisions on their part.

The Limits of Executive Discretion

Every executive is free to operate within certain more or less definitely established limits of discretion. One of the earmarks of the government enterprise executive is that he must operate within carefully established and relatively narrow limits of discretion. This is not only true of the top executive in a government proprietary business, but also of all of his subordinate executives. In a municipal utility, discretion of executives is rigidly limited by the laws, ordinances, and motions which affect the operation of the business. Among the areas of management in which discre-

tion is usually limited by passage of detailed laws or ordinances are the pay, employment, and retention of employees; the procedure of purchasing; the procedure of selling junk or used equipment or unoccupied property; the procedure of making and enforcing the budget; and the procedure of depositing and paying out money.

It is common practice in municipal utility management to permit executive discretion to be exercised within certain limits by blanket authorization passed by the trusteeship committee. For example, the top executive may be empowered to approve purchases of less than $1,000; to employ temporary workers on *per diem* pay; to settle claims or approve refunds of less than $50; to authorize temporary transfers, even of executives, and to grant "trial" promotions without increase in pay subject to final approval by the trustees. Limitations such as these, which are typical of government proprietary management, are far more confining than is true of the limits of discretion placed upon the private business executive.

In addition, there is the great class of intangible and psychological limitations that exist only in the mind of the executive. The careful top executive of a municipal utility will take up many problems with his trustees before they are decided on the off-chance that some member or members will have some decided objection to the proposal. This brings into the realm of actual limitation the whole field of engineering and construction. A change in fuel is clearly a matter for the trustees to consider, because the abandonment of coal in favor of electricity, for example, is sure to bring a protest to one or more members of the trusteeship group from interested and influential dealers in coal. Similarly, an irate citizen is often permitted to appeal his case, no matter how positively the trustees have ruled on similar cases, on the theory that the citizen will never be satisfied until he has had his "day in court" with the trustees themselves.

When one considers that metropolitan city owned utilities are among the larger businesses of their respective communities, the rigidity and narrowness of the limitations within which the top executive of the utility finds himself can be better appraised. The Denver water utility, for example, serves a metropolitan area having more than 400,000 population. During a typical recent year it had a working force of 450; a capital investment of over $30,000,000; a plant with fifteen major operating points distributed on a line more than 100 miles long into a mountain watershed; and an annual income of $2,500,000. The work of top management of this moderately large business is a problem in coordination, and results are achieved only by the skillful use of the extremely narrow range of permitted executive discretion.

The rigidity of this whole structure of governmental limitations upon executive discretion does not lend itself well to the handling of emergen-

cies. To cope with this difficulty, by California statute, the Los Angeles water and electric utilities, along with other agencies of the city government, have created a special emergency district to operate only in the event of disastrous earthquakes. The chief executive of each of the municipal utilities, as part of the earthquake organization, is thus empowered to cut through all red tape to be the general-in-command for the period of the emergency should such an occasion arise. The authority granted includes the right to issue city warrants in a limited amount with which to purchase needed supplies, if no other funds are available.

It is a mistake to think that the narrow limits of discretion available to the coordinator type of executive proves that such an executive is weak and ineffectual. To operate a government proprietary business successfully under the typical trusteeship group of elected or appointed "amateur" administrators and board members requires a thorough understanding of the exact limits of discretion and certainly requires more skill because of the existence of such narrow limitations.

The Formulation of Policies

In private business, the profit motive is thought to be the dominant objective to which all others can be related. In public business, the objective commonly accepted is satisfactory service. All policies can ultimately be related to this service objective. However, as in private business, there are many subsidiary basic policies or motives, and it cannot be assumed that a "profit," in the sense of an excess of total income over total expense, is to be avoided. Rather such a balance remaining above expense is highly desirable.

The general service objective is motivated by much more than the desire for operating economy. The economy motive is far less effective in causing actual action than almost any other factor. The reason is not because the municipal utility does not desire economy, but because the problem of economy usually appears before the trustees and executives together with some other problem which commands major attention. In such circumstances, the tendency is to submerge the economy motive under arguments of "absolute necessity," such as population growth, good will, or some other subject. Economy has few champions before the trustees, other than the operating executives, and they are often unwilling to experiment with it and rather desire to let well enough alone.

The less stable and less effective the trusteeship group in charge of a government proprietary business is, the farther down within the operating organization the true responsibility for policy tends to be concealed. By this is meant that operating executives, trying to work under an unstable group of trustees, tend to avoid and evade the responsibility of carrying problems up to higher authority for solution. In a large organization, there

is usually sufficient precedent for an action to make its repetition possible without its becoming an issue of importance to the trusteeship group. This use of precedent puts the unstable trustees in a curious and ineffective position. By ordering that all details of some specific character come before them, they are swamped with petty problems and difficulties. On the other hand, by adroit reference to precedent, operating executives can and do increase their actual authority and responsibility for policy and action in fields which do not interest the trustees. Obviously this is only done at the expense of progress, since precedent provides no basis for advance.

FUNCTIONAL DEPARTMENTATION

The actual departmentation of the typical government proprietary enterprise is essentially functional, except at the very lowest level where the geographical dispersion of operating centers results in territorial control. There is, of course, some difference between the theoretical spread of a particular function and the actual spread of the duties it involves. There is a strong tendency, chiefly because of "legal functionalization," to broaden the scope of each functional department to include the largest possible portion of its theoretical operations. The detailed summary of the actual departmentation of typical water utilities as shown in Figure 53 brings out clearly the tendency toward as complete functional organization as possible.

The principal functions of a departmental character which are sometimes placed directly under the trusteeship level and sometimes under the top executive of the government proprietary type of utility are purchasing, major construction, and accounting which includes billing and collections. In the four water utilities compared in Figure 53, these functional departments are equally divided between the two situations.

Purchasing

The argument in favor of the combined use of the purchasing organization of the general city government is, of course, that the function of purchasing is viewed from the standpoint of the entire city. It is pointed out that the purchases of the water utility, added to those of the city, will provide a larger buying power with which to bargain for quantity discounts. It is also contended that it will permit reduction in varieties of articles purchased, thus reducing the investment of the city in inventory. And, finally, it is held that centralized purchasing will permit more intelligent and detailed study of sources of supply and of qualities offered as compared with specifications. Against these forceful arguments, there is presented by the water utility the claim that the variation between typical city and typical water utility purchases is so great as to minimize

Baltimore	Detroit	Denver	East Bay (Oakland)
Organization of the Trusteeship Level of Management Activity			
City council	City council	City council	(Independent)
Civil service commission	Civil service commission	Civil service commission	(Independent)
Mayor	Mayor	Mayor	(Independent)
	Water board	Water board	Utility board
Organization of the Coordination Level of Top Executive Activity			
Mayor	Mayor	Mayor	(Independent)
City engineer	(Independent)	(Independent)	(Independent)
Water engineer	General manager	Executive secretary	General manager
Departmentation Independent of the Water Utility Top Executive			
Legal	Legal	Legal	Legal
Treasurer	Treasurer	Treasurer	Treasurer
Auditing	Auditing	Auditing	Auditing
Civil service	Civil service	Civil service	
Purchasing	Purchasing		
Major construction		Major construction	
Accounting, including billing and collecting			Accounting, including billing and collecting
Departmentation under the Water Utility Top Executive			
	Personnel	Personnel	Personnel
		Purchasing	Purchasing
	Major construction		Major construction
Customer service		Customer service	Customer service
	Business accounts and records		
		Accounting, including billing and collecting	
		Flat rate inspection	
Minor construction	Minor construction	Minor construction	Minor construction
Maintenance	Maintenance	Maintenance	Maintenance
Engineering	Engineering	Engineering	Engineering
Filtration		Filtration	Filtration
Purification	Purification	Purification	Purification
Pumping	Pumping	Pumping	Pumping
		Conduits and reservoirs	Aqueduct maintenance and operation
		Water rights administration	Land management

Fig. 53.—Organization and departmentation of typical water utilities in four representative cities, in 1940.

the possible economies of consolidated buying. Furthermore, emergency needs make it necessary to carry an inventory directly under the control of the water utility, thereby eliminating any savings through reduction in total inventory. And with respect to discounts, it is contended that the suppliers of water utility materials commonly charge more, that is, offer a smaller discount to the purchasing agents of cities than to the purchasing agents of water utilities.

Major Construction

Major construction is apparently also evenly divided. Actually, there is a strong trend toward complete separation of this functional activity. In Detroit, the major construction is carried on by an almost completely separate organization, with its own accounting department, specialized in the accounting problems incidental to bond funds and payrolls of large numbers of temporary workers. In East Bay, the chief engineer, who is also general manager, is selected in part because of his ability in handling major construction and in part because he is able to assume the responsibility for design and inspection, though construction work itself is commonly on a contractual basis.

Accounting

The same conditions prevail in accounting which includes billing and collections. Although apparently evenly divided in the four water utilities cited, pressure has been exerted in Detroit and Denver, despite legal requirements in connection with the city auditing and accounting department, to maintain independent departments. In Denver, it was the judgment of an outside accounting expert that better organization could be obtained, and fewer functional difficulties would appear if such independence were recognized. He urged that differences of opinion between the head of the accounting department and the top executive be arbitrated by the water board itself. Such a procedure would automatically grant autonomy to the accounting function and place it directly under the water board.

To summarize, this illustration of departmentation development and trends in one field of government proprietary management brings out problems common to the entire field. Often the trusteeship level consists of several separate individuals and groups, each having its own independent and partially conflicting authority and responsibility over the government proprietary business. Often the top management, or coordination level, is similarly divided among several independent individuals. The trusteeship group almost always organizes certain departments, such as the legal, financial, accounting, civil service, and construction departments, independent of their chosen top executive. And finally,

the trend is toward almost complete functional departmentation, leaving the top executive little direct authority over, and responsibility for, operation of the utility.

REORGANIZATION FOR EFFICIENT OPERATION

Reorganization for any but political reasons is difficult to accomplish. This is especially true of reorganization of system and method which involves change in the duties and habits of subexecutives and employees. In order to accomplish reorganization, it seems to be necessary to employ the strategy of emphasizing the fact that an emergency has arisen, of substituting new and improved machinery that carries improvement in employee skill along with it, or of educating employee leaders, at least, to the point of acceptance. The development of criteria of performance by various agencies has greatly aided in this latter educational process. Formulated criteria are simply statements in exact language of the application of the basic objective of service to the particular situation. Once they are accepted by the employees, reorganization along the formulated lines is greatly facilitated.

When a new machine is installed, as for example a new electric pump, the entire operating force of a municipal utility—executives and employees alike—understands that the old steam pump which was replaced was junked because it was obsolete. There is no feeling of resentment, nor any desire to protect the new electric pump from ultimate replacement for similar reasons of further improvement at some future date. This attitude will persist even though the new electric pump can be operated by one employee per shift instead of two and no longer requires the attention of both an engineer and a fireman.

On the other hand, when a new method or procedure, such as a new office system, is installed, executives and employees do not always understand that this came about because the system in use was obsolete and deserved to be replaced. There is sometimes the keenest kind of resentment, even though the immediate effect of the new installation is to increase employment.

In private business, reorganization can and does cope with uncooperative or obstructionist executives or employees by dispensing with their services. In the government proprietary enterprise, civil service hampers such action. As a result, reorganization may have to fight its way inch by inch against the outspoken resistance of executives or employees. A new system or plan of organization may have to be intrusted to its own violent enemies, namely, the employees and executives to be displaced by the change. Politicians do not hesitate to step in to organize this resistance for their own ends. The public sides with the employees, perhaps taking

the position that reorganization is a kind of punishment to be barred from "model" governmental employment.

Criteria play an important part in smoothing the way for system reorganization. A criterion has much the same effect as installation of a new machine. A reasonable criterion, precisely formulated, capable of attainment by improvement not of plant but of system, can usually be attained with little internal opposition. Some of the criteria now generally accepted by municipal water utilities may be indicated.

Criterion of Social Responsibility

The basic criterion is that every occupied house must be equipped with hot and cold running water and have a private inside toilet. During depression years, this criterion has been a live issue with metropolitan water utilities who were forced to acquiesce in the social responsibility point of view by delaying turnoffs of thousands of delinquent customers for months.

Criterion of Fire Protection

The National Board of Fire Underwriters has been very successful in bringing about improvements in construction and in operation of water utilities in the larger metropolitan cities with the end in view of maximum fire protection. The commendations and recommendations of the National Board of Fire Underwriters are taken very seriously, especially by operating executives, who press every opportunity to persuade the trusteeship group and top executive of the water utility to take whatever steps are suggested in the report.

Criterion of Rate-Making

The work of associations and of various experts has developed the goal of a scientific meter rate structure toward which to plan and work. Where the opportunity to revise the meter rate has been presented, operating executives and top executives have worked long to try to develop an ideal or scientific meter rate for their cities.

Criterion of the Budget

Formulation of an operating budget and its acceptance by the trustees has an important effect upon the operating executive. His minor construction or system projects, pet ideas, and necessities acquire new status when they appear in his "allowed" budget. If the budget appeals to him as fair, he will spend long hours cutting it and fitting it, mentally, to permit it to accomplish all he wishes to do without incurring an overrun. If the budget seems unfair, he will spend equally long hours trying to circum-

vent it, either by finding some additional funds, or, as a last resort, by honest economizing. Most budgets, from the standpoint of any particular operating superintendent, are a mixture of both fairness and injustice to his department or sub-department.

With all its defects, however, the budget does provide the trustees, the top executive, and the operating executives with a yardstick by means of which to measure relative progress in any given period of time.

Criterion of Optimum Balance

Closely related to the operating budget is the new criterion of "optimum balance" of income, operation and maintenance expense, development of plant and equipment, and population growth and shift. During the era of rapid population growth and rapid evolution of water supply inventions, now drawing to a close, all that water utility executives could do was to concentrate on the major problems of catching up with growth. Now that population growth is clearly slowing down, especially in the heart of the metropolitan center where the central city water utility chiefly operates, it is possible for the more mature point of view of "optimum balance" to develop.

A difficult problem to which the criterion of balance must be applied is that of the ultimate relationship of suburbs and central city. This problem must be solved by the trusteeship group. If we may say with confidence that the typical utility trusteeship group must have periods of instability, it is even more true that relations between two such groups of trustees are more often strained than happy when one group represents the central city water utility, which has by huge expenditures assured itself an ample water supply, and the other represents the suburb, which is anxious to grow and resentful of interference. The criterion of balance is a leavening influence in such a situation. Thus Baltimore, required by state law to provide water supply for suburban pipe systems, now, as a matter of operating routine, prescribes water main sizes and routes both inside and outside of the city limits, to the end that the metropolitan distribution system may be developed in a balanced fashion.

CIVIL SERVICE AND PERSONNEL MANAGEMENT

Public employees generally have what may be called the "civil service point of view." That is to say, they are apt to feel that their position is secure, or ought to be secure, under all conditions except grossest personal negligence. This civil service point of view has a tendency to retard the development of complete functional personnel divisions. Employees, in the belief that security is the main consideration, sometimes resent attempts to develop training and selection activities and the formulation of specific measures of employee efficiency as a basis for promotion and

pay. This attitude toward security in employment extends to the public with the result that public support of sound personnel procedures is often lacking.

On the other hand, experience sustains the assertion that salary classification is the chief means for motivation of employees. Classification creates a sense of status and causes employees to try to live up to expectations. When used as a positive procedure, it makes possible the promotion of employees for long service, and in its negative aspects, it may be used as a disciplinary device. Employee classification, however, may also tend to curb initiative in the higher brackets of service by depressing rates of pay in response to pressure from the public and from officials in the city government. Lack of ability may thereby be rewarded by reason of higher than prevailing salary levels for the lowest classes of employees on the theory that a certain minimum wage scale must be established.

Collective bargaining in public personnel management operates in two ways. One of these, and the most important, has been to take the issue direct to the public at the polls for the purpose of securing the passage of definite "standing orders" concerning civil service rights and privileges. With the development of stronger management at the coordination level, collective bargaining has sought a shorter route to gain its ends by dealing directly with the top executive and the utility trusteeship group.

In public business management, there has been a tendency to separate personnel management into two parts. One of these parts which has to do with hiring (or the certification for hiring), firing, and sometimes salary classification and promotion has been developed as a civil service activity, and as such it has been organized as an independent function of the trusteeship level of management. The other part of the personnel function has been left to haphazard organization under operating executives.

Under civil service, the personnel problem of the government proprietary enterprise is commonly well unified. This is true because civil service rights apply to all but the very highest executives and the appointed, or elected, representative of the public owners. There is no sharp line of distinction between executives and employees or between office force and other employees.

The Danger of Mediocrity

Because civil service emphasizes the guaranty of employment, it has a tendency to perpetuate mediocrity. For example, a new appointee, clearly unfit, instead of being dismissed, will often be retained for months through the indulgence of fellow employees and operating executives, in the hope that by training and experience the employee in question will become satisfactory. Similarly, an old employee who occupies a position with a relatively high rate of pay will be carried along for years by his

subordinates, thus delaying the promotion of younger well-fitted persons to a period well beyond their own middle life. Finally, when promotion does come, the employee's desire to make good by improving on past practices has been dulled by age. Instead, he harbors resentment and a feeling that he has been the victim of past injustice because he has done valuable work for so long a time without receiving just remuneration for his services. A situation of this kind perpetuates mediocrity and unprogressiveness.

Slow turnover and delayed promotion in turn stimulate the process of self-selection by encouraging the more alert and ambitious to resign, thereby leaving the average level of ability and efficiency so much lower. Conditions of this kind are well understood by executives of government proprietary enterprises. They will retain the worker who is slightly below average and try to train him up to his job, because such a person, having to "stretch" to reach his position, never dreams of leaving. The highly educated individual, on the other hand, gets little encouragement from these same executives, because they expect him sooner or later to desert them.

Civil service, even under the best conditions, is not divorced entirely from the patronage system of appointment. Under the worst conditions, where civil service simply means guaranteed employment and contains no machinery for selection or examination in actual cases, half or more of the new employees may secure their positions through patronage.

Discipline, Obedience, and Merit-Rating

Reasonable discipline and obedience to rules and regulations are as important elements of good management in a municipal utility as elsewhere. To enforce such requirements, a carefully prepared system of demerits and other penalties is often worked out and applied against infractions. Lay-offs, transfers to unpleasant work, and demotion to jobs classified at lower rates of pay, are examples of such penalties which are effective in maintaining discipline and efficient service.

Stimulating Efficiency by Transfer

Since the annual labor turnover from all nonpolitical causes is low, it usually happens that the municipal utility is too stagnant to be stimulated to any marked extent by the "new blood" brought in by employment of workers to replace those who have dropped out. Promotion also goes on too slowly to permit the organization to have a young and progressive viewpoint. Small increases in pay, scattered through the organization, are not usually sufficient or frequent enough to provide a real incentive. If such increases were generous and numerous, they could not be repeated

year after year without raising the average rate of pay to a level out of line with that of other city employees.

In such conditions of stagnancy, an effective plan is that of deliberately increasing the rapidity of transfer. Transfer brings to at least two individuals—and often many more in the process of adjustment—a slight change in duties, a new environment, and a feeling of interest in new work.

Advantages to be obtained by this process of stimulated transfer are many. For example, older employees, the props supplied by younger persons having thus been removed, drop more naturally into lower-paid positions commensurate with their "working pensioner" status. Such transfer opens the way for the promotion of younger men. Transfer causes employees to acquire new interest in their work. It is not uncommon that through this practice, men acquire multiple skill of great value to their public employer. Pay classifications are also improved by a policy of rapid transfer of employment. Such improvement comes about because the shifts effected supply proof that certain skills, while different in character are nevertheless comparable in other respects and, therefore, merit comparable remuneration. And finally, provincialism between divisions is reduced when many employees are assigned to duties elsewhere in the city. It is obvious, of course, that transfer could become so frequent as to lose its effectiveness and stimulus. Under such circumstances, transfer would result in a substantial drop in efficiency.

PUBLIC RELATIONS ACTIVITIES

Public relations work, viewed broadly, is a system of mutual education of the municipal utility and its employees, on the one side, and the public —both as owners and customers—on the other side.

"Public relations activities" may be defined as the art of evaluating and molding the shapeless mass of individual impressions dispersed within the general body public. It may also be defined as the management function of conducting a particular business in such a manner as to leave with the public a preponderance of favorable individual impressions. For example, it is often a vital necessity to educate the public with respect to the need of additional water supply. This frequently involves skilled campaigning. It is obvious that politeness, fair play, and efficient management create good will in the minds of both customers and the public which simplifies the educational problem.

It is incorrect to regard public opinion as an impregnable rock which bars the progress of management along well-recognized lines, though that sentiment often prevails. It is more correct to think of public opinion as a changing and fluid mass so enormous that it moves slowly, scattered

among thousands of individuals. But because of its mass, it moves irresistibly in the direction established at the moment; and like any other large object, it is diverted into a new course slowly; but once diverted, it tends to move with its former irresistibility along the new path.

It follows that within this slow but persistently moving mass there will be those who are so far below the average current of public opinion that they resist and object to the progress that is being made. There will also be those who are so far above it that they desire and demand progress at a far more rapid rate. The extreme resisters find the progress of the current of mass average opinion a veritable juggernaut; the extreme progressives find it moving at less than a snail's pace and become impatient with its apparent immobility. To keep just ahead of the average of public opinion has long been the art of the politician, and is, therefore, the goal and task of the trusteeship group at the head of the municipal utility.

A natural alternative develops in government proprietary enterprises when a salaried executive, after years of service and rebuffs, develops the "civil servant attitude" of waiting to be forced to take action by public emergency. Since public experience with bad tastes and odors in drinking water due to defective filtration, with threats of disease and fears of drought due to inadequate water supply, and with insufficient water pressure at times of big fires prove to be a quick and forceful teacher, the water executive, for example, may become indifferent to other methods of education. Not being able to raise the opinions of the mass of the public up to his own informed progressiveness, he goes to the opposite extreme and waits for the "average attitude" to pass beyond him, from sheer necessity.

Aggressiveness in Public Relations

An aggressive public relations policy permits a municipal utility to "keep just ahead of the average," and therefore, to be just as progressive as its public will permit it to be. As this educational process continues and mutual confidence develops, the government proprietary enterprise may find itself able to introduce direction into the mass of public attitudes. This change of the government enterprise from follower to leader may well result in a higher degree of flexibility and a more rapid rate of progress in management, with the approval of its citizen-owners, than would have been possible without a public relations program.

The tools of an aggressive public relations policy are much the same, no matter what the purpose may be. One device is to establish close contact with the local newspapers, affording them opportunities to write general feature stories about the utility system and to report news while it is still news, thus diluting editorial criticism, if any, with column inches of facts. Another method is to establish a regular direct contact with the

public, as for example, by distributing a *W[redacted] Bulletin* with the bills for water rent. Such a publication gives information concerning the reason for rules or changes of policy; it explains financial problems and decisions; it depicts improvement progress pictorially; and it frankly asks for the support of the public for its own trustees and management.

The use of other means of publicity, as the opportunity arises, may also be encouraged. This includes descriptive bulletins given to customers at the office and to school children; invitations to the public to visit scenic points and key portions of the utility system; talks before clubs of all types; display of motion pictures before club and school groups; display of movie "shorts" in the regular commercial theaters as part of newsreels; the use of the radio for the diffusion of information in an emergency, or to explain any radical change in rules; the use of newspaper and free circulation advertisements for similar purposes; and inculcation of the ideal of courteous treatment of the public among all employees.

Policy Initiated by Public Insistence

Just as it is possible to find illustrations of public resistance to a particular management policy, so it is also possible to demonstrate instances where the public takes the initiative in forcing a policy upon the government enterprise. In one instance, the public is unprogressive and resists necessary improvement. In the other occasion, the public is more progressive than the management of its utility. In both cases an aggressive public relations policy is the most effective mediator because it brings the public into tune with its own management. Public relations work educates the management as well as the public and makes each group more responsive to the other and less likely to take action on a proposition which will be criticized by the other.

Public relations considerations, for example, have always been a determining factor in financial policy. The financial structure of a public utility at any given moment, is, therefore, the inevitable resultant of past decisions motivated by public relations considerations.

The typical metropolitan city owned utility has usually come into being through purchase of a private water company. This transition has commonly been accomplished by the issuance of city bonds for all of the initial cost. In a campaign leading up to the authorization of such bonds, the public is commonly persuaded that the new municipal utility will pay for itself out of its own earnings, including the interest payments and the redemption of the bonds as they fall due.

This method of accomplishing municipal ownership, by which the public buys the business from the stockholders and bondholders of the private concern on a kind of installment plan and then meets these installments with appropriations from the excess earnings of the utility

itself, is contrary to the common ethical concept held by the same public with reference to private utilities. In the public regulation of private utilities, the public and the law almost universally take the position that capital for plant and equipment should come from some other source than the rate-payers. This difference exemplifies the effect of the attitudes and opinions evolved by public relations upon the financial structure of the utility.

Employee Reactions to Public Relations

The hazards of leadership are too apparent to the civil service employees of municipal utilities to make them court it. As a result, their attitude toward aggressive public relations is often one of evasion and doubt as to its value. They are inclined to favor the complete separation of the contacts of public relations from operation, such as exists in the mayor and council type of utility organization. Under the latter plan, the salaried operating executive of the utility system who ventures far into public relations is simply invading the politician's domain.

This attitude of indifference to good public relations easily becomes characteristic of both minor and major employees. To the public, such employees exhibit indifference that is taken to be either insolence or incompetence. "These are the rules handed down to me from above, and you may take them or leave them," becomes the watchword of those in contact with the public. Thus the effort to avoid trespassing in the politician's domain of public relations causes the utility to disregard and to deal carelessly with the citizen-customers whose ultimate authority controls the administrative machinery of the trusteeship group. This disregard is gradually transmuted into a new kind of disease in society and government, namely, the widespread conviction among the individual members of the public that they have become the victims of "institutional persecution," by their own government proprietary enterprise.

An aggressive public relations policy on the part of the utility forces it to make progress in tune with the mass of public opinion. In a situation like the case of the bitterness of suburban citizens toward what might be characterized as "arbitrary and high-handed" treatment of their water supply problems on the part of the central city, no amount of paid publicity will conceal from the public the reality of an "out-of-tune" situation, because the utility is but one of the many sources of group contact with water system matters. It follows, therefore, that public relations activities have a twofold effect. In the first place, they tend to make the public more willing and flexible through understanding and confidence. Such understanding is a remedy, and sometimes a cure, for what may well be called the disease of "institutional persecution." In the second place, the effect upon managament is to make it less arbitrary, more sympathetic

with public desires and interests, more likely to plan to meet the demands of the public in ways which will keep the organization and physical structure of the water system in reasonable balance, and therefore less likely to be forced into hasty or rash action by public clamor.

Viewed in this light, an aggressive public relations policy which reaches into every corner of the government proprietary enterprise is a substitute for the formerly practical town-meeting techniques of representative government, now outgrown in all but the smallest communities. Without active public relations work, the citizen-owners tend to be out of touch with their own enterprise, receiving no information except through secondary channels, which inevitably add their own interpretation to the original data. With active public relations work, each executive and employee of the government enterprise can and does develop proper understanding and resulting ability to play his own proper public relations role.

CONCLUSION

As indicated in Chapter XV, there is an important place for comparative studies of organization and management of enterprises under differing conditions and circumstances. This chapter offers such a possibility. Its analysis of the management characteristics of government proprietary enterprises may, and should be compared with private business management, association management, and "mutualized" management as analyzed and discussed in earlier chapters.

The cumbersome interrelations of public trustees and government enterprise top management, the overemphasis on functionalization and duplication of work, the resistance of progress and the encouragement of mediocrity at both executive and employee levels, the poor public relations attitudes and practices, all fully justify constructive criticisms of "government ownership." Yet the real purpose of the analyses that have been presented is not to condemn, but rather to compare, to the end that the student may learn and may contribute in his own way to the solution of organization and management problems.

QUESTIONS

1. Prepare a diagram in two parts—one part illustrating private business management and the other part government proprietary management. Include the following units of management in your diagram so that the comparisons in organization are clearly shown:
   a) Stockholders and bondholders in private enterprise.
   b) Citizens and bondholders in government proprietary management.
   c) Boards of directors in both types of management.

d) A second board of directors in government proprietary management, such as a city council.

e) The president of a private enterprise and his general manager.

f) The president of a public board of directors or trustees and the salaried manager of the government proprietary unit.

g) An outside firm of certified public accountants employed by a private enterprise to audit its books and report thereon.

h) A separate governmental unit, such as a treasurer, having authority and responsibility for some phase of operation of the government proprietary unit such as accounting.

2. Answer the following questions concisely but completely:

a) How can a proprietary enterprise live within its income unless its income is permanently appropriated in one way or another to its exclusive use?

b) How can the public be served courteously and quickly by a government proprietary unit unless all contacts with its patrons are included in its management and not scattered among various departments of government?

c) How can extensions and betterments in a public utility be planned and constructed efficiently and serviceably unless the agency that operates the utility also has a part in its planning, or at least in the approval of such improvements?

3. Review briefly the board of directors level of management as presented in Chapter V. Describe clearly the differences that can be observed between the functions and procedures of a board of directors of a private enterprise and a board of trustees of a government proprietary enterprise.

4. The statement is made in this chapter that "the executive of a public enterprise is almost entirely a coordinator," and as such should perhaps be content with a normally lower salary as compared with higher payments "for the broader kind of leadership characteristic of general management in private business." Indicate fully how this statement can be justified. For purposes of comparison, refer to the exposition of executive coordination activities in Chapter VI.

5. Write out comparative definitions of the following terms, referring freely to earlier chapters:

a) "Functional departmentation."

b) "Functional authority."

c) "Legal functionalization."

6. Enumerate and explain the differences, advantages and disadvantages of dual management in the following situations:

a) In private business management, it sometimes happens that other executives beside the company president serve as members of the board of

directors. An example is a salaried chairman of the board as well as a salaried president of the company.

b) In association management, it is customary to have an unpaid president or chairman of the board of directors. In addition, the board selects and appoints a salaried executive manager of the association.

c) In government proprietary management, it is common practice for one governmental level, such as a city council, a board of trustees, a mayor, or on a national scale, the President of the United States, to have appointive and general supervisory relationships with the next lower level of management represented by a salaried manager of a proprietary unit.

7. The following statements are intended to advance arguments why private business management is theoretically superior to government proprietary management. Defend or attack these statements, but explain fully the views you maintain:

   a) The effect of legally prescribed functionalization is to draw sharp lines of demarcation between departmental activities within a government proprietary enterprise and between it and other parts of the same government. This condition hampers efficient management and is in sharp contrast with the efforts of private business executives to avoid such rigidity.

   b) The use of the device of a regularly constituted committee of major executives of the government proprietary unit primarily to prepare the agenda for the "amateur level" or board of directors of the agency, is cumbersome and amounts to a duplication of effort as compared with the definite decisions that can be made by similar executives in a private business enterprise where greater executive discretionary freedom prevails.

8. Explain what is meant by the popular epithet, "red tape," in governmental matters, and show its relation to the following points quoted from the text:

   a) If we say with confidence that the typical utility trusteeship group must have periods of instability . . . .

   b) The less stable and less effective the trusteeship group in charge of a government proprietary business is, the farther down within the operating organization the true responsibility for policy tends to be concealed. . . . In a large organization there is usually sufficient precedent for an action to make its repetition possible without its becoming an issue of importance to the trusteeship group. . . .

   c) . . . . a new kind of disease in society and government, namely, the widespread conviction among the individual members of the public that they have become the victims of "institutional persecution" by their own government proprietary enterprise.

9. Analyze Figure 53 in such a manner as to indicate clearly the special problems of organization and management inherent in government proprietary

management that are not present in either association management or the management of a private business enterprise.

10. Outline in what particulars the salient aspects of (1) efficiency and (2) incentive appear in the problems of government proprietary management with respect to the following:
    a) Reorganization for efficient operation.
    b) Civil service.
    c) Stimulating efficiency by transfer.
    d) Employee reactions to public relations activities.

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Chapter XVII

MANAGEMENT AS A CAREER

IT IS difficult to prepare a discussion of this important subject without seeming to preach. It is even more difficult for the reader to retain his normal attitude of impersonal consideration and to avoid the substitution of emotion for reason.

Because the executive organization of every group heads up to one top executive, most of our thinking is about this "conspicuous" leader. He holds the dominant position on the business stage. His comings, goings, plans, theories, and statements are the stuff of which general and financial news is made. The daily press, the radio, books and magazines, and even the government take notice of his doings. Whether fitted for such a career or not, all of us desire to be this "conspicuous" leader. Ambition, quite understandably, clouds our reason.

The first fact which should be understood by the young person who aspires to become an executive is that the average executive career is not one of conspicuous leadership, any more than that of the average doctor, lawyer, or other professional man. A review of the levels theory of organization verifies this statement. The executive pyramid consists of many individuals in the lower levels—and of few in the higher levels of management. Obviously, the average executive will be found in the intermediate levels, not at the level of conspicuous leadership.

The spotlight that gives prominence to the so-called "conspicuous leader" is generally the income he is reported to receive, especially if the enterprise with which he is connected is not sufficiently large to receive continual public notice. Too often success in a career in management is measured in terms of personal financial gain alone. To do so is an obvious fallacy in this profession as well as in any other life work. Studies made of the incomes of professional men indicate that many doctors, lawyers, and members of the other professions do not receive high financial earnings. Only a few persons in each profession realize high incomes for their work, and still fewer receive princely returns. The same is true of business executives.

The young ambitious individual should not assume that there is either more or less opportunity for his personal advancement in the profession of management. Rather, he should understand that the opportunity for a successful career in it is about the same as in any other profession. In

brief, he should embark on a career as an executive because he wants to be an executive, not because he craves or envies the high monetary reward attained by a few conspicuous leaders.

PREPARATION FOR A MANAGEMENT CAREER

The first step toward a career in management is education and training prior to employment. More and more attention is being given to this fundamental matter. There has been, and presumably there always will be, a conflict between the advocates of cultural and vocational education. Usually this conflict is merely a battle of words whose issue depends upon a definition of terms. On the basis of a narrow distinction, cultural education has been called "educating men for living," whereas vocational education has been limited to the development of skills applicable to the pursuit of one's calling or profession. To attempt to put education into compartments so narrowly restricted is neither helpful nor realistic.

From the point of view of preparation for a career in management, knowledge of and for itself is not enough. Knowledge without the power to use it is sterile. It is not merely appreciation or understanding that is needed. Knowledge can be no more than intellectual baggage unless it can be drawn upon to develop competent persons to do things and to get things done.

Therefore, as a background for management, it is better to regard a proper education as a combination of both culture and training. Along with educating for living through intellectual enlightenment and refinement, there is the obligation of achieving qualifications for responsible work in directing business affairs wisely and effectively. Education may provide knowledge, wisdom, and a sense of values. Through training it should also enhance the effectiveness of existing talents and skills, and develop new ones. In the final analysis, competence in management will depend upon personal behavior. That is to say, what sort of a career a person may be prepared to assume will depend upon what he chooses to learn; what work he undertakes to perform; and how he does it.

Methods of Educational Preparation

Methods of preparation for management may be classified into six different types. They differ from each other partly because of their historical development and partly because they exemplify different personal and intellectual philosophies. They may be designated as follows: (1) parental training; (2) the "self-made man"; (3) general education; (4) vocational training; (5) business college training; and (6) university business education.

Parental Training

Before the present system of academic training developed, parental training was a distinctive system of education. For example, the youthful

heir to an English title and estate received careful instruction in the problems of management of his inheritance from his parents. He was trained to regard himself as a leader and to act as such among his associates. That is, he was nurtured as an executive. He found his friends and associates from his own social strata and thus gained more training through discussion of mutual experience.

Similarly the master craftsman or merchant of the Middle Ages trained his son with special care to follow in his footsteps in the management of the family business. After serving his craft apprenticeship, the young heir would become, in effect, a junior partner in the business, learning its every angle under the watchful eyes and counsel of his parents.

In the United States, until late in the nineteenth century, business employment usually began at the twelfth year or even earlier. This early starting age precluded academic training beyond the sixth grade. Furthermore, neither the citizen nor the state considered formal schooling important beyond reading, writing, and arithmetic. Hence, an individual who desired to gain experience and training in business had no choice other than entering the occupation of his parent and to achieve his first executive position through inheritance. Even though the age at which business employment begins has been advanced considerably and an ever greater emphasis is being placed on formal education, parental choice is still an important element in the preparation for management. If one's father is a business executive, and especially if he is an owner of part or all of a business, it is natural for him to try to influence his children, or the children of his relatives, to prepare for professional business management in his industry.

The "Self-Made" Man

In the years before the Civil War, there appeared in the United States a type of business executive who came to be known as the "self-made man." Formal schooling was conspicuously absent in his preparation for management.

His training consisted of a variety of speculative business ventures with resulting varied experiences. Learning by experience, the "self-made" man found out how and what to do in order to make his ventures profitable. Relatively unschooled, reading little, doing no studying in the academic sense, the "self-made" man found the infinite variety and opportunity of the frontier his personal schoolroom and his ideal environment.

Both the opportunity offered by the frontier and the likelihood of success as an executive without academic schooling have long since disappeared. Nevertheless, if we view the term "self-made" broadly as meaning that a person has selected and trained himself for an executive career, there is probably a larger proportion of self-made executives today

than a century ago. The combination of self-selection and prolonged study and training continues to produce outstanding executives who are worthy descendants of the self-made businessmen of the frontier.

Benjamin Franklin is an illustration of the typical combination of parental training and of the self-made man of a century ago. Born in 1706, he went to school for only two years between the ages of eight and ten. After two more years working for his father, a candlemaker, and five years apprenticed to his brother, a printer, he broke away from Boston to Philadelphia where he soon, at seventeen years of age, was established as a journeyman printer. Franklin retired from active business twenty-five years later, at the age of forty-two, a relatively wealthy man. From that time until his death in 1790, he achieved such recognition in scientific research and in politics that he is considered to be one of the founders of our country and one of our greatest Americans.

General Education

The increasing emphasis which is being placed upon a general educational background as a part of the preparation for careers in management is due to several factors. One factor is the legal age for leaving school, which has been gradually advancing in most American states toward eighteen years. Another is the growing tendency of employers to require completion of high school, which normally takes place at eighteen years of age, as prerequisite for employment. A third factor is the fear of protracted juvenile unemployment, which undoubtedly keeps many young people at their school desks, regardless of their own personal inclinations.

Inasmuch as relatively prolonged academic training is now a characteristic prerequisite for all types of employment, inheritance, and self-education without schooling may be considered almost obsolete as satisfactory training for management except in combination with formal schooling which goes well beyond the grammar school level. Their continued importance is derived primarily from the fact that training cannot be separated from selection.

The medical profession will serve as a good illustration of the relationship between selection and training. In it prolonged academic training amounting to six years or more of college study—both general and specialized—is now required. No one can practice as a licensed physician without such training. From the standpoint of vocational selection, the trainees in American medical schools are more or less clearly divided into two groups. In the first place, there are those who have been selected by others, particularly their parents, to enter the medical profession. This is the parental factor. Then there are those who have selected themselves, for any reason whatever, to enter the medical profession. This is the "self-made" factor.

In some countries, there is a third method of selection for professional training, namely, assignment by the state to such academic study. This method has its extreme form in the caste system of such countries as India where it combines with the influence of hereditary selection to cause each caste to perpetuate itself and eliminates personal selection of one's vocation.

When Ulysses S. Grant and Robert E. Lee studied for four years at the United States Military Academy at West Point in the 1820's, the curriculum they followed was general rather than vocational. As Douglas Southall Freeman puts it in his biography of Lee:

> From the firing of the sunrise gun until seven o'clock, the first-classmen studied mathematics. . . . Thirty minutes for breakfast, then came guard-mount at 7:30, and at eight, class parade. . . . Once the class in mathematics was in place, instruction began. . . . At eleven o'clock the class was dismissed, and the cadets went back to their rooms where they spent an hour, presumably reviewing the lesson in mathematics, and preparing for the next day. . . . At two there was formation, and then two hours of study and recitation of French. . . . From four o'clock until sunset or later was the time given over to military exercises. . . . When supper was done, the signal was given to retire to quarters, where the cadet was to wrestle once more and until 9:30 with mathematics. . . .
>
> Conversational French was not taught. . . . The reason for this shortcoming was the institution's emphasis on mathematics. . . . With the return to barracks on September 1, 1826, Lee and his class plunged into more advanced mathematics. . . . French was continued. . . . The one added academic study was free-hand drawing of the human figure. . . . Drawing alternated in the afternoons with the study and recitation of French. . . .
>
> Shortly after his return to the academy on August 28, 1827, Lee . . . . entered on scientific studies that were entirely new to him. Mathematics was dropped. Drawing was continued . . . . Chemistry and . . . . physics became his major studies for the year. . . . .
>
> Now began the term for which all else was preparatory, the term into which was crowded all the technical military training, together with a second course in chemistry and a hurried, superficial survey of geography, history, ethics, and moral philosophy. . . .[1]

History attests, in the case of Grant, Lee, and other graduates of the United States Military Academy who led the northern and southern armies of the Civil War, that the general curriculum of that period did produce military leaders with great ability in their profession. The same test may be applied to Great Britain, which for generations has been led by an upper class trained in the so-called "public schools" which offer only a general curriculum. In the United States, there may be found many executives whose academic training has followed a similar pattern.

[1] Douglas Southall Freeman, *Robert E. Lee* (New York: Chas. Scribner's Sons, 1935), Vol. I, pp. 56–75.

Vocational Training

In the United States, by 1880, there had already developed the familiar educational system of grammar schools, academies, high schools, colleges, and universities. An emphasis upon a general education predominated at first and is still important. However, even into the liberal arts curricula offered by high schools and colleges, there have been introduced such departments of instruction as economics and statistics, so that the general educational curriculum of the present time includes many subjects that properly may be called "vocational."

The advanced age at which young people leave school to enter employment is one of the chief reasons for additional academic vocational training. Broadly speaking, young people leave school at four levels, that is, after some training beyond the eighth or ninth grade (end of grammar or junior high school), after finishing high school, after finishing college, and after completing advanced or graduate work.

Even at the junior high school level (seventh, eighth, and ninth grades), educators must face the fact that their pupils have both varied interests and varied native abilities. In some states, such as Massachusetts and New York, which have struggled longest with this problem, four distinct types of training have developed: college preparatory courses, training in business skills of the office type, training in trade skills of the factory type, such as machine operation, and the continuation school training. The latter institution gives additional schooling to young people who are permanently or intermittently employed, but have not yet completed the minimum education required by law.

If the junior high school finds vocational training an essential part of its curriculum, it is clear that vocational studies will form an even more important part of the advanced levels, that is, the high school, the college, and graduate schools. In fact, at the graduate level, the college student has completed the usual cultural studies. If he remains enrolled as a university student, he must pursue some specialized, and, therefore, vocational study.

During the nineteenth century many professional schools such as engineering, law, pharmacy, and dentistry, to mention but a few of them, were established in American universities. In doing so, institutions of higher learning undertook to provide preprofessional and pre-executive preparation through prolonged general and specialized study.

The need for education for business of vocational type, and at the college or university level, is well stated by President Conant of Harvard University:

> The United States has developed its greatness as a nation in a period in which a highly fluid society overran a rich and empty continent; one of the

highly significant ideals of the American nation has long been equality of opportunity. Our educational system, our political institutions, and our social ideals form a closely interwoven pattern. Equality of opportunity could be realized only in a political democracy; it would have meaning only in a competitive society in which private ownership and the profit motive were accepted as basic principles.

As never before, business needs men who appreciate the responsibilities of business to itself and to that unique society of free men which has been developed on this continent. Such men must understand not only the practical workings of business organizations, but also the economic and social climate in which business operates; they must be as well trained as our professional men in law and medicine.[2]

One reason why more and more emphasis is placed on vocational training at all school levels above the sixth grade is the increasing importance of the possession of personal knowledge and skill in the use, maintenance, and operation of complex machinery. An apt illustration of this fact is to be found in the field of mass transportation. In the old days, the driver of an omnibus or stagecoach needed no academic training to do his work. His work was simple and his pay was low.

Similarly, the driver of a streetcar or motor coach in modern urban transportation, certainly requires little more than a high school education plus a limited job-training course to do his work properly.

In the movement of modern trains, the locomotive engineer is clearly a step above the streetcar operator. His advanced position is reflected in his better earnings. But the locomotive engineer, in addition to a high-school education, needs to undertake prolonged study under the supervision of his employer in the construction, maintenance, and repair of locomotives. Furthermore, he must be able to operate different types of engines, such as steam, diesel, and electric locomotives, under many different conditions of weather, type of signals, and quality of track. In addition, he must progress slowly through the various levels set up by the union and thus establish his seniority, or right to employment, as compared to his fellow engineers.

The pilot of a transport airplane which carries passengers and cargo in scheduled service ranks today at the top among transportation employees. This rank is reflected in the salary he receives. In preparation for his job, the air transport pilot must have theoretical training at the college level or its equivalent. This training includes such subjects as air navigation, engine and plane construction and operation.

This trend toward a greater complexity of the machinery which is

[2] James B. Conant, Foreword in *Education for Business Responsibility* (Boston: Graduate School of Business Administration, Harvard University, May 3, 1947) (pamphlet).

used in business is universal. Factory employees are surrounded by complex machinery. So are the truck driver and the traveling salesman, both of whom are commonly charged with the use of a truck or automobile in the performance of their work. Likewise, office workers must learn to operate and maintain machines ranging in complexity from simple devices up to those involved in the intricate operations of sorting, tabulating, and accounting.

The Business College

During the last quarter of the nineteenth century, or after 1875, there came into being in the United States, in almost every city of any importance in the country, private enterprises known as "business colleges." These private schools undertook to provide training in minor business skills, usually bookkeeping, penmanship, and business letter writing. Gradually the public high school has entered and extended this same field by establishing commercial departments which offer courses in shorthand, typewriting, business arithmetic, and other skill subjects. Thus vocational training in the high school has developed along with its traditional college preparatory or cultural program.

University Business Education

Since the turn of the twentieth century, there has been a growing development of collegiate schools of business in American colleges and universities. Generally, these schools are recognized as professional divisions of institutions of higher learning. They are staffed with specialized teaching faculties who control their educational policies. The programs of work they offer lead to professional academic degrees after a minimum traditional four-year course of study. To avoid overspecialization, it is usually stipulated that approximately half of the units of work presented by a student to satisfy the requirements for the degree must be earned in nonbusiness or general subjects. A few collegiate schools of business require that applicants for admission to them must possess bachelors' degrees or the equivalent.

As a matter of policy, a collegiate school of business of recognized standing is committed to the development and administration of a professional curriculum in terms of significant conditions and relationships that obtain in modern business management. By means of discussion and analysis of business problems in appropriate fields, its purpose is to train men and women to think effectively about such problems and to form sound business judgments. The collegiate school of business is founded on the premise that the educational program it has to present materially shortens the apprenticeship of those who successfully pursue its offerings and who possess the personal qualities of executive leadership.

Collegiate education is the most advanced step in pre-executive prep-

aration for a management career. It satisfies a growing demand for a broader knowledge and critical understanding of the complexity of modern business affairs, as well as a desire for training in advanced skills and techniques of management. The reason for this urge toward prolonged education for business is the desire of the individual to find a higher status at the time of entering employment. Status should not be confused with starting pay nor with the apparent importance of the initial position. Status means rank or position in the executive scale. Remuneration may be affected by such rank, but it is incidental to it. Likewise, the initial assignment of duties may look unimportant without an executive title attached to it, whereas it may be most significant in the long run.

There is a strong tendency for those who select themselves or who are selected by others for executive careers to postpone entry into employment until completion of college at about twenty-two years of age or older. This tendency gives the high school applicant for a position non-executive status since he has not elected to secure for himself further pre-employment training at a cost of additional time and expense.

The high school graduate, upon entering employment, must often identify himself as a worker by becoming a member of a union. This confers worker status, chiefly by subjecting the young employee to union regulations covering his transfer and promotion. Also, the high school graduate who has steady employment has limited opportunity for broad study of the higher business skills, such as accounting, statistical control, financial management, sales management, and engineering. He is therefore at a disadvantage in competition with the college graduate since the latter has had ample opportunity to become familiar with these fields of study.

The young employee who takes routine work after finishing high school must spend years learning his job and qualifying for his first promotion to a supervisory position. Only then is he ready to work upward to a higher business position. In other words, it takes less time for the college graduate to move up the executive ladder because he does not have to climb through all the lower levels, beginning as an ordinary worker. The high school graduate usually does not have time, in his normal lifespan, to make the entire ascent. The college graduate, under modern conditions, becomes a skilled assistant to some executive after a short apprenticeship, and thus has less climbing to do to reach executive status and eventually to the top.

OBTAINING THE RIGHT INITIAL JOB

There is an important distinction between securing one's first job and obtaining the right initial job. In other words, the young person aspiring to become an executive may make several false starts before getting an

initial job which will lead to executive employment. This is natural, yet it deserves emphasis because it is an apparent contradiction of the basic principle of loyalty which is inculcated by schools and employers alike. When the beginner has become convinced that he has made a false start, the quicker he can arrange with his employer for a voluntary resignation the better. However, the beginner should first identify his present work as a false start by relating it to objective facts and not arrive at a decision on the basis of emotion, or he will only fool himself and damage his career.

The problem which every unemployed person must solve is to find someone who can and will offer him employment either in his chosen career or some related field. How it can be solved will depend upon several considerations. Briefly, the factors he will have to take into account are, (1) choice of positions; (2) the supply and demand of available recruits; (3) current methods of recruitment, including canvassing for employment; and (4) present and future status of the successful applicant.

Making the Choice of a Career

The individual may already have decided for himself the field he desires to enter. The preparation he has chosen may limit his range of choice, though it often happens that apparent specialized preparation may be pertinent to positions not realized in advance of actual opportunity and experience. A sound background of education and training has a curious way of failing to reveal its fitness for a particular career until it meets the tests of practical application. It is safe to say that whatever one has learned in formal education is never a loss. It is rather a resource that can be drawn upon when an unsuspected need arises. Therefore, during the period when a young person is gaining his education and training in preparation for his future lifework, he should be wary of making snap judgment as to what might or might not be useful to him in later life. In reality, he is in no position to make such a decision with assurance because, obviously, what the future will require of him neither he nor anyone else can completely foretell.

Nevertheless, the wise choice of a career is an important factor in achieving subsequent success as an executive. How early one should make this choice may be open to question. However, there are many indications that young men and women who set before themselves definite goals in their formative years are the one whose chances of satisfactory accomplishment in later life are the best. For those who have chosen collegiate preparation for future employment, the junior year is generally not too early to choose a prospective career, at least with respect to such broad fields as business, law, medicine, engineering, teaching, and other professional occupations.

It is recognized that to make a definite decision as to one's lifework is not easy. It is a vital matter that merits considerable time and thought. At the same time, important sources of information are available that provide pertinent suggestions regarding the choice of careers. Excellent literature —of books and periodical publications—on this subject that could be read and studied with profit is constantly appearing. In addition, placement bureaus and testing and counseling services are rapidly becoming established departments in educational institutions for the special purpose of affording expert and unprejudiced vocational guidance to students.

Vocational Competition

When once an individual has determined upon the kind of work in which he will seek his initial employment, he must then take into account the comparative relationship of the supply and demand of available recruits in the particular field of his choice, or in the other fields closely related to it. In general, it may be said that the more numerous the number of qualified individuals, the more rigorous is the employer's inspection, and the more strict will be his requirements. Therefore, when a surplus of qualified candidates exists in a particular field, the choice of a career should be governed very largely by the possibility of competing successfully with the best equipped persons who are seeking to enter it. This is particularly true with respect to so-called "glamorous callings" and "white-collar" positions. Aviation, radio broadcasting, civil and industrial engineering, and personnel management appeal to many young people. As a result, the supply often exceeds the demand for qualified personnel.

In radio broadcasting alone, it is estimated that only one announcer is hired for every thousand auditions conducted. About one-third of the nation's population is employed in white-collar jobs, and two-thirds are employed in the "blue-shirt" or working-clothes class. It is said that two out of three high school graduates plan to seek white-collar employment, despite the fact that the blue-shirt worker quite frequently carries home a larger pay check.

Methods of Recruitment

Of basic importance to the job-seeker are the methods of recruiting used by the prospective employer. How and when the employer hires his help will naturally determine the method of canvassing for a job.

The applicant is particularly fortunate if the employer will come to him. This happens, for example, when employers of large groups of persons send their recruiting officers to colleges and universities to interview seniors with special training or unusual ability. In such cases, the placement or employment bureau does the preliminary interviewing of the students on its registry.

Most of the large-scale business enterprises and many of the smaller ones have a centralized personnel or employment department which interviews almost all applicants for employment. Such an employment department almost never hires executives, and usually has little to do with employment of those who aspire to executive positions. The big task of the employment office is to recruit rank and file workers, machine operators, and the clerical staff of employees.

The most common method of recruiting executives and potential executives is that of employment, after personal interview, of a job-seeker by the person who would be his immediate superior. In other words, an executive hires someone to serve him as an assistant of some sort.

The Employment Interview

The employment interview is the means by which the prospective employee and the available job are brought together. The interview deserves increasing attention paid to it, not only because it has long been neglected as a phase of management, but also because of the high degree of skill which can and should be developed and used in its procedure by both the applicant and the interviewer.

The employment interview is a kind of sales interview in that the applicant is attempting to sell his qualifications for a job, and the interviewer is considering a purchase of his services. The applicant for employment does not need to sell a complete line or prepare the way for repeat business. He wishes merely to present the facts concerning himself and his desire for employment in as convincing a manner as possible and thereby make *one* sale. The interviewer likewise has *one* purpose, that of getting the facts about the applicant by encouraging him to talk freely, and without prompting, in order to judge and evaluate his education and experience as well as his emotional attitudes and responses. The interview will be more successful if the applicant understands this purpose and cooperates readily with the interviewer's promptings.

As pointed out above, the purpose of the employment interview is to establish the facts concerning the applicant. Many supplementary tests have been developed which help to establish such facts. For example, when the application for employment is written out by the applicant, it helps to establish such facts as birth date, residence, skill, and previous employment. Furthermore, it assembles the data in a uniform manner. If properly constructed, the application form will itself trip up the applicant who is trying to hide, distort, or simulate information. The follow-up of previous employers and other references, named in the application form, also helps to establish facts.

A careful physical examination by a competent physician is necessary in order to reveal the facts having to do with health and physical energy.

A check-up of the applicant's record in school and the comments of his teachers is another important fact-finding technique. Certain psychological tests have been found helpful, especially in establishing the facts as to intelligence and potential skills in operations where manual dexterity is a prime factor. Tests of actual skill such as speed and accuracy in stenographic and other office work, are other means of establishing facts. Finally, the obtaining of a credit-rating report from a responsible agency sometimes develops facts not otherwise obtainable.

The purpose of the interview and its related techniques in obtaining the facts is not to select employees but to weed out undesirable candidates. In general, the facts are helpful in a negative rather than in a positive sense. Establishment of the facts of health, social situation, previous experience, education, and even aptitude, proves that certain applicants should be rejected because they lack the potentialities of success. The facts themselves never prove that an applicant, if employed, will make good in his position.

It follows, therefore, that the less tangible the purpose of the employment interview is, the more important it will be. By getting acquainted and thereby achieving a mutual understanding, the interviewer and the applicant measure each other. Skillfully handled, the interview permits the applicant to reveal to his prospective employer his thoughts, ambitions, ideals, and even his potential ability. This is the positive process which results in employment. The young man or woman who cannot use the employment interview as his first steppingstone, and through it win a desirable initial job, probably deserves no better fate. If he cannot "sell himself" to his employment interviewer, he is likely to fail in his future attempts to secure promotion up the executive ladder.

Canvassing for a Job

First in importance and frequency among many methods of canvass is the intelligent use of suggestions and assistance of friends and relatives. For example, a college graduate may secure his first job because a friendly faculty member has recommended him to one of his employer friends. A relative may ask or even insist that one of his kin receive a certain position. Family friends or personal friends may hear of an opening, and may bring job and job-seeker together. A competing traveling salesman may recommend his rival to his own company for employment.

There is a tendency to use the slang word "pull" to describe this method of job-hunting with the aid of friends and relatives. The implication is that it is unfair, or even unethical and immoral, to seek a job through such channels, and that the test of ability is not applied to such job-hunters by their biased friends and relatives. But such condemnation is pointless in most cases because the job-seeker is usually well equipped

to do the work in question. To suggest that a job-seeker should not use every means of canvass, including friends and relatives, is absurd, particularly when it is realized that a large proportion of all jobs are secured through such contacts. To use the assistance of friends and acquaintances in giving personal ability an opportunity to prove itself may be properly considered to be a demonstration of commendable initiative.

A firm-to-firm canvass of all possible employers is also an important method of securing initial employment. It is used by many aggressive job-seekers. Anyone who really wants a job leaves no stone unturned in his search for one. At any given moment, for example, among one hundred employers only a few will be seeking employees of particular qualifications. To find these potential jobs, the seeker after employment must be willing to canvass a large number of employers; or, alternatively, he must interview a few employers many times. In either event, the applicant builds contacts and makes his search more complete and personal.

Specialized Employment Agencies

Closely related to the contact method of canvass is the use of specialized employment agencies. Most agencies able to function effectively in this manner are organized on a nonprofit basis. They include employment services offered by colleges and universities, the federal and state unemployment bureaus, and the employment activities of professional associations, such as engineering societies and trade associations. Some private agencies, such as those for teacher placement, operate effectively. In brief, an agency of this sort makes a canvass of possible employment openings on behalf of the specialized group of persons registered with it. Having found a possible opening, the agency submits to the prospective employer all who qualify according to his specifications. Because the agency limits its work to a special group of candidates of known preparation and ability, its contact with prospective employers is direct and personal. In general, it is best to register with a private agancy only when the position desired falls within the agency's specialized placement field.

General Methods of Canvass

In addition to the specific methods described above, many job-seekers make use of more general methods of canvass—methods which because of their general nature are less effective. Principal among them are the following: (1) the personal unsolicited letter of application; (2) the reply to advertisements; (3) the situation-wanted advertisements. Where a personal unsolicited letter of application is used as a means of introduction prior to a personal call by the applicant, it is of great value in securing the desired interview. It often opens the way for further negotiations and

establishes the availability of a candidate in the mind of a prospective employer.

Answering advertisements yields the best results when the advertisement, whether signed or blind, has been placed by a legitimate employer. Such a reply takes the nature of a response to an invitation. Seeking employment through "situation-wanted" advertisements is usually successful only when the advertiser has some special and well-developed skill or experience to offer. Since few personnel executives in large organizations read want ads even when seeking additional employees, such advertisements are most effective when they are placed in trade or professional journals or directed to the attention of employers in small business concerns.

The Status of the Successful Applicant

It is a fair assumption that the young person who wishes to become an executive will try to shorten the road and make the path less difficult. He does this by obtaining specialized training before seeking employment. If he enters employment at a fairly early age, such as eighteen years he will naturally tend to acquire some trade or craft skill like shorthand and typing or machine operation. If he enters employment after finishing college at a later age, such as twenty-one or twenty-two years, he will tend to acquire some higher business skill, such as accounting in the office field, or engineering or chemistry in the factory field.

Obviously, the longer employment is postponed because of specialized study and preparation, the smaller will be the number of competitors who have acquired the same distinctive skill. As a result, the particular applicant will represent a more restricted supply as compared to the demand. This improved relation of demand to supply increases the likelihood of the applicant's finding initial employment of the right sort.

Another reason why older beginners have relatively more chance to find desirable starting work is their maturity. Beginners are beginners no matter what their age. However, if an employer can choose between a beginner of sixteen years of age and one of twenty years, for example, he will probably choose the older applicant because his greater maturity is an asset.

Finally, the effect of postponed entry into employment upon initial and ultimate status is important. In its narrowest sense, status is rank or position in society. In a caste society, status is determined entirely by birth. Likewise, in many European countries, status is still largely a matter of birth, as, for example, the English nobility.

In a broader sense, and as used in this chapter, status means both hereditary and acquired rank or position in both business and society. Thus one man may inherit his business and social position. Another may

become head of a large business, but may never establish for himself and his family comparable social standing. Still another may win social rank, but not business preferment. Or he may inherit social position, but never earn a position of business leadership. Status also implies well-being, in addition to rank. Obviously, the status of a happy, well-adjusted common laborer may be better than the status of a higher paid, but irregularly employed and spendthrift skilled workman. Similarly, the status of most white-collar office workers is higher than that of factory employees, though the latter frequently receive higher average compensation.

The young man or woman who leaves high school at about eighteen years of age to seek business employment finds advancement to executive rank made increasingly difficult because of status. Specifically such an individual has the problem of executive advancement complicated by several factors. To begin with, it is difficult or impossible for the high school graduate to obtain a starting position as assistant to an executive because he lacks both the necessary skills and maturity. As a result, he obtains his position through routine employment channels and perhaps acquires the status of clerk or machine operator. About the only opportunity that is open to the young man or woman who has only a high school education is to obtain a starting position as a secretary to an executive because of competence in typing and stenographic skills. These skills, plus a knowledge of secretarial duties, bookkeeping, and office procedures and management, frequently permit the young person to start in a clerical position which brings him in close contact with an executive. In this way, the individual learns about the business and some of its executive problems and techniques. Eventually he may win promotion into junior executive ranks after three to five years experience. Such close association with the executive group, plus continued study and application, are often the only way open to the noncollege graduate for advancement to executive status.

Tests of a False Start

After a person has entered upon his first job, it is only natural that he should be concerned as to whether he has made an error in his selection of employment. It is easy for the young college graduate to develop an emotional conviction that he is in a "blind alley" and that his employer and his immediate associates are all conspiring against him. It is important for this individual, if he has executive aspirations, to distinguish between an emotional disturbance and facts. A survey made by a large national corporation reveals that it is the common experience for the college graduate, man or woman, to undergo a period of emotional disturbance and unrest during the first three to three and one-half years of full-time employment. During this interval the tasks of the initial assignment have

been fairly well mastered. But it is a period when the individual may be considering marriage, or for some other reason, has assumed new and additional financial or family responsibilities. Also it is not unusual for an employee to develop a feeling of dissatisfaction with his present job and with the rate of progress that he is making.

Some persons overcome this mental condition, redefine their objectives, evaluate their status, and settle down in their jobs. Others resign to seek more desirable employment. Still others remain on the job but lose interest in their work, develop difficult personalities, or become disciplinary problems and eventually failures. At this point the crucial decision of the acceptance of status must be made.

Certain important objectives tests of a false start and an unsatisfactory status can be made. These tests may be stated as questions: Does the starting position carry with it a status high enough to be accorded a recognized title? Are authority and responsibility sufficiently limited in the status assigned to make satisfactory progress by a beginner possible? Do fellow employees recognize the beginner as an apprentice in his status, and are his rank and salary appropriate to his position? Are fellow employees willing and able to teach the new apprentice, and is the latter willing and able to learn from them? Is the opportunity for promotion from the starting position dependent upon demonstrated ability, or is it subject to rules so rigid that they retard rather than encourage advancement? Are the steps in the scale of advancement well defined and reasonable? These questions can be used to evaluate not only the status in a starting position but also that of any subsequent one which a person may attain.

If, in the service of an initial position, the one who aspires to an executive career can answer all of the foregoing questions in the affirmative, he should not allow himself to be tempted away from his employment. On the other hand, if the position does not meet these tests, it would be to his own best interest for the beginner to seek new and more promising initial employment at the first opportunity.

THE CONDITIONS OF PROMOTION

The common expression, "to make good," is often used to mean that the individual has met certain tests or standards of performance in his work and can therefore look forward to permanent employment. As applied to an executive, however, there is the additional problem of "making good" as a candidate for promotion.

Since an executive must "make good" in his present position in order to merit promotion, the latter phase includes the first problem. That is to say, both performance and eligibility for promotion are involved. To qualify in the former is not necessarily a guaranty of the latter. This point is of great importance to the young individual who desires to become an

executive. The entire group of executives in an enterprise constitute an interlinked device of management. Like a football team or an army command, the success of the group depends, in part, on ability to fill gaps in order to keep the effectiveness of the group at its highest possible level. This means that each executive ought to be worthy of promotion—even though he never receives it—just as baseball players must be able to play at various positions in the game.

In order to become worthy of promotion, a beginner must demonstrate ability in several different ways, all of which are the tests of a good executive. He must adjust himself successfully to the personalities and the internal politics of the organization. He must handle his present job well, both in its technical and in its personal aspects. Finally, he must win recognition in the eyes of those executives with whom he works as a *successful* rather than an *unsuccessful* businessman. While it has been demonstrated that few can ever become "conspicuous" executives, all executives have an opportunity to become conspicuously successful in their particular jobs. The degree of success achieved is the chief measure of their right to a promotion.

Reaction to Internal Politics

Of all the problems which face the person who would become an executive, the one which causes the most heartaches is the problem of internal politics. To the young man imbued with self-confidence, eager to rise rapidly, and aggressively ambitious, internal politics is a serious and annoying obstacle. He may become so resentful of its presence that his attitude and remarks concerning it will harm his own career.

Politics is a human or psychological phenomenon which is present in all groups. It seems strange that the college graduate, who has enjoyed the play at politics all through his college career, should have so difficult a time in understanding and accepting internal politics in a business institution. In college the student becomes familiar with hazing. He joins a fraternity or club and thus often becomes a member of a political party in campus affairs. He participates in campus elections and in other group activities, such as rallies. In all of these, he normally takes part in displaying and developing sentiment. He learns his college tradition, and he finds out how stubborn groups either favor or oppose campus issues. He frequently wins some student office or position and thus has experience in political leadership.

Hazing of beginners in business is as universal as hazing of freshmen in college. As in college, business hazing can be carried to harmful extremes, but most of it consists of harmless pranks and of restricted privileges. The factory apprentice who seeks vainly for a "sky-hook" or the office beginner who is talked into voluntary overtime to do some one

else's work may be angry, but no injury has resulted from the practical joke. The practice of giving beginners the poorest hours, such as the "graveyard" shift from midnight to morning, or the poorest lunch-hour time, or of assigning to them the least desirable machines or jobs, makes the beginner feel hampered and restricted, just as the college freshman does when told to wear a "dinky" and to keep off the grass.

Hazing cannot be entirely stamped out in any group. Instead of resenting and complaining, the beginner does well to recognize its personal value and to accept and endure it with a smile. Hazing is an important element in creating group unity. In a sense, the group in this way tests its new recruits, trains them in its emotions, and accepts them as full-fledged members.

An important psychological factor in hazing is the tendency for resistance or resentment on the part of the victim to cause the group to increase rather than diminish its punishment. Some college graduates have had the experience of becoming virtual outcasts, because, while serving in minor apprenticeship positions, they have asserted themselves as superior beings, executives-to-be, and have resented being subjected to the conditions of worker employment. Their fellow workers have been quick to sense this attitude of aloof superiority and have become even more ingenious in their hazing of the unfortunates. Since successful employee relations is one of the prime tasks of management, obviously such a situation is proof of lack of executive ability on the part of the college graduate just entering the business world.

The charge of internal politics is often used as a reason for the failure to win promotion or even to retain one's position. It is rarely correct and is more often an alibi rather than a demonstrable reason. On the other hand, it is often true that an executive fails because he has himself become an undesirable internal politician. In every executive organization there are always at least two parties, namely, the "ins" and the "outs." The young executive who openly criticizes the major policies of the higher management has by this act become a member of the "outs" party. Before taking such a step, it would be well for him to answer two questions. First, does the beginner down at the bottom of the executive ladder really know the issues and facts sufficiently to make his criticism any more valid than idle yapping or gossip? Second, is the "outs" party within the management strong enough to win control of the organization? If not, the young beginner is committing his future advancement in the business to a hopeless and lost cause.

In any voluntary human group at any given time, there is a certain purpose or objective. Obviously working toward this objective is more politically desirable and popular than working in some other direction. It follows that what seems to the young beginner fresh from college to be a

progressive proposal may appear to be radical and extreme to his fellow executives. Before demanding reform, the young man should be sure that he is sound in his theoretical position and, at the same time, that he is also proposing something practical—something which will make more profit for his business. Otherwise his radicalism will finally be shown to be folly. In any typical large-sized executive organization there will be older executives who will look with favor on the attempts of youth to make contributions and other older executives who will resent this attitude and label it as interference. Before venturing to make a suggestion as to policy or control procedure, the young man would do well to appraise its reception by the higher executive who will probably pass on it, entirely aside from its merits or demerits.

The best advice which can be given to the young man who wishes to become an executive is that he shall make himself worthy of promotion by accepting the internal politics of his business as he finds it. He is too small a factor in the total executive group to change the internal political complexion of the enterprise, even if he does have convictions on the subject. He can use all of his training and mental ability in studying his fellow executives. His problem is to develop an awareness of, and sympathy for, the emotions and attitudes of the executive group of which he is a part. His task is not to resent but to understand and participate with pleasure in this group emotional experience. If he cannot do so, he had best seek employment elsewhere.

Satisfactory Performance of Work

To become worthy of promotion, the beginner must do his immediate job well. In fact, after he has become an important executive, he must still do the job in hand well in order to be eligible for further advancement. To "make good" in the future, one must "make good" in the present. The ancient biblical injunction, "To him that hath shall be given," is particularly pertinent to remember as a terse statement of prerequisites for personal advancement.

In this discussion, it is assumed that the apprentice executive has a minor position involving both line and functional authority and responsibility. In other words, he has charge of one or more subordinate employees, and he has supervision over some technique or process.

His first problem is to convince his immediate superior that he is doing his work well. Some young executives lose sight of this fact and scheme to bring themselves and their work to the attention of one or more of the major business executives. If such activity convinces his immediate superior that he is being disregarded or that his assistant is "going over his head," the complications which inevitably result will probably hamper rather than help the beginner. Because of his educational background and

his relative maturity, the college graduate can often hope to rise faster than the supervisor or junior executive to whom he reports in his initial employment. To allow this fact to become a source of resentment and conflict between himself and his immediate superior is proof of the apprentice's lack of executive ability. An executive must be able to adjust himself to his surroundings and then mold and adjust his surroundings. Open conflict means maladjustment. Furthermore, every executive should strengthen rather than weaken the unity and group effectiveness of the executive hierarchy of which he is a part.

A basic rule of conduct for the young executive is to do his work in the way his immediate superior wants it done. This involves several considerations. The relations between executive and assistant should be so close that the superior feels that he is familiar with, and in favor of, all the important actions and decisions of his subordinate. From a psychological standpoint, it is often possible for the subordinate to lead his superior's thinking up to the point of decision, so that the superior in office will initiate the idea, insist on the subsequent action, and feel entitled to the credit. Contrary to common opinion in such a situation, it is far better for the higher executive to take the credit, since it hastens rather than retards the promotion of the minor executive who did the work.

There is only one sound rule of conduct in cases where there is a definite difference of opinion between a subordinate and his superior. The subordinate should try to convince his superior, but if he is unable to do so, he must either resign or carry out his superior's commands. His relations with his superior must be so intimate as to permit this difference to be aired between them without rancor or tinge of personal feeling. The subordinate is often wrong and should be more than ready to compromise and to accept his superior's instructions. An apprentice executive cannot expect to prove his worth unless he can "handle his own boss."

One of the most important problems of the young executive is to develop his own personal code of business ethics. He must be able to distinguish right from wrong, and he must be willing to resign rather than do wrong. On the other hand, he must be sure of his facts before he endangers his future career by refusing to obey the orders of his immediate superiors. Many business acts draw close to the fine line of distinction between right and wrong, yet are clearly right in an ethical sense because their intent is just and right. Furthermore, there are vital distinctions between personal and social ethics and between basic laws and government regulations. The apprentice executive should avoid the attitude of fault-finding and reforming, but should rather assume that almost all business transactions are honest and that the burden of proof rests with the accuser to prove dishonesty.

A most complex situation arises when orders come down from above

or when there arises an emergency involving technical knowledge possessed to a higher degree by the apprentice executive than by his immediate superior. Here is opportunity for the use of all the tact the subordinate possesses. Rarely should the situation be allowed to develop to the point of firing the "boss" in favor of his more capable assistant. Nine times out of ten the aim of the apprentice executive should be to use this opportunity to make a strong friend and ally of the person to whom he is immediately accountable.

Some executives are psychologically unable to tolerate a subordinate who on occasion may say "no" to them. They want only "yes-men" as subordinates, men who will do as they are told and who do not try to think things through for themselves. Obviously to work in such an atmosphere for long would ruin one's future executive career. When it is definitely proved that such a situation exists, the young executive should seek another initial job as quickly as possible.

Relationships with Subordinates

It is generally true that the duties of a beginner in an executive position include the direction and supervision of one or more persons who must look to him for leadership. Whether he has only one or many subordinates, his basic problem is to develop an organization which will "attorn" to him, to use a little known, but expressive word which is inclusive of all the group ties between a leader and his followers. It means to turn or transfer service to another as chief. The first aspect of the development of an "attorning" group of subordinates is to convince the members of the group that they must look to their new superior in rank as their natural leader. The time-honored method of accomplishing this is to replace the key men within the group with others who, personally selected by the new executive, will attorn to him.

The president's right to choose his own cabinet, for example, is a recognition of this principle. When it is not practical to do this, the new leader can often take over the assistants of the former leader and make them his own. To do this, he "picks a fight" with them on some minor problem, or he transfers them temporarily to distasteful duties, or in some other manner he shows them that he is boss, and he beats them in a token fight and wins from them tokens of submission. This all seems rather silly, a sort of horseplay among grown men, yet it is so natural and fundamental an aspect of leadership that few executives give it a second thought. There is an obvious parallel between this human process of assuming leadership of a group and the ancient practice of armed battle between opposing leaders rather than their armies.

Having assured himself of attorning loyalty in the key positions subordinate to himself, the young executive must then develop, through trial

and error, proper balance between tight and loose supervision of his employees. Before the automobile, everyone knew that some horses were best driven with a tight rein, others with a loose rein. Similarly, some employees work best under close supervision, others work best when on their own with little supervision. Some phases of work take care of themselves, and others demand close attention by the executive as well as his employees. If all detail is forced through the executive's hands, his span of control will be extended too far, and he will become inefficient.

There is no rule to guide the young executive in deciding when and where to use tight, close supervision, and vice versa. The balance he achieves in his executive position determines in large part his success as an executive. It is proof of his skill as an executive if he controls just enough. Thus he becomes like the jockey on a race horse, or the coxswain of a racing boat, contributing skilled direction and control to his group to insure their effectiveness.

The end result of an attorning organization which has the right degree of executive supervision is teamwork and morale. Teamwork means proper distribution of trained skill within the employee group. To achieve this end, the apprentice executive must acquire a necessary mastery of the technical problems of his job. He must be master of all the skills and techniques in the eyes of his subordinates. Anything less than mastery is defeat. He must train his employees and assign them to the different parts of the task in order to achieve teamwork and efficiency.

The result of a relationship of this kind will be the development of morale—a sense of integrated loyalty to the group as a whole. With morale established it becomes possible to meet emergencies as well as routine requirements, since the group will respond effectively to unusual problems and will rise above themselves to cope with new and untried situations.

Discharge of Nonroutine Duties

It has been pointed out that the executive pyramid or hierarchy forms a roughly accurate measure of the proportion of routine activities as compared to varied work. The unskilled laborer performs a routine task. The higher executives are confronted with constantly changing work. In fact, executive work at the higher levels consists of an endless chain of problems, each different from all others in at least some respects. Some problems come up from within the management organization, appealed upward in accordance with the exception principle. Others are originated by the major executives. Still others develop out of the work of staff and functional executives.

As for the young apprentice executive, half or more of his working hours will be devoted to routine, that is, to performance of his normal and

customary duties. As already discussed, he must make good in these current duties in order to merit promotion. However, much of his hope for preferment is to be found in the proficiency with which he handles the nonroutine or unusual problems which develop, or which are inherent, in his particular work.

In contrast with routine operational problems of the immediate present, all unusual problems presented to an executive for solution have a future aspect. In solving the unusual problem, a policy-type precedent is developed, or a method is evolved, which will affect the future of the business.

One of the important qualities developed by successful mature executives is a "sixth sense" which may be defined as the ability to visualize future problems and future results from the fragmentary evidence available in the present. If the young executive can prove that he possesses this vital management skill, his promotion becomes more certain.

One of the tests of this sense of awareness is perceived in the young executive's method of handling failures. If something goes wrong, if a machine or a system breaks down, the most serious kind of nonroutine situation has developed. If it hits without warning or preparation, obviously the "sixth sense," or awareness of future potentiality, is undeveloped. On the other hand, if the young executive handles his problem calmly and makes his fellow executives and his own subordinates feel that he knows exactly what to do, his future advancement becomes more certain.

If the young executive has developed to the point of having forecast the failure situation and of having taken steps in advance to minimize loss or turn defeat into victory, his ability as an executive is proved to be very high. Or if he can make practical suggestions to his superior executives, at or before the moment of failure, which point the way out of the trouble, his executive value is already well developed.

Ethical Standards of Conduct

One of the most difficult and critical situations which will confront a beginner in a management career is the matter of ethics. He will not long have been in even a minor executive position before he will face decisions which will challenge his own conceptions of what is right and what is wrong. He will find that hasty judgment in such instances is not only unwise but dangerous because his immaturity and inexperience may lead him to biased conclusions. A personal code of ethics does not issue full blown in youth to remain unchanged thereafter. It is a matter of gradual development and refinement out of which there comes standards of conduct supported by convictions rather than prejudices.

Because a beginner in a management career finds himself in a new

environment, he must develop new standards of conduct that reflect his personal code of ethics. Foremost among these standards will be his behavior among his new associates, whatever their status, rank, and position may be. He will have to determine his standards of conduct in his relationship to older executives, superior in rank, who are not as efficient as he thinks they ought to be. To guide his attitude toward them his wisest course is to adopt the Golden Rule, since his youthful enthusiasm may lead him into pitfalls of misjudgment of those above him.

Then again, the young executive must develop standards of personal conduct toward his associate executives of equal rank. For example, he must avoid becoming a mere "tattle-tale" or gossip. He must refrain from attempting to extend the boundaries of his job at the expense of his fellow executives. He must seek their personal friendship and merit their sincere respect. On the other hand, he must not become a party to their attempts to hide their mistakes or, in any other way, to obstruct the progress of the business to achieve its objectives.

The beginner in an executive position must also develop his own code of ethics in his treatment of subordinates. He must decide between arbitrariness and a "soft" attitude toward employees who must be discharged or laid off. He must "make the punishment fit the crime" when insubordination and a disregard for instructions develop. He must decide whether to favor or to oppose nepotism or racial and religious cliques in his own working group. He must also decide whether to adopt the democratic, the autocratic, or the aristocratic attitude toward the employees over whom he exercises leadership.

In addition to standards of conduct in his association with other persons, the young executive has other ethical decisions to make. He must develop a moral code against which he will judge whether a prevailing policy of his company is right or wrong. Even if he is inclined to believe the policy to be wrong, he may still be willing to conform to it because his sense of duty to his commitment of employment outweighs his confidence in his own judgment.

Closely related to policies are the directives, orders, and commands that come down to the beginner from higher authority for his execution and enforcement. Here again, the performance of the tasks assigned to him will be conditioned by his sense of right and wrong. Also, he must have an even more lively consciousness of moral justice to apply to the orders he himself issues, and to the decisions he is compelled to make. As already stated, the beginner should be slow to judge and anxious to have all the facts before making up his mind. But having decided that some required act is wrong and having failed to change the policy or decision of his superiors regarding it, he should "refuse to live the lie" and should seek another initial position. No executive can expect to merit promotion

if he has not developed within himself a sure sense of right and wrong and a rigorous, unswerving personal honesty.

Approval and Support of Superiors

In order to merit promotion, the young executive must convince his superiors of his value to the organization by a manifestation of his ability. To accomplish this end he may become conspicuous without being obtrusive. Through the channels of internal company publicity, he will naturally attract attention if his work is customarily outstanding. For example, if a concern has undertaken an intensive safety campaign and the young executive can rate the highest score for his group of workers in preventing accidents and injuries, he will attract favorable attention. If in compliance with a policy of strict operational economy, he finds ways and means of cutting expenses in his own department without sacrificing quality and service; or if he makes helpful suggestions that will implement economy throughout the company, he will find himself a favorably marked man.

Obviously, the apprentice executive must avoid seeking publicity for its own sake. On the other hand, if he is alert enough to know what his executive group is interested in, and if he is able enough to enter into competition with the older executives and win, the resulting internal attention and publicity will be highly desirable.

Another method of attracting favorable attention used by many candidates for promotion, is to enter upon special study with the knowledge and approval of superior executives. The young executive, for example, who has graduated from college in economics and business subjects without a background in engineering, but secures a position in a manufacturing industry, proves his sincerity to his factory superiors by taking courses in night school in such subjects as his previous training may lack. Or he obtains books, he asks questions at every opportunity, and he finally proves through some actual accomplishment on the job that he has mastered the required techniques.

As stated at the beginning of this chapter, heredity is not the most important nor the most pervasive basis upon which executives select subordinates for promotion. This fact can be demonstrated in different ways.

A study of the executive pyramid or managerial hierarchy reveals that there are many more executives at the subordinate levels that at the higher levels of management. Obviously, only the higher executives are in the necessary position of authority to transmit by inheritance or selection the right to executive opportunity to their children or relatives. But since the smaller group of higher executives is only a minority of the entire organization of any one business, it follows that only a minority of those

who aspire to become executives will obtain their initial opportunity because of heredity.

No business organization could hope to make profits if all of its executives were incompetent. The typical business cannot afford to have incompetents in important executive positions, drawing high pay and impeding the work of abler executives. It is clear, therefore, that even the minority of apprentice executives who owe their start to heredity, must, with few exceptions, win promotion because of their ability. Because their relatives make them conspicuous beginners, their rise up the executive ladder is thereby hastened, but their rise must be matched by ability to do the job. Business history is full of examples of companies that have become great because they have promoted executives on the basis of ability and have "sidetracked," "shelved," or "kicked upstairs" the less competent heirs and relatives of the founder.

The more important reasons for the selection of a particular apprentice executive for promotion can be briefly summarized. He has been observed by his superiors in such a way as to convince them of his executive ability. Reports from the executive to whom he is immediately accountable and from his associates indicate that he has succeeded in his present job and that a competent successor is available if the promotion is made. His record may show that the young executive has been studying his next job and is therefore ready for advancement. By virtue of his code of ethics and his personal conduct, he has demonstrated that he has the earmarks of a good executive. In particular, there have been no tales or reports damaging to his character, nor are there any currently in the channels of internal politics.

The young candidate for promotion has attained sufficient age and maturity, adequate experience as an executive, and appropriate status in the business and in society. And finally, it is an established policy of management to encourage promotion on the basis of merit within the organization as the natural method of executive advancement. When an apprentice executive can meet all of these qualifications and conditions, including the final merit test, his progress toward a successful career in management can be expected.

PERMANENT ESTABLISHMENT IN A CAREER

In this discussion of a career in management, it has been assumed that the goal of the beginner is a place in a business organization as a major executive. Major executives are, of course, general executives with a wide variety of duties. Emphasis is placed on their effective leadership in the management of large numbers of subordinates.

When an individual has received his initial promotion, he has made the first step that leads to permanency in his career. He will thereby auto-

matically become more closely associated with persons who have been in the business and are seasoned in their occupations. To improve his fitness for further advancement, now that he has served his apprenticeship, it is essential that the young executive seize upon every opportunity to understand his older colleagues in the executive group and to have sympathy for their problems. It is then easier for him to work with them and to gain by their experiences as well as his own because he must realize that he too, will grow old.

As an executive contemplates advancement over the years, there are some characteristic situations with which he, like all other executives, will be confronted. One is the practice commonly described as bringing in "new blood" to management; another one is the transfer of older executives within the organization itself; and finally, there is the possibility of discharge or, eventually, retirement.

Appointments of "New Blood"

The term "new blood" is usually applied to the appointment of persons to executive positions from the outside, or it may mean promotions within the organization whereby customary advancements from one status or rank have been disregarded. An eventuality of this kind concerns every executive, but more particularly the individual who has just begun his career because such an opportunity may suddenly come to him. If it happens to him within the organization it could mean that he would be advanced "over the heads" of some of his associates, and even over other executives in superior positions. His chances of attaining top ranking in the management group will, thereby, be materially increased.

Generally, the term "new blood" refers to appointments from the outside. For example, an outstanding minor executive in a sales department in one company may be selected to become a major sales executive in a competing concern. Such an appointment is a promotion to him while it has, at the same time, retarded the advancement of certain executives in the organization of which he has become a new member. The young executive could conceivably find himself in one of these situations. On the one hand, his ability as an executive might make him eligible for more rapid advancement than his current position permits him to realize. By going to another firm, he has deviated from his otherwise natural course of promotion and gained an advantage over his former associates. On the other hand, he might be one who would logically be in line for promotion in his own organization, but when the position next above him became vacant, it was found that he was not qualified to be assigned to it, so "new blood" is brought in to fill the spot that normally would have been his.

One of the peculiar characteristics of the normal path of promotion,

from supervisor to assistant department head, to department head, to major executive, to president or top executive, is that it causes executives to develop a high degree of functional specialization, but it does not give opportunity to develop all-round executive ability. For example, the highly trained purchasing agent has usually had little or no opportunity to learn how to handle large numbers of employees or many subordinate executives.

It is, of course, dangerous for an executive to jump from job to job without regard for the welfare of his employer and not caring about the damaging implications of becoming a "rolling stone" or "floater." On the other hand, the young executive who seeks to have more than one employer and who makes good in more than one functional field often prepares himself for substantial promotion. If he cannot obtain varied experience under one employer, he should seek to obtain it from several different employers. Thus he will be available as "new blood," should such an opportunity present itself.

The apprentice executive, on the other hand, may have the equally desirable but opposite goal of becoming the outstanding functional executive in his chosen field of specialization. If this is his goal, he need not seek variety of experience by working for more than one company. He can obtain the desired variety in his own business by study and contact with the varied problems of specialized character which will come to his department. If he becomes an outstanding functional expert, he may become "new blood" at a higher executive level, in his own or another company, because his skill has attracted attention to him.

An important warning should be kept in mind by the young executive who seeks substantial promotion as "new blood." The apprentice executive, in his enthusiasm, runs the risk of becoming known as the "betrayer" of his predecessor. This is a harmful accusation since it will cause at least some of the employees and associates of the former executive to regard the newcomer as an interloper, or even as a sort of criminal who should not be permitted thus to profit from his treachery. This "internal politics" situation may make success at the new job impossible for the representative of "new blood" who has been the recipient of the promotion. As stated above, the young executive should remember the Golden Rule in his dealings with and about older executives, if he would be honest and fair with them, and avoid their biting and effective counterattack.

Transfer of Older Executives

Another problem facing older executives, but of importance to the young executive, is that of transfer. "Promotion" means upward movement, "demotion" downward, and "transfer" a sidewise shift within the executive organization. A transfer is neither a promotion, nor a demotion,

though it may be a prelude to either one. It is merely a change in duties, caused in one of the following ways. In the first place, a transfer may be necessary in order to recognize a change in the size or the functions of a particular department. This is important to the apprentice executive in that department, since it may make his own training and experience more valuable or less valuable. In other words, the forces causing the transfer of an older executive may later have an effect on the younger.

In the second place, a transfer may be necessary in order to stimulate an older executive who is "losing his punch." Transfer, properly used, has a strongly stimulating effect on older executives. This is important to the young executive because of the lesson it brings to him to try to maintain his enthusiasm and interest so as not to have to be put through a "shake up" in order to redevelop his value to the company. Also, a transfer may be made as a prelude to promotion of the older executive. For example, he may stand out as the logical next president and be transferred to give him more varied experience within the company, at the major executive level, before assuming the top position. In this case again, the alert young executive who reads the indications of the future correctly will use this information in guiding and shaping his own conduct.

Finally, a transfer may be made as a prelude to retirement, demotion, or discharge. This often is worked out by splitting an executive position into two parts, so that a younger executive, perhaps the former assistant, can be promoted. The older executive retains his rank and pay, unchanged, but relinquishes a portion of his duties to the complete control of a younger executive. This type of transfer is easy to identify, and often results in "grading up," or promoting, the entire line of subordinate executives in the particular department, including the young beginner at the bottom of the executive ladder.

Discharge or Retirement

Demotion of an older executive is a bitter pill for him to swallow, no matter what its "sugar-coating." It may be a blunt and peremptory discharge. It may be honorable retirement, after long years of good service. It may be plain demotion, that is, reduction in duties or pay, or both.

Many older executives, faced with probable demotion, make false moves that cut short their executive career. They become uncooperative with their superiors, and thus invite discharge rather than better treatment. They may seek out another job which seems better but is in fact poorer and resign rather than face the injury to their pride. The younger executive does well to know as little as possible and to be as neutral as possible with respect to the "internal politics" or the pressure of this sort which top management is forced to put on the older executives. He should try to learn the lesson, by watching his older associates, to "grow old

gracefully." When he in turn passes through maturity into old age and begins to slip, perhaps he will have been able to prepare for and welcome honorable retirement.

RELATION OF THE YOUNG EXECUTIVE TO SMALL BUSINESS

This survey cannot be considered complete without discussion of the beginner executive and his potential opportunities in small business. Much of the foregoing discussion has necessarily used illustrations of practices and situations from within larger enterprises. Internal politics is an example, as this problem need not exist at all in a closely-knit, well-managed small business concern.

It is desirable to remind ourselves of the large number of small businesses. Consider the comparatively few manufacturers of automobiles, and the large number of small businesses within the automotive field. General Motors, for example, reports that it does "business with 13,000 such firms, and what we buy from them represents nearly one half of the value of our products. Such cooperative effort is the essence of mass production."

In the automotive field, in addition to the parts suppliers, there are an estimated 34,000 dealers, 240,000 filling stations, 24,000 taxicab companies, 38,000 trucking concerns, 50,000 automobile repair shops, and 19,000 tourist courts.[3]

The parental, or inheritance, method is an important and useful avenue for entrance of the beginner executive into a smaller business concern. Personal contacts count for much within the executive group of a small enterprise. The young man or woman whose parent is already employed, even though the latter be in a relatively minor position, may expect a friendly hearing if he offers adequate preliminary training, good personality, and obvious loyalty.

The beginner executive in a small enterprise encounters the two special problems—not present to any important degree in larger companies—of stability and of variety.

There are more than three million small business concerns in the United States. Every year several hundred thousand are liquidated or are so merged as to lose their identity and their separate executive group. Every year several hundred thousand new small businesses are started. During each year an even larger number of these small-sized companies and partnerships change their form, or their objectives, or their activities to a radical degree, if the employment or discontinuance of even one executive position is considered in its proper relation to the entire business. All this means to the beginner executive more likelihood of his position,

[3] Albert Bradley, *Let's Stop Taxing Progress*, in pamphlet reprint of address delivered at Swampscott, Mass., September 6, 1947, pp. 18–19.

even though it be at the lowest rung of the executive ladder, being disturbed in a manner adverse to his own continued job.

The other problem is at the least a challenge, and may be a great opportunity. Because of the small executive group, the apprentice or beginner executive necessarily has more responsibility, more authority, and more accountability for a great variety of problems than could be true of a similarly titled executive position in a large concern. Such variety of experience, offered to the right person early in life, has training values not obtainable in any other way. It is often true that executives trained in this varied manner in a small enterprise find themselves potential "new blood" for a larger concern in the same field.

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