Sect 2.6 - Balanced Scorecard excerpt from

The Integrated Enterprise Excellence System: An Enhanced Unified Approach to Balanced Scorecards, Strategic Planning and Business Improvement

Forrest W. Breyfogle III
Founder and CEO
Smarter Solutions Inc.
Forrest@SmarterSolutions.com
512-918-0280

Reprinted with Permission of Bridgeway Books and Citius Publishing, Inc, Austin, TX

For more information about our books, please write to us, call 512.478.2028, or visit our website at www.bridgewaybooks.net.

Printed and bound in the United States of America. All rights reserved. No part of this book may be reproduced in any form or by any electronic or mechanical means including information storage and retrieval systems without permission in writing from the copyright holder, except by a reviewer, who may quote brief passages in review.

Library of Congress Control Number: 2007936770


Copyright © 2008 by Citius Publishing, Inc.
The Integrated Enterprise Excellence System

- Table listings for performance-measure action limits can lead to the wrong activity. This format for action-limit establishment does not systematically address process shift and other situations that can be addressed only through charting. Performance-measure action limits set without examining a 30,000-foot-level control chart can lead to firefighting (see Breyfogle 2008c, for chart-creation methods).

These issues are overcome when the concepts of hoshin kanri are blended within an IEE infrastructure. Hoshin kanri techniques can be integrated into the E-DMAIC roadmap to systematically address not only the creation of projects but also day-to-day business activities (see Breyfogle 2008b).

2.6 The Balanced Scorecard

The balanced scorecard, as presented by Kaplan and Norton (1992), tracks the business in the areas of financial, customer, internal processes, and learning and growth. In this model, each area is to address one of the following questions:

- **Financial**: To succeed financially, how should we appear to our shareholders?
- **Customer**: To achieve our vision, how should we appear to our customers?
- **Internal business process**: To satisfy our shareholders and customers, what business processes must we excel at?
- **Learning and growth**: To achieve our vision, how will we sustain our ability to change and improve?

Figure 2.5 illustrates how these metrics are to align with the business vision and strategy. Each category is to have objectives, measures, targets, and initiatives.

Scorecard balance is important because if you don’t have balance you could be giving one metric more focus than another, which can lead to problems. For example, if we only focus on-time delivery, product quality could suffer dramatically to meet ship dates. However we need to exercise care in how this balance is achieved. A natural balance is much more powerful than forcing balance through the organizational chart using a scorecard structure of financial, customer, internal business process, and learning and growth that may not be directly appropriate to all business areas. In addition, a scorecard structure that is closely tied to the
organization chart has an additional disadvantage in that it will need to be changed whenever significant reorganizations occur.

In IEE, we achieve natural scorecard balance throughout the business via the enterprise value chain (see Figure 7.3), noting that overall learning and growth would typically be assigned to HR but, when appropriate, can also be assigned to other functional performance. We assign metrics to the owner who is accountable for the metric’s performance. These metrics can be cascaded downward to lower organization functions, where these metrics also are assigned to owners who have performance accountability. With this IEE system whenever there is an organizational change the basic value chain metrics will not change. Only the ownership will change.

When we create these metrics it is not only important to determine what to measure but it is also very important to also focus on the how to report so that this metric performance tracking leads to the most appropriate action, which may be to do nothing. Later we’ll describe a system to accomplish this.

Jim Collins describes in Good to Great (2001) a level five leader as someone who is great while leading an organization and whose effect remains after the person is no longer affiliated with the organization. I describe the level-five-leader-created legacy as being a Level Five System.

... it seems to me that it would be very difficult for an organization to create a level five system when the primary guiding light for the organization is its strategy, which can change with new leadership.
In my workshops, I often ask, Do you think your organization’s strategy would change if there were different leadership? A vast majority give a positive response to this question. Because of this, it seems to me that it would be very difficult for an organization to create a Level Five System when the primary guiding light for the organization is its strategy, which can change with new leadership.

I don’t mean to imply that organizational strategies are bad, but I do believe that strategies created without structurally evaluating the overall organizational value chain and its metrics can lead to unhealthy behavior. To illustrate this, consider the following example.

Parameters for a global service corporation dashboard were defined by the following underlying strategic executive goals for the year: grow revenue 25 percent per year, earn minimum of 20 percent net profit, achieve 60 percent of revenue with repeat customers, balance regional growth, fill open positions corresponding with growth, ensure that all employees are competent and high performers, realize projects within time and cost targets, limit ratio of overhead to productive time to 20 percent, and satisfy customers 100 percent.

These objectives, measures, targets, and initiatives were then set up to be monitored, as shown in Figure 2.6, where each metric is to have an owner. Color-coding is used to help clearly identify actual performance versus targets and forecasts. The exclamation marks indicate red flags, where objectives are not being met and attention is needed.

These executive dashboard metrics can then be drilled down further, as shown in Figure 2.7. Would you like to sign up to own this metric and its achievement? The strategic objectives described previously set a customer-satisfaction metric goal of 100 percent. Not a bad target; however, meeting this number is not easy. Simply setting this goal will not make it happen, at least not as the team setting the goal would like it to happen. One might wonder how this goal was determined. Do you think this goal is SMART; that is, specific, measurable, actionable, relevant, time-based?

For this metric type, an unachieved goal earns an exclamation mark, indicating that the metric’s owner may need reminding that his or her job-performance rating depends on achievement of this goal. What kind of activity might this type of pressure create, especially when improvement detection is immediately needed? We might initially think that the owner would, as soon as possible,
start an investigation into where quality improvements need to be made. But we need to be realistic. Immediate improvements are needed to make this scorecard look better. Might there be other ways to make this happen?

Before we react, let’s step back to see the bigger picture. A customer-satisfaction goal is not being met; however, is this level of customer satisfaction really a problem? What were the scores from previous reporting periods? If the scores are better now, this would be good since improvements are being demonstrated, even though the strategic goal is not being met. Without a historical time-dependent reference, could there be disagreements for what is good or bad?

Keeping in mind the type of metric described in Figure 2.7, consider the following situation:

A few years ago, when my wife and I were buying a new car, negotiating the price of the car with the sales associate got to be a game with me. After we closed the deal, the sales associate pointed to a survey that was facing us under his Plexiglas desktop. This survey had all...
26  The Integrated Enterprise Excellence System

The salesman said we would receive a survey in the mail. Then he said that he always gets 5s on his survey. He pointed to my wife and said that he wanted her, not me, to fill out the survey.

Consider the following points:

- The salesman said we would receive a survey in the mail.
- He pointed out that he always gets 5s, as noted on the survey form on his desk.
- He wanted my wife, not me, to fill out the survey.

Do you think he might be trying to bias the survey in his favor, perhaps a bonus is riding on these results? Do you think this type of behavior is what the metric should be creating? This is one form of trying to manage the output of the metric process, rather than systematically working to change the process, or the inputs to the process, so that an improved response occurs. Simply setting high-level goals and then managing to those goals can lead to the wrong behavior. Making true long-lasting gains in customer satisfaction is more involved than working to get satisfactory scores on evaluation sheets. Attaining long-lasting customer satisfaction involves improving the process and the inputs to the process.

Let’s next examine the profit scorecard in Figure 2.8. Notice that the x-axis units are 1–12. What do you think this indicates? Months is a good bet since the metric starts with 1, which is probably the first month after the company’s fiscal year. Notice, also, how this tracking is made only against the goal with no indication of what kind of performance has been experienced in

---

![Executive Dashboard Customer Satisfaction Example](image-url)

**Figure 2.7:** Traditional performance measures: The balanced scorecard/dashboard customer satisfaction drill-down.
Business Systems Can Stimulate the Wrong Behavior

the past. Since the goals are annualized, the target line is drawn beginning the first month of the year, but there is no record of performance the previous year, or whether the goal is reasonable or simply a pie-in-the-sky objective.

If people are really held accountable for achieving this metric objective, very undesirable behavior can result. Since there is an exclamation point, the owner of this metric would need to take immediate action to drive these numbers in the right direction. A high-level metric such as this could lead to the Enron effect, where money could be simply shifted from one area to the next to make things look better; Or the metric could lead to immediate cost-cutting measures that might significantly damage the company’s future outlook. You can cost cut your into profitability for only so long. At some point in time you will see diminishing returns and possible increase in fixed costs due to inefficiencies created by the lack of resources. This form of metric reporting can also lead to the previously described behavior, where Krispy Kreme shipped donuts that they knew would be returned so that quarterly expectations would be met.

Metric reporting, where focus is given only to whether output-type goals are met, can cause behavioral problems lower in the organization as well. Consider the following:

A prison representative purchased a commodity item only at the end of the supplier’s quarterly financial reporting period. Near the end of every quarter, the salesperson for the supplier called,
offering the prison a price incentive for immediate purchase. Because of the type of product sold, there was no reason for this cyclic behavior. Since manufacturing personnel were on overtime and were under pressure to increase production volume, quality problems were more prevalent during this period than others.

This odd behavior was eventually noticed and an investigation was conducted. Asked why the prison waited until the end of the quarter to purchase the product, the representative responded that the salesperson called at the end of the quarter with the discounted price.

Additional company investigation revealed that the salesperson typically had difficulty in meeting his quarterly target objective. Near the end of every quarter, the salesperson would ask his manager for approval to give customer discounts, which would help their department meet its targeted goals. If these goals were not met, there would be no personal or departmental bonuses. The manager routinely complied.

What makes this situation even worse is that the salesperson was getting paid off the top line (total products sold), while the company was taking a significant impact at the bottom line. That is, the salesperson was getting rewarded for total products sold, while the company’s true profit from the transaction was reduced by the sales commission as well as additional overtime costs due to demand spike.

All these negative corporate-profitability behaviors originated with the company’s salesperson commission policy. Rather than someone noticing and investigating, this type of situation could be readily identified in an E-DMAIC structure during the analyze phase. In this structure, a project could have been created that later resolved the undesirable behavior of the sales department through changing either the reward policy or the discounting policy so that these demand spikes would no longer occur.

The shortcomings of many traditional performance metrics are that they often reflect only fiscal year metrics, make comparisons to a point estimate from a previous month or year, and don’t have a procedure for improving the process so that gains occur and are maintained. These traditional methods don’t view the enterprise process as a system of processes, where the performance metric is the result of these processes along with the variability that
occurs within them. Long-lasting change is a result of systematic improvement to these processes.

The shortcomings of many traditional performance metrics are that these metrics often reflect only fiscal year metrics, make comparisons to a point estimate from a previous month or a previous year, and don't have a procedure for improving the process so that gains occur and are maintained.

This form of metric reporting is always after-the-fact reporting and not predictive. Imagine if a customer said, “Based on past experience, our products will have a consumer half-life of only years. If innovations and improvements are not sustained, our revenues will decline by – percent over the next – years.” This type of data-driven statement leads to long-term thinking that can have long-lasting results.

2.7 Red–Yellow–Green Scorecards

The previously described balance scorecards and other scorecards that are not balanced often use red, yellow, and green to show whether actions are needed relative to meeting established objectives. The Office of Planning and Performance Management of the U.S. Department of Interior uses these metrics in the following way (U.S. Dept. of Interior, 2003):

Office of Management and Budget (OMB) has established an Executive Branch Management Scorecard to track how well departments and agencies are executing the five President’s Management Agenda (PMA) components. The Scorecard also strengthens the sense of accountability on the part of these agencies. The Scorecard presents an updated assessment of the status and progress being made to address each of the President’s Management Agenda (PMA) goals.

Status is assessed against the standards for success that have been developed for each initiative and are published in the 2003 Budget. They are defined as follows:

- Green: Meets all of the standards for success.
- Yellow: Achieved some, but not all, of the criteria.
- Red: Has any one of a number of serious flaws.
Description of the Integrated Enterprise Excellence Book Series

In this book *The Integrated Enterprise Excellence System: An Enhanced Approach to Balanced Scorecards, Strategic Planning and Business Improvement*, illustrations exemplify how traditional business systems can lead to undesirable activities and then presents an IEE alternative. **Table of Contents**

In the three-volume series, *Integrated Enterprise Excellence: Beyond Lean Six Sigma and the Balanced Scorecard*, there is both further elaboration on the shortcomings of traditional systems and the details of an IEE implementation. Volumes of this series build upon each other so that readers can develop a true appreciation and understanding of IEE benefits and its implementation. When explaining the concepts to others, readers can reference volumes or portions of volumes at the other person’s level of understanding or need. Series volumes make reference to other volumes or *Implementing Six Sigma* (Breyfogle 2003) for an expansion of topic(s) or a differing perspective. These volumes are written to stand alone; however, there are some volume overlaps in the building of this IEE methodology series progression.

A content summary of this volume series is:

- **Integrated Enterprise Excellence Volume I - The Basics: Four Golfing Buddies Going Beyond Lean Six Sigma and the Balanced Scorecard** --An IEE onset story about four friends who share their experiences while playing golf. They see how they can improve their games in both business and golf using this system that goes beyond Lean Six Sigma and the balanced scorecard. The story compares IEE to other improvement systems. **Table of Contents**

- **Integrated Enterprise Excellence Volume II - Business Deployment: A Leaders’ Guide for Going Beyond Lean Six Sigma and the Balanced Scorecard** --Discusses problems encountered with traditional scorecard, business management, and enterprise improvement systems. Describes how IEE helps organizations overcome these issues utilizing an enterprise process define-measure-analyze-improve-control (E-DMAIC) system. Systematically walks through the execution of this system. **Table of Contents**

- **Integrated Enterprise Excellence Volume III - Improvement Project Execution: A Management and Black Belt Guide for Going Beyond Lean Six Sigma and the Balanced Scorecard** --Describes IEE benefits and its measurement techniques. Provides a detailed step-by-step project define-measure-analyze-improve-control (P-DMAIC) roadmap, which has a true integration of Six Sigma and Lean tools. **Table of Contents**