



# Principles for Structuring Small Businesses and Farms

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While the owners of farms and small businesses are often portrayed as self-reliant individuals working against overwhelming odds, the reality is that often several people make important contributions to the success of the business. These people may be a spouse, family members, unrelated employees, or business associates such as a lender, technical consultant, or market advisor.

In any small business, there is always plenty of work to be done. This work includes the physical labor—doing things—as well as planning, organizing, and evaluating—thinking about things. What are the jobs that need to be done? How are these jobs going to be divided up? Who is responsible for what? If problems or questions arise, who does the person go to for help or to get answers?

All of these questions and others about personnel get answered by someone. But in many cases, the answers are not explicitly stated. Often, a problem arises, and you decide on a solution without giving much attention to the long-term implications of your quick-fix solution or the message that your solution may be sending to other family members or business employees.

## Organization Structure

Small businesses have a small number of employees, so there is not a great deal of formality associated with the development of an organizational structure. Often this lack of formality is accompanied by a high level of secrecy or just assumptions that people know what is happening and why changes are being made. The reasons that a particular organizational structure is being used are seldom communicated.

**Audience:** Owners and managers of a family business or other small business

**Content:** Introduces five principles used for guiding the organizational structure of a small business and provides three common organizational structure examples

**Outcome:** Users will understand the importance of organizational structure and be able to draw an organizational chart for their business.

As changes are made in the business, especially when a new employee is added, reviewing the organizational structure of the business can be helpful. Rather than hoping people will learn to fit in and get along, it is often more productive to give careful thought to the responsibilities associated with each position in the business and the relationships among these positions.

No two small businesses are organized identically because managers, employees, families, and the work involved vary from one business to another. However, there are five key organizational structure principles to keep in mind. These principles have two uses. First, these principles are helpful in the actual design of the organization's structure. Second, these principles can serve as a check list for evaluating and improving the current organization structure. (The information provided here on key organizational principles is from Bernard Erven's *Organizational Structure of the Family Business* <<http://aede.osu.edu/people/erven.1/HRM>>.)

## 1. Exception Principle

Someone must be available to handle the exceptions to the usual, i.e., someone must be in charge. When an employee or worker has a problem he or she can't handle, the organizational structure should provide for someone higher in the organization to give assistance.

To illustrate, a tractor driver on a grain farm hearing an unexpected noise in an engine should be able to discuss the noise with his or her supervisor. This discussion should either reassure the driver that the problem is not serious or lead to repair work to solve the mechanical problem. If the noise appears to the supervisor to be an early indication of a major engine problem, the supervisor may want to discuss the problem with the owner of the business. The discussion may lead either to a decision to wait until the problem becomes more serious or repair the engine immediately.

Note that both the driver and supervisor had a person higher in the organization to consult about the unusual engine noise problem. Hoping that the driver would solve the problem does not substitute for application of the exception principle.

## 2. Decentralization

Decisions should be pushed down to the lowest level possible in the organization. The more routine a decision, the lower the level in the organization on which it should be handled. To illustrate, workers waiting each morning to be told what to do and where to do it can be a great waste of manager and worker time. Decentralization means that workers have been provided the training that allows them to handle decisions within their job descriptions confidently.

The objective is to overcome the waste of time stemming from too much centralization of decision making. Working managers rather than managed workers should be the goal.

## 3. Parity Principle

Decentralization requires delegation. With delegation comes responsibility. Authority should be delegated along with responsibility.

To illustrate, assume the 18-year-old son of the owner of a landscape firm has been given the responsibility of taking a crew of three people, each over 25 years old, to a landscaping site to plant five trees and 30 bushes. Further assume that the son has no authority to decide how hard it has to be raining

before the crew stops working, no authority to correct a person who is digging the holes for the trees and bushes too deep, and no authority to reward the crew member who is doing by far the best job. It is easy for the three workers to ignore the son if they have been accustomed to taking orders only from the owner and the owner has given the workers no indication of what authority the son does and does not have.

## 4. Span of Control

The span of control is the number of people a manager supervises. The organizational decision to be made is the number of subordinates a manager can effectively lead. The typical guideline is a span of control of no more than five to six people. However, a larger span of control is possible depending on the complexity, variety, and proximity of jobs. The ability, experience, and style of the manager also affect the desirable span of control. Finally, worker characteristics affect the span of control. Well-trained, motivated, experienced, and satisfied workers require relatively little supervision.

Owner/managers of family businesses often have span of control problems because of a "me" attitude. As a family business grows and people are added, the manager still may want everyone reporting to him or her rather than delegate responsibility and authority to a middle manager.

## 5. Unity Principle

Ideally, no one in an organization reports to more than one supervisor. Having more than one supervisor often results in an employee receiving conflicting instructions and assignments. Some business owners think that they can develop a level of communication between supervisors that is good enough to prevent this conflicting message problem. However, supervisors typically lack the time for the necessary coordination and communication. This requires the employee to decide which set of supervisor instructions he or she will not follow.

To illustrate, imagine a cashier in a roadside fruit market being told by the market manager to read a new bulletin, "A Baker's Guide to Apple Varieties." The manager suggests that the cashier read it during slack times in customer traffic. The market manager wants the cashier to take initiative in helping customers select apples. The same afternoon, the owner of the market stops by for the first time in four days and catches the cashier "wasting time" reading. The owner quickly orders the cashier to find a broom and get busy cleaning.

Employees should not have to decide which of their supervisors to make unhappy because of the impossibility of following all the instructions they get.

## The Organization Chart

An organization chart is a useful tool to illustrate and understand the organizational structure of a business. Such a chart typically lists the title of each person's position and, by means of connecting lines, who is accountable to whom and who is in charge of what area.

The organization chart shows the chain of command between the top of the organization and the lowest positions in the chart. The chain of command represents the formal path a directive should take in traveling from the president to employees at the bottom of the organization chart or from employees at the bottom to the top of the organization chart.

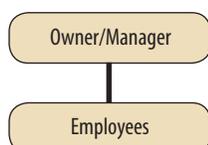
One thing the organization chart does not show is the informal organization—the informal, habitual contacts, communications, and ways of doing things that employees develop. In the case of the cashier at the roadside fruit market, the owner thought it was quicker to just issue orders to the employee rather than consult with the market manager.

Actions that do not follow the agreed on structure are a common occurrence in businesses, especially in small closely held businesses where management employees have several roles. While eliminating all such events may not be possible, developing a formal organizational structure and resisting the temptation to violate the organizational structure can help the business and family operate more smoothly.

### Simple Organization Structure

A common structure used in small entrepreneurial businesses is a structure that identifies two groups, management and workers (Figure 1). Decision making is usually highly centralized, with the owner-manager making all the important

Figure 1. Simple Organization Structure



decisions and being involved in every detail and phase of the business. Workers usually have little decision-making authority, and the owner-manager supervises the activities of every employee. Managers and workers tend to be generalists and jacks-of-all trades.

This organizational structure provides the business flexibility and dynamism. Decisions can be made quickly. When the owner-manager decides that a change is needed, he or she can communicate this decision directly to the workers.

### Functional Organization Structure

As the business grows, oversight becomes too large a task for only one person. The owner-manager needs to delegate some responsibilities and authority to other individuals. As responsibilities are delegated, how should they be organized? One approach is to organize activities around common business functions. This approach is illustrated in Figure 2. In this situation, someone specializes in production or operational aspects of the business, another person specializes in marketing, and a third is responsible for the financial aspects of the business. Finally, someone is responsible for being the general manager.

Figure 2. Functional Organization Structure



With this type of structure, managers are able to specialize and often will become more efficient at performing their duties. This structure reduces duplication of managerial effort. And it allows the general manager to concentrate on overseeing the entire business, develop and maintain important relationships with suppliers and customers, and establish an overall strategy for the business.

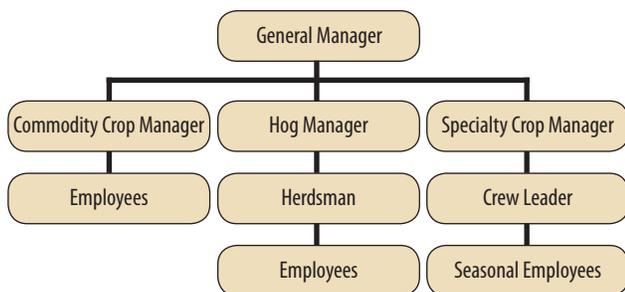
Although this structure has advantages, there can be disadvantages. While managers in the various areas can develop expertise in their functional area of responsibility, they may lose sight of how the various parts fit into a whole. It is also easy to fall into the trap of thinking that the responsibility for overall business performance rests with one person, the general manager.

## Enterprise or Product Organization Structure

A third common organizational structure is illustrated in Figure 3. This structure is organized around the enterprises or products produced by the business. In the Figure 3 example, the commodity crop manager would be responsible for all the activities required for producing and selling the commodity crops. The hog manager would be responsible for all the activities required for producing and selling hogs.

In this situation, each of these managers is expected to give continuous, undivided attention to the enterprise or product for which they are responsible. This means that the manager is likely to develop expertise in production methods, resource acquisition, and marketing the particular product. Because the product manager is responsible for all product aspects, some of the decision making commonly done by the top manager can be shifted to the product manager.

Figure 3. Enterprise or Product Organization Structure



A disadvantage of this organizational structure is that there is duplication of effort. Each manager is responsible for procuring the needed inputs, managing employees, and selling the products produced. This duplication can reduce efficiency. This organizational structure also has the disadvantage that the person in charge of each specific enterprise or product may not give much consideration to the business as a whole. This is the role of the general manager—making sure that the parts work together.

Because the duties of general management involve more thinking than doing, these duties often get overlooked.

## Final Comment

The organizational structure of your business is important. No two family businesses are organized alike. Keys to effective organizing include:

1. Proper planning of the organization,
2. Clear relationships among the people in the organization,
3. Delegation of responsibility and authority, and
4. A structure that is neither too complex nor too simple.

If your business is to continue beyond the current managers, one responsibility of the current management is to develop the next generation of managers. In this situation, the organizational structure needs to be one that assists in the development of these new managers.

What is the current organizational structure of your business? Sketch out the current reporting relationships in your business. Draw boxes for each family member and employee involved in the business. Connect these boxes with lines to show to whom each person reports. Now examine the structure, and ask yourself the following questions:

- Does the organization structure follow the key organizational structure principles?
- Does anyone report to more than one person?
- Is it clear to everyone in the business who has responsibility for what?
- Will this organizational structure help accomplish your business vision?
- Does the organizational structure aid in training the new generation of management?

If you think changes are needed in the organizational structure, sketch out a new organizational structure. Keep in mind the key organizational structure principles as you develop your new structure.

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