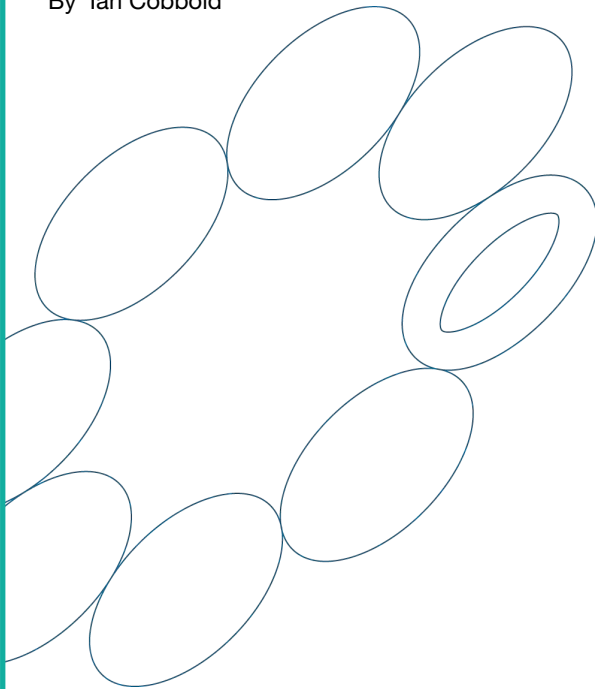


# Implementing the Balanced Scorecard – lessons and insights from a financial services firm

## Balanced Scorecard Case Study – Arran Ltd

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# Arran Ltd.

## Introduction

**NB: The identity of the organisation examined in this case study has been disguised**

Arran Ltd. is a multi-divisional retail financial services firm based in UK.

The Balanced Scorecard concept was first introduced to Arran Ltd. in the mid 1990's by the General Manager of the Retail Division (the largest division in the organisation). It was initially developed as a performance measurement system for the Retail Division with the objective of providing core management information on retail branch performance.

The Balanced Scorecard design was undertaken almost entirely by in-house development teams and was supported by implementation activities that led to complementary changes in the Retail Division's operating processes. The performance measurement system was built in part around custom designed performance management software system. The design and implementation of the software system was undertaken with the help of external consultancy teams.

Successful application of Balanced Scorecard within the Retail Division prompted Arran Ltd. to consider wider use of this approach. After a time, a Corporate Balanced Scorecard and several other Divisional Balanced Scorecards were developed using the Retail Division design and systems as their basis.

Although Arran Ltd. generally believes that Balanced Scorecard has been a useful development for the company as a whole, it is clear that the Balanced Scorecards developed subsequent to that designed for the Retail Division were less successful, and over time all the Balanced Scorecards developed have become less valuable. The Balanced Scorecard system has become marginalised, and at the time this case study was prepared, only the financial perspectives of the various Balanced Scorecards developed were still being used.

The causes of the problems experienced with the Balanced Scorecards derived primarily from their inability to accommodate effectively changes in market conditions and in organisational goals. This was caused partly by inflexibility within the software solution used, and partly because the Balanced Scorecard design team had only a limited perception of the impact different types of application of Balanced Scorecard have on the design processes required for their effective development.

This case looks at these experiences and draws some conclusions concerning best practice relating to Balanced Scorecard design and implementation. It does this by considering the case from seven different viewpoints.

## Standards

Many organisations use standard measures in the design of systems of multiple Balanced Scorecards. Others prefer to use measures structured similarly to financial reporting system where the measures on subsidiary Balanced Scorecards 'add up' to give the higher-level Balanced Scorecard data. This section outlines 2GC's viewpoint and explores how Arran Ltd. approached the use of standardised measures.

### 2GC View

Use of a standardised vocabulary defining the components of a Balanced Scorecard system (e.g. what do we mean by Vision, Objectives, Measures, Initiatives etc.) is good practice. Using

a standardised design process and review cycle is also valuable, as it can support horizontal and vertical dialogue concerning organisational goals, often becoming a component of a corporate planning framework. However the adoption of 'standard content' (e.g. requiring some or all Balanced Scorecards to adopt standard measures or objectives) is less likely to be helpful, as it risks diminishing the 'local' relevance of each Balanced Scorecard to the issues of the management teams that will use them. The external imposition of elements also can reduce the sense of ownership of specific designs felt by management teams.

### **Arran Ltd. Experience**

The initial application of Balanced Scorecard was as a performance measurement tool for the Retail Division. It was primarily an operational Balanced Scorecard used for management control purposes. The selection of measures chosen was ultimately based upon the information needs of the division's senior managers, and this led to a large element of design standardisation and ensured commonality of measures across many levels within the division. Hence, although the majority of measures were viable indicators of performance, not all the measures and objectives were strategically or locally relevant; this weakness reduced the utility of the tool to individual managers.

As the design approach used Retail Division centred on the adoption of performance indicators that were already in place, many elements of the Balanced Scorecards introduced were already regularly reviewed as standard performance indicators by staff. This helped ensure the acceptance of the Balanced Scorecards, and was helped by the continuity of activity being monitored across the whole retail division. In due course, Balanced Scorecards were introduced across the Retail Division from the top all the way through the organisational structure to branch and even individual level.

Although the use of standardised elements on the Retail Balanced Scorecard proved useful to Arran, for example by promoting design consistency, the system also proved very rigid. The further down the organisation the measures adopted became less relevant. Measures relevant at a regional level appear not to have translated very well into meaningful objectives for individual employees. A more flexible design with local relevance may have worked better in this respect, but this would have sacrificed some standard elements the retail division management were looking to see used, and made the development process more complicated.

## **Transparency**

Organisations typically use measurement systems to control the business at either a strategic or an operational level. This section considers why Balanced Scorecards were developed by Arran Ltd. and how they used.

### **2GC View**

Balanced Scorecards can be used to monitor and control the business for one of two purposes - to communicate and monitor delivery of strategic goals or to micro manage and enforce compliance in operational processes. These two types of control are generally referred to as Strategic Control and Management Control respectively. Balanced Scorecard can be used as an effective tool to monitor and control either strategic plans or operational performance; however these applications are different, and require different design approaches. When introducing Balanced Scorecards, organisations must first become clear about their objectives the new tool, and then use a design and design process appropriate to these objectives.

### **Arran Ltd. Experience**

The Retail Division Balanced Scorecards developed at Arran Ltd. were operational Balanced Scorecards for management control. When the use of the Balanced Scorecard was attempted at a Corporate level it was without the same degree of success. The reason the Retail Balanced

Scorecard was successful owed principally to the fact it was the right tool for the right purpose: Arran Ltd. developed these Balanced Scorecards for the purpose of gaining management information and monitoring compliance within the retail operation. In addition the design project had had the full support of the General Manager who was the driving force behind its introduction. The Corporate and other Divisional Balanced Scorecards developed subsequently were less successful as they drew heavily from the design and design approach developed for the Retail Division – in part due to the requirement to re-use the electronic reporting system developed for Retail Division elsewhere within the organisation. The Corporate and other Divisional management teams had a less operational focus than that for Retail Division, and Arran Ltd. would have benefited from using an alternative design method for the Corporate and Divisional Balanced Scorecards that more clearly reflected their role as a strategic rather than operational management tools.

## Simplification

Some organisations implement Balanced Scorecard as an add-on to existing systems as opposed to using it at the centre of a strategic management system. In Simplification we examine how Arran Ltd. used their Balanced Scorecards and whether they simplified the whole management system or added to existing measurement practices.

### 2GC View

Taking a holistic viewpoint it is important that organisations avoid having simply ‘more information to review’ and ensure they have ‘right information to review.’ Balanced Scorecard when used as a strategic control system is designed to improve focus on what is important in order to achieve long-term goals. This increases clarity and reduces ambiguity - not more information, just relevant information. An effective strategic control system will not make existing performance measurement tools redundant, rather it will help to align all systems in support of the same goals and perhaps refine their content.

### Arran Ltd. Experience

If an organisation is using Balanced Scorecard as a performance measurement and management tool it is likely that there will be conflict or overlap with existing systems. In the case of Arran Ltd, Balanced Scorecard was chosen as the preferred performance management tool because it was recognised that the Retail Division of Arran Ltd. needed ‘better sources of management and performance information’ and ‘better ways of rewarding management performance.’ It was felt that the Balanced Scorecard approach offered a more clearly organised methodology to presenting an array of performance measures including the traditional financial elements of control. It was applied in a similar way in other divisions of the firm, but this focus on operational issues did not facilitate significant simplification of the management processes used by the firm outside of the operational domain. Arran Ltd. therefore used Balanced Scorecard as the dominant management system, adding to and tying together existing systems rather than trying to run two sets of management control systems in parallel.

## Management Information for the centre

One of the goals for any management system is to provide decision makers with correct, relevant and timely data to aid them in the process of making decisions about managing the business. The type of information will depend upon what the organisation is trying to manage.

### 2GC View

The type of management information required by the centre builds on the communication vs.

compliance discussion from the Transparency section. What does the centre need to know to achieve overall goals as opposed to what they would like to know in order to intervene and micro manage? In 2GC's experience a good approach at the top-level is to use a strategic control system (such as the Balanced Scorecard) as contracting tool between management teams rather than a management control system to micro-manage.

Too much intervention and top-management participation in the SBU decision-making process is more likely to stifle it than help it along. It is important that the central departments or board communicate clearly what they are trying to achieve at the central level; the 'centre' discusses and agrees with each Department/SBU what they can offer to help achieve the goals; and that the 'centre' follows up through constructive dialogue whether or not they are getting the help they were promised and whether it is still relevant.

### **Arran Ltd. Experience**

The Retail Division of Arran Ltd. required a performance measurement system that would deliver an ability to control the business at an operational level. In order to achieve this they used Balanced Scorecard to monitor their operation from the divisional level all the way down to operators within each branch. The whole system was controlled by software. Each employee's individual Balanced Scorecard linked to the branch and subsequently back to the top level Retail Division Balanced Scorecard. This system worked effectively for a number of years and proved a highly successful way of monitoring the business. The biggest drawback however was the inflexibility of the Balanced Scorecard system used by Arran. The system design and its use procedures limited Arran's ability to change elements of the Balanced Scorecard designs and their associated management processes. The heavy constraint meant that they 'could only change the system once maybe twice in a year', and was in part driven by characteristics of the software system used to report Balanced Scorecard data. The system was eventually changed when the software became too outdated being almost 5 years behind the standard. At this point, Arran Ltd. ceased using the Balanced Scorecard, although the best practice Balanced Scorecard had brought, such as the organisational capabilities, has still remained within the company.

## **Growth and Diversity**

Communicating strategic direction and high-level target setting are two areas where organisations sometimes experience difficulty and where Balanced Scorecard can be employed to good effect. This is especially true if it is used for strategic control purposes. The Growth and Diversity section explores how Arran Ltd. approached these areas.

### **2GC View**

High-level target setting and strategic communication should be based on ongoing interactive dialogue between management levels and support functions, as opposed to instructions and directives. One cause of difficulty however, especially regarding target setting, is how to tackle and capture the rapid pace of change in the external environment in relation to target setting and strategic choices. Using Balanced Scorecard correctly can help this. Effective design coupled with best practice methods of use allows Balanced Scorecard to support what academics call double loop learning<sup>2</sup>, building on inclusion of operational insights and market knowledge from the whole organisation.

<sup>1</sup> Double loop in this context is a feedback mechanism. Double loop feedback is where a simple feedback mechanism such as a process control exists in conjunction with a more sophisticated feedback mechanism. This feedback loop serves to analyse the outcome and the process of the first loop.

<sup>2</sup> "Double Loop Learning in Organizations", Argyris, C. (1977) Harvard Business Review, 55 (5), pp 115 - 125

## Arran Ltd. Experience

Arran Ltd. did not really use the Balanced Scorecard to support communication or target setting, only really applying the Balanced Scorecard as a mechanism with which to organise and collect performance measurement data in the Retail Division. In attempting to use the Balanced Scorecard in a similar way at a Corporate level, Arran Ltd. met with less success; the main focus of the Corporate Balanced Scorecard being on financial rather than non-financial elements. The design process used appears to have not helped the Corporate level clearly establish and report on other elements of performance that were strategically relevant, rather it appears to have set out to report on an easy to collect, but strategically less relevant wide basket of operational activities.

## Ownership and Space

For a management system to have real impact upon the running of an organisation it is important that the information gained drives actions and change. Ownership of the management system and subsequent results are key factors in this success.

### 2GC View

Without the active endorsement and support of managers using it, it is unlikely that a management system will be able to drive required changes within an organisation. It is essential therefore to actively involve the relevant people both within the design process, but also in the design of use procedures that will ensure they can act on the information and insights provided. An important part of any Balanced Scorecard design process is to ensure that management team processes are modified to allow the management team sufficient scheduled time to discuss outputs arising from the Balanced Scorecard reports (i.e. to initiate changes in behaviour and routines connected with the strategic or performance management review process). The benefit of re-evaluating the use of management time in this way is that the management team will subsequently be able to focus more on the future through discussions about strategy, causality and strategic choices as opposed to focussing on historic reviews of financial discrepancies and “who's fault it all was”.

### Arran Ltd. Experience:

For the Retail Division's Balanced Scorecards, the General Manager senior personnel within the division championed the project. This was important, as top level management 'buy-in' is required to ensure the success of any new system. Balanced Scorecard was driven all the way through the business- 'even the cashier would have a Balanced Scorecard'. Each branch would have a Balanced Scorecard and 'the branch manager had to deliver on objectives against the four sections of the Balanced Scorecard'. However, although the branch manager had some say in the content of the Balanced Scorecard in terms of certain objectives such as recruitment, there were many standard objectives and targets imposed on them. Although this way of using Balanced Scorecard appears to move away from the idea of 'space' within which to act, Arran Ltd. were using this system at quite a low level and it was important to introduce consistency and heavy control with which to measure performance. The Balanced Scorecards at the top end of the Retail Division had more scope within which to dictate the design and content of the Balanced Scorecard.

## Software

This topic looks at the need to make software an enabler of effective strategy implementation and how to avoid technology getting in the way of change.

### 2GC View

Balanced Scorecards are often linked to three distinct types of software application: software

for data reporting, software for data analysis, and software to promote improved management process. Many commercial packages combine two or more of these in a single vended application. Thus, before committing to the choice of software system, it is imperative that an organisation becomes aware of how it hopes the software will contribute to the effectiveness of its management activity, and choose products that work accordingly. Ultimately, software solutions will not be adopted if they do not tangibly benefit the individual managers who are using Balanced Scorecard. Introduced appropriately, software can be a powerful and valuable investment for an organisation; introduced inappropriately software can undermine the potential for Balanced Scorecard to contribute to an organisations success.

### **Arran Ltd. Experience**

One common way of enabling the execution of Balanced Scorecard is through the use of software. Balanced Scorecard can be heavily reliant on data and software tools are an excellent means by which to collect, manage and present this data. However, as Arran Ltd. found, using software can present problems when technology restricts change.

Arran Ltd. relied heavily on software to deploy their Balanced Scorecard, in addition using it to support collecting, managing and presenting performance data. In the beginning, the software used in the Retail Division Balanced Scorecard provided an excellent focus for management attention – visual element even helping on a daily basis. However, as needs evolved and different types of Balanced Scorecard application were introduced into the system, the system became ‘a bureaucratic nightmare’. Arran Ltd. became increasingly constrained by the software and as a result became limited in its ability to change both the Balanced Scorecard and the way it was used. Arran Ltd. found that their technology increasingly undermined the utility of the Balanced Scorecard, and as a result both the software and the associated Balanced Scorecards became less useful in their ability to assist management teams in operating more effectively and increase the speed of detection and change.

### **Conclusion**

It is clear that, at least initially, the Balanced Scorecard systems at Arran Ltd. met the firm’s expectations and the initiative was considered as a success; the need for a more organised performance management system drove wider changes in management style and behaviour that was generally and persistently beneficial to the organisation. They wanted ‘a system that examined a number of different factors rather than focusing solely on financial data’. Arran Ltd. believed that if they used the concept it would help them in the long run.

The Balanced Scorecards used in the Retail Division delivered on these objectives. It provided a comprehensive well managed performance measurement system that enabled management to receive richer, more relevant data about the retail operation. But as the system was developed to include other components of the organisation, the appropriateness of the Retail Division design and software system was diminished – these other Balanced Scorecards needed more appropriate Balanced Scorecard designs and more flexible reporting systems.

Modern Balanced Scorecard theory has clarified many of the causes of the issues experienced by Arran Ltd., and best practice design and implementation methods are able to reflect and accommodate these causes. Potential adopters of Balanced Scorecard should, however, take care to ensure that their internal design teams (or external consultants) are able to deploy such best-practice understanding in their work. Failure to do so could compromise the long term success of a Balanced Scorecard initiative.

## Key learning points from this case are:

- Remember that there are two types of Balanced Scorecard application, each requiring a specific design and implementation methodology
- Balanced Scorecards need to be dynamic and flexible, able to accommodate the changes in organisational objectives, structure and markets that can be expected to occur during their lifetime
- Software systems have powerful benefits but if mismatched to the organisational needs can also be a cause of problems.

## About 2GC

2GC is a research led consultancy expert in addressing the strategic control and performance management issues faced by organisations in today's era of rapid change and intense competition. Central to much of 2GC's work is the application of the widely acknowledged 3<sup>rd</sup> Generation Balanced Scorecard approach to strategic implementation, strategy management and performance measurement.