

## INTRODUCTION

Global competition, information technology (IT), new knowledge, the growth of knowledge workers, and a host of other business environment changes are forcing organizations to constantly evaluate how they operate. In many cases, organizations are embracing new strategic initiatives and fundamentally changing how they operate. They are using new technologies, changing their structures, and improving work processes to respond to an increasingly demanding and global customer base. These initiatives entail fundamental change that has significant implications for the human resources and the HR function of organizations.

It is obvious that HR management practices should be an important part of the strategy of any large corporation. The annual reports of many corporations argue that their human capital and intellectual property are their most important assets. In addition, in many organizations, compensation is one of the largest costs, if not the largest. In service organizations, compensation often represents 70 to 80 percent of the total cost of doing business. With training costs and other HR management costs added to compensation costs, the HR function often has responsibilities that affect a large portion of an organization's total expenditures.

But the cost of HR is not the only or even the most important consideration for many organizations. Even when HR accounts for very little of the cost of doing business, it can have a significant impact on the organization's performance. In essence, without effective human resources, organizations are likely to have little or no revenue. Even the most automated production facilities require skilled, motivated employees to operate. Knowledge work organizations depend on employees to develop, use, and manage their most important asset, knowledge. Thus, although a company's human capital does not appear on its balance sheet, it represents an increasingly large percent of many organizations' market valuation (Lev, 2001).

### Present Role of the HR Organization

Despite compelling arguments supporting HR management as a key strategic issue in most organizations, HR executives often are not strategic partners (Lawler, 1995; Brockbank, 1999). Instead, the HR function is largely an administrative function headed by individuals whose roles are focused on cost control and administrative activities (Ulrich, 1997).

One study of large corporations and another study that focused on a cross section of firms found that the major focus of most HR functions is

on controlling costs and on a host of administrative issues (Lawler, Cohen, and Chang, 1993; BNA, 1994). Missing almost entirely from the list of HR focuses were key organizational challenges such as improving productivity, increasing quality, facilitating mergers and acquisitions, managing knowledge, and improving the ability of organizations to bring new products to market. Because the organizations likely saw these areas as important, we must ask why they were not the most important areas for the HR executives. Most likely, the executives in these firms simply felt that the HR function could not have an impact in these areas.

Studies provide some evidence that the situation is changing and that the HR function is beginning to redefine its role. One study found that 64 percent of the companies examined were transforming their HR organization (Csoka and Hackett, 1998). Our two previous studies found some change but noted that companies may be discussing change more than actually changing (Mohrman, Lawler, and McMahan, 1996; Lawler and Mohrman, 2000).

During the 1990s, a number of studies focused on the HR function (for example, the Conference Board study by Csoka and Hackett, 1998; the Human Resource Planning Society study by Eichinger and Ulrich, 1995, and one by Wright, Dyer, and Takla, 1999; the American Productivity and Quality Center study by Smith and Riley, 1994; studies by Becker and Huselid, 1998, 1999; Michigan studies by Ulrich, Brockbank, Yeung, and Lake, 1995). Among other issues, they focused on the competencies of the HR function and its executives, change efforts to revitalize the role of HR in initiatives such as Total Quality Management, and HR services and programs that will position the HR function acting as a business partner.

An interesting view of the HR function of the future is presented in the Corporate Leadership Council's book *Vision of the Future* (1995). It projects a gutting of the HR function as we know it today as many HR functions are transferred to the line, outside vendors, and high-efficiency processing centers. The HR function is expected to focus almost exclusively on business consulting and the management of the organization's core competencies. Ulrich (1997; Ulrich, Losey, and Lake, 1997) has further developed the argument that the HR function needs to be redesigned to operate as a business partner. He has also argued that organizations should develop a balanced scorecard for their HR function (Becker, Huselid, and Ulrich, 2001). Brockbank (1999) has argued that the HR function needs to become strategically proactive.

Describing the new HR role and defining the new competencies it needs are only the first steps in easing its transition to becoming a strategic

business partner. For decades, the HR function has been organized to carry out an administrative function. Changing that role will require a different mix of activities and necessitate reconfiguring the HR function to support changing business strategies and organization designs (Mohrman and Lawler, 1993). It also will require the employees in the HR function to have very different competencies than they traditionally have had (Ulrich, Brockbank, Yeung, and Lake, 1995).

It is becoming increasingly clear that IT will play a very important role in the future of the HR function (Wright and Dyer, 2000). Many of HR's administrative tasks can be done by employees and managers on a self-service basis when companies use eHR systems. The intranet-based systems that currently exist can handle HR activities such as salary administration, job posting and placement, address changes, family changes, and benefits administration—in short, virtually every administrative function that the staff of an HR function typically does. In addition, these systems are available around the clock and can be accessed from virtually anywhere.

Perhaps the greatest value of eHR systems will result from their ability to integrate and analyze organizations' HR activities. They have the potential to make HR information much more accessible so that executives can use it to guide strategy development and implementation. eHR systems also can be used to more effectively develop and allocate the human capital of organizations.

### **Forces for Change: Strategic Change and the Value-Added Organization**

The forces of global competition have sent shock waves that have left very few organizations untouched (Lawler, Mohrman, and Benson, 2001). Survival in today's world demands that organizations develop the capabilities to compete on many fronts: speed, cost, quality, service, technology, innovation, knowledge management, and new products, to name a few. Increasingly, the only sustainable competitive advantage is the ability to organize effectively, respond to change, and manage well (Mohrman, Galbraith, and Lawler, 1998). Lawler, Mohrman, and Benson's study (2001) of the Fortune 1000 provides confirmation of this, showing a significant relationship between the adoption of new management practices designed to increase the firm's capabilities and its financial performance.

A growing body of evidence indicates that HR can be a value-added function in organizations. The most important work on the relationship between firm performance and HR practices has been conducted by Becker and Huselid (1998). In their study of 740 corporations, they found that firms with the greatest intensity of HR practices that

reinforce performance had the highest market value per employee. They go on to argue that HR practices are critical in determining the market value of a corporation and that improvements in HR practices can lead to significant increases in the market value of corporations. They conclude that the best firms are able to achieve both operational and strategic excellence in their HR systems.

Staff functions in general, and HR functions in particular, are under fire in organizations because they are frequently perceived as controlling rather than adding value and as not responding to the demands for change that come from operating units. Staff functions are being asked to provide expert support to the strategic initiatives of the company and to take advantage of technology and other approaches to deliver more efficient and responsive services.

Organizational design is increasingly being recognized as a key factor that enables organizations to develop capabilities and therefore to perform in ways that produce a competitive advantage. Organizations are adopting design features with an eye to the value they contribute, that is, how they help the organization accomplish its mission effectively (Galbraith, 2002). All parts of the organization, operating units and staff functions alike, are being redesigned to deliver higher value. For staff groups, this requires developing a *business model* that defines what kind of value the staff will deliver. It needs to make clear both how it will enhance company performance and why the company should pay for it. It then requires an organizational design for the support function that fits with that business model.

Researchers have noted two important trends in organizational design (Mohrman, Galbraith, and Lawler, 1998). First, design is being recognized as more than structure; it includes elements such as management processes, rewards, people systems, information systems, and work processes. These elements must fit with the strategy and with one another for an organization to perform effectively (Waterman, 1982; Nadler, Gerstein, and Shaw, 1992).

The HR organization must think about whether the elements of its design create a high-performance HR system, one capable of delivering maximum value while consuming the least possible resources. This means concentrating on the way it organizes to deliver routine transactional services, traditional HR systems development and administration, and strategic business support. The HR staff must think about HR's own structure, customer linkages, competency development, management processes, rewards, and use of IT to ensure that they optimally deploy their scarce resources to deliver value. In addition to making sure the HR function is optimally designed, HR may also add value by helping design the total organization and its business units.

Second, organizational designs are being acknowledged to involve complex trade-offs and contingencies, and that as a result one design does not fit all organizations. New business models are emerging, and many new approaches and organizational forms are springing up to deal with the complex requirements that organizations must address (Mohrman, Galbraith, and Lawler, 1998). These include complex partnerships, globally integrated firms, customer-focused designs, and network organizations. Furthermore, multibusiness corporations are recognizing that different businesses exist in different markets and face varying requirements. Consequently, there is increasing variation in organizational design within multibusiness corporations and between businesses (Galbraith, 2002). This means that one type of HR function does not fit all situations. Different organizational forms require different kinds of HR contributions and thus different HR designs and systems.

### **Designing the HR Function**

Organizational design decisions must be made in four key areas for the HR function as well as for organizations as a whole:

- Which functions should be centralized and leveraged, and which should be decentralized in order to provide focus on the unique needs of different parts of the organization? Organizations are combining centralization and decentralization: trying to be big (coordinated) in functions such as purchasing when there is an advantage to being big and trying to be small (decentralized and flexible) in functions such as new product development when there are advantages to being small and agile.
- Which functions should be performed in-house and which should be outsourced? Companies are outsourcing when they can purchase high-quality services and products more inexpensively or reliably than they can generate them internally (Arthur Andersen and Economist Intelligence Unit, 1995).
- Which functions should be hierarchically controlled, and which should be integrated and controlled laterally? In some areas, organizations function best laterally, integrating and creating synergies across various parts of the organization, creating cross-functional units to carry out entire processes, and collaborating with suppliers and customers (Mohrman, Cohen, and Mohrman, 1995). Organizations are searching for ways to leverage across business units while setting up organizational and management approaches to allow the optimal levels of flexibility and control to various business units.
- Which processes should be IT based? Many organizations have gone through process reengineering (Hammer and Champy, 1993) to re-design and simplify processes, eliminate processes that do not add

value, and take maximum advantage of automation capabilities. They are rapidly adopting enterprise resource planning (ERP), Web-based, and e-commerce IT to speed up their operations, reduce costs, and better integrate their activities.

Traditionally, HR and many other staff groups such as IT have been organized hierarchically and have seen their mission as designing, administering, and enforcing adherence to HR policies and systems. They have been seen as expensive: a necessary evil consuming resources disproportionate to the value that they add to the company. Among the changes in structure and process that are being advocated for staff functions such as HR are the following (Lawler and Galbraith, 1993; Mohrman, Galbraith, Lawler, and Associates, 1998):

- Decentralizing business support to operating units in order to increase responsiveness
- Contracting with business units for the services that will be delivered and perhaps even requiring services to be self-funding as a way of ensuring that businesses get only the services they are willing to pay for and that they see as contributing to business performance
- Finding the most efficient way to deliver processing and transactional services, such as creating efficient central services and/or contracting out centralized processing units
- Using IT to make processes more efficient and/or to deliver increased value
- Participating in cross-unit teams in order to deliver integrated services, partner with customers to increase line ownership over HR systems, and bring the HR perspective to cross-functional team activities
- Creating shared centers of excellence that provide expert services often in a consulting capacity to the businesses
- Increasing the rotation of people within various staff functions and between staff and line, making for fewer lifelong careers within a narrow staff function, in order to broaden the perspectives of HR staff professionals and their awareness of business issues, as well as to increase depth of understanding of HR issues among line management

### **Future Role of the HR Organization**

The future of the HR function in organizations is very uncertain. On the one hand, if current trends continue, it could end up being largely an administrative function that manages an IT-based HR system. Alternatively, it could become a driver of organizational effectiveness and business strategy. This opportunity exists now because many of the key determinants of competitive advantage depend on effective human

capital management (Jackson, Hitt, and DeNisi, 2003). More than ever before, the effectiveness of organizations depends on their ability to address issues such as knowledge management, change management, and capability building, all of which could fall into the domain of the HR function. The unanswered question at this point is whether they will rise to the occasion.

In order to increase their contribution to organizational effectiveness in the future, HR professionals must rethink their function's structure, services, and programs to address how it can add value in today's economy with its new organizational forms and business strategies. HR faces a formidable challenge just in helping organizations deal with the human issues that are raised by large-scale strategic change. To face these challenges effectively, HR has to focus on how it can add value and how it is organized; it must improve its competencies and in some areas develop new ones.

A number of studies have addressed the new competencies required as the HR function strives to be a business partner in this changing environment (for example, Smith and Riley, 1994; Csoka, 1995; Eichinger and Ulrich, 1995; Ulrich, 1997; Csoka and Hackett, 1998) and to align with the business. Identifying these competencies is only the first step. It needs to be followed by organizing the HR function to develop these competencies and to provide services in a manner that adds value as organizations change their overall architecture and strategy.

To develop, the HR function must get out of the control and audit role and take on a management and development role. Lawler (1995) develops this line of thought further by arguing that the HR management approach (Figure I-1) does not go far enough in meeting business needs. He argues that the HR function should take a business partner approach (Figure I-2).

The business partner approach emphasizes that the role of the HR function involves developing systems and practices to ensure that the company's employees have the needed competencies and are motivated to perform effectively. HR has a seat at the table when business issues are discussed, and it brings an HR perspective to these discussions. When it comes to designing HR systems and practices, the line organization is involved in the process so that they own the systems. HR relies on the line to effectively implement many of the HR practices; HR measures the effectiveness of these practices and focuses on process improvements.

The business partner approach clearly positions the HR function as a value-added part of an organization. In this approach, the HR function contributes to business performance by effectively managing the most important capital of most organizations, their human capital. But even

AIMS	Business orientation. Services provided expressed as outputs or products. Voice of the customer.
PROCESS	Build performance-management capabilities. Develop managers: link competencies to job requirements and career development. Plan for succession. Enhance organizational change capabilities. Build an organizationwide HR network.
PLANNING	HR (and all other functions) inspect business plans; inputs from HR may be inserted in the planning process.
<i>Source: Based on Evans (1994).</i>	

*Figure I-1. HR Management*

AIMS	Line management owns human resources as a part of its role. HR is an integral member of management teams. Culture of the firm evolves to fit with strategy and vision.
PROCESS	Organize HR flexibly around the work to be done (programs and projects, outsourcing). Focus on the development of people and organizations (road maps, teams, organizational design). Leverage competencies, manage learning linkages; build organizational work redesign capabilities. Develop leadership.
PLANNING	An integral component of strategic and business planning by the management team.
<i>Source: Based on Evans (1994).</i>	

*Figure I-2. Business Partner*

this may not be the approach that leads to the HR function adding the most value it can. By becoming a strategic partner (see Figure I-3), the potential exists for the HR function to add more value.

When HR is a strategic partner, its role includes helping the organization develop its strategy, as well as transform and develop itself. In the knowledge economy, a firm's strategy is closely linked to its human tal-

AIMS	HR is a major influence on business strategy. HR systems drive business performance.
PROCESS	Self-service for transactional work. Transactional work outsourced. Knowledge management. Focus on organization development. Change management. Human resource processes tied to business strategies.
PLANNING	HR is a key contributor to strategic planning and change management.

*Figure I-3. Strategic Partner*

ent. An HR function that is positioned and designed as a strategic partner participates in both strategy formulation and implementation because expertise in attracting, retaining, developing, deploying, and motivating human capital is critical to both. Ideally, the HR function is knowledgeable about the business and expert in organizational and work design issues, so it can help the company develop needed organizational capabilities and change rapidly as new opportunities become available.

In order for HR to be a strategic partner, HR executives need an expert understanding of business strategy, organizational design, change management, and the integration of HR practices and strategies to support organizational designs and strategies. They need to bring to the table a perspective that is often missing in discussions of business strategy and change: knowledge about the human capital factors and organizational change that are critical in determining whether a strategy can be implemented. This is a particularly important perspective given that many more strategies fail because of implementation problems rather than conceptual flaws.

### **Focus of Study**

There has been a great deal of rhetoric about change in the HR function. A recent report from the Human Resource Planning Society (Wright, Dyer, and Takla, 1999) makes the point that a consensus now exists about what the HR organization should become but that the function has been slow to develop the capabilities to execute that vision. The overarching focus of this study is on how HR organizations are changing in response to the strategic and organizational initiatives that businesses are undertaking. The present study examines the extent to which

the design and activities of the HR function are actually changing by comparing data from 1995, 1998, and 2001. We examine the prevalence of the practices that we earlier said represent the new directions that HR organizations should take to fit with the strategic changes that are occurring in the broader organizations they serve. We also examine whether these changes are uniform across organizations and whether they characterize some kinds of companies more than others. Finally, we examine the impact of changes in the HR function on its effectiveness, as seen from within the function. This gives us a sense of the developing business models and belief system within the HR function about what constitutes effective HR practice (its value proposition), whether fully in place or not.

This study focuses in depth on eight areas:

1. *The HR Role and Activities.* Because of change in the business environment, it is reasonable to expect that the HR function may have changed the amount of emphasis it places on a variety of HR roles and activities. A major focus of this study is on how much the HR function is becoming a strategic partner and on what organization designs and HR practices are associated with this. Of particular concern is whether increased attention to strategic services, such as organization design and development, affect the perceived effectiveness of the HR function. The study will also focus on measuring how much change has occurred in the emphasis on traditional HR functions such as HR planning, compensation, recruitment, selection, and benefits administration.
2. *The Design of the HR Function.* We will examine whether changes have occurred in the way the HR function is organized in order to increase the value that it delivers.
3. *Shared Services Units.* Because of its linchpin role in the balance between efficiency and leverage and customer-focused support, we focus extensively on the adoption of shared services and centers of excellence. Companies create these units in order to gain economies of scale and improve expertise. These approaches may be particularly effective when a company has multiple business units; it can gain economies of scale and has the potential to gain in expertise by having parts of the HR function that serve the entire corporation. Key issues that we study involve what functions are best put into shared services units and, of course, how effective the shared services units are.
4. *Outsourcing.* Another increasingly popular way to deliver HR services and gain HR expertise is outsourcing. It is one way to deal with changes in the demand for HR services as well as a way to control costs. Thus, this study focuses both on how common outsourcing is

and the problems that it produces. Clearly, managing contractors is sometimes difficult; thus, it is also important to know how effectively HR deals with vendors.

5. *IT.* eHR has the potential to radically change the way HR services are delivered and managed. Thus, the present study examines how companies are using IT in their HR functions. It looks in detail at how computer systems are being used and at how effective they are with respect to such activities as salary planning, performance management, and new-hire orientation. It also focuses on how eHR systems are developed and how effective organizations consider their eHR systems to be in positively influencing employee satisfaction and loyalty, business effectiveness, and the analysis of strategic information.
6. *Talent Strategy.* Numerous books and articles have highlighted the fact that organizations are increasingly competing for human capital. They also, of course, need to effectively manage the talent. The present study focuses on the approaches that are involved in company's talent strategies. One particular focus is on whether organizations have singled out employees with high potential and whether they get special treatment.
7. *HR Skills.* A critical issue in the effectiveness of any HR function is the skills of the HR professionals and staff. Thus, the present study asks about how satisfied organizations are with their HR professionals' skills in a variety of areas. It particularly focuses on those skills that HR professionals need in order to serve as true business and strategic partners.
8. *HR Effectiveness.* The effectiveness of the HR function in a number of areas is a critical issue. Thus, any study of the HR function needs to gather data about how effectively the HR function is currently performing. Particular emphasis in the present study is on the HR function's effectiveness in doing many of the new activities that are required in order for HR to be a business and strategic partner. These include managing change, contributing to strategy, managing the outsourcing of HR, and operating shared services units. Perhaps the crucial issue with respect to effectiveness concerns what practices lead to an effective HR organization. Thus, the present study will determine what HR structures, approaches, and practices are associated with the effectiveness of the HR organization.

Overall, the focus of the present study is on how the HR function is changing in response to changes in the business environment. We are uniquely able to look at and measure the degree of change because of the longitudinal nature of the study.