CHAPTER 1

ORGANISATIONS

1. Organisations

Introduction

Chances are, you used Google today. The search engine is part of our everyday lives. But have you ever wondered who runs this organisation? How do they make decisions? To whom are they accountable?

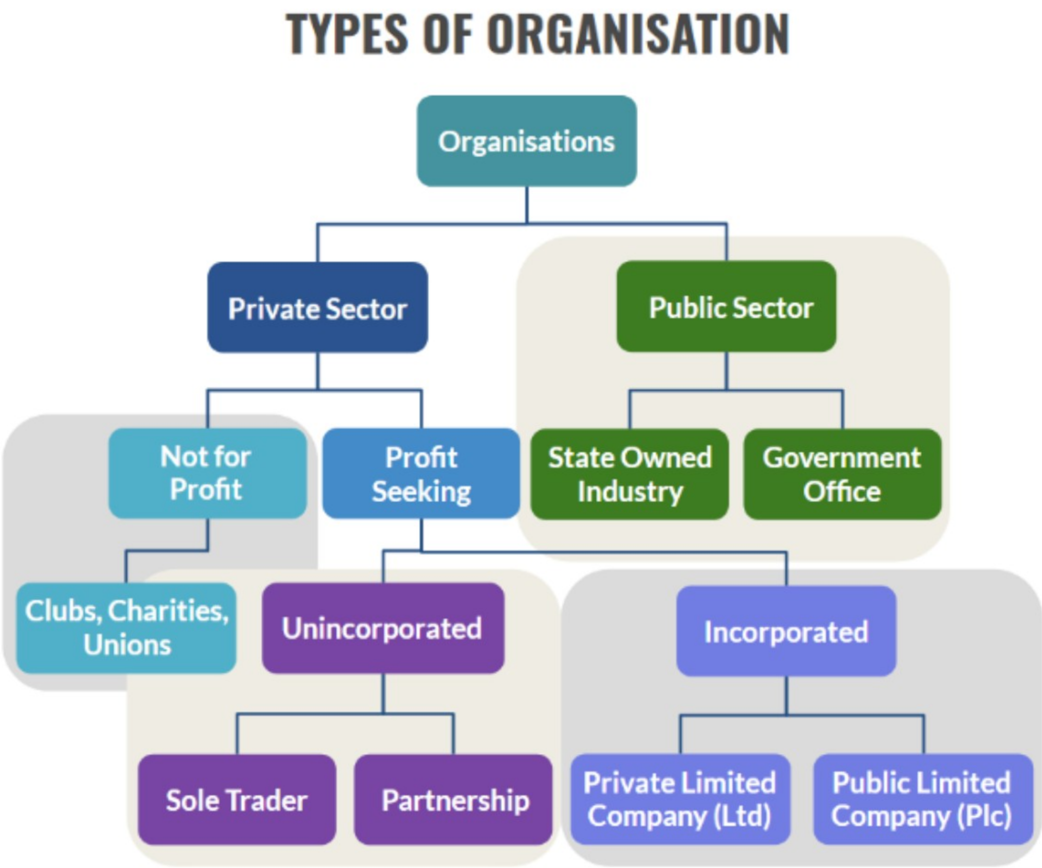
Well, Google is just an organisation of people, like any other. **An organisation is a group of people that are organised and managed in a way that aims to follow a unified goal or need**. All types of businesses follow a structure that is controlled by management, who determine how the business performs in particular activities and the key roles and responsibilities of its members. For example, Google is part of a bigger company called Alphabet, each division with its own unique focus. Within the Google division they will have a group of people organised together to create their goal to 'organise the world's information'.

What about smaller companies, though? For example, if Fred starts freelancing as a painter and decorator, he will have to do everything, from painting to marketing and to accounting. If he then takes on an assistant to manage his social media pages, he will have an organisation. The more people Fred takes on, the more and things he will need to organise! He may even need to change the structure and legal status of his organisation to manage and account for its growth and activities.

This chapter works as an introduction to organisations and how they work.

2. Types of organisation

We said that Google was an organisation like any other. But actually, not all organisations are created equally. **The economy of a country can generally be split into two sectors: the private sector and the public sector**. Within these sectors, **organisations can be profit-seeking or not for profit**.



Profit-seeking organisations

As the name suggests, **the primary objective of profit-seeking organisations is to maximise returns for owners or shareholders**. For example, Saudi Aramco is a profit-seeking organisation in the public sector. It is a state-owned oil company in Saudi Arabia which is one of the most profitable companies in the world.

Profit-seeking organisations can be further **split into two main groups; unincorporated and incorporated**.

Unincorporated organisations

In unincorporated organisations, the business owners and the business itself hold the same legal identity. For example, if Fred Smith becomes self-employed as a painter and decorator, he may decide not to incorporate and simply trade solely as Fred Smith. It certainly keeps things simple!

But there's a catch. Not incorporating means that the **owners are held personally responsible for the debts** the business activity may incur. Therefore, they are considered to have **unlimited liability for the business's debts.**

The two main types of ownership in this category are:

- **Sole trader** – One sole owner of the business (wholly liable for debts)

- **Partnership** – A collection of owners working together (jointly liable for debts)

  Imagine that Fred and some friends pooled together their savings and took out a loan at a bank, in order to start an unincorporated partnership. If things go badly for them (which hopefully they won't!), then they would not only lose their combined savings, but would also have to repay any debts to lenders (such as the bank and any suppliers). This is what we mean by an unlimited liability.

There are other approaches available, to help Fred, and his friends, avoid this sticky end – they can become incorporated...

Incorporated organisations

To protect their personal finances, the business owners may decide to create a separate legal identity for their business. This means that the owners are not held personally responsible for the debts the company may incur. Therefore, they are considered to have **limited liability for the business's debts**.

The two main types of ownership in this category are:

- **Private limited companies** (**Ltd**) – In a private limited company, **shares cannot be issued to the public**. These are often smaller companies, such as a market town retailer. However, larger companies looking to retain a high degree of control sometimes stay private. By choosing to stay private, they don't have to report to a large number of shareholders. They still have to publish their finances to companies, though. For example, Walkers Snack Foods Ltd or Virgin Group Ltd.

- **Public limited companies** (**PLC**) – In a PLC, **shares can be issued to the public.** Usually, larger companies go public when they wish to increase funding for business ventures through a public share offering, for example, Tesco Plc and British Airways Plc. However, the **owners risk losing control by selling stakes to the public**. **They must also comply with additional regulations** when trading publicly.

Example

So, looking back at our last example, if Fred and his friends had set up an incorporated business instead of an unincorporated partnership, they would still lose their initial investment (their pooled savings), but they would not be personally responsible for repaying the company's debts. Now, that is an important difference in the business world and Fred's family are more secure, knowing they can still pay the mortgage even if the company fails!

Cooperatives

A cooperative is an organisation which is owned and controlled by the members, rather than shareholders. Those members may be staff such as with the John Lewis Partnership, or customers as with The Cooperative Group. While profits are important, the welfare of members is also a key goal.

Not-for-profit organisations

Now, on the other side of the fence, we have not-for-profit organisations (or non-profits). As the name suggests, **non-profits do not set out to make a profit** for their owners.

Like profit-seeking companies, **non-profits aim to operate efficiently and to be cost-effective.** Not-for-profit organisations include trade unions, charities, clubs, societies and educational establishments. Not-for-profit organisations can exist in both the public and private sector:

Public sector

Public sector not for profit organisations are **owned by the state and are responsible to the government** for their business activities. These organisations can be **in the form of a state-owned industry**, **which can also be profit seeking as we saw earlier with Saudi Aramco**, **or a government run department**. For example, the NHS in the UK and the Peace Corps in the US.

Private sector – Non-Governmental organisations (NGOs)

Private sector not-for-profit organisations have a similar structure to profit-seeking companies in that **they are owned by investors and responsible to the shareholders/owners**. **However**, **their goals and objectives do not focus on profit maximisation**. Instead, they focus on other goals, such as ethical standards and service delivery. For example, Oxfam and The Make-A-Wish Foundation. These organisations are called Non-Governmental Organisations or NGOs.

3. Stakeholders

Do you have shares in Google? Well, you might have! But even if you do not stand to gain financially from Google's business activities, you still have an interest, or a stake, in how they do. This is because you use the service every day. If Google went out of business, it would make your life more difficult. This makes you, as a customer, a stakeholder in Google.

What are stakeholders?

Stakeholders are **any parties that can affect**, **or be affected by, an organisation's strategy and policies**.

Let's imagine a publicly funded school, who would the stakeholders be? Well, we would probably quickly come up with a list that included:

- Teachers
- Pupils
- The pupils' parents and families
- The administrative staff
- The local education authority

All these groups can clearly affect or be affected by the school's strategy and policies.

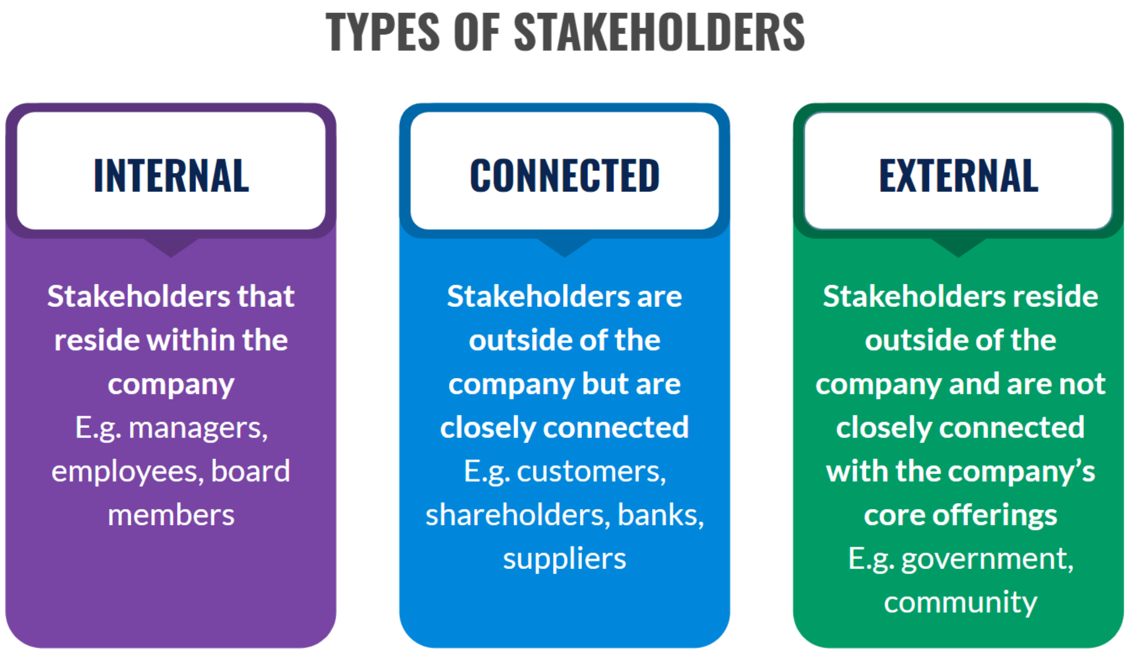
So would this be it? No! It would also include:

- Teachers' unions – Who could organise a strike if they didn't agree with the school's policies
- Local businesses – Who may offer work experience or internships to pupils
- The wider community – House prices may be affected by a school with a great reputation, or a bad one!
- The local council – Who will run other services for pupils that will require collaboration with the school
- Other local schools – Who may be competitors, trying to achieve better results to attract more pupils
- Local media – Who will report, favourably or unfavourably on incidents at the school
- Exam boards – schools must hold exams based on the rules of the exam boards they choose to use
- The government – Who decide how much of the national budget goes towards education

So there we go, a list of lots more stakeholders that you may not have immediately first thought of. However, this is still not an exhaustive list and the brief examples of how they may affect/be affected by the school are also not the only ways it could happen!

Classifying stakeholders

To make informed decisions and policies regarding all the business's stakeholders, **it is crucial that an organisation classifies its stakeholders** into various groups. This can be done in a number of ways; for example, the organisation can determine whether the stakeholder is internal, external or connected.



The ICE mnemonic can be a useful way to remember these.

Stakeholders and objectives

Organisational objectives should always be considered in relation to the objectives of different stakeholders. This **ensures that a wide range of needs are considered in the objective-setting process** and balanced objectives are produced.

Bob owns a chain of cafes and is the sole director and the sole shareholder in his business, so he can just go ahead and do what he wants, right? Wrong!

For the new objective to be a success, Bob will still need to get the support of other internal stakeholders: his employees must be fully behind the plan, especially any that will go on to run the new store.

He will also need to get buy-in (this just a management term that means a commitment to a decision) from some external stakeholders. For example, his local suppliers will need to be able to scale up production to meet his increased demand. He will definitely need to get buy-in from his bank if he needs to borrow funds. He'll also want to get buy-in from his customers. Will they accept a new chain store approach from their favourite independent?

Lastly, he may need to get permission from connected stakeholders, such as local government to open in certain neighbourhoods and, depending on where he plans to open, he may need to consult with local residents and traders.

You can quickly see how an objection or obstruction from any of these stakeholders could alter Bob's plans.

What do stakeholders need?

So, we've seen that organisations have a range of stakeholders and that they have varying needs. Let's examine the most common ones:

Category	Stakeholder	Needs of stakeholder
Internal	Directors	Pay, bonus, overall performance, job security
	Employees	Pay, bonus, personal performance, job security
Connected	Shareholders	Share price growth, dividend payments
	Customers	Prices, quality, delivery times, assured supply
	Suppliers	Assured custom, high prices
	Financiers	Interest payments, ability to pay back loans
External	Government	Tax, law, wealth of nation
	Pressure groups	Environment or other ethical issues, pricing etc
	Local community	Employment, nice place to live
	Wider community	Environment, local jobs etc

Exercise

Spend some time examining who you think the stakeholders for a low-cost airline such as Ryanair would be.

As you do so, consider what those stakeholders' interests are.

Once you've finished, take a look through our list and see if there are any you missed.

Solution

Ryanair's stakeholders would include:

Stakeholder	Explanation
CEO	As of 2019 Michael O'Leary was the chief executive officer of Ryanair and also had a significant amount of shares, as a result O'Leary could both affect and be affected by Ryanair's strategy and policies.
Funders (e.g. Irish Air)	Irish Air provided a loan and equity to Ryanair in return for shares. As shareholders they would be interested in the performance of the company, which can be affected by the organisation's strategy and policies. Also, as shareholders, it will have voting rights which could shape the strategy and policies of Ryanair.
Trade Unions	Some of Ryanair's employees in certain countries, such as England and Italy, are eligible to join a union if they wish. Trade unions are able to affect the policies and strategy of Ryanair by taking strike action if they feel the strategy and policies of Ryanair are not fairly affecting their members.
Employees	Employees of any business can obviously be affected by an organisation's strategy and policies. Of course, depending on the position of the organisation they occupy, they can also affect the organisation itself.

Stakeholder	Explanation
Airports	How are airports stakeholders? Well they are really interested in the strategy and policies of Ryanair, because if Ryanair flies to them it will bring lots of revenue to the airports, both from Ryanair directly, and from their passengers.
Suppliers	Ryanair will have a multitude of different suppliers; from on-board food suppliers to the manufacturers or lessors of planes. All of them will be affected by Ryanair's strategy and policies, after all, what if Ryanair decided to use a competitor or double the number of planes they own?
Competitors	Competitors too will be affected by Ryanair's strategy and policy choices, for example, if Ryanair changed its pricing structure its low-cost competitors would have to respond and vice versa.
Customers	And lets not forget Ryanair's customers! If they chose not to use Ryanair any more they would dramatically affect Ryanair's strategies and policies! Let's imagine that Ryanair, a low-cost airline, decided to change its policy to become a more expensive airline, offering its customers more extras, that may mean it would lose its existing customer base but possibly gain a new one. This is an extreme example but it demonstrates what an important group of stakeholders customers are!

This is not an exhaustive list of all of Ryanair's stakeholders but hopefully it demonstrates the wide array of different individuals and groups that have to be considered when setting a strategy.

Stakeholder power

Power

If stakeholders are characterised as having **power it means they are able to influence and affect the organisation.**

The degree to which stakeholder needs are considered as part of the objective-setting process depends on the level of power they have to impact the organisation and its results. The needs of powerful groups will tend to be prioritised.

For example, large customers (those who can buy in large quantities, e.g. companies) have significant power; products, prices, location of production facilities and so on may be impacted by their needs. Small customers (those who buy in smaller quantities, e.g. individuals) have far less power, and less consideration will be paid to their individual needs.

So who would have the power at a school? Well the teachers in senior positions have the ability to affect the policies of the school due to their position, as do the board of governors who would decide the strategic direction of the school.

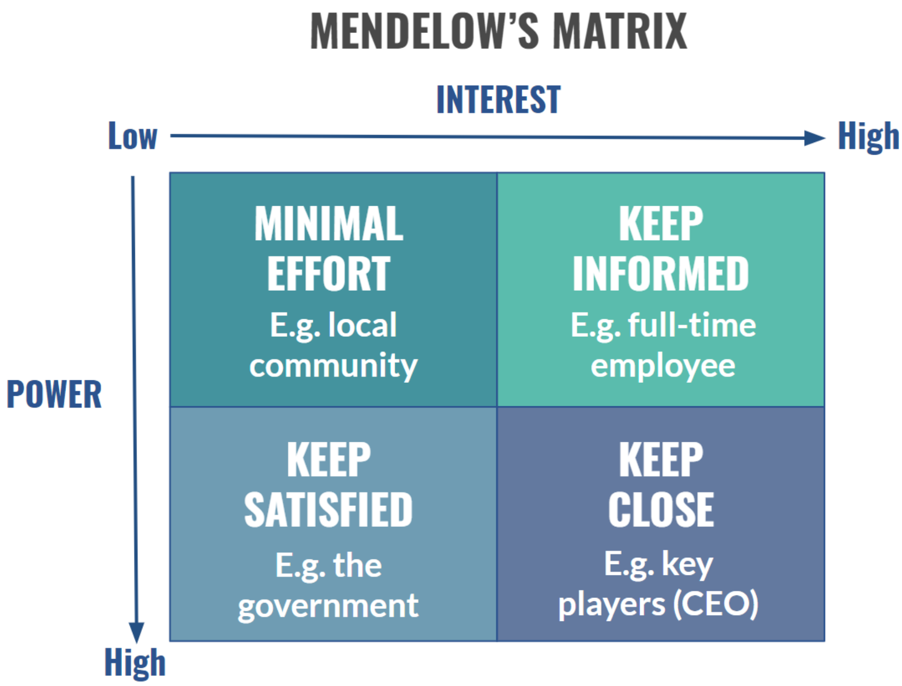
A stakeholder who wouldn’t have much power would be a dinner lady. This is because dinner ladies only work for the school on a part-time basis and their limited role means they would be unable to affect any policy or strategy changes.

4. Stakeholder mapping (Mendelow’s Matrix)

Mendelow's matrix **helps to identify the relationships that should be built with different stakeholders**. A stakeholder's position in the matrix depends on two factors:

Power: The power to influence the organisation and affect its decision-making.

Interest: The interest which the stakeholder has in the organisation. The greater the interest in the organisation, the greater the level of communication that will be required with them. Many employees have little power, but good communication of plans is important to retain their loyalty and motivation.



Each **stakeholder is categorised** depending on each factor and **then treated differently** depending on where they are:

Minimal effort

These stakeholders have a **low interest in the business and low power.**

For example, a member of the local community isn't interested in the business, its policies, procedures and long-term strategy and has no influence.

With these stakeholders, the company will **give them basic information to meet their needs but do little else**. A member of the local community might, for instance, be contacted if the company were doing building works that might affect them.

Keep informed

Stakeholders in the keep informed box have **high interest but low power**. For example, a full-time employee. They are interested in the policies, procedures and pay as that affects them day-to-day. Strategic changes that affect them are also of concern. An employee working in a factory will be very concerned with a redundancy programme or if the factory were going to close. However, ultimately an individual member of staff has little power. Should they threaten to leave, the company would probably just wave goodbye to them and employ someone else!

With these stakeholders, **the company should regularly communicate with them, particularly in the things they are interested** in. This helps retain good relationships and avoids them seeking to increase power (e.g. through staff grouping together in a union).

Keep satisfied

Stakeholders in the keep satisfied box have **high power but low interest**. For example, the government. They can impose rules, laws and taxes on the company should they wish and so have very high power, but they are not interested in most businesses most of the time.

To avoid them exercising their power, they should be kept satisfied, e.g. with the government, by abiding by the law and paying taxes on time. As they usually have little interest, only necessary information is given to them (e.g. profit information to the government to help assess the tax payable).

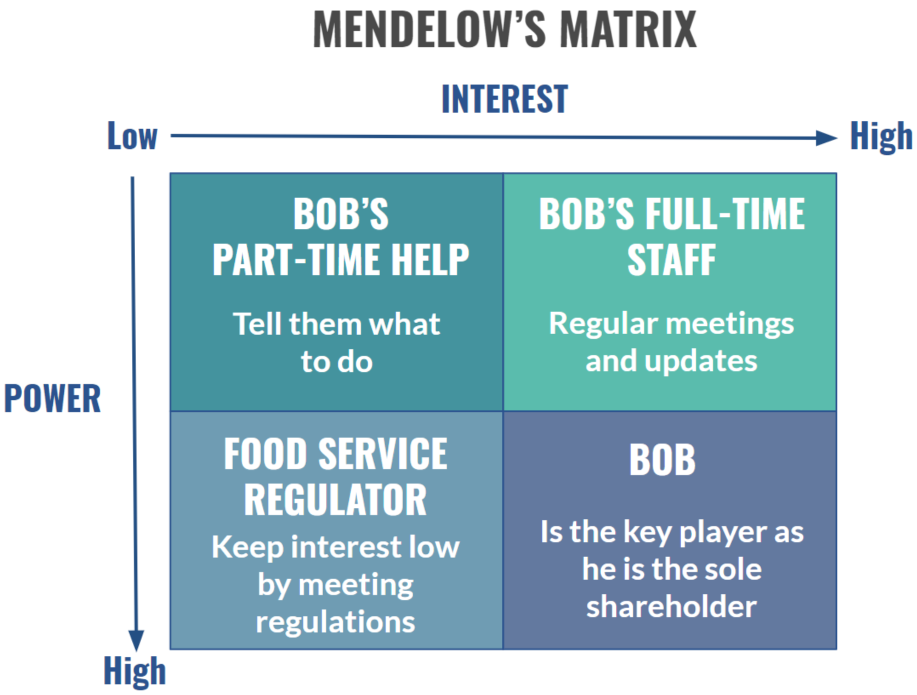
Key players (Keep Close)

Key players are both **interested in the company and have high power**. For example, the CEO who is interested in getting a good salary and can exercise power through voting in director meetings.

Key players should be kept close. **Regular communication is maintained, and their goals and objectives included as part of the strategy setting process** and business approach.

Example

For Bob's small local chain of cafes, some examples could include:



5. Stakeholder conflicts

Let's say Bob is concerned that they might be overstaffed in one of the cafes. He is proposing to make one full-time employee redundant. The employees are all outraged. They don't want to be the one who is made redundant and feel that with one less employee, the shop will be understaffed. This is a stakeholder conflict.

It is crucial that an organisation realises its **stakeholders have different sets of needs and expectations**. These needs and expectations **may result in conflict**. Therefore, **it is critical to consider varying stakeholder needs when making decisions and to resolve conflicts wherever possible**.

Cyert and March

Cyert and March proposed four ways in which a company can look to resolve stakeholder conflict:

Satisficing

This means **holding negotiations between key stakeholder groups and arriving at an acceptable compromise**. For example, Bob and the employees meet and decide to reduce all employees' hours, instead of making one of them redundant.

Sequential attention

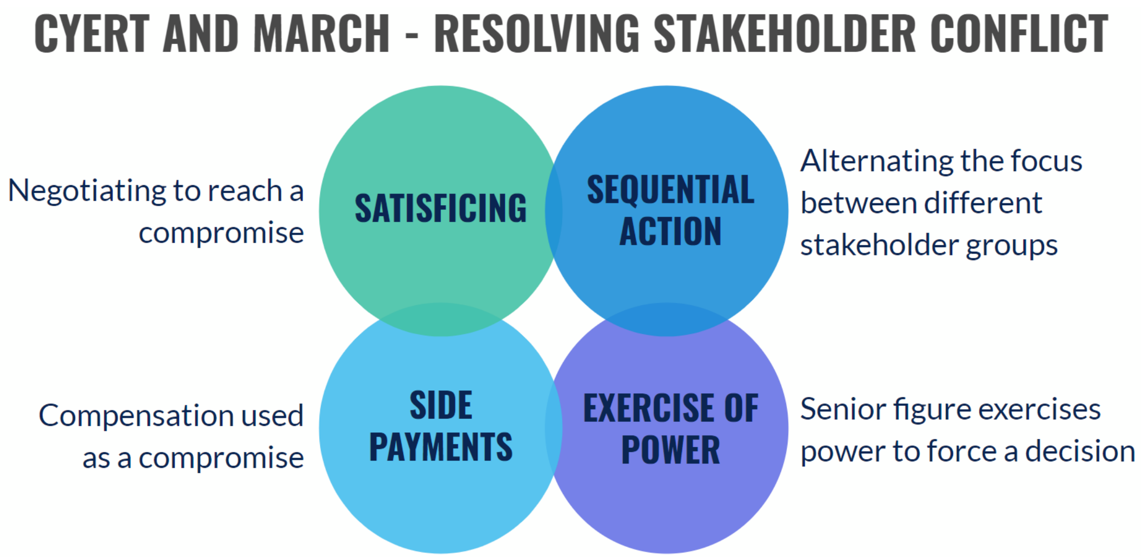
This involves **taking turns focusing on the needs of different stakeholder groups**. For example, the employee is not made redundant but the agreement is that next time redundancies need to be made, it will be from this shop. The idea is that the needs of the employees are met this time, but next time a different stakeholder's needs will be met, namely Bob.

Side payments

When a stakeholder's needs cannot be met initially, they are compensated in some way as a compromise. For example, one employee is made redundant but is given a larger than expected redundancy package.

Exercise of power

When a compromise or action cannot be agreed upon, it is resolved by **a senior figure who exercises their power to force through a decision**. For example, Bob decides that the redundancy is the best option and pushes through the decision.



Stakeholders and not-for-profit organisations

In a profit-seeking organisation, the shareholders will be the key stakeholders. However, **in a not-for-profit organisation, other stakeholders will be more important.** Due to the competing demands of a variety of stakeholders, the organisation must manage expectations and balance demands.

Stakeholders in not-for-profit companies exercise influence in the following ways:

Objectives and goals – Without the need for objectives based on profit, goals and objectives may vary depending on stakeholder influence. For example, charitable donors may require objectives based on the delivery of funds to beneficiaries rather than the money being spent on administration.

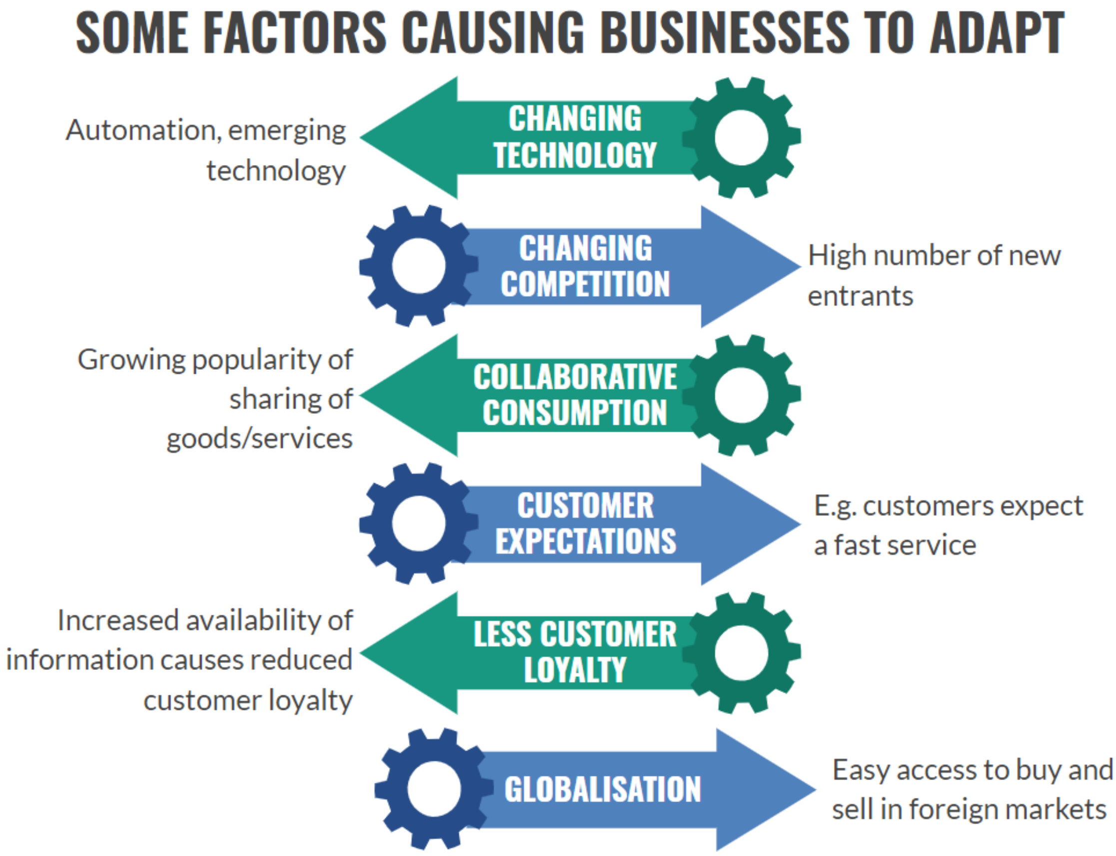
Strategies – In terms of how the company operates as a whole, again, profitability will not be a key strategy. However, there may be a focus on efficiency and effectiveness of service and also compliance with ethical standards.

Management style and practice – How employees are treated is likely to be of critical importance as many are working for minimum wage or as volunteers. There may be an impetus to manage in an open and democratic style with few levels of hierarchy.

6. Change in organisations

The **rate at which change happens in the world is accelerating**. We can see evidence of this change all around, especially in the way that **technology is becoming more integrated into our live**. Next time you're in a public place, take a look around to see just how many people are using some form of technology. It's almost guaranteed that you'll see someone on a mobile phone! Yet only 30 years ago, the Internet hadn't been invented and very few people had mobile phones or a personal computer.

We can see evidence of the increasing rate of change in business, with the number of patents filed to protect intellectual property increasing, and the average life-span of products decreasing. Change is becoming an everyday reality of an organisation, and in this increasingly volatile environment, **organisations are having to adapt the way they do business**.



Some **key factors of change which are forcing organisations to adapt are:**

- **Changing technology** – The key driver of the changes we are experiencing is thought to be the increasingly rapid rate of technological change, unparalleled in recent history. Organisations are having to adapt to emerging technologies, with capabilities that allow them to take over routine tasks, such as data entry, and carry out new tasks which have never been possible before, such as the analysis of massive data sets.

- **Changing levels of competition** – Organisations are also having to deal with rapid changes to the levels of competition, with new entrants entering the market seemingly out of nowhere or causing disruption to whole industries. For example, the ride-share company Uber quickly established and grew rapidly in cities across the world, causing massive disruption to the taxi industry.

- **Growing collaborative consumption** – This is the growing popularity of sharing of goods and services, which is causing disruption to their respective industries. A good example is Airbnb, in which owners rent out their private accommodation to others, which is causing disruption to the hotel industry. This is creating new business models which existing competitors are having to adapt to.

- **Changes to customer expectations** – A number of factors are changing what a customer expects from an organisation and its products. For example, with faster communication channels, enabled by social media and improvements in technology, consumers now expect speedier customer service and greater efficiency from an organisation. Organisations are having to adapt to ensure that they are fulfilling changing customer needs.

- **Less customer loyalty** – With greater access to information, through the development of the Internet and mobile technologies such as smartphones, combined with a more competitive market, businesses are finding that consumers are no longer loyal to a particular brand. Consumers are more likely to 'shop around', and studies have shown that over 80% of customers will research a product online before buying it.

- **Globalisation** – Economies and cultures are becoming more integrated with one another through interconnected networks, such as trade, and the spread of technology and media. It is getting easier for businesses to source supplies from other countries, and sell their products to foreign markets.

Changes to roles in the finance function

In line with how organisations are adapting to change, the roles of business professionals are evolving, and of particular interest to us in the E1 syllabus, **the roles of those working in the finance function are evolving**.

You will hear the term 'finance function' a lot in subsequent chapters, with whole chapters dedicated to it! For now, to understand this last point, you just need to know that **the finance function is the part of the organisation which controls and manages anything related to finance and so as wider changes happen to the organisation so the finance function has to change too**.