WORKFORCE ANALYTICS: A CRITICAL EVALUATION

Huh? We're Switching Back Again?

How Centralized and Decentralized HR Department Structures Influence HR Metrics

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Introduction

Many HR departments over the last decade transformed their HR structures. Economic downturns, changes in organizational strategy and increasing dissatisfaction with HR's contribution have led executives to seek more effective HR function designs that lead to more hard measures of outcomes and lower costs while increasing HR's flexibility and business focus.[1] As the business environment changes in the future, we can expect HR transformations to continue.

Another business driver for changing HR structures is the outsourcing of noncore activities, including administrative HR. Such a move for HR is intended to free up staff so that it can better contribute to strategic business initiatives. Many of these revised organizational models reflect attempts at balancing the need for centrally managing standardized HR practices with the need for locally driven responsiveness.[2]

For the past 30 years, HR departments have primarily used four organizational designs:

- **Centralized**: Strong corporate HR office that serves as a central decision-making authority that supplies HR services throughout the organization.
- **Decentralized**: Autonomous HR functions housed in separate business units (e.g., by product line or geography) that operate and make decisions mostly independent of the other units.
- **Mix of both/matrix:** A shared centralized corporate HR body combined with other relatively independent localized HR functions that benefit from both centralization and decentralization.
- **Outsourced**: HR structures that primarily use external brokers and networks to perform the HR function.[3]

Centralized HR departments typically have high economies of scale, consistent standards and control, a critical mass of HR competencies, and a focus on the organization's long-term business outlook. As organizations centralize their HR functions, shared service models and centers of expertise (formal and informal groups that provide various types of HR expertise to produce policies and decision support around staffing, compensation, diversity, etc.) help complement HR's centralization strategy. Shared service models typically use technology or outsourcing to perform standardized work while providing high-value service and results.[4] Centralized HR departments, however, are often inflexible to regional needs and have communications challenges and misunderstandings (for example, when dealing with multiple languages).[5]

With decentralized departments, business units remain in control of decisions and recognize local priorities so that they can respond quickly to internal and external client needs. Decentralized HR structures, however, suffer from lower economies of scale, higher transaction costs and variable standards of HR practices that often lead to duplicated efforts within the HR function.[6]

The vast majority of large multinational organizations have a highly matrixed business model, and therefore, alignment of the HR function also follows a matrix model.[7] A matrix HR model operates on a continuum of centralized versus decentralized services. Along with shared services, this model may also contain centers of expertise to help support specialized HR policies and decisions.[8]

This report focuses on data collected and analyzed by SHRM regarding centralized, decentralized and mix of both/matrix HR structures to better understand the influence different HR structures have on key HR metrics. Unless otherwise noted, the results we present in this report are from the 2015 SHRM Human Capital Benchmarking database of over 2,000 organizations. We analyzed the following metrics based on differences in HR structure:

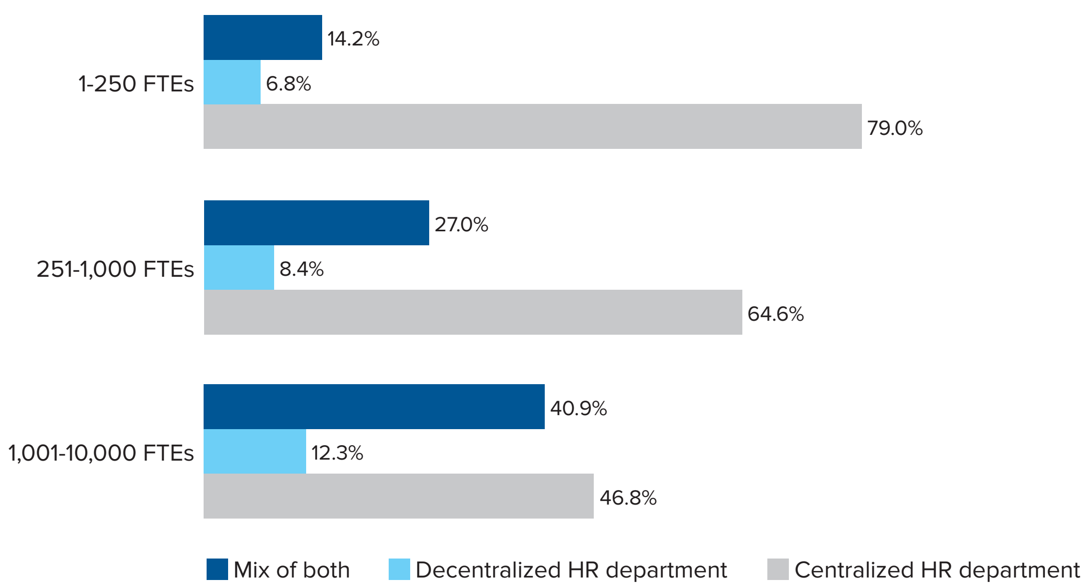
- Organization staff size.
- Organizations with employees residing outside the U.S.
- HR staff in supervisory roles.
- Annual employee turnover rate.

HR Department Structure by Organization Staff Size

Organizations use a variety of HR department structures. For all staff sizes, 70.7% of all organizations surveyed used a centralized HR structure, 20.8% used a mix of both and 8.5% had a decentralized environment. Figure 1 compares HR department structure based on organizations' staff size: small (1-250 employees), medium (251-1,000 employees) and large (1,001-10,000 employees).[9] The percentage of organizations using centralized HR structures decreases as staff sizes increase, whereas the number of organizations using a mix of both (centralized and decentralized structures) increases with staff size. The percentage of centralized HR departments decreased from 79% for small-staff-sized organizations to 64.6% and 46.8% for medium and large organizations, respectively. The percentage of HR department structures using a mix of both, however, increased from 14.2% for small organizations to 27% for medium and 40.9% for large organizations.

When organizations grow in staff size, they are more likely to have greater organizational complexity in the form of multisite locations, disparate business and product lines, and diverse recruiting and employee relations issues. Structuring HR departments to use a mix of both centralized and decentralized functions allows organizations to tailor local HR functions and/or staff to address local needs while ensuring a consistent HR strategy companywide. For example, a corporate HR department that is centralized in the U.S. may develop a corporate benefits philosophy to be applied throughout its U.S. offices. Yet, if the organization has an office in California, where state laws and benefits regulations may be significantly different from other states, the California HR function can tailor the firm's benefits philosophy to be legally compliant.

FIGURE 1. HR DEPARTMENT STRUCTURE BY ORGANIZATION STAFF SIZE



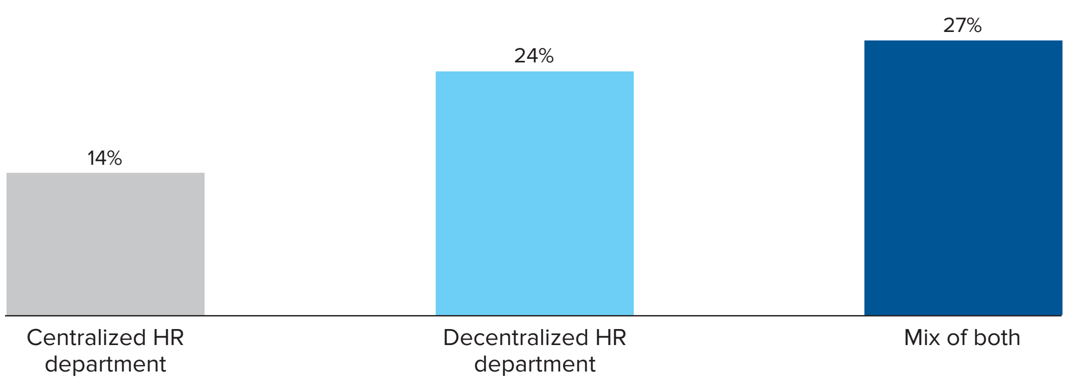
Source: Workforce Analytics: Huh? We're Switching Back Again? How Centralized and Decentralized HR Department Structures Influence HR Metrics (SHRM, 2016)

HR Department Structure in Organizations with Employees Residing Outside the U.S.

To increase sales of products and services or to reduce costs in production or service delivery, organizations often seek a presence outside of their home country. For example, results of SHRM's Human Capital Benchmarking Survey indicate that 18% of organizations have employees working outside the U.S., either local citizens or U.S. citizens working on temporary assignment.[10]

Figure 2 compares HR department structures among organizations that have employees residing outside the U.S. Mixed HR structures (27%) were the top HR structure used by organizations with employees outside the U.S. This percentage, which was statistically higher than centralized HR structures (14%),[11] suggests that having centralized HR structures may not be as effective as having a mix of both or a decentralized (24%) HR function structure. Centralized structures may not be able to provide in-country HR expertise and decision-making responsibilities to quickly resolve onsite HR issues. For example, local HR experts can operate within the employee's time zone, know local tax and benefits requirements, and be aware of local economic and employment conditions to source talent.

FIGURE 2.
HR DEPARTMENT STRUCTURE IN ORGANIZATIONS WITH EMPLOYEES RESIDING OUTSIDE THE U.S.



Source: Workforce Analytics: Huh? We're Switching Back Again? How Centralized and Decentralized HR Department Structures Influence HR Metrics (SHRM, 2016)

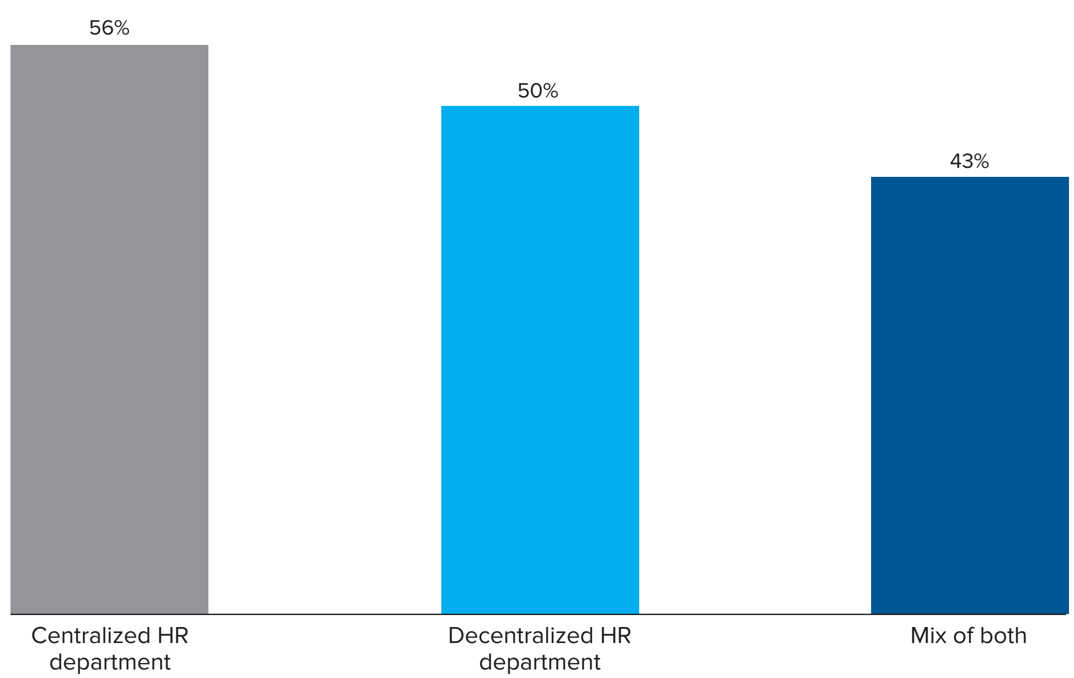
Percentage of HR Staff in Supervisory Roles, by HR Department Structure

The percentage of HR staff in supervisory roles (i.e., supervisor, manager, director or above) is calculated by taking the number of HR supervisory positions (FTEs) and dividing it by the total number of HR staff (FTEs). As organizations design their HR function, it is a useful metric to benchmark against their competition to ensure the employer has the depth of HR management to address complex HR issues. The percentage of HR staff in supervisory roles was 53% for all organizations.[12]

Centralized HR structures had a significantly higher percentage of HR staff in supervisory roles (56%) than did decentralized structures (50%) and mix of both (43%).[13] Centralized HR departments, which are often found in small organizations, may have a higher percentage of supervisory roles because organizations may initially hire supervisory talent to lead a functional area and then hire less experienced staff if more resources are required.[14] For example, an organization may first hire an experienced supervisor to develop and execute a talent acquisition strategy. As recruiting requirements increase, the centralized talent group will hire additional nonsupervisory staff, such as sourcers to create a diverse candidate pool and recruiters to work with managers to fill position openings.

If organizational growth continues with the development of new locations and diverse product lines, however, the HR department structure may change to a mix of both centralized and decentralized structures combined. This allows the organization to centralize job boards and applicant tracking expenses while deploying recruiters to local sites.

FIGURE 3. PERCENTAGE OF HR STAFF IN SUPERVISORY ROLES, BY HR DEPARTMENT STRUCTURE



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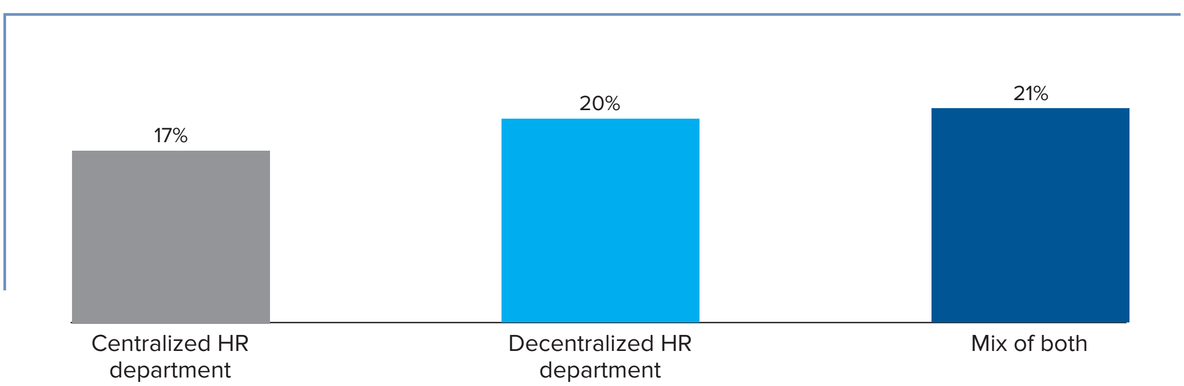
Average Annual Overall Turnover Rate, by HR Department Structure

Employee turnover is an important metric that is critical to an organization's workforce planning and talent acquisition strategy. Calculated as annual overall turnover,[15] it measures the rate at which employees enter and leave a company in a given fiscal year. The overall turnover rate includes employees who voluntarily decide to leave the organization and also employees who are terminated from the organization involuntarily. Organizations whose employees have high levels of job satisfaction typically have lower turnover. Conversely, when employees are dissatisfied, organizational turnover rate goes up. Organizations with HR structures that were a mix of centralized and decentralized (21%) had statistically higher turnover than organizations with centralized HR structures (17%).[16] Decentralized HR departments, however, reported annual turnover of 20%.

Centralized HR structures, which are more prevalent in small organizations, may have lower turnover than a mix of both because annual turnover for small organizations is also low. Conversely, a mix of both HR structures is found in large organizations, which have higher turnover than small organizations. This suggests that turnover varies by staff size and HR structure. Large organizations have more complexity and therefore greater risk for lack of communication that can frustrate employees and foster turnover. In addition, employees in small organizations may face less bureaucracy or levels of approval when accomplishing goals, leading to greater satisfaction and engagement. Finally, turnover may be higher in organizations with a mix of both HR structures because employees in specific business units or local geographical sites may feel centralized HR policies don't support the business realities they face at the local level.

FIGURE 4. AVERAGE ANNUAL OVERALL TURNOVER RATE, BY HR DEPARTMENT STRUCTURE



Source: Workforce Analytics: Huh? We're Switching Back Again? How Centralized and Decentralized HR Department Structures Influence HR Metrics (SHRM, 2016)

Conclusion

HR transformations occur to support the organization's business strategy. For example, the emergence of a strong economy caused organizations to shift away from a focus on cost reduction toward putting more strategic goals first. In fact, a majority (62%) of organizations have undertaken initiatives to reengineer key HR processes: 43% are working to redefine the roles of HR business partners and 37% are implementing new or leveraging existing self-service functions. Seen as a whole, these initiates work together to enable HR to rethink its role in providing greater value to the business.[17]

Analysis of HR department structures shows that centralized HR departments are found in small organizations whereas a mix of both HR structures is found in large organizations. Global organizations, which are typically large, frequently used a mix of both structures to inculcate consistent HR philosophies for both domestic and international offices while also decentralizing the HR function to address local and cultural HR practices. Centralized HR departments have a higher percentage of HR staff in supervisory roles, but lower annual turnover rates compared with mix of both/matrix organizations. Interpretation of these results suggests that staff size signals what HR structure is chosen by organizations. Given similar business and environmental factors, this could mean that HR structure and staff size co-vary, indicating that both components—structure and staff size—affect key HR metrics at the same time.

As organizations evaluate which HR structure optimizes HR effectiveness, it is important to think holistically about HR in terms of how work gets done and how it delivers value to the business. Critical to a successful HR transformation is the quality of the HR leadership team and communication around changes being made as a way to foster credibility within the HR function. HR transformations also create opportunities for HR staff to develop and assume new HR responsibilities. The SHRM Competency Model, which identifies key behavioral competencies for both at early, mid, senior and executive career levels, can be used as a foundation toward designing an HR functional area and can assist HR professionals as they progress throughout their careers.[18]

Methodology

Since 2005, SHRM has been collecting human capital benchmarking data on an annual basis. The current 2015 SHRM Human Capital Benchmarking Survey was conducted to create a database of human capital metrics across various industries. In February 2015, an e-mail that included a link to the survey was successfully sent to 27,614 SHRM members, and 3,018 HR professionals responded. The study collected data on human capital metrics such as succession planning, turnover, cost-per-hire, time-to-fill and salary increases. In addition, organizational data, such as staff size and geographic region, were obtained. Data were collected for 2014, along with expectations for hiring and revenue changes in 2015. The response rate was 10.9%. Given the level of response to the survey, SHRM is 98% confident that response given by respondents can be generalized to all SHRM members with a margin of error of approximately +/-4%. The survey was created by SHRM's Workforce Analytics Program and was reviewed by the SHRM Human Capital Measurement/HR Metrics Special Expertise Panel.

Endnotes

[1]Holly, N. (2009). HR Models – Lessons from Best Practice: Initial Desk Research, Henley Business School. [PowerPoint slides]. Retrieved from http://www.henley.ac.uk/web/FILES/corporate/cl-Henley_Centre_HR_models_desk_research_October_2009.pdf

[2]Ibid.

[3]Ulrich, D., & Grochowski, J. (2012). From shared services to professional services. *Strategic HR Review, 11*(3), 136-142.

[4]Rison, R., &Tower, J. (2005). How to reduce the cost of HR and continue to provide value. *Human Resource Planning, 28*(1), 1-17.

[5]Maatman, M., Bondarouk, T., & Loosie, J. (2010). Conceptualizing the capabilities and value creation of HRM shared service models. *Human Resource Management Review, 20*(4), 327-329.

[6]Ibid.

[7]Ulrich, D., & Grochowski, J. (2012). From shared services to professional services. *Strategic HR Review, 11*(3), 136-142.

[8]Deloitte Development, LLC. (2012). *Global business HR transformation: The journey continues.* Retrieved from http://www2.deloitte.com/global/en/pages/human-capital/articles/global-business-driven-hr-tansformation.htm

[9]Super-large organizations of 10,001 or more employees were excluded from this breakdown because they were underrepresented in the sample.

[10]SHRM Human Capital Database. [Unpublished data].

[11]Mean differences are significant at the .05 level.

[12]SHRM Human Capital Database. [Unpublished data].

[13]Mean differences are significant at the .05 level.

[14]Society for Human Resource Management. (2105). *Workforce Analytics: A Critical Evaluation: How Organizational Staff Size Influences HR Metrics.* Alexandria, VA: SHRM.

[15]To calculate annual turnover, first calculate turnover for each month by dividing the number of separations during the month by the average number of employees during the month and multiplying by 100: # of separations during month ÷ average # of employees during the month x 100. The annual turnover rate is then calculated by adding the 12 months of turnover percentages together.

[16]Mean differences are significant at the .05 level.

[17]Towers Watson. (2011). *New horizons, no boundaries: an expansive landscape of HR service delivery opportunities.* HR Service Delivery and Technology Research Report. Retrieved from http://benefitcommunications.com/upload/downloads/Towers_Watson-HRSD-Survey-Executive-Report-2011.pdf

[18]SHRM Competency Model. (2016). Retrieved from https://www.shrm.org/hrcompetencies/pages/default.aspx

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