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ABC: An Introduction to Balanced Scorecard

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What is a "balanced scorecard"?

The balanced scorecard methodology, an outgrowth of prior measurement and management methodologies like total quality management (TQM), has existed for decades, but it was formalized in the early 1990s by Robert Kaplan and David Norton. Kaplan and Norton not only gave it a formal name but also put structure around the way organizations can measure how well they are functioning and how to predict future performance. Basically, it's a way to map and translate complex business information into something that's understandable to everyone. The methodology starts with targets defined by the organization, followed by scorecard measures. These usually include both corporate targets and business unit targets, which are then honed into individual measures and targets. It's a very flexible approach, designed to be adapted to any organization's needs. And virtually anything can be measured.

What are the benefits of implementing a balanced scorecard?

Major benefits include increased structure and shared objectives; these often lead to greater financial return. It allows organizations to become more functional and enabled. For specific programs, a balanced scorecard can raise the profile of key projects, which can help with funding and internal support. It's also possible to use the strategic map that a balanced scorecard approach creates to help guide programs toward success. And it's catching on. According to Bain & Co., about 70 percent of organizations had at least partially implemented a balanced scorecard by 2006.

How is it different from other methodologies, such as Six Sigma, activity-based costing and IT governance?

Activity-based costing was a precursor to balanced scorecard; it evaluated the costs, rewards and benefits of specific activities. The balanced scorecard concept builds on this idea. Six Sigma is a product of the balanced scorecard, imposing even greater structure. The balanced scorecard is often part of the IT governance process and is generally used as a performance measurement to help determine how much is being spent and where IT is making a contribution in achieving business goals.

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Does every organization need a balanced scorecard of some type?

Most, but not all, organizations can benefit from a balanced scorecard approach-both public and private. In general, the larger and more complex the organization, the more it will benefit. Companies that are heavily regulated also benefit, as well as companies in crisis. Both of these types of organizations can use the structured approach for more detailed reporting to those overseeing them. The amount of structure already in place is another factor. Depending on what types of teams are in existence, how they make decisions and the mechanisms in place for measuring individual performance, they may or may not benefit. Small organizations sometimes work fine without them; their entrepreneurial culture might be enough to sustain them. One example is Home Depot; as a small company, it had few measures in place until the current CEO came on board. During its early years, it was important for Home Depot to remain fluid, but as it grew, it needed more structure, which the CEO provided.

Who is the champion within the organization?

Generally, the edict comes from the top-the CEO, who, with his or her team, develops top-level corporate objectives for the balanced scorecard. The CEO then appoints either the CIO or the Chief Knowledge Officer (CKO) to spearhead not only those corporate objectives and measurements but also department and individual objectives and measurements.

How can you determine your scorecard measures?

Start at the top, and define both corporate objectives and business unit targets, advises Louis Carter, CEO of Best Practice Institute in North Palm Beach, Fla. For example, a goal may be to double the corporate value in seven years; that requires defining that value. Or you may want to increase your earnings by an average of 20 percent per year. Specific business unit targets are devised in the same way, always using focus groups that comprise both stakeholders and users whenever possible. Then get down to individual measures.

How is the balanced scorecard implemented?

According to the Balanced Scorecard Institute, it consists of multiple steps:

1. Assess the company's organizational structure
2. Identify strategic themes
3. Define perspectives and strategic objectives
4. Develop a strategy map
5. Derive performance metrics
6. Craft and prioritize strategic initiatives
7. Automate and communicate
8. Cascade the balanced scorecard throughout the organization
9. Collect data, evaluate and revise

Are there software tools that can help?

The problem with these tools is that every organization is unique, as are every organization's needs and goals. It's difficult for any software tool to be able to take all that into account, and committing to one tool means you have to buy into a structured approach that might or might not work for your company. That said, there are literally more than a hundred such tools, all claiming to help develop balanced scorecards. They can be useful in some cases, with some caveats. And some are more customizable than others: Make sure to determine how customizable they are. The more, the better. Openness, collaboration, and understanding of your employees and business are critical to the product's functionality. Try to find a tool that is customizable and fits well with the structure of your company and how your employees think. But before using any tool, make sure you have all of your ducks in a row: Get training on the balanced scorecard approach, and determine what you want to measure and what your objectives are.

What if you choose not to use off-the-shelf software?

That's certainly an option. For small companies-those under the Fortune 500, anyway-there are many free sources that can be very fruitful. Using wikis, for example, can be a great way to start. Another option is to learn XML or ACML and put the entire effort on a corporate intranet. There are as many ways to structure balanced scorecards as there are things to measure. Either way, though, the latest way organizations are structuring balanced scorecards is through dashboards. This method of viewing balanced scorecard metrics allows leaders to quickly identify problems and view key performance indicators associated with business processes.

What are the challenges when implementing a balanced scorecard?

Corporate culture changes, and with change can come fear, especially if it is tied to performance standards. Much of that can be abated if you are honest with stakeholders and employees. It can also be a time-consuming process, taking up to a year to fully implement, although the original estimate from Kaplan and Norton indicated a time of 26 months to implement everything down to the level of individual employees. It also requires full top-level support over a long period of time, during which other priorities and emergencies almost certainly will take center stage, at least temporarily. And it's certainly not cheap. Depending on the scope of the project, it can cost from thousands to hundreds of thousands of dollars. Costs include team members and time spent, facilitator cost, software licensing costs, installation and testing costs, and annual maintenance and upgrade costs.

How can you determine ROI?

That's an easy one. You justify the cost by virtue of the measurement itself and the results it presents. That's the ROI.

Can you dip a toe in the water, or is it an all-or-nothing proposition?

It's a good idea to start slowly. Start simple by focusing on just three indicators, and put a few employees in charge who are champions of the effort. Do a pilot program with those parameters, and expand from there. Also, don't jump into expensive software-try the grow-your-own approach first.

Is this something a company can do internally, or is external help advisable?

It's certainly possible to do it internally if you have sufficient executive commitment, if your balanced scorecard leaders are motivated to learn and lead, and if you have the internal bandwidth to do it right. It all depends on how much time you have, how much you can spend, how much time you can afford to take from your employees, and how much internal expertise and willingness to learn you have. Sometimes it does make sense to use an external consultant, such as when your effort or company needs a jump-start, when you don't have the internal expertise or manpower, or when the cultural change is just too difficult to handle without an outside influence.

available?

Even with tools, consultants and books, this is a huge undertaking. Are there general guidelines available?

There are several independent, technology-agnostic organizations with reams of good material. They include:

- Best Practice Institute, North Palm Beach, Fla., www.bpinstitute.net
- Balanced Scorecard Institute, www.balancedscorecard.org
- Foundation for Performance Measurement, www.fpm.com
- Benchmarking Network, www.benchmarkingnetwork.com
- Best Practices LLC, www.best-in-class.com

Using a balanced scorecard methodology is as good a way as any-and better than many-to measure and track processes and progress, and there are plenty of resources, many of them free, at your disposal. It doesn't make sense not to give it a try; after all, you don't have that much to lose, and you have much to gain.

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