

Efficient Organizational Design - Balancing Incentives and Power

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Abstract Incentives to create value and power to influence the distribution of value are the two most important parameters of organizational design. The efficiency of an organizational design, such as a firm, is only maximized if ex ante incentives to generate economic rents through specific investments are balanced with the ex post power to appropriate these rents. An organizational design that does not adequately balance incentives and power falls short of achieving the highest degree of efficiency.

Incentives and power can be influenced through several building blocks. The configuration of the organization's strategy, its boundaries, its internal structure and its governance thus matters, and the way in which the elements of these building blocks are configured influences the efficiency of the organizational design. Using the ideas of systems theory, the author argues that a consistent configuration has to take account of any complementarities between these elements in order to achieve such a delicate balance between incentives and power to exhaust all possibilities for value creation.

The theoretical ideas of organizational design developed in Part I are supplemented by three case studies in Part II of the book, where the framework of efficiency in organizational design through the balancing of incentives and power are applied to three diverse settings. The optimal design for the European securities transaction industry, the success of the German cooperative banking group and the understanding of the functioning of open-source communities in the software business can all be explained by the theory developed in the book.