University of Oxford
Novak Druce Centre for Professional Service Firms
Saïd Business School

THE TRANSNATIONAL PROFESSIONAL SERVICE FIRM: **THE RISE OF THE MULTIPLEX PSF**

NOVAK DRUCE CENTRE INSIGHTS No. 1

CONTENTS

'OUR RAISON D'ÊTRE IS TO DELIVER GLOBAL SERVICES. IT RUNS RIGHT THROUGH THE DNA OF THE FIRM – THAT WE ARE GLOBAL OR WE ARE NOTHING.'
(Partner in a leading transnational PSF)

Based on the article, 'The Organizational Design of Transnational Professional Service Firms' by Royston Greenwood, Samantha Fairclough, Tim Morris and Mehdi Boussebaa, published in Organizational Dynamics, 39 (2), April–June 2010.

THE **MULTIPLEX PSF**

Transnational professional service firms (PSFs) are hugely significant in today's global economy. They support financial markets, facilitate complex international transactions and deliver managerial ideas and advice to the world's largest corporations and most powerful governments. They 'sell' expertise – that most intangible of products – providing customized solutions to demanding clients on a global basis. Other businesses will face the same challenges as the world becomes more globally connected and customers more demanding, seeking products and services to fit their particular needs. As such, professional service firms represent critical models for 21st century multinational firms.

Transnational PSFs face major challenges, however. They have grown in scale and complexity to the point where traditional organizational arrangements have proven inadequate. How are these challenges being met, and what lessons can we learn?

Research at the Novak Druce Centre reveals the emergence of the 'multiplex' PSF. Transnational PSFs have responded to their complex environments by developing highly sophisticated structures that capture the benefits of deep multidimensional specialization without losing overall coordination. This briefing focuses on accounting firms as exemplars of this knowledge-intensive, multiplex organizational form, but our research into other professional service sectors confirms they too are pursuing similar practices as they adopt the multiplex structure.

THE RISE OF THE **TRANSNATIONAL PSF**

Transnational accounting firms have evolved through three broad phases. Initially, accountants serviced clients from local offices distributed in a particular country. Each office was more or less self-contained: as such, the 'firm' was made up of relatively independent, geographically dispersed units. Coordination across local offices was under the umbrella of the 'national firm', which provided broad-based marketing and managed clients with a national scope. But the centre of gravity was the local office, where professionals were grouped by 'line of service' (for instance, audit and assurance, tax, or management advisory services).

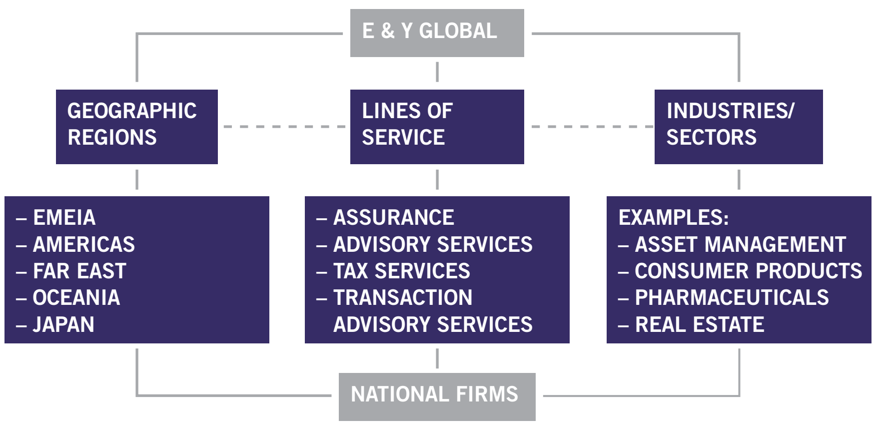
The second phase occurred as clients over time became more international. National professional service firms followed suit and merged to form international PSFs. Given their increasing size and geographical scope, these firms required new levels of governance – notably, a global headquarters to provide coordination across national jurisdictions and take responsibility for strategic issues such as entering new territories or markets. But the centre of gravity of these organizations remained at the national level.

The third phase was triggered as PSFs found it useful to add a new 'axis' of specialization – industry knowledge. As well as professional expertise, clients began to expect their advisers to have close, in-depth knowledge of their industries and their markets. In response, PSFs developed industry-specific expertise and became innovative 'thought leaders' in particular industries and markets.

Reflecting this, they created organizational structures designed to focus attention on specific markets and generate new ideas and products for them. Accounting firms now focus their know-how in geographic hubs of industry expertise. For instance, KPMG's automotive industry advice is organized around a global automotive centre which pulls together resources from Detroit, Stuttgart, Shanghai and Tokyo. Furthermore, firms have re-organized themselves regionally to coordinate client service delivery. Deloitte, for example, focuses its services in regional groupings such as the Americas, Asia Pacific, and Europe/Middle East/Africa.

By the mid-1990s all the basic elements of the global multiplex were in place. Transnational PSFs had organized themselves along three main axes: location, line of service, and industry/market. These axes are critical for firms competing on the basis of their expertise in multiple jurisdictions and advising clients in very different industries and markets. An example is given in Figure 1.

FIGURE 1: INTERNATIONAL ORGANIZATION OF ERNST & YOUNG LLP



THE DILEMMAS FACING **TRANSNATIONAL PSFs**

These high levels of differentiation create considerable problems of coordination and control. Transnational PSFs confront daunting challenges of size, geography and diversity of service and must reconcile several tensions and dilemmas:

TENSIONS BETWEEN NATIONAL AND INTERNATIONAL INTERESTS

On the one hand, the historical centre of gravity lies in the national firms, partly because they were the original building blocks of today's international firms, partly because they remain the home base of professionals who need to be near their clients, and partly to meet the demands of national legislation. On the other hand, the strategic emphasis of the evolving firms is transnational: delivering cutting-edge services seamlessly and consistently to global as well as national and local clients.

TENSIONS BETWEEN LINE OF SERVICE AND INDUSTRY/MARKET AXES

The line of service axis, which emphasizes professional standards and norms of conduct, is the traditional core of the organization and where expectations of professional independence are likely to be more pronounced. The industry/market axis, on the other hand, is a focal point for a more business-oriented perspective and emphasizes commercial expertise and market growth.

These tensions are intensified by PSFs' unusual ownership and governance arrangements. Typically, PSFs are partnerships in which senior professionals own and manage their respective national firms and lead client engagements. This means, in principle at least, that important decisions have to involve all partners.

Unsurprisingly, partners in particular countries are especially sensitized to the interests of 'their' clients, and this is reinforced by incentives that reward them on the basis of their client fees and satisfaction. As a result, partners are not always motivated to devote time and resources to building the international firm, particularly if their own clients are relatively small and local rather than large and global.

Despite these challenges, the largest transnational accounting firms are coping successfully. Revenues have grown markedly. In 2000, for example, Deloitte's fee income was $11.2 billion; in 2004 it was $16.4 billion and in 2008, $27.4 billion. The other Big Four firms have recorded similar growth rates. And the largest PSFs are still growing. Between 1990 and 2009, Ernst & Young more than doubled its number of employees and increased its revenue over fourfold.

Transnational PSFs appear to have evolved an organizational form that works for them. They have discovered how to gain the powerful benefits of multidimensional specialization without losing overall coordination. How have they done it? How have they overcome the challenges of geographical complexity and size? Our research reveals that they have learned to apply four key principles:

1. **DEVELOPING MULTIPLE DIMENSIONS OF SPECIALIST EXPERTISE**
2. **CREATING OVERLAPPING PROFESSIONAL COMMUNITIES**
3. **PRIORITIZING CLIENT MANAGEMENT**
4. **DEVELOPING TRANSNATIONAL 'CULTURES OF RECIPROCITY'**

PARTNERS ARE NOT ALWAYS MOTIVATED TO DEVOTE TIME AND RESOURCES TO BUILDING THE INTERNATIONAL FIRM

1. MULTIDIMENSIONAL **SPECIALIZATION**

The multiplex PSF is grounded in the recognition that in order to compete successfully in the global market, PSFs must develop their expertise along several different 'axes' simultaneously. Successful PSFs have created structures such as departments and practice groups that target core practice areas serving sectors such as health care or issues like mergers and acquisitions. Each dedicated practice area brings together a deep professional expertise and knowledge of markets and institutions, and offers the specialization and sophistication that multinational clients increasingly demand of their advisers. In addition, each axis opens an avenue to explore new markets, allowing the firm to avoid shrinkage in its clients and maximize the exploitation of resources.

2. NASCENT COMMUNITIES **AS A ROUTE TO INTEGRATION**

The paradox at the heart of the multiplex PSF is that a potential cause of fragmentation – multiple in-depth specialization – is used to achieve a sense of community and integration. The axes of specialization are deliberately made to intersect, so that structural diversification is offset by an overlap in personnel. Professionals become members of multiple groups in terms of service line, industry, location or client. In this way, each axis does not form an insular silo; instead, structures that are usually seen as sources of fragmentation in fact create a framework for coordination and reciprocity within the PSF. The different axes – line of service, geography, and industry or market – continuously bring together different ranges of professionals in changing lattice-works of community within the larger organization.

For example, lines of service such as tax or audit do not form exclusive communities isolated from industry teams. Each professional plays multiple roles simultaneously – working as part of a service line, an industry group and a particular place, as well as in different client management teams over time. The benefits are twofold: professionals do not assume entrenched positions, seeing the world from only one angle, but learn to understand and identify with the different viewpoints of the diverse communities they belong to; secondly, the relationships between professionals created by their criss-crossing membership in different communities result in extensive personal networks, which enable expertise to be identified and leveraged promptly and appropriately in the course of strategically critical client engagements.

THE PARADOX AT THE HEART OF THE MULTIPLEX PSF IS THAT A POTENTIAL CAUSE OF FRAGMENTATION IS USED TO ACHIEVE A SENSE OF COMMUNITY AND INTEGRATION

COORDINATED CLIENT MANAGEMENT SYSTEMS TAKE INTO ACCOUNT THE STRATEGIC IMPORTANCE OF MEETING THE DEMANDS OF INTERNATIONAL CLIENTS

3. PRIORITIZING **CLIENT MANAGEMENT**

Key to resolving the tensions in transnational PSFs has been the development of coordinated client management systems (CMSs). These are designed to take into account the strategic importance of meeting the demands of international clients for a seamless customized service. Transnational PSFs distinguish themselves from their competitors by virtue of the resources and knowledge they mobilize. The CMS focuses and tailors these resources to fit the needs of the client, enabling the firm to offer consistent and coherent quality service across national boundaries.

Another of the key functions of the CMS is to classify clients according to their strategic importance. Compared to large manufacturing multinational corporations, which may have twenty or thirty global account relationships, the largest accounting firms may have up to fifty top priority clients, and a further 200–300 of high priority. A clear benefit of the CMS is that professionals throughout the firm are led to recognise which international clients are critical for the firm's global success and give them appropriate attention.

At the heart of the CMS is the client management team, a cluster of professionals engaged upon projects for a particular client. The size and range of this team requires careful recruitment and management. PSF client management teams may resemble those in manufacturing multinational corporations (MNCs), but whereas manufacturing MNC teams are relatively small, typically involving only one to five people, PSF teams often have over forty members.

Heading each team is a 'lead partner' with responsibility for ensuring the client receives the appropriate level of service on a worldwide basis. Lead partners recruit personnel, manage relationships with the client and resolve any conflicts that might arise. They play a key role in identifying the competencies and the individuals needed for a project and negotiating their involvement.

However, a dilemma can arise. Withdrawing a valued partner from, say, Australia to work for several years in a North American team may seriously disadvantage the Australian firm, especially as that partner will no longer be available for marketing and client development purposes in the home country – activities in which close personal relationships based on local knowledge are crucial.

So why would partners cooperate in these arrangements? Why would they agree to the transfer of valuable professional resources out of their national jurisdictions? The answer lies in perhaps the most significant feature of multiplex PSFs: their cultures of transnational reciprocity.

TRANSNATIONAL RECIPROCITY CULTURES ACT AS A 'GLUE', TIGHTLY BINDING THE ELEMENTS OF THE MULTIPLEX TOGETHER

4. CULTURES OF **RECIPROCITY**

Four mutually reinforcing factors contribute to the culture, as depicted in Figure 2: positive role models; aligned organizational processes; organizational strategy/rhetoric; and the beneficial consequences of reciprocity.

Typically the leaders of transnational PSFs promote one-firm global cohesion via mission statements and other forms of rhetoric, which envision the firm as an integrated whole and emphasize the benefits of collaboration between practices and countries. This language of unity of purpose helps foster a common transnational mindset amongst partners and staff. But, of course, in itself this is not enough. Senior partners need not only to 'talk the talk' of unity and reciprocity but also 'walk the walk', serving as positive role models for partners and associates.

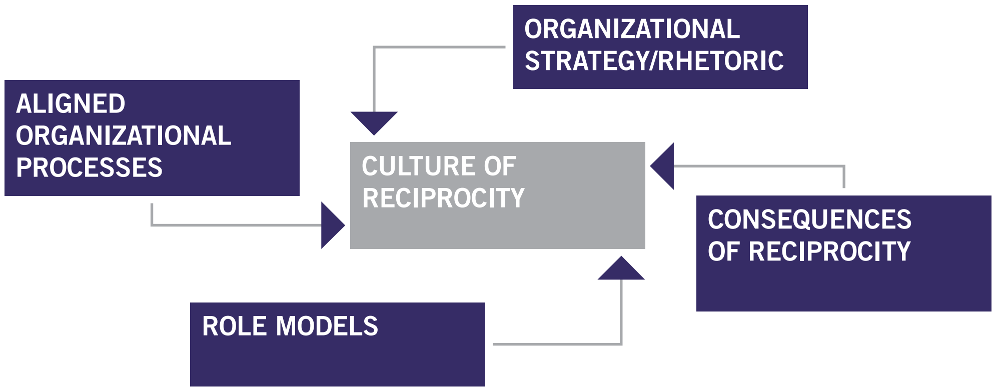
Another factor that contributes to the culture of reciprocity is various organizational processes which are aligned together and with organizational strategy to promote norms of collaboration. For example, recruitment and socialization contribute to the creation of homogenous communities, which reproduce and transmit the values of the firm from generation to generation.

Firms also invest heavily in global training programs that bring together professionals from around the world and internalize a shared purpose. These programs build commitment, encourage the diffusion of ideas and practices, and, perhaps more critically, establish extensive face-to-face relationships between professionals who might, in the future, be looking to each other for help.

Performance appraisals, too, serve to cultivate norms of reciprocity. Senior partners are evaluated by a range of partners to whom they provided resources in their service line activities and broader client relationships. A weak or reluctant performer will be noted, and under-performance will be reflected in their subsequent remuneration. Appraisal processes thus send a clear signal to more junior professionals, reinforcing the message that collaboration is highly rewarded.

Finally, another key factor in the creation of a culture of transnational reciprocity is foreseeing the beneficial consequences of reciprocity. By helping overseas colleagues, partners can expect to receive similar assistance in turn. Non-partners, too, have much to gain by cooperating with colleagues in associated firms. Working for transnational clients carries high status. It exposes professionals to the most complex professional activities, the highest rated colleagues, and client engagements central to strategic goals. Additionally, it introduces individuals to the working practices of colleagues in other countries, and particularly the global knowledge hubs in which cutting-edge industry know-how is concentrated. These engagements offer non-partners the opportunity to build networks across the firm, and forge the reputations on which their future promotions will depend.

FIGURE 2: ELEMENTS REINFORCING A CULTURE OF RECIPROCITY



SUSTAINING **THE CULTURE**

Cultures of reciprocity nevertheless take time to build and are not easy to maintain. Critical to their success are a number of factors:

CLARIFYING THE FINANCIAL AND OPERATING TARGETS THE FIRM USES

Successful transnational multiplex PSFs employ complex financial formulae for calculating the distribution of profits produced from global projects. These formulae accommodate the hourly rate of those participating in transnational work so that team members are not inhibited by financial concerns from collaborating between offices. This ensures that those national offices who lend their resources to teams in other countries are compensated for the costs of the people they have lent. Removing this obstacle to cooperation is critical.

STABILITY OF PERSONNEL

Most PSFs favour the development of their junior staff over external recruitment and only rarely make lateral appointments at the partner level. Senior partners work their way up through the ranks of one organization from the most junior appointments, and there are very low rates of turnover among the highest ranks. This philosophy of building careers within a single firm strengthens the commitment of professionals and helps embed the culture of reciprocity.

PARTNERSHIP GOVERNANCE

Particularly relevant to PSFs, the partnership form of governance is highly symbolic as a unifying concept. The values of peer control and professional self-monitoring embodied in the notion of partnership nurture an attitude of collective interest whereby the interests of the firm outweigh partners' inclinations to 'free ride' or focus exclusively on their individual interests.

The resulting rewards of reciprocity are many. Multiplex PSFs secure the best work from the biggest clients, thereby setting themselves apart in scale and scope from their competitors. And access to such clients creates enormous benefits, opening up lucrative revenue opportunities and strengthening the firm's brand. Furthermore, engagements of this scale and complexity foster the development of deep expertise and help firms attract, motivate and retain the best and brightest talent.

THE IMPLICATIONS FOR **21ST CENTURY ORGANIZATIONS**

This briefing has focused on accounting firms, but there are wide-ranging implications for other international businesses seeking to create global organizational designs fit for the 21st century.

The multiplex organizational form represents a means by which the complex competing demands in transnational businesses can be identified and articulated and their associated problems resolved. Businesses have long applied the organizational matrix as a useful but cumbersome structure. The multiplex, if properly designed, offers a viable sophisticated alternative.

The multiplex combines both structural and cultural features to achieve its ends. Superficially the multiplex may look like a straightforward three-dimensional matrix structure, but in practice it is precisely the fusion of structural and cultural features that ensures its effectiveness.

The multiplex works because of the multiple roles that professionals carry on a continuous basis. In their day-to-day work professionals are simultaneously engaged as market sector specialists, experts in a line of service, and practitioners working in a particular place. This means they are sympathetic to the demands that each dimension places on the multiplex and never become narrowly entrenched in one point of view.

The client management system plays a critical role by focusing large numbers of professional staff on the common goal of serving the client and delivering client satisfaction.

As knowledge-based businesses – widely hailed as the firms of the future – face the demands of operating in increasingly globalized markets and are confronted by ever-more demanding clients seeking tailored solutions, the challenge will be to respond with the right sort of organizational design. PSFs have evolved a sophisticated design model – the transnational multiplex – that allows them to mine multiple deep seams of expertise while pursuing a globally coordinated strategy.

THERE ARE WIDE-RANGING IMPLICATIONS FOR OTHER INTERNATIONAL BUSINESSES

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Series Editor: Peter Snow
Academic Editor: Tamar Parush
Design: SampsonMay www.sampsonmay.com

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THE NOVAK DRUCE CENTRE
FOR PROFESSIONAL SERVICE FIRMS

Saïd Business School
University of Oxford
OX1 1HP
Tel: +44 (0)1865 288 949

novakdruce.centre@sbs.ox.ac.uk
www.sbs.oxford.edu/novakdrucecentre