

Balanced Scorecard Functional Standards™ Release 1.0a

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1.0 Background

Within the past few years the Balanced Scorecard has become a key tool for managing and implementing strategy in organizations. Responding to this business demand, many analytical application, ERP, and database vendors are developing and releasing software to support executive decision-making using the Balanced Scorecard methodology. This development of software-enabled Balanced Scorecards will inevitably lead to the implementation of Balanced Scorecards at an increasing number of organizations throughout the world. Central to the Balanced Scorecard methodology is holistic vision of a measurement system tied to the strategic direction of the firm. The Balanced Scorecard is based on strategic implementation through focus on four perspectives, with financial objectives and measures supported by customer, internal, and learning and growth objectives and metrics. By measuring and managing the business using this balanced set of measures, an organization can ensure rapid and effective implementation of strategy and facilitate organizational alignment and communication.

Many organizations are accelerating the benefits from their Balanced Scorecard by using enabling technology to facilitate their Balanced Scorecard management process. If an organization is to capture the full potential of the Balanced Scorecard management system, the enabling technology it implements should support the requirements of the desired management process. If the elements of the management process are not reflected in the application, the resulting process will be sub-optimal. Currently, many software vendors are offering applications that bear the name Balanced Scorecard. Some of these applications support a strategic management process, while others do not. This has made the Balanced Scorecard technology marketplace confusing for potential buyers.

To facilitate consistent and appropriate use of the Balanced Scorecard globally, a need has arisen for harmonization and standardization of the methodology of the Balanced Scorecard as envisioned by the creators of the concept, Dr. Robert Kaplan and Dr. David Norton. Therefore, Balanced Scorecard Collaborative, a global center of excellence on all things related to Balanced Scorecards, founded by Drs. Kaplan and Norton, has created Balanced Scorecard Functional Standards.

Balanced Scorecard Functional Standards identify user requirements and needs, based on the experience professionals from the Balanced Scorecard Collaborative have had with more than 300 clients. These observations have been codified in the functional standards to provide guidance for organizations preparing to purchase a Balanced Scorecard application and to provide a functional baseline for technology vendors developing a Balanced Scorecard application. These standards should be viewed as a minimum threshold upon which vendors will innovate to meet any additional requirements of their market.

The purpose of this document is to provide an overview of Balanced Scorecard Functional Standards.

2.0 Document References

The functional standards listed below are based on the published methodology of Drs. Kaplan and Norton and the expertise of the staff of Balanced Scorecard Collaborative. For more information about the methodology behind the standards, and the best-in-class application of Balanced Scorecard methodology, please refer to the following documents:

"Linking the Balanced Scorecard to Strategy" in *California Management Review*, by Robert S. Kaplan and David P. Norton, October 1996.

Abstract: The Balanced Scorecard was developed to measure both current operating performance and the drivers of future performance. Many managers believe they are using a Balanced Scorecard when they supplement traditional financial measures with generic, non-financial measures about customers, processes, and employees. But the best

Balanced Scorecards are more than ad hoc collections of financial and non-financial measures. The objectives and measures on a Balanced Scorecard should be derived from the business unit's strategy. A scorecard should contain outcome measures and the performance drivers of those outcomes, linked together in cause-and-effect relationships.

Balanced Scorecard: Translating Strategy into Action, by Robert S. Kaplan and David P. Norton (Harvard Business School Press, 1996).

Abstract: The Balanced Scorecard translates a company's vision and strategy into a coherent set of performance measures. The four perspectives of the scorecard—financial measures, customer knowledge, internal business processes, and learning and growth—offer a balance between short-term and long-term objectives, between outcomes desired and performance drivers of those outcomes, and between hard objective measures and softer, more subjective measures. In the first part, Kaplan and Norton provide the theoretical foundations for the Balanced Scorecard; in the second part, they describe the steps organizations must take to build their own Scorecards; and, finally, they discuss how the Balanced Scorecard can be used as a driver of change.

"Using the Balanced Scorecard as a Strategic Management System" in *Harvard Business Review*, by Robert S. Kaplan and David P. Norton, January 1996.

Abstract: As companies transform themselves to compete in the world of information, their ability to exploit intangible assets is becoming more decisive than their ability to manage physical assets. Several years ago, Robert S. Kaplan and David P. Norton introduced the balanced scorecard, which enabled companies to track financial results while monitoring progress in building the capabilities they would need for growth. Recently, some companies have gone further and discovered the scorecard's value as the cornerstone of a new strategic management system. Traditional management systems rely on financial measures, which bear little relation to progress in achieving long-term strategic objectives. The scorecard introduces four new processes that help companies connect long-term objectives with short-term actions.

"Putting the Balanced Scorecard to Work" in *Harvard Business Review* by Robert S. Kaplan and David P. Norton, September 1993.

Abstract: In an earlier, groundbreaking article, "Balanced Scorecard – Measures That Drive Performance", the authors proposed a new measurement system that provided managers with a comprehensive framework to translate a company's strategic objectives into a coherent set of performance measures. Now the authors show how several companies are putting the balanced scorecard to work. Effective measurement, the authors point out, must be an integral part of the management process. Much more than a measurement exercise, the balanced scorecard is a management system that can motivate breakthrough improvements in such critical areas as product, process, customer, and market development. Several examples—Rockwater, Apple Computer, and Advanced Micro Devices—illustrate how the scorecard combines measurement and management in different companies. From the experiences of these companies and others, the authors have found that the balanced scorecard is most successful when it is used to drive the process of change.

"The Balanced Scorecard: Measures That Drive Performance" in *Harvard Business Review* by Robert S. Kaplan and David P. Norton, January 1992.

Abstract: During a year-long research project, the authors developed a "balanced scorecard" performance measurement system that allows executives to view a company from several perspectives simultaneously. The scorecard includes financial measures that reveal the results of actions already taken, as well as three sets of operational measures that show customer satisfaction, internal processes, and the organization's ability to learn and improve. Creating a balanced scorecard requires translating a company's strategy and mission statement into specific goals and measures. Managers then track those measures as they work toward their goals.

3.0 Definitions

For the purpose of this document, the following definitions apply:

Balanced Scorecard is a multi-dimensional framework created by Dr. Robert Kaplan and Dr. David Norton that uses measurement to describe an organization's strategy (see references in Section 2.0).

Balanced Scorecard Application refers to any software package which uses the methodology of Drs. Norton and Kaplan to facilitate strategic decision-making using the Balanced Scorecard methodology, or any package which uses the term "Balanced Scorecard" in its marketing material, title, or external communications.

Standards as defined in this document refer only to the functionality of the software package as it relates to the Balanced Scorecard methodology. This standard does not specify any technology solutions, refer to scalability of the solution, or discuss interconnectivity of the package with other systems.

Balanced Scorecard Methodology refers, in the context of these standards, to the Balanced Scorecard methodology as initially defined by Drs. Kaplan and Norton and as currently practiced by Balanced Scorecard Collaborative. The methodology is under continual development, and the standards will evolve to reflect current best practices and thought leadership in the Balanced Scorecard concept.

4.0 Balanced Scorecard Collaborative

Balanced Scorecard Collaborative, Inc. facilitates the worldwide awareness, use, enhancement, and integrity of the Balanced Scorecard as a value-added management process. The Collaborative offers a variety of education, training, research, and development services designed to share best practices to achieve best results. Founded and managed by Balanced Scorecard creators Drs. Robert Kaplan and David Norton, the Collaborative provides organizations and individuals with a global center of excellence and expertise on all things related to Balanced Scorecards.

5.0 Basic Functional Requirements for Balanced Scorecard Applications

Balanced Scorecard applications must be able to facilitate management of the organization through the Balanced Scorecard methodology as documented in the literature above and as practiced by Balanced Scorecard Collaborative. The standards as outlined below represent the minimum functionality for a Balanced Scorecard system. Software providers are encouraged to differentiate their products beyond the minimum standards outlined below. The standards documentation has been divided into four sections:

Balanced Scorecard Design (Section 5.1)

The application should be able to flexibly accommodate the basic elements of a proper Balanced Scorecard design. The application must be able to (1) view the strategy from four perspectives (financial, customer, internal, and learning), (2) identify strategic objectives for each perspective, (3) associate measures with strategic objectives, (4) link strategic objectives in cause and effect relationships, (5) assign targets to measures, and (6) list strategic initiatives.

Strategic Education and Communication (Section 5.2)

One of the key reasons for implementing a Balanced Scorecard software solution is the facilitation of strategic education and communication. Therefore, a certified application will enable users to document and communicate descriptions of objectives, measures, targets, and initiatives aligned with the strategy.

Business Execution (Section 5.3)

Initiatives (discretionary investment programs) are the testing grounds for the strategy expressed in the Balanced Scorecard. Therefore, a certified application must make explicit the relationship between initiatives required to achieve the strategy and the associated strategic objective.

Feedback and Learning (Section 5.4)

Through proper system design, the feedback cycle time for management information can be significantly reduced. Analysis of the measure results against targets will allow managers to understand which areas of the organization require further attention. However, the system should not override the judgment of a senior executive – the Balanced Scorecard system should rely on both objective and subjective judgments, as well as graphical indicators, to report on progress of a particular measure against its target. These design principles are outlined in greater detail in the text that follows.

As of September 30, 1999, Balanced Scorecard Collaborative considers these the minimum functional standards that a Balanced Scorecard application should have in order to reflect the methodology endorsed by Balanced Scorecard Collaborative. Release 1.0a, published on May 5, 2000 includes minor modifications that do not affect the substance of the functional standards.

5.1 Balanced Scorecard Design

A certified Balanced Scorecard application will accommodate the basic elements of a proper Balanced Scorecard design. Naming conventions may differ, but the design structure of certified applications must include the following six features: (see Figure 1, Basic Balanced Scorecard Design, for an example)

1. Perspectives

A perspective is a component into which the strategy is decomposed to drive implementation. Typically, there are four perspectives; financial, customer, internal and learning and growth. Others may be added or replace these based on a specific strategic need. A perspective is a major element of the strategy often representing a stakeholder category or point of view. Certified applications will include at least four basic perspectives (financial, customer, internal processes, learning and growth) and have the ability to rename perspectives at the user's option.

2. Objectives

An objective is a statement of strategic intent. An objective states how a strategy will be made operational. Generally, the objectives form the building blocks for the overall strategy of the organization. Certified applications will allow strategic objectives to be aligned with at least one perspective.

3. Measures

A measure is a performance metric that will reflect progress against an objective. A measure must be quantifiable. The measures communicate the specific behavior required to achieve the objective and become the actionable statement of how the strategic objective will be accomplished. Leading measures are predictors of future performance, while lagging measures are outcomes. A certified application will allow a reasonable number of measures explicitly linked to at least one objective.

4. Targets

A target is a quantifiable goal for each measure. The set of targets found on the Balanced Scorecard become the overall goals of the organization. Targets create opportunity to succeed, help the organization monitor progress toward strategic goals, and communicate expectations. A certified application will allow quantifiable targets with a specified timeframe.

5. Cause and Effect Linkages

Objectives are related to one another through cause and effect relationships. The cause and effect linkages are similar to "if-then" statements. For example, *if* an airline decreases the on-ground turn-around time (objective 1), *then* the airline will require fewer planes (objective 2) *and* customers will be more satisfied with on-time take off (objective 3) and corporate profitability will increase (objective 4). These cause and effect linkages should be explicit. A certified application will allow objectives to be linked and graphically represented on-screen as a series of cause and effect linkages (strategy map). The linkages should be able to be easily changed and edited as appropriate.

6. Strategic Initiatives

Strategic initiatives are those action programs (discretionary investments or projects) that drive strategic performance. These are the activities that groups will focus on to ensure attainment of strategic results. All initiatives underway in an organization should be aligned with the strategy in the Balanced Scorecard. A compliant package will allow for a set of strategic initiatives to be linked to at least one objective.

5.2 Strategic Education and Communication

Certified applications must include the following functionality:

Base Level Descriptors

The six key elements of the Balanced Scorecard (perspectives, objectives, measures, targets, linkages and initiatives) are typically defined in greater levels of detail. For instance, *objectives* may be further defined through a sentence or two describing the strategic situation or issue. *Measures and targets* are typically broken down into formulas, units of measure, frequency of reporting, target owner, reporting responsibility, data sources, target effective date, and target history. *Initiatives* also require greater description such as timeline, resources, budget, benefits, and risks. Such documentation is important to users to ensure consistency and repeatability of reporting and to capture the strategic intent of each element. Certified applications will facilitate the documentation of qualitative descriptions of each element of the Balanced Scorecard.

5.3 Business Execution

Link of Initiatives to Objectives

Strategic initiatives are the base elements of work that drive strategic change. They are the discretionary programs such as training, advertising, reengineering and others that are put in place to make the strategy happen. They must be monitored on a continuous basis to insure that they are being implemented as planned and producing the desired results. A strategic initiative should be explicitly linked or mapped to achieving one or more strategic objective. Certified applications should be able to display matching initiatives and objectives and should allow initiatives to be tied to more than one strategic objectives. (Reference Figure 1 for example)

5.4 Feedback and Learning

Base Level Reporting

Base level reporting includes reporting of performance data for each measure. Historical performance against targets and multiple reporting views are desirable features. Certified applications should be able to display current performance data for each measure.

Subjective Performance Assessments

The decision whether or not a *measure* is on track for meeting a *target* must ultimately be made by a manager who can subjectively analyze the data. The subjective performance assessments should also be backed up by a memo-style qualitative assessment of the external or internal variables underlying the assessment. Certified applications will

permit subjective assessments of performance (e.g., red, yellow, green) as well as memo-style qualitative descriptions of performance.


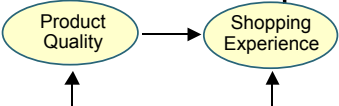
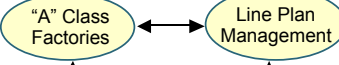
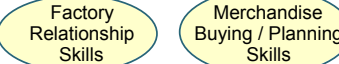
Visual Status Indicators

Each element of the scorecard must have a visual indicator of performance status, e.g., green or a plus sign if a measure or objective is on plan, red or a minus sign if behind plan. Certified applications will graphically display performance against targets in an easy-to-comprehend format, and will allow for modification to suit individual end-user needs.

6.0 Conclusion

It is anticipated that by following these guidelines software developers will be able to develop Balanced Scorecard applications, which enable users to capture the benefit of the Balanced Scorecard management system. Buyers of Balanced Scorecard applications will also benefit, as they will be able to leverage the expertise of Balanced Scorecard Collaborative and numerous successful organizations, as expressed in these standards, to select appropriate Balanced Scorecard software that will meet their needs.

Figure 1: Basic Scorecard Design (Example)

Perspective	Cause & Effect Linkage	Objectives	Measures	Targets	Initiatives
Financial		<ul style="list-style-type: none"> Profitable Business Growth 	<ul style="list-style-type: none"> Operating Income Sales vs. Last Yr 	<ul style="list-style-type: none"> 20% Increase 12% Increase 	<ul style="list-style-type: none"> Likes Program
Customer		<ul style="list-style-type: none"> Quality Product from a Knowledgeable Associate 	<ul style="list-style-type: none"> Return Rate Customer Loyalty – Ever Active % – # units 	<ul style="list-style-type: none"> Reduce by 50% each yr 60% 2.4 units 	<ul style="list-style-type: none"> Quality management program Customer loyalty program
Internal Process		<ul style="list-style-type: none"> Improve factory quality 	<ul style="list-style-type: none"> % of Merchandise from "A" factories Items in-Stock vs. Plan 	<ul style="list-style-type: none"> 70% by year 3 85% 	<ul style="list-style-type: none"> Corporate Factory Development Program
Learning & Growth		<ul style="list-style-type: none"> Train & equip the workforce 	<ul style="list-style-type: none"> % of Strategic Skills Available 	<ul style="list-style-type: none"> yr 1 50% yr 3 75% yr 5 90% 	<ul style="list-style-type: none"> Strategic Skills Plan Merchants Desktop