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Executive Summary

This article describes the development of an enterprise-wide change capability at Capital One Financial. Despite the rhetoric that organizations need to be more flexible and adaptable to meet the demands of change, globalization, competition, and innovation, few organizations have been able to muster neither the organization designs necessary to support flexibility or the orchestration capabilities to ensure that change can be routine. Capital One has met both of those criteria and we describe their journey toward adaptability.

For organizations seeking to develop a change capability, the Capital One case yields three practical learnings. First, organizations must consciously decide to increase the amount of change-related skills and knowledge in the organization. Second, they must implement supporting organizational systems and structures, and third, they must engage in and learn from change. Only by embracing change as a normal part of organizational functioning can they build the social capital necessary to make change a competitive advantage.

Building a Change Capability at Capital One Financial:

Separating Rhetoric and Reality

In an era when environments are changing faster and faster, the rhetoric on organizational effectiveness is clear: successful organizations must be more agile and adaptable. Redesigning work processes, integrating acquired businesses, implementing large-scale IT systems, and entering foreign markets are a few of the challenging changes companies are implementing. Any one of them can prove very difficult to accomplish - most estimates put the success rate for a large-scale organization change at about 25-30 percent – while successfully implementing several of them in a short time period is virtually impossible.

Capital One, the very successful financial services company, has built an organization that loves to change. It does not "manage change" as if it were some unwanted intruder, and it does not view change management as an afterthought to improve the chances of getting some key resistors to "buy into" a new initiative. Change is integrated into the way Capital One formulates strategy, structures itself, and measures and rewards performance.

Capital One created an enterprise-wide change capability to give it the ability to orchestrate a variety of changes. Matt Schuyler, the Chief Human Resources Officer, states the goal clearly: "We purposefully set out to create an organization change capability that would allow us to execute changes, both large and small, faster and more efficiently while minimizing the effect on our associates. We wanted to make change management a core competency at

Capital One, one that enables and supports our business strategy." Partly because of its change capability, Capital One is proud of having changed the rules of the game in the financial services industry and bullish about its ability to remain successful in the future.

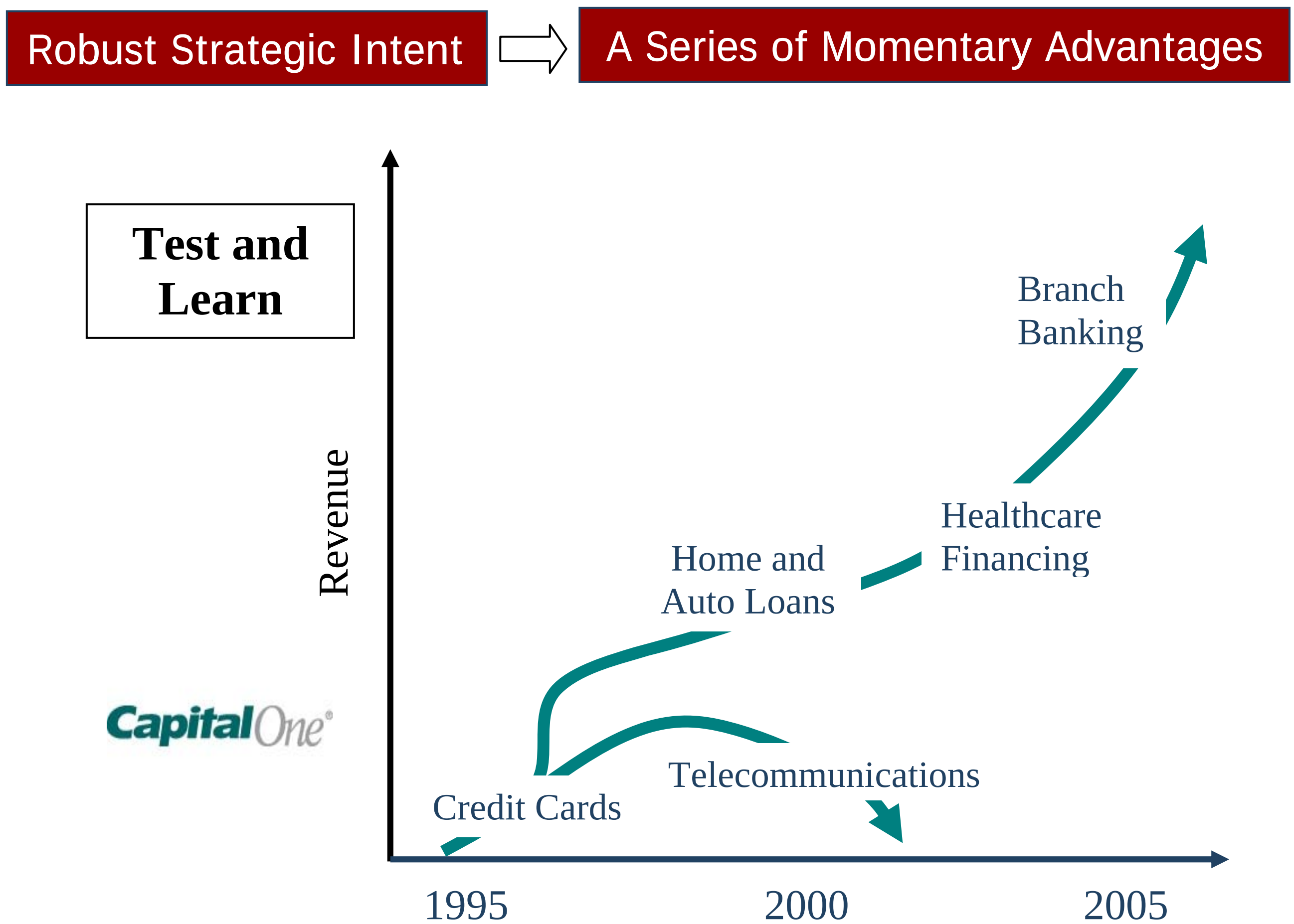
Capital One Financial – Creating a Built to Change Organization

Capital One's founder and CEO, Rich Fairbank, was the first to see and believe in the logic and power of marrying information technology and rigorous analytic programs to uncover market opportunities. When he joined Signet Bank, he got a chance to pilot his information-based approach. In 1993, Signet tested the assumption that people were dissatisfied with carrying high interest credit card debt. They offered a targeted group of customers the opportunity to transfer their credit card balances to a Signet credit card at lower interest rates. The enormous success of this campaign and the promise of the information-based approach encouraged Fairbank to lead Capital One's spin off from Signet.

Since going public in 1994, Capital One has expanded the credit card business, entered the auto loan and home mortgage businesses, grown internationally, and most recently acquired two traditional banks (see Figure 1). They have also weathered unsuccessful ventures into telecommunications and vacation property management. The organization's return on investment is over 1368% since its founding, it employs 31,800 people, and in 2007 had revenues of more than $12 billion.

Figure 1

Evolution of Capital One's Strategy and Revenues



Capital One's organizational approach puts change at the core of its identity. Research suggests that "built to change" organizations have a strong focus on the future, use a robust strategy to generate a series of momentary competitive advantages, and leverage flexible organization features (Table 1). They also build-in the capability to implement and orchestrate major changes.

Table 1

Elements of a Built to Change Organization

Built to Change Feature	Definition	Capital One Dimensions
Strong future focus	Improve the chances of success by spending more time thinking about the future - give potential future scenarios equal weight in current strategic decision making	Dedicate a large percentage of analysts' time to thinking about future trends and their implications on a line of business
Robust strategy and a series of momentary advantages	A recurring metaphor that explains a series of advantages over time	"Test and learn" strategy generates products matched to the risk profiles of consumer segments
Flexible organization design	Create empowered organizations, flat structures, flexible performance management systems	Few tiers of jobs, pay for results and competencies related to changing, reorganize frequently
Orchestration capability	Create a change capability	Building a Change Capability Project

Strong Future Focus

Capital One is obsessed with the future. Each business line has its own analysts – as high as 20% of FTEs in some cases – who are skilled at exploring future trends and how the business is likely to evolve. Instead of focusing solely on a current large customer or a set of existing strengths and weaknesses, Capital One's businesses focus on what might happen in the future and the skills and knowledge that will be needed to be successful. Fairbank has said, "Eighty percent of strategy is figuring out where the world is going, and twenty percent is figuring out what you are going to do in response. If you can figure out where the world is going, what you need to do usually becomes obvious."

According to Mike McDermott, former Director of Organization Effectiveness, "Strategic thinking goes pretty deep on two levels. On one level, the strategic planning organization runs a variety of scenarios that look several years out. On another level, the executive committee meets regularly to discuss and debate a set of annual 'imperatives' or bold challenges. The imperatives are just that…they are things that *must* be done if we are to achieve our long-term vision. The imperatives are also a good tool because they can morph and change over time – they reinforce the importance of change management." Some of the more important corporate imperatives to come out over the last several years include diversification, customer experience, and several related to human capital management.

Robust Strategies and Momentary Advantages

The information-based approach Fairbank created thrives on data, experiments, and analysis. One manager joked, "We count everything here. There's probably a spreadsheet somewhere describing the ratio of tables to chairs in the cafeteria." It results in a robust "test and learn" strategy, and it works like this. Terabytes of consumer data are analyzed statistically to generate potential risk profiles. For example, someone who responds to an invitation is less of a credit risk than someone who calls up on the phone and asks for credit. Combined with guesses about how the environment is changing, a profile or hypothesis can be tested with an offer –

interest rate, payment options, perquisites, or rewards – for credit services. Over the course of a year, Capital One's managers can conduct over 50,000 of these "tests."

When an identified risk profile and its associated offer get a response rate greater than some threshold amount, a potential momentary competitive advantage exists. The offer is broadened based on this learning and as new accounts are generated, managers must rearrange the human capital, resources, systems, and structures necessary to monetize the advantage. However, because consumer profiles, competitor behaviors, and other market forces change, any current advantage is fleeting and new ones must be identified to grow revenues. Constant change, or moving from one competitive advantage to the next, is at the core of Capital One's strategy and identity.

Flexible Organization

An agile organization is necessary to adapt quickly to new competitive advantages. Capital One's approach to creating a flexible organization begins with a hiring process that selects for people who like change. As part of the rigorous interviewing process, candidates are asked about their leadership of and learning from change. The interviewers also focus on identifying people who have a passion for excellence and collaborate well with others.

Complimenting the hiring process is an organization structure that is decentralized and fluid. Capital One managers like to say, "what gets resourced, gets done," and so the organization has traditionally relied on a few tiers of responsibility instead of multiple layers of management. This has pushed decision-making down into the organization and allowed people to take on a variety of tasks without having to worry about job descriptions and pay grades.

For example, associates can have three or four bosses in a year. Suzanne Newton, an HR Client Consultant, described her first year experiences, “All the change does take some getting used to, you really learn to develop your own ability to change. As an intern, I facilitated organization change projects and worked on the Building Change Capability project. Shortly after I became full-time, I was asked to join the cultural integration team to support our bank acquisition. It was tough to have to refocus on a narrower set of tasks and to figure out how a new boss preferred working. When Katrina hit, a whole new, but temporary team, was assembled with new leadership to help in disaster relief. It was dizzying at first, but it really helped me to understand that every shift, every change was made to align resources to the highest priority work…there’s always a line of sight.”

An adaptable performance management system completes Capital One’s flexible design. It keeps managers and associates focused on current performance as well as change. Carol Anderson leads the performance management process and notes, “One overlay to the whole performance management strategy is that the actual philosophy and core infrastructure of the program has not changed. We’ve always had a system that included 360-degree feedback and well-grounded compensation models. And importantly, there’s always been an equal emphasis on rewarding current results as well as developing and demonstrating competencies we think are important for the future.” This ongoing balance of rewarding results *and* the development of competencies allow Capital One to adjust the criteria for current performance but also encourage associates and managers to learn new skills for future success.

Figure 1 supports the idea that over time, Capital One’s robust test and learn strategy has been able to identify momentary advantages in a variety of markets and leveraged those advantages with a flexible organization. What Figure 1 does not show is the way they were able to transition from one advantage to another. That is, while the test and learn strategy can identify the advantages, and the flexible organization features allows reconfiguration of the resources and systems to support the advantage, the strategy and design cannot orchestrate the transition from one advantage to another. The missing built to change ingredient – what Capital One's organization effectiveness group saw and created – was an enterprise-wide change capability that gives the organization the ability to reconfigure itself over and over again.

Developing the Change Capability at Capital One

Events between 2000 and 2002 led to a general awareness and acceptance within Capital One that change was going to be a constant companion. In July 2000, for example, regulators imposed a memorandum of understanding requesting that Capital One increase its reserve requirements and tighten up internal control systems. The test-and-learn strategy was a novel business model, and regulators who understood (and probably preferred) more conservative approaches to financial management judged the strategy too risky. Although the strategy was centrally concerned with determining risk, it was the informal decision making process, symbolized by impromptu meetings between Fairbank and co-founder Nigel Morris, that made regulators uncomfortable. The unexpected regulator announcement sent a temporary shock through the market and Capital One's stock dropped 40% in one day.

Within days, the organization increased reserves, tightened controls, and created a more formal executive committee to review data and decisions. Although the stock price rebounded quickly, the increased cost of borrowing resulting from its damaged reputation pointed to an important strategic weakness – Capital One was too dependent on a narrow range of institutional investors. Its increasing size and related growth goals strongly suggested that the organization broaden its source of funds.

Shortly thereafter, Capital One announced a diversification imperative and as shown in Figure 1, between 2001 and 2003, Capital One broadened its product lines to include auto, home, and healthcare financing. The success of the diversification imperative led to explorations of entry into traditional consumer banking eventually leading to the acquisition of Hibernia Bank in 2005 and North Fork Bank in 2006.

Designing a Change Management Architecture

However, aggressive growth and diversification by Capital One often left associates feeling overwhelmed by the rapidly changing product/service offerings. Frequent updates in the knowledge base of associates, reorganizations that tested an associate's ability to remain flexible, and changes in work processes added to the stress. The organization needed tools, methods, and processes to help make change more comfortable and even routine.

Initial attempts to be more change ready followed the conventional wisdom of the day. In early 2001, McDermott's organization effectiveness group offered a leadership development program to 20 high potential human resource generalists. Researchers from the University of Southern California's Center for Effective Organizations delivered courses in change management and organization design. Using principles from the courses, participants conducted eight action-learning projects to demonstrate the value of a disciplined approach to change. The visible and dramatic success of these change projects created the support needed to continue the effort.

With 20 HR generalists trained in change management, Capital One could have increased its change capability by deploying these generalists throughout the organization or creating a center of excellence that line managers could draw on. However, McDermott was concerned that neither of these models provided the kind of support required by an organization where change was the norm. Something did not feel quite right.

McDermott gave voice to his discomfort by convening an informal group of HR associates and line managers interested in change management excellence. As they debated the relative advantages of the different ways to leverage change knowledge, the group worried that both approaches increased line manager’s dependency on the HR function. If an outstanding HR person was deployed to the business unit or if the business unit was able to access good talent from the center of excellence, a good change result was likely. But what if the deployed HR generalist was stronger in compensation than change management or the best internal consultants were unavailable?

The group also worried that neither of these architectures guaranteed an enterprise-wide capability. If the skills and knowledge about change were deployed to the line, there was a strong likelihood that a variety of customized change processes would develop and any accumulated knowledge and skills were unlikely to scale up to an organization-wide capability. Moreover, leveraging the assets across the corporation would still require the creation of a corporate program management office.

On the other hand, if the skills and knowledge about change were centralized in a center of excellence, change resources would be out of sight (and probably out of mind as well). Instead of building change into their thinking about strategy and organization, the organization would be rewarding managers for "calling for help" and reacting to the need for change.

A New View. The idea for an alternative change capability architecture emerged, oddly enough, from discussions about the dot.com business model of the late 1990s that gave away products and services to capture market share. What could not work in a competitive market economy had every chance of working inside an organization. The group envisioned an embedded model where line managers possessed sufficient knowledge and skills to lead most organizational changes. The model suggested giving all of the knowledge, skills, tools, and methods associated with managing change to the whole organization, not just the HR function. It involved making everyone comfortable and conversant with the processes and tools of change.

This approach deviated significantly from the deployed HR generalist and center of excellence architectures. In the group's way of thinking, Capital One needed to create "versatilist" managers. Specialists can impress their peers and solve specific problems; generalists can do many things but not very well. Versatilists excel at a particular blend of skills. Change versatilists can shorten change cycle times because they do not need to ask for help, they already possess the information and skills needed to carry out most changes on their own.

But tasking managers with change management responsibilities raised important questions. Critics in the organization argued, "Shouldn't a line manager's focus be on understanding the business, market, people, and technology challenges?" The answer, of course, is "Yes, they should." But in fast changing environments, the group argued that such knowledge is not enough. Managers need to be able to combine their business expertise with knowledge about change so that as new momentary advantages come along, the organization can shift quickly.

Such an embedded change architecture, however, implied an important assumption: the organization required a simple, standardized change methodology. Like organizations that have bought into the logic of a single, shared information system architecture, such as PeopleSoft and SAP, there is a great deal of efficiency in shared models, language, and mindsets. For any large-scale change that requires the cooperation of, say, the credit card business, IT services, regulatory compliance, and HR, all parties need to be familiar and comfortable with the same change model. If every business unit has different change management models and tools, coordinating large-scale change efforts is bound to be expensive and time consuming.

<u>Selecting a Model</u>. The grassroots group created an internal website to display and compare the different change models and tools being used in the organization. The first surprise was that Capital One was using over 17 different change models, including GE's change acceleration process, Kotter's 8-step change model, Lewin's change process, and a variety of action research models. In addition, there were more than 160 different change navigation tools, including numerous variations of stakeholder mapping processes, change readiness surveys, project planning guides, and vision development protocols.

As the grassroots group had feared, the absence of a coordinated change strategy had resulted in a broad range of change perspectives. Each practitioner defended his/her model and tools as “best practice.” During one video conference call to discuss the models, the group began to understand and struggle with the criteria for an acceptable model. An internal consultant presented a “best practice” change model to the group noting that it had worked for several years within the Capital One organization. The group began to ask questions to support the best practice claim. “In what other organizations has this model been applied successfully?” (Answer: none) “What studies have been done or articles have been written documenting its effectiveness?” (Answer: none)

Two events pushed the group toward consensus. The first event was the identification of a change methodology that no one in the organization was using. In her Internet searches, Teresa Spinicci, a consultant in the organization effectiveness group, found the change management model developed by Prosci’s Change Management Learning Center. This methodology centered around the ADKAR model that suggested successful individual and organization change followed a process of 1) creating *awareness* of the need for change, 2) having the *desire* to change, 3) possessing the *knowledge* to change, 4) having the *ability* to change, and 5) being *reinforced* for change. The methodology was simple, easy to understand, had a case database to support claims of “best practice,” and supported the principles from the USC training. This event helped to overcome the win/lose dynamics of picking one model over another. Although each member in the grassroots group may have believed their model was best, they agreed that all of the models were more similar than different.

The second event was more a function of serendipity than conscious planning. At about the same time that the grassroots group was debating models, Capital One had initiated a process called Achieving Competitive Economics (ACE) to understand the requirements of being a world-class financial services organization.

Steve Arneson, a human resources senior vice president and ACE leader, needed help managing the HR-related change initiatives expected to come out of the ACE process, so he went to the website to find some ideas. What he found was lots of tools but no help. The site, reflecting the state of the group's progress, was full of change management models and tools with no taxonomy to sort them out. Arneson saw clearly the need for a single, organization-wide change model, and he encouraged the grassroots group to identify it.

Implementing the BCC

The pressure from Arneson's ACE group and the discovery of the ADKAR framework pushed the mostly informal effort into the mainstream. During the 2005 planning cycle, the Building a Change Capability (BCC) project was formally endorsed as an HR imperative. This legitimacy provided the project with the management attention and resources required for implementation.

Spread the Word. During 2005, Capital One offered two change courses through its corporate university. The two-day certification course – attended by both managers and staff – went deep into the change methodology. A key feature of the course was the opportunity to apply and use the model on real-life change projects brought by class participants. This helped to teach the concepts, gave the participants practice with the model, and actually drove change in the organization.

The second course was a one-day program specifically designed for line managers. It provided an overview of the methodology and linked change management behaviors, such as "describes and explains change clearly and constructively," in the organization's competency models to the organization's values of "communication." This helped managers see the connection between the BCC project and the performance management system. By leveraging the existing resources and capabilities of Capital One's corporate university, it was possible to quickly build common change-related skills and knowledge.

A major makeover of the grassroots group's original website also helped spread the word about change in the organization. A key feature of the ADKAR process that attracted Capital One was the availability of and support for a variety of web-based tools, case studies, and webinars. The new change management portal featured best practice case studies and research findings; assessment tools to diagnose organizational features, resistance, or training needs; and templates to help managers develop change and communication plans. It also contained a variety of Capital One generated PowerPoint presentations that provided an overview of the ADKAR methodology, why it was important, and how to use it.

Transfer Knowledge and Skill. The BCC project set the goal of *eliminating* all FTEs in the HR organization committed exclusively to change management efforts. The focus of the BCC effort was *not* on providing change management resources to projects but on distributing the capability throughout the organization. Exemplifying the managerial attitude the embedded model was hoping for, Judy Pahren, an Operations VP in the card business and one of the first managers to go through the training said, “People know I know this stuff and I’m always getting calls from other line managers to think through a change issue. I consider it part of my job.”

The BCC project targeted several visible, large-scale change demonstration projects and created an internal “buzz” for the methodology. It supported the change initiatives coming out of the ACE process described above, a large-scale systems conversion project, an HR reengineering effort, and a workplace redesign process called the Future of Work. In general, they targeted projects where a “don’t teach it, use it” approach could be applied.

For example, the Future of Work project involved shifting the physical workplace from “cube farms” to “neighborhoods” and to virtual work approaches. Associates changed to shared spaces and mobile personal productivity technologies, such as laptops, PDAs, and instant messaging, to support flexible work schedules, telecommuting, and virtual meetings. Managers were guided through the change methodology in a very deliberate fashion, and it was made clear that the successful implementation of the change depended on their active support and sponsorship, including diagnosis, communication, financial support, training, and execution. Leading the process through hands-on application embedded the change management capability in the manager’s skill set.

<u>Adjust and Align the Systems</u>. The BCC project worked closely with Carol Anderson’s performance management team to measure and reward competencies related to change management. At the time that the BCC was gaining critical mass, Anderson’s team was working to revise the rating process as well as updating the competencies. Local champions, in the form

of senior VPs who represented their line of business, were made a part of the performance management design team. The design team increased the number of change-related behaviors in the competencies and highlighted them in the training on the change methodology as described above. This sent a clear message about the importance of these behaviors for the future. The champions were able to reinforce the importance of the new behaviors in the implementation of the performance management process and provided important synergies for the BCC implementation.

Today, Capital One managers believe that meeting aggressive but achievable goals requires them to lead change and build new operational capabilities. Achieving results – which accounts for 50% of their appraisal score – requires that managers drive change in their organizations. Reflecting this, one manager remarked, "If I lead change in the group but leave my people behind, I'm not doing my job and my bonus is at risk." The other 50% of the appraisal score is on the extent to which associates and managers are demonstrating the values and competencies of the corporation.

The performance management system's consistent balancing of current results and competency demonstration is critical. It reinforces the belief that results cannot be achieved without change.

From Capability to Advantage

Capital One's development of a change capability is a way to bridge what we call the change rhetoric-reality gap. At the core of this gap is the observation that getting people to rally around a specific change is easier than getting an organization to commit to being more agile.

All too often, organizations say they want to be innovative, but invest in a new product development initiative that yields one good idea and then fades away; they say they want to be flexible, but invest in six-sigma processes that promote efficiency and predictability and stifle creativity. In each case, the intention to be a more agile organization is thwarted by a change effort that more often than not contradicts their intent.

In building an enterprise-wide change capability, Capital One used specific change projects to create an integrated, embedded capability that complemented Capital One's organization design and strategy. Capital One's change capability marries a business leaders' intimate knowledge of technology, markets, and customers with the processes of change. The specifics of the business and the resources that leverage a momentary competitive advantage are what drive the capability. When the process of change is integrated with the content of the business, it creates an organization that delivers both current performance and future results. It creates an organization that loves to change. When we look back at the development of a change capability at Capital One, three important lessons emerge about how to turn a change capability into a competitive advantage.

Change-related Human Capital. An organization's capabilities are built on resources, such as knowledge, skill, physical assets, and intellectual property, as well as processes and routines that coordinate action and behavior. The knowledge and skills underlying most traditional capabilities are technical, economic, and marketing related. As a result, most organizational capabilities drive new product development, supply chain integration, or lean manufacturing.

If an organization wants to develop a change capability, it must signal that commitment by increasing the level of change- related skills and knowledge in the organization. To develop a bigger reservoir of change management skills and knowledge, it is important to invest in everyone's knowledge related to change.

Creating a Change Architecture. Capabilities are supported by organization design elements – structures, policies, and systems – that provide an architecture within which to operate. Capital One rejected the traditional corporate staff center of excellence approach and the deployed human resource generalist model. It created a third option - the embedded model that integrates change, strategy, and organization design.

The adoption of a simple but standardized model was directly related to implementation success and the ease with which the organization built its change-related human capital. A common framework allows change agents, change leaders, and change participants to share a common language and learn similar skills. It increases communication efficiency, the speed of change, and organizational integration.

Experience Builds Social Capital. Organizational capabilities, and especially change capabilities, do not come fully developed and ready to go, nor do they exist in a vacuum. Organizations must have experience with behaviors to build up the deep and often tacit knowledge that underlies a capability. If the organization has no conscious experience with change, then it cannot have a change capability.

Early on in the change capability effort, there was a focus on small but visible change projects. Using the “don’t teach it, use it” approach, and in the classic tradition of organization development efforts, the early efforts transferred knowledge and skill to the line managers and built capacity for change. In addition, the learnings from the change efforts, were carried forward into subsequent change efforts through postings on the change management portal, learning events among managers and change consultants, and perhaps most importantly, conversations among the managers who worked with each other to solve change problems.

Conclusion

Like a muscle that gets better with exercise, Capital One’s change capability got more sophisticated as it was applied to more and more issues. The change methodology was originally applied to local and then broader change issues; from physical office arrangements to call center closings to system conversion projects. Eventually, the ability to change became an important reason to adopt strategic imperatives. Currently they are leveraging the change capability to implement their customer experience imperative.

Organizations that are good at change, not surprisingly, engage in lots of change. At Capital One, the implementation and success of its change capability has left it with the feeling that “We can take on more change because with this new muscle, it doesn’t seem like we are changing all that much. It feels like we are changing less because we are capable of handling more change than most organizations.”

Organizations must carefully think through the calculus of investing in a change capability vs. buying the capability when it is needed for episodic change. For some organizations, the investment may not be worth it. But in fast-changing industries, the shift in economic logic – from execution and stability to changeability – may provide the impetus – as it did for Capital One - to see an internal change capability as the "missing ingredient" in organizational effectiveness.

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Built to change organizations are based on a variety of organization design principles. Jay Galbraith's *Designing Organizations* (San Francisco: Jossey-Bass, 2002) is one of the most popular overviews of the field. In addition, other articles and books contribute more specialized knowledge about certain features in organizations. For example, Ed Lawler's *Talent* (San Francisco: Jossey-Bass, 2008) speaks directly to the issue of managing people and building a flexible workforce. Mary Jo Hatch has done great work on integrating organizational culture with brand, image, and reputation to describe organizational identity (M. Hatch and M. Schultz, "The Dynamics of Organizational Identity," *Human Relations* 2002, 55, 989-1018). Finally, we

were very interested in how Tom Friedman (T. Friedman, *The World is Flat* (New York: Farrar, Straus and Giroux, 2006) picked up on the idea of a versatilist in the second half of his book on globalization.

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