

# THE INFORMATIONAL SYSTEM AND THE MANAGEMENT OF ENTITY

**Boghean Florin**

*Faculty of Economic Sciences and Public Administration, University of Suceava, Universitatii Street, no.9, 720225 Suceava, Romania, Phone: ++040230520263, Fax:++40230520263, E-mail: www.florinb@seap.usv.ro*

**Boghean Carmen**

*Faculty of Economic Sciences and Public Administration, University of Suceava, Universitatii Street, no.9, 720225 Suceava, Romania, Phone: ++040230520263, Fax:++40230520263, E-mail: www.carmenb@seap.usv.ro*

*Abstract: A decision is a judgment. It is a choice among alternatives. It is rarely a choice between good and bad. In the best case it is a choice between “almost good” and “probably bad”. In the best case it is a choice between two action directions of which none can say it is closer than the other one of what is good. Our demarche is included on the line of granting the decision maker with the most important weapon, information. In this paper, I tried to emphasize those instruments that help the manager in carrying out the performance criteria in the conditions of global economy. The complexity of the economic activities in competitive conditions imposed by the market economy determines the growth of the role of the economic-financial information in taking decisions. The quality of the current decisions and those taken on long term and also the results predicted by the entity depend on the quality of information.*

*Key words: managerial accounting, decisional processes, information, control systems.*

## **Systems of managerial control**

A system of managerial control is a method of gathering and using information in order to support and coordinate the planning and control decisions as part of an organization and for guiding the behavior of managers and employees. The system of managerial control gathers and presents information for the managerial control at different levels:

1. The general level of organization- for example, the stock exchange course, net profit, the investments profitableness, the exploitation treasury flow, the total number of employees, the control of pollution and community contributions.
2. The consumer's level/ of market- for example, the consumer's satisfaction, the necessary time for answering the consumers' requests for certain products and the cost of competitive products.
3. The level of individual production means- for example, the costs of raw materials, labor costs, the rate of absenteeism and accidents in certain divisions or economic functions (such as research and development, production and distribution).
4. The level of individual activity- for example, the necessary time and costs afferent to receiving, stocking, assembly and coordination with the goods from a warehouse the proportions of rejects, the break downs and the number of processed units repeated on a line of production, the number of selling operations and the income per employee in sales, the number of deliveries per employee at the distribution centers.

As these examples indicate, the managerial control systems collect financial information (for example, the net profile, the costs of the raw materials and the stocking costs) and non financial information (for example, the necessary time for answering the clients' changes, the rate of absenteeism and accidents). A part of information, such as the net profit or the number of deliveries per employee, is obtained from inside the company. Another part, such as the stock exchange course or the costs of the competitive products, is obtained from outside the company. Some company's present non financial and financial information in a single report named *balanced board panel*.

The managerial control systems refer to formal and informal control systems. The formal managerial control system of an entity includes the settlements, procedures, performance indicators and motivation

plans that determine the managers and employees' behavior. The formal managerial control system is made of several systems. The system of management accounting is a formal accounting system that offers information regarding costs, incomes and profits. Other formal control systems are the human resources system, which offers information regarding the personnel recruitment, training, absenteeism and accidents such as the quality systems, that offer information regarding rejects, break downs, repeated processing and late deliveries to clients.

The informal managerial control system includes aspects such as common values, mutual obligations of the company members, its culture and unwritten norms regarding an acceptable behavior from the part of the managers and employees. Examples of slogans of a company meant to strengthen the values are:

“To us, quality is the number 1 task” and “The low prices are only the beginning”.

### **The evaluation of the managerial control system**

On order to be efficient, the managerial control systems must be tightly related to the company strategies and objectives. Different examples of strategies develop innovative products in order to increase the market quota in the key segments or the maximization of the short term profit through reducing costs and giving up on long term risky investments in research and development. Let us imagine that management decides, in a wise way or not, to maximize the short term profit. In this case, the managerial control system must support this objective. The control system should offer managers information, such as the marginal contribution for each product, in order to help them take short term decisions. Also, the control system should establish the bonuses obtained by managers according to the short term profit.

The managerial control systems must be projected in order to be in conformity with the entity structure and managers' responsibility to take decisions. For example, the situation of the manager responsible for the research and development department of a pharmaceutical company. In his case, the managerial control system should put the accent on certain research and development activities that re necessary for certain projects, on the necessary number of specialists, on the dates programmed for the conclusion of different projects and on the elaboration of reports through which are compared the effective results with the budgetary ones.

In continuation, we will analyze the case of a manager of operational level responsible with the production, selling and distribution of food products. The managerial control system of his entity should offer information about the clients' satisfaction, the market quota. The costs of production and profitableness of the production line, information that helps the manager plan and control better the operations. The manager of the production line needs totally different information from those necessary to the manager of the research and development department of the medicine company. Still, in both cases, the information offered has the purpose of helping the manager in the decisional process.

The efficient managerial control systems should also motivate managers and employees. The motivation is the desire to reach a certain objective (the aspect of purpose agreement) combined with the ulterior tracking of that objective (the effort aspect).

The purpose agreement appears when individuals and groups work in the direction of reaching the objectives of the organization, meaning the managers that work in their own interest, undertake actions according to the general objectives of the superior management. For example, in the budgeting of the capital expenses, taking decisions based on the bringing up to date the long term treasury flows at the requested rate of profitableness leads to the closest results to the objective of the entity. But if the managerial control system evaluates managers on the basis of short term profit according to the cumulative accounting, the managers will be tempted to take decisions that maximize the profit of the cumulative accounting, but which do not correspond to the long term interests of the organization on the whole.

The effort represents the actions undertaken on order to reach a certain objective. This is more than a physical effort, such as a worker's effort to produce in amore alert rhythm and includes physical and intellectual actions.

The managerial control system motivates managers and employees to make efforts through a variety of rewards related to the reaching of objectives. These rewards can be financial (under the form of money, company shares, the use of a company car or the quality of a club member) or non financial (such as the power and the pride to work for a successful company). The managerial control systems must be according

to the organizational systems. An organization that has a decentralized structure has an extra element that must be taken into consideration, meaning the efficiency of the managerial control system.

Decentralization is the freedom to take decisions, which is given to managers from all the inferior levels of the organization. Autonomy refers to the degree of freedom in taking decisions. The greater the freedom is, the greater is the autonomy. As we talk about aspects related to decentralization and autonomy, we use the term subunit in order to refer to each part of the organization. Decentralization gives managers and employees the right to undertake decisive actions.

Total decentralization means minimum constraints and maximum freedom to take decisions for managers situated at the lowest levels of the organization. Total centralization means maximum constraints and minimum freedom to take decisions for managers situated at the lowest levels of the organization. The enterprises structures are situated somewhere in the middle of these two extremes because there are benefits and costs afferent to the decentralization.

Which is the best degree of decentralization? Managers try to choose the degree of decentralization that maximizes the benefits in comparison with costs. From a practical point of view, the superior management rarely quantifies the benefits or costs of decentralization. Still, the cost - benefits approach helps concentrate on problems. The supporters of the taking decisions decentralization process and choosing responsibilities by the subunits managers identify the following benefits (Marchand, D.A. 2000):

1. It increases the sensibility towards the local necessities. Good decisions can not be taken without good information. In comparison with the superior managers, the subunit managers are better informed regarding clients, competitors, suppliers and employees, and also in which concerns the local factors that affect performance, such as the reduction method of costs and quality improvement. There can also be identified two advantages of decentralization: the improvement of the company knowledge related to market and the improvement of clients attendance.
2. It leads to gains thanks to the acceleration of the taking decision process. Decentralization accelerates the taking decisions process generating an advantage in the competitive area in comparison with the centralized organizations. Centralization slows down the decision process as the responsibility for decisions increases form one level to the other on the organizational structure.
3. It increases the motivation of the subunit managers. The subunit managers are more motivated when they can put into practice their own initiative: "Decentralization= Creativity= Productivity".
4. It supports the development and learning at a managerial level. Through the distribution of more responsibilities to managers there can be made groups of experienced and talented managers that can meet the responsibilities at a higher managerial level. In this way, the company can also determine who do not have the necessary managerial qualities. The decentralized units offer an environment of training for the general managers and a transparent confrontation environment of the best ideas concerning the product.
5. It increases the concentration of the subunit managers. The manager of a subunit of small dimensions concentrates better in a decentralized environment. A small subunit is more flexible than one of large dimensions and can adapt faster to the opportunities that are always changing on the market. Also, the superior management, exempted from the burden of the daily operational decisions, can offer more time and effort for the strategic planning oriented towards the organization as a whole.

The supporters of a more centralized decisional process (Charles T. Horngren, 2006) identify the following costs afferent to the decentralization of the decision process:

1. Suboptimal decision process (named also non congruent or non functional decision process) which appears when the benefits obtained by a subunit after some decisions are exceeded by costs of the benefit losses for entity. This cost is registered because the superior management renounced at the decision process.

A suboptimal decision process can appear when:

- a) It lacks harmony or congruence between the general purposes of the entity, the purposes of subunits and the individual ones of the decision factors or
- b) The subunit managers are not informed about the effects of the decisions on other behaviors of the entity.

The suboptimal decisions are taken mostly when the subunits of the entity are mostly interdependent, like in the case in which the final product of a subunit is used or sold by another subunit. For example, a production manager evaluated on the basis of production costs may not respond to the request from the part of the marketing department to program an urgent order for a certain client if the production program changes and that will lead to the increase of the production costs. Still, from the point of view of production, the supply of that product to the client can be preferable for the reason that the client is ready to pay a higher price, and also from the point of view of the company, which expects this client to make many other orders in the future.

1. The manager's attention focuses on subunits and not on entity, on the whole. The managers of certain subunits can be considered in competition with the managers of other subunits of the same entity as they were competitors from the outside. In consequence, the managers can be reticent in which concerns the partitioning of information or offering help when another subunit faces an emergency situation. Also, the subunit managers can use in their own interest the information they have referring to the local conditions and not for reaching the entity objectives. For example, they could request from the mother enterprise more resources than they need in order to reduce the effort they must make.
2. The costs afferent to the information gathering increase. Managers can spend too much time obtaining information about the subunits of the entity in order to coordinate their activities.
3. It is reached a duplication of actions. More subunits of the company can develop the same activity separately. For example, there can appear a duplication of the personnel functions (accounting, human resources, judicial aspects) if an entity is strongly decentralized. The centralization of these functions helps with the strengthening, organization and the reduction of the resources necessary for these activities.

In order to choose an organizational structure that can implement the strategy of an entity, the superior managers must compare the benefits and costs afferent to decentralization. Often, this comparison must be made for each function. For example, the function of the financial inspector can be extremely decentralized in other purposes (such as the management of receipts from accounts and the development of strategies for the profit taxation). The budgetary decentralization and that of report allows the subunit marketing manager, for example, to adapt the already made report to the specific information that he needs in order to take better decisions an increase profit. The centralization of the profit taxation strategies offers the organization the possibility to balance the profit obtained by a subunit with the losses registered by another subunit in order to evaluate the impact on the organization.

The carried out studies put into evidence the fact that the majority of the decisions taken at a decentralized level and less at a corporative level, are those that are related to provisioning, to the range of products and promotion. In these compartments, the subunit managers must take fast decisions on the basis of local information. The decisions related to the type and the long term financing source are often taken, and not so often at a decentralized level. In these cases, the managers have better information about the financing conditions on different markets and can obtain the best interest rate. The decentralization benefits are in general bigger when the entities face uncertainties in their activity area, situations that request a good knowledge of methodology and less interdependency between divisions.

In order to measure the subunit performances in the centralized and decentralized entities, the managerial control system uses a type or a combination from the four types of responsibility centers:

- Costs center- the manager is responsible only for costs
- Income center- the manager is responsible only for incomes
- Profit center- the manager is responsible for costs and incomes
- Investment center - the manager is responsible for investments, incomes and costs.

A wrong conception that can be observed in the majority of cases is the conception that a profit center and in certain cases an investment center is the synonym of a decentralized unit, and a cost center is the

synonym of a centralized unit. The profit centers can be combined with a strongly centralized organization and the cost centers can be combined with a strongly decentralized organization.

For example, the subunit managers of a division organized as a profit center can have less freedom in taking decisions. They could be obliged to request the agreement from the central head office for each expense that exceeds let us say 10.000 euro and can be obliged to make what the personnel desires at the head office. In other entities, the divisions can be organized as cost centers, but their managers can have great freedom in which concerns the capital expenses and the choice of the services and raw materials sources. Shortly, the denominations of “profit centers” and “cost centers” are independent from the centralization or decentralization degree of a company.

## Conclusions

The management of the activity of an organization implies the carrying out of a decisional process whose complexity is determined by the hierarchic level on which is situated the responsible human factor and the necessity for documentation and substantiation of that decision. Costs represent a key element in the management of the economic systems.

Information is a product of the human mind, is the fundamental capital, the central cost and the essential resource of economy (P. Drucker). That is why, for the development of the management control it is necessary the study of the relation between information and decision. The relation between these two elements can take different shapes, according to the decisional universe in which is situated:

1. As part of the cybernetic vision on enterprise, “the decision is taken according to information; the most important thing is to improve the information offered to the decision maker” (H. Loning, 1998). This postulate is based on:
  - The informational determinism – the information determines and explains the decision;
  - Sequentially – the information precedes the decisions;
  - Pertinent information- according to the reality
2. Reality is not something exterior, but it is a construction, because the observer is part of what he observes: this vision bears the name of constructive paradigm. In this case, “to decide means to produce the possible and the impossible”.

Essential in the process of decision elaboration and the post-decision analysis, accounting introduces evaluation instruments of the enterprises performances. It is possible and necessary the improvement of the accounting information qualities, with influences on the decisional act, in this sense we can underline:

1. The five phases of the decision process are: information gathering, the prevision establishment, the choice of an option, the application of decision and the results analysis.
2. In order to be significant in which concerns taking a decision, a sale or an expense must satisfy two conditions: a) must be a future sale or expense and b) the total amount must depend on the decision.
3. The decision criteria can be quantitative and qualitative. The quantitative criteria are expressed through numbers. Some can be expressed in monetary units, others not. The qualitative criteria, such as the employees’ mood can not be measured through numbers. The decisions must be based on these two criteria categories.
4. The unit costs can mislead the decision factors in two ways: a) when the unit costs include the expenses that are not significant for the examined decision and b) when the unit costs calculated with different volumes of production is compared. The fixed unit costs are often misinterpreted as variable costs. It is suggested the use of total costs rather than the unit costs in order to analyze the elements of a decision.
5. There are often met two traps when the significant expenses are studied: a) to believe that all the variable expenses are significant and b) to believe that no fixed expense is significant.
6. The opportunity cost represents the loss of gain that results from the fact that we give up to allocate a limited resource to an alternative operation. The notion of opportunity cost appears when a resource may have different utilizations and when we renounce to some of them. The opportunity cost that must be included in the significant costs in which concerns a certain

decision represents the net profit of the best utilization of the resources in the lack of taking that decision.

7. For choosing from more products under the capacity constraint, the decision factors must privilege the product for which the reserve per unit of the factor is rarely maxim.
8. The sales and expenses established for the future are the only ones that must be significant in taking decisions. The accounting net values of the equipments represent the expenses of the past. It is not significant in taking the decisions of renewing these equipments.

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