ACCT30002: Enterprise Performance Management Summaries

Lecture 1: Introducing organisations, strategy and management control systems

Explain the concepts of management accounting and control

"*Management accounting is the process of gathering, summarising and reporting financial and non-financial information used internally by managers to make decisions*".

Management control information has evolved to include a broader scope of information than a traditional management accounting definition to include external information (markets, customers, and competitors), non-financial information (processes), predictive information, as well as informal personal and social controls.

Management accounting and controls are essentially about *managing* the organisation. This information might be required to direct resources, consider investment opportunities, manage and evaluate risks, evaluate performance of managers and sub-units, evaluate and improve production and service delivery performance, improve quality, meet customer expectations, evaluate customers and suppliers, and develop suitable incentives.

Ultimately, management accounting and control information helps in the management of organisations through:

- Directing behaviour (e.g. through the use of performance measures, incentives, bonuses and rewards.)
- Providing a mechanism for information provision and therefore facilitating decision-making (e.g. providing cost information for pricing decisions) and/or influencing decision making (e.g. advising on strategy)
- Providing feedback on performance across the organisation (e.g. formally in performance appraisals)
- Facilitating learning (e.g. getting better at what we do.)

Organisational Control

Organisational control is the process of influencing the behaviour of people as members of a formal organisation to increase the probability that they will achieve the organisation's goals. Organisations require control because they consist of people with different interests, tasks and perspectives. The efforts of people require integration and directions and this, in turn, creates a need for control. The larger the number of people in an organisation, the greater the need for some form of organisational control mechanism.

Four functions of control

In order to motivate people to behave in ways consistent with organisational goals, control systems must perform 4 related tasks –

1. Motivate decisions and actions consistent with organisational objectives (GOAL EMPHASIS)

Goal emphasis is about motivating people to make decisions and take actions which are consistent with organisational objectives ("goal congruence"). Personal goals = organisational goals.

Without control systems, people take actions or make decisions designed to fulfil their own needs rather than the organization's goals. For example, the organization may be concerned with cost control while an individual is tempted to travel first-class.

2. Integrate the efforts of several different parts of the organisation (ORGANISATIONAL INTEGRATION)

The control system must encourage integration of different parts of the organisation, otherwise problems may be caused by a lack of co-ordination ("silos").

Even when people are trying to act in the organizations' best interests, they may find themselves working at cross-purposes. For example, a sales unit may want to offer a customer expedited delivery to make a sale, while from manufacturing's perspective, this may mean a 'rush order' which disrupts carefully designed production schedules and causes inefficiency.

3. Provide information about the results of operations and people's performance (AUTONOMY WITH CONTROL)

This refers to the decentralisation of day-to-day operations (freedom of lower level managers to make their own decisions without having to have every decision reviewed) while simultaneously ensuring the organisational objectives are met.

This permits managers to run their habitual operations as they wish and to evaluate the results of their decisions and actions, thus giving managers a lot of autonomy (the degree of freedom and discretion given to an employee over his or her job) while still allowing top management to control the overarching goals and strategy of the organisation. The control system must provide useful information about the results and performance of the organisation.

4. Facilitate the implementation of strategic plans (IMPLEMENTATION OF STRATEGIC PLANNING)

A function of control systems is to facilitate the implementation of strategic plans and the planning process (component of a control process.)

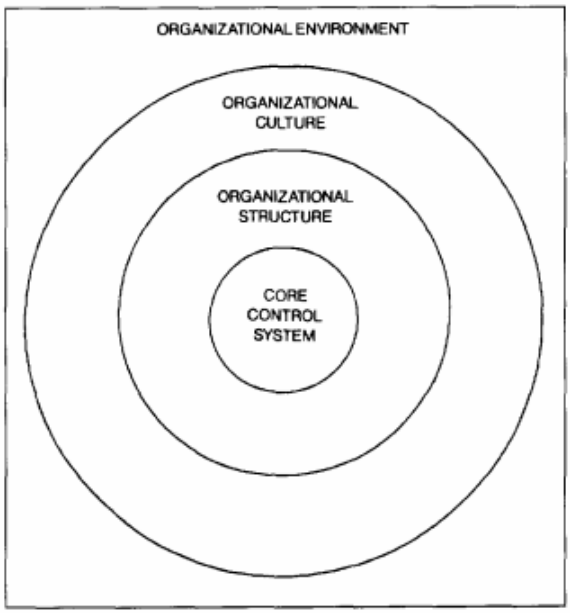
Many organizations complain that 'strategic planning does not work'. Many organizations mistakenly believe that planning is complete when a written plan has been developed. Unfortunately, this is merely the end of the beginning, and an effective control system is required if plans are to be fulfilled.

Organisational control system and the Core Control System

It is a set of mechanisms – both processes and techniques – which are designed to increase the probability that people will behave in ways that lead to the attainment of organisational objectives. The ultimate objective of an organisational control system is not to control the specific behaviour of individuals, but to influence them to take actions which in their judgement are consistent with the organisational goals.

Depicted below is a Framework for an Organisational Control System.

The inner-most circle is called the Core Control System. It consists of 5 subsystems (planning, operations, measurement, feedback, and evaluation-reward). The CCS focuses on any aspect of human behaviour which has to do with the attainment of organisational objectives (e.g. acquisition, allocation, utilization, development, conservation, or disruption of organisational resources).



The 5 sub-systems of the CCS

1. The Planning Sub-System *is the process of deciding about the objectives and goals of an organisation (and members) as well as the means to attain those objectives' goals* (an objective is a broad statement about things an organisation wishes to achieve in a given performance areas, like markets, products, personnel, financial results, etc, and goals represent the quantitative level of aspiration sought to be attained for a given objective – e.g. a financial objective may be to 'earn a satisfactory return upon net assets employed in the business' and the goal might be '18% ROI'). Goals may be used to establish desired performance levels, to motivate performance, and to serve as a benchmark against which actual performance can be assessed.

2. The Operational Sub-System *refers to the on-going system for performing the functions required for day-to-day organisational activities*. It can refer to any level of organisational analysis: individuals, teams, departments, divisions, the total enterprise, etc.

3. The Measurement Sub-System *is the process of assigning numbers to represent aspects of organisational behaviour and performance.* It includes the accounting system with its measures of financial and managerial performance, and non-financial measures including production indices such as scrap rates, capacity utilisation and product quality (reject ratios) as well as social accountability measurements. Numbers generated may be used to monitor the extent to which goals and standard have been achieved, so that the organisation may be provided with corrective and/or evaluative feedback. In addition to this, the fact that something is the subject of measurement tends to influence the behaviour of people in organisations – thus measurement itself is a stimulus.

4. The Feedback System consists of information about operations and their results. 2 types: *corrective* and *evaluative*. Corrective feedback is information about the performance of the operational system which is designed to help adjust operations in order to improve performance. Evaluative feedback is information about how well the operational system is doing. It provides a basis for performance evaluation as well as the administration of rewards.

5. The Evaluation-Reward Sub-System *refers to the mechanisms for performance assessment and the administration of rewards.* Evaluation involves assessing the performance of individuals or groups in meeting organisation goals, and the measurements of performance commonly used are accounting measures such as budgets and standard costs. The evaluation process determines how rewards shall be administered to people. Rewards can be *intrinsic* (e.g. the task is interesting) or *extrinsic* (e.g. they will be praised/paid). The purpose of rewards offered by a control system are to motivate people to behave in ways which will helps attain organisational goals, to reinforce positive performance, and to modify negative performance.

Organisational structure also functions as a control mechanism by specifying the behaviours expected from people in the performance of their roles and by specifying the authority and reporting relationships of the entire set of roles which comprise the organisational structure (e.g. the degree of decentralisation, functional specialisation, degree of vertical or horizontal integration, span of control, etc).

Organisational culture *is the set of values, beliefs, and social norms which tend to be shared by its members and tend to influence their thoughts and actions*. It refers to the broader values and normative patterns which guide worker behaviour practices and policies.

Distinguish between formal and informal planning and control mechanisms

The difference between formal and informal planning is that formal planning has objectives which are well stated, procedures that have been put in place to be followed, is structured and there are explicit rules. Informal planning does not have any rules and regulations. They include things like shared values, mutual commitments, corporate culture, and unwritten norms about acceptable behaviour.

FORMAL (Formal systems include explicit rules, procedures, performance measures, and incentive plans that guide the behaviour of its managers and employees)
Formal budgeting and planning processes; customer profitability analysis; idea brokers; cost system data for costing, pricing, product and customer profitability analysis; Activity-related analysis for improved process management; strategic-related data collection to assist with decisions (outsourcing, capital investment, involvement in strategic alliances and collaborative ventures; formal evaluation procedures of units and managers; incentive programs and reward system structures.

INFORMAL (Informal systems include shared values loyalties, and mutual commitments among members of the company, corporate culture, unwritten norms about acceptable behaviour)
Informal meetings and social work settings; practises such as observation/copying and employee engagement that permeate the organisation; Recruitment and hiring practises that might result in seeking new employees more suited to the existing culture; feedback processes which may include consultations or informal meetings; employee development and organisational learning practises; Cultural and belief systems; cultivating a culture to promote quality; employee development and training to emphasise importance of service, etc..

Explain the concepts of incentives, sustainability and risk as they effect the contemporary organisation

Do incentives improve performance?

- Bonuses are used to direct and motivate the behaviour of managers
- Incentives by government to influence organisation and individual behaviour (carbon tax)

Different forms of risk

- Competitive: Probability of loss from a decline in a firm's competitiveness (Nokia and Apple)
- Operational: The risks a company or firm undertakes when it attempts to operate within a given field or industry (BP oil spill)

Wherever it may emanate from, the end result is usually an impact on the reputation of the organisation

Sustainability

- *Environmental* (Resource usage and management including: water, energy, emissions and more generally, the carbon footprint for which the organisation is responsible)
- *Social* (impact of organisation on local community; OH&S)
- *Ethical* (labour and work practises)

Describe the key contingent factors influencing the nature of the management accounting and control system in an organisation and the key influences on control system design

Contingency theory is a class of behavioural theory that claim that there is no best way to organise a corporation, to lead a company or make decisions. Instead, the optimal course of action is contingent (dependent) upon the internal and external situation.

Key influences on control system design:

- Organisational culture and belief systems as well as national culture (Focus on sales/ quality/ profitability)
- Organisational structure (Functional/ Divisional/ Matrix)
- External environment (Competition)
- Size of organisation (small – don't need a formal control system, Decentralise v. Centralise)
- Technology

Porter's five forces model

This model identifies and analyses 5 competitive forces that shape every industry, and helps determine an industry's weaknesses and strengths. Frequently used to identify an industry's structure in order to determine corporate strategy, Porter's model can be applied to any segment of the economy to search for profitability and attractiveness.

1. Rivalry among existing companies
2. Threat of new entrants (how easy is it for new entrants to infiltrate the market?)
3. Threat of substitutes (a substitute performs the same or a similar function as an industry's product but by a different means)
4. Bargaining power of suppliers (powerful suppliers can charge higher prices for their goods)
5. Bargaining power of buyers (powerful buyers can demand lower prices for goods)

Additional information

How to achieve performance management?

Three core elements to an organisation's formal control system:

1. Managerial decision rights (decentralised vs. centralised)
2. Performance measures (key attributes of PMs: Types/for whom?)
3. Incentives (Why?: Types/for whom?)

Centralized organisational structures rely on one individual to make decisions and provide direction for the company

Advantages	Disadvantages
Efficient decision making Outlined by single manager Small business	Negative effects of bureaucracy Owners responsible for every decision

Decentralized organisational structures often have several individuals responsible for making business decisions and running the business

Advantages	Disadvantages
Utilise individual expertise & knowledge Greater responsiveness to needs Quicker decision making Large business	Managerial conflicts Incongruent decision making Results in duplication of activities

Advantages and Disadvantages of Decentralization

Advantages

• Decisions are better and more timely because of the manager's proximity to local conditions.
• Top managers are not distracted by routine, local decision problems.
• Managers' motivation increases because they have more control over results.
• Increased decision making provides better training for managers for higher level positions in the future.

Disadvantages

• Lack of goal congruence among managers in different parts of the organization.

• Insufficient information available to top management; increased costs of obtaining detailed information.

- Lack of coordination among managers in different parts of the organisation

Lecture 2: Responsibility accounting, structure and the organisational sub-unit

Explain alternate organizational structures and the advantages and limitations of each

Divisional

ADVANTAGES	DISADVANTAGES
- Directs attention to marketplace results rather than process results (under a functional structure) - Greater responsiveness to demands of specific product/regional markets or clients - Can hold divisional managers accountable for end-to-end results in their region/product/market - Good model for developing future leaders and managers (experience running divisions) - Clearer management accountability for results in a particular product market - Divisions work well because they allow a team to focus upon a single product or service, with a leadership structure that supports its major strategic objectives. - Increases customer and market responsiveness in the core product markets - Clearer divisional manager accountability for results in a particular product market, and it promotes decentralised decision making - The divisional managers had been appointed on the basis of their long-term history with the company as well as their expertise associated with their division's activities – thus, this directly allows the divisional managers, who have the most knowledge about their product, to have the DM rights. This, in turn, frees up senior managements' time to focus more on attending to strategic related issues. - There is greater autonomy and DM power for managers which may result in greater motivation and a sense of empowerment, and are more likely to identify more profitable product lines and attend to the more unprofitable lines. - Because the divisional structure is based on an extensive delegation of authority, the performance of each division can be measured directly. In addition, managers can be held accountable for the sales and profits of their division. As a result, division managers usually perform better and employee morale is generally higher. Other advantages of a divisional structure include a more	- Duplication of functions within divisions - Loss of economies of scale within functions - Horizontal (across division) information flows are problematic o Incentive to share information with other divisions? ▪ Fosters competition rather than collaboration (resulting in 'silos') ▪ Divisional silos assume more importance than the organisation as a whole o May result in loss of learning within functions o If interdependencies between divisions are high these problems will be exacerbated and divisional structure will break down o A company comprised of competing divisions may allow office politics instead of sound strategic thinking to affect its view on such matters as allocation of company resources. Thus, one division will sometimes act to undermine another. o Potentially dispersing technical competence and expertise or fostering unhealthy rivalries among divisions.

efficient and effective ability in coordinating activities among divisions, greater flexibility in responding to changes in the local market and a simpler process in changing the size of the business by merely adding or removing divisions. - The divisional structure organized by product is most advantageous when an organization offers only a few products or services that differ substantially. These types of structures allow you to more easily implement business strategies and give special emphasis to products where needed. - Ensures more customer focus and promote goal congruence. - Opportunity to eliminate unprofitable product lines or at least become aware of them - Clearer span of control of managers	○ Moreover, because there is an overemphasis on divisional rather than organizational goals, the divisional structure may result in duplicating resources and efforts -- such as staff services, facilities and personnel -- across divisions.