

## CONTROL SYSTEMS

What is meant by control?

- Management control is the process by which management ensure that the behaviour of employees is consistent with carrying out the organisation's objectives and strategies. It looks at all the devices/mechanisms managers use to encourage, enable, or sometimes 'force' employees to act in the organisation's best interests.
- Control is the backend of the management process.

**Purpose/function** of management is simple and that is to get done what management wants done and to influence behaviour in desirable ways.

The **benefit** of management is an increased probability that the organisation's objectives will be achieved.

- This is where strategy is important because an organisation needs to establish goals in order to allow management to aim to achieve them.

### **Process of setting organisational goals/objectives:**

#### Objective setting

- Firms need to set goals
- Objectives are a necessary pre-requisite for any purposeful activities
  - o Need to know what you are trying to accomplish
- Without objectives, it is impossible
  - o To assess whether the employees' actions are purposive;
  - o To make claims about an organisation's success
- Objectives can be:
  - o either financial or non-financial.
  - o quantified, explicit vs implicit.
    - Explicit objectives clearly set out this is the measure we are trying to achieve
    - Implicit objectives are more personal goals. They are based on three motivational needs: the need for achievement of something (accomplishing something), the need for power (I need to show that I can do it) and the need for affiliation (the need to show that I belong)
  - o economic, social, environmental, or societal.

#### Strategy formulation

- Forming a strategy on how to achieve the goals
- An organisation must select a strategy which seeks to attain its objectives
- Strategies define how organisations should use their resources to meet their objectives
- Hence, strategies put constraints on employees to focus activities on what the organisation does best and also the areas where it has advantage over competitors.

#### Management control

- Control system telling us whether we are achieving the goals or not. You need to know whether you are achieving the goal through the strategy.
- Management control systems focus on how the employees do things and on controlling the way employees do things.
  - o Management use control systems to influence the behaviour of employees.
- Management control is about encouraging people to take desirable actions
  - o Management control guards against the possibilities that employees will do something the organisation does not want them to do or fail to do something they should do.
- Three key questions to ask about employees in management control analysis:

1. Do the employees understand what is expected of them. Do they understand what management is trying to get them to do?

2. Will the employees work consistently hard and try to do what is expected of them. Now that they know what they need to achieve, will they try to do it? Will they pursue the organisations objectives in line with the strategy? (are they motivated to achieve the objectives?)

3. Are the employees capable of doing what is expected of them?

No to any of these questions identifies a **basic control problem**.

### Basic control problem

- A basic control problem is a failure to get employees to do what we need them to do when we want them to do it.
- Management control is about encouraging people to take desirable actions
  - o That is, it guards against the possibilities that employees will do something the organisation does not want them to do or fail to do something they should do.
- Hence, management control has a **behavioural orientation**, and a basic control problem is a behavioural issue.
- If all personnel could always be relied on to do what is best for the organisation, there would be no need for a management control system.

The causes of a basic control problem can be put into three categories:

- **Lack of direction**
  - o Do they understand what we expect of them?
    - Employees do not know what the organisation wants from them
    - Don't know what to do or how to do it,
    - When this lack of direction occurs, the likelihood of the desired behaviours occurring is small.
    - FUNCTION OF MANAGEMENT CONTROL IS communication + reinforcement
      - Tell employees what is expected of them
      - Tell employees how they can direct their activities to help the organisation achieve their objectives
- **Lack of motivation**
  - o Will they work consistently hard and try to do what is expected of them?
    - When employees "choose" not to perform as their organisation would have them perform
      - Lack of goal congruence
        - o Motivational problems are common because individual goals do not naturally coincide with organisation goals
      - Self-interested behaviour- everyone acts in their own best interest
        - o Generally, individuals are prone to being 'lazy'
          - For example, take long lunches, overspend on things that make life more pleasant, use of sick leaves when not sick, etc.
          - More extreme examples of motivational problems are employee crime (fraud and theft)
- **Personal limitations**
  - o Are they capable of doing what is expected of them?
    - Sometimes, people are unable to do a good job because of certain personal limitations they have.
    - Some examples/causes:
      - Lack of requisite knowledge, training and experience
      - Employees are promoted above their level of competence
      - Some jobs are not designed properly, the job cannot be done in the way the firm wants.
      - FUNCTION OF MANAGEMENT CONTROL IS job assignment/promotion and job design
        - o Providing good job training
        - o Employing people who are properly qualified.
        - o Good job design

### Complications in management control:

- The problem does not always occur in a direct system. Management controls do not always involve a simple cybernetic system like a thermostat
- A direct system has three factors:
  - o Detector- measure performance
  - o Assessor- compare with pre-set standard (set goal)
  - o Effector- take corrective action
- Many controls don't focus on measured performance
  - o For example, direct supervision, employee hiring standards and codes of conduct
- Many controls are proactive rather than reactive
  - o That is, they are designed to prevent control problems before the organisation suffers any adverse effects on performance.
  - o E.g., a HR system that hires the right people rather than trying to train anyone to do the job.

### Control problem avoidance:

- Management are going to try and avoid as many problems that arise from failure of control as they can
- Control problem avoidance is eliminating the possibility that a control problem will occur.
  - o Cannot avoid all control problems but can avoid them by reducing exposure to certain types of problems or reducing the loss if the problems occur.

### Avoidance strategies include:

- **Activity avoidance**
  - o Eliminate the activity that caused the problem
  - o For example, subcontracts, licensing agreements and divestment
  - o Contract it out, licence somebody else to do it, consider whether it needs to be done at all
- **Automation**
  - o Computers/ robots eliminate the human problems of inaccuracy, inconsistency and lack of motivation
  - o Only applicable for "programmable" decision situations, not always possible
- **Centralisation**
  - o Superiors reserve the most critical decisions for themselves.
  - o Bring important decisions causing problems into higher level decision makers jobs
- **Risk sharing**
  - o Sharing with outside entities the burden of loss or the benefit of gain from a risk.
    - Buying insurance to protect against certain types of potentially large losses the organisation might not be able to afford.
    - Insurance contracts pass a portion of risk of large losses to insurance providers.
    - Entering into a joint venture agreement.

When an avoidance control becomes useful is determined by what the firm focuses on:

- If a firm focuses on the actions that have been taken, they use **Action controls**
- If a firm wants to focus on the results being produced, they use **Results controls**
- If a firm focuses on the types of people employed and their shared values and norms, they use **People controls**.
  - o **OR any combination of these together.**

## CONTROL ALTERNATIVES

### Action controls

- If you can't measure what you're doing at end result, measure what you are getting out to make sure it is being done properly.
- For action roles to be effective, their role is to control behaviour- to get people to do what is required.
  - o to ensure that employees perform (or do not perform) certain actions known to be beneficial (or harmful) to the organisation
- Take the form of either prevention or detection activities.
  - o most action controls are aimed at preventing undesirable behaviours

### **What is required for an action control to be effective?**

- They are usable and effective when managers:
  - o Know what actions are required/desirable (what do you need to do to get the outcome you are looking for)
    - Difficult in highly complex and uncertain task environments (e.g. research engineers or top-level managers)
      - Understand what actions are desirable by looking at the patterns of specific situations- when we do this, what happens? Use this as a guide to establish what behaviour is required to achieve the goal
  - o Need to be able to link the accountable actions to the probability of achieving the outcome required.
    - If we do A then the result will be B. If we want result B we need to do A.
  - o Have the ability to make sure that the desirable actions occur
    - For example, effectiveness of organisational procedures.

### **Four forms of action controls:**

- Action controls are either preventative or detective:

### **Behavioural constraints**

- Physical constraints
  - o Locks, passwords on computers so only people who know how to perform the appropriate action can use it, limited access to particular areas etc
- Administrative constraints
  - o Restriction of decision-making authority- limiting possible actions (who can perform a task, who is allowed to make a particular decision)
  - o Separation of duties etc. (important in situations where there are asset issues, person who is banking the money, shouldn't be the person receiving the money)

### **Pre-Action Reviews**

- Looking at the action plan before it is implemented to make sure it is doing what it is supposed to do
- Look at what we are trying to achieve, set the plan in place and make sure that it will achieve it.
- Scrutiny of action plans, investment proposals and budgets
  - o Review and approval
  - o The budget is an important example of this, it is the financial plan, put in place what we intend to spend on things, intended revenue for the period.
  - o Part and parcel in (capital) budgeting processes, which are otherwise mainly a results control mechanism.

### **Action Accountability**

- Holding employees accountable for the actions they take
- In order to make people accountable for the actions they take it requires these conditions:
  - o Defining what actions are (un)acceptable.
  - o Communicating these definitions to employees
    - For example, work rules, policies and procedures, codes of conduct
  - o Observing or otherwise tracking what happens
    - Direct observation/supervision
    - Periodic tracking (e.g. mystery shoppers)
    - Evidence of actions taken (e.g. activity reports)
  - o Rewarding good actions or punishing actions that deviate.

## Redundancy

- Having more or extra people (or machines) than is necessary to make sure a task is completed
  - o E.g. "backup" people or facilities to do the job when not necessary is bad use of redundancy control
- It will mean having other people working in the organisation with the capability to complete the task when necessary.

## Pros of Action Controls

- It is the most direct form of control
- It is absolutely controlling what employees' do
- Generally, these controls are well documented
  - o Tend to lead to documentation of the accumulation of knowledge as to what works best
    - Good addition to the **organisational memory**
- An efficient way of coordination
  - o Everybody knows what is going to happen and what should be done and everybody can see it
  - o That is, they increase the predictability of actions and reduce the amount of inter-organisational information flows to achieve a coordinated effort.

## Cons of Action Controls

- Only for highly 'routine' jobs, only good for tasks that are repetitious.
  - o Not suitable for actions that require some form of creativity.
- May discourage creativity, innovation and adaptation.
- May cause sloppiness.
  - o Lack of concentration when not thinking about the task at hand
- May cause negative attitudes
  - o For example, little opportunity for creativity and self-actualisation
  - o Can be very restrictive, limiting.
- Sometimes very costly
  - o Comes from the lack of creativity, not finding out a better way to do a task, not allowing for creativity means you may not be employing the most efficient method to complete the task.

## Results controls

- This form of control looks only at outcomes- what has been achieved
- These controls are used for controlling the behaviours of employees.
- Results controls are an indirect form of control
  - o Do not control what is being done and do not focus explicitly on the employees' actions
    - Involves rewarding employees for generating good results (or punishing them for poor results)
      - E.g. Pay for performance, incentive schemes
      - Or results accountability
- Indirect influence over employee actions because it causes employees to be concerned about the consequences of the actions they take
  - o However, employees actions are not constrained through this control
  - o On the contrary, employees are empowered to take whatever actions they believe will best produce the desired results
    - Management control analyses the outcome of the employees' and not the actions
- In order to assess the results, employees' need to be aware of the objectives
  - o Management needs to define the performance dimensions/ the desired outcome
    - If you can't measure something and know the result, how do you know you are improving the outcomes.
    - What you measure is what you get; hence,
    - If not congruent with the organisation's objectives, the controls will actually encourage employees to do the wrong things
- Measuring performance on these dimensions
  - o Objective measurement> financial> market-based: for example, stock price OR accounting based: for example, return on assets
  - o Objective measurement> Non-financial> for example: market share, customer satisfaction
  - o Subjective measurement> for example: managerial characteristics ("being a team player", are they working for the organisation)

- Performance targets on employees' should be motivational
- Performance targets should induce people to do what is needed to be done to achieve organisational objectives.
  - o Relevant – relate to the objective
  - o Simple
  - o Aligned
  - o Measurable
  - o Achievable- most importantly
- Providing rewards (or punishments) for achieving or failing to achieve the outcome desired.
  - o "Incentives"- monetary and non-monetary

**For a results control to be effective certain conditions are needed**

- Results controls work best only when all of the following three conditions are present:
  - o Superiors/ managers must know what results are desired in the areas being controlled
    - If there is more than one result they are aiming for, the need to know which one to aim for first.
  - o The individuals whose behaviours are being controlled must have significant influence on the results in the desired performance dimensions (controllability principle)
    - If you are judging an employee for what they have achieved and for what could be improved, they need to have the capacity to improve.
  - o Superiors/managers must be able to measure the results effectively

The ability to influence outcomes fits into the **controllability principle**

- The evaluation of a manager should be based only on the elements that are under a managers control- and the same goes for employees.
- The person whose behaviours are controlled must be able to affect the results in a material way in a given time span

Results controls are useful only to the extent that they provide information about the desirability of the actions that were taken

- If the results are uncontrollable, the controls tell us little about the actions that were taken:
  - o Good actions will not necessarily produce good results
  - o Bad actions may similarly be obscured

**Effectiveness of a results control:**

The effectiveness of a results control is measured by their ability to create the behaviour that is needed to achieve the result required.

- Measurement properties
  - o Congruence- measurement should be congruent with the outcome required
  - o Controllability- somebody needs to make sure it happens
  - o Precision
  - o Objectivity- no one saying I think this happened
  - o Timeliness- no point finding out a result six months down the track
  - o Understandability- need to understand what you are measuring
  - o Cost efficiency

**Pros of results control**

- A good results control will influence behaviour while allowing significant autonomy.
- They yield greater employee **commitment and motivation**
- They are often 'inexpensive'
  - o For example: performance measures are often already collected for reasons not directly related to management control (e.g. financial reporting)
  - o Not spending time watching over people as you would in an action control, just ensuring the outcome of the task is correct.

**Cons of results control**

- Often less-than-perfect indicators of whether good actions have been taken

- They shift the risk of failure to the employees (due to uncontrollable factors); hence, employees may demand a **risk premium** to compensate for this.
  - o Placing more responsibility on employees' may mean that they demand payment for it such as pay rises.
- Sometimes conflicting demands:
  - o Need to ensure that the target results are motivating and challenging for the individual employee but are overall good for the entity.

### People Controls (Personnel/Cultural controls)

- People controls ensure that employees:
  - o Will control their own behaviours
    - Through personnel control
    - Self-monitoring
      - Based on the natural tendency that people have to control and motivate themselves- personal desire to get things done and to do them properly
      - Leads to employees understanding just what it is that employers want.
  - o Will control each other.
    - Through cultural controls
    - Mutual monitoring
- People controls are part of virtually every management control system, and essential in... "flatter and leaner organisations with empowered employees who control and motivate themselves".
  - o When an organisation is wider- tend to employ cultural controls heavily.

### **Personnel controls**

- Personnel controls build on employees' natural tendencies to control themselves because most people
  - o have a conscience that leads them to do what is right
  - o find self-satisfaction when they do a good job and see their organisation succeed
- Different labels used to describe self-motivation are:
  - o self-control
  - o intrinsic motivation
  - o ethics and morality
  - o trust and atmosphere
  - o loyalty

### **Implementing personnel controls**

- There are different ways of implementing personnel controls
- Generally, it is about "finding the right people, giving them a good work environment and the necessary resources".
  - o This is the overall desire of a personnel control
- First step: Selection and placement
  - o Finding the right person with the potential aptitude to do a particular job appropriately
- Second step: Training
  - o Give employees a greater sense of professionalism- awareness of being trained at something
  - o Create interest in the job by helping employees to understand their job better
- Overall Importance: Job design + provision of necessary resources
  - o Making sure the job can be done, it is achievable, they have the right equipment to do the job.
  - o So that motivated and qualified employees have a high probability of success (e.g. equipment, staff support, freedom from interruption).

### **Cultural controls**

Personnel controls can extend to a wider organisation through cultural controls.

- For individual employees it is referred to as personnel controls, when referring to an organisation as a whole they are cultural controls.
- Cultural controls or mutual monitoring extend personnel controls into mutual action.
  - o They tap into social pressure and group norms and values because employees want to be a part of the group
- Cultural controls are effective because members of a group have emotional ties and a sense of responsibility to one another, "I am part of this group and I must help this group"
- Cultures are built on shared:
  - o Traditions

- “I am employed by the University of Adelaide, it is over 100 years old, it means something”.
- Norms
  - Normal behaviour for people in a particular group to do things in a particular way
- Beliefs
- Ideologies
  - When selecting employees, the employers have the same set of ideologies when deciding
- Attitudes
- Ways of behaving

### Ways to shape culture:

There are various ways to shape culture, some are formal and some are informal:

- **Codes of conduct**
  - Code of ethics, corporate credos, mission statements etc.
  - Formal written documents with broad statements of corporate values, commitments to stakeholders, and the ways in which top management would like the firm to function
    - Statement of what is expected and the corporate culture expected, “how we do things- how management want the firm to function”
  - Fundamental guiding principles of the company
- **Group-based rewards**
  - For example, profit-sharing, employee ownership of company stock
    - Issue with this: one person carries others who do not work as hard.
  - These are *cultural controls* (although of a results control nature (rewarding for the results achieved) because the link between group (individual) performance and rewards is stronger (weaker)
    - Designed to support organisational culture.
- **Intra-organisational transfers**
  - Move people around within the organisation, understand what the firm is trying to do and the culture from different places in the organisation by understanding the people better
  - Improve the socialisation of individuals in an organisation and alleviate the formation of incompatible goals and perspectives across departments.
  - Improve identification with the organisation as a whole as opposed to subunit identification
- **Physical and social arrangement**
  - How the environment is set up, all add to the corporate culture of the workplace
  - For examples, office plans, interior décor, dress codes and vocabulary etc.
- **Tone at the top**
  - Top management statements must be consistent with the culture they are trying to create, and importantly, their behaviour should be consistent with their statements.
    - How are top management perceived?
    - Lead by example.

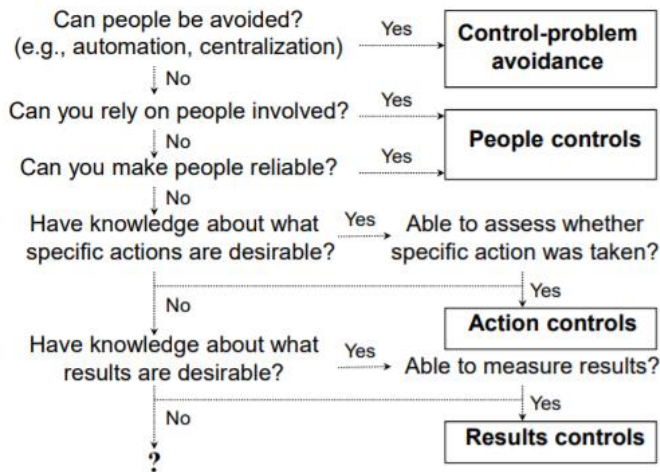
### Start with people controls

- **People controls are very important because other controls will not work if employees are not on side.**
  - We need to be able to rely on people controls to get the right people.
  - A failure in people controls can usually be corrected/adjusted quickly with relatively few harmful side-effects.
    - Getting other people or training the people to do things the right way.
  - Involve relatively low out-of-pocket costs to get the right people in the right place at the right time.
- However, it is rare that people controls will be sufficient; hence, in most cases, it is necessary to *supplement* them with...
  - Action controls
  - Results controls
    - Need to have a full range of controls to ensure desired outcomes are being achieved.



**HOW TO DETERMINE THE TYPE OF CONTROL THAT IS NEEDED:**

First observation is to ensure that an organisation has got the right people doing the right thing:



- Have knowledge about what specific actions are desirable- do we know what we need to get done?
- If you do not know what you are trying to achieve than you have no direction.

**HOW TO DETERMINE WHICH CONTROL IS APPROPRIATE:**

- The nature of the control will depend on what is measurable and knowing what is required

Ability to measure results on important performance dimensions

Excellent	<b>Action Control</b> and/or <b>Results Control</b>	<b>Action Control</b> (e.g., large projects)
	<b>Results Control</b> (e.g., movie director, entity manager)	<b>People Control</b> (e.g., research lab)
Poor	High	Low

Knowledge of which specific actions are desirable

- If the ability to measure the performance/outcomes is high and the person has a good knowledge of the desired result
  - o ACTION OR RESULTS CONTROL
    - These controls are used to just check in on what is supposed to be done and what is supposed to be provided
    - Trust the employees to do the right thing because they understand it.
- Inability to measure and lack of understanding of the desired result.
  - o PEOPLE CONTROL
    - Low level of ability to measure employee performance and the people don't really know what the real action is, what the outcome will be
    - Getting the right people, motivating them and training them so they do it properly.

## MANAGEMENT CONTROL IN NOT-FOR-PROFIT ORGANISATIONS

### Not for Profit Organisations

- An NFP exists when the financial results are **not the primary consideration or objective**.
- Different from for-profit corporations because they have **no shareholders** and **no single individual or body of individuals have ownership rights** to the firm's residual earnings or exercise control of the firm.
- Instead, control is exercised by a board of trustees.
- The defining difference between for-profit and not-for-profit organizations does *not* lie in **how much profit** they can generate, but instead in how it is **distributed**
  - **A not-for-profit organization's profit cannot be paid out to the owners or anyone else associated with the organization** but is dedicated to the mission or goal of the organization.
  - **NFP do not pay dividends and all the resources must be used to further the organization's purpose.**
- Hence, the major defining characteristic of a not-for-profit organization is the that the **organization's primary purpose** takes the form of a *mission or goal*.
  - E.g., such as to offer education, pursue cancer research, provide healthcare.
- **But, NFP's do still have to generate revenues to fund their operations and are subject to financial constraint like any corporation.**

### CONTROL

- Despite their structural differences, NFP organisations have to address the same set of control problems as for-profit organisations, particularly regarding personnel controls- lack of direction, lack of motivation, lack of ability (personal limitations).
- NFP's also have the same set of control tools- action, results and personnel/cultural controls at their disposal.
- They face the same problems like needing to implement goal-congruent performance measurement and incentive systems and to avoid the dysfunctional and behavioural side effects on employees.
  - But, NFP's are subject to issues that for-profits are not.
    - Inability to compete with for-profits in providing compensation packages (provision of incentives is unfeasible or unaffordable) so are restrained as to which personnel they attract and retain.
    - Resource constraints
    - Extreme public or political pressure causing goal conflict.
    - NFP objective impossible to measure with financial performance measures.

### Non-profits different from "Corporations"

- **Investor-Owned Corporations**
  - Owners (shareholders) exercise control by voting for its directors who provide control over management.
  - The residual earning of the firm belongs to the owners.
  - Management is responsible primarily to the shareholders for the profitability of the firm.
  - Primary goal of C-Corporations is shareholder value maximisation.
- **Benefit corporations**
  - **Allow boards and managers to sacrifice shareholder value for the greater good under specified conditions.**
  - B Corporations can focus on social and environmental objectives therefore changing emphasis from shareholder value to stakeholder value.
    - Requires that they **specify their social and environmental goals in** the corporation's bylaws.
    - That they have sustainability and corporate social responsibility strategies certified as credible and transparent by a third party.
      - They must publish an annual report that measures how well these goals are being met.
  - When they meet these criteria, benefit corporations are allowed to shift their firm's emphasis from shareholder value to stakeholder value.

## Types of not-for-profits

### **PUBLIC BENEFIT**

- A not-for-profit is an organization whose primary purpose is typically to provide some kind of **public service**
- It includes a large and diverse set of organizations where the types of services provided vary widely.
  - Charitable, religious, scientific, educational, and political
  - Governmental organizations and their various institutions, authorities, agencies, and programs
  - Private organizations operated for **public benefit**:
    - Museums, hospitals, universities, and schools

### **PRIVATE BENEFIT**

- Some not-for-profit organizations, such as religious organizations and charitable foundations, serve various **private benefit** purposes.
- Some, such as cooperatives, and labor, fraternal, trade and homeowners' associations, are operated for the **mutual benefit** of their members.

## **Characteristics of NFPs with MCS implications:**

### Goal ambiguity and conflict in NFPs

- Goal clarity exists and is more likely to be commonly shared and understood in for-profit organisations by virtue of their value-maximising mantra.
- Managers of publicly traded firms can obtain timely feedback on their goal achievement through market measures (by monitoring their firm's stock performance) and comparing it to that of their competitors and the overall market.
- This level of goal clarity does not usually exist in NFP organisations.
  - General Organization Goal: provide some kind of public service
    - Governmental, scientific, educational, charitable, religious, etc.
- VARIOUS CONFLICTING CONSTITUENTS: A NFP has many constituents that have an interest in the organisation, its goals and its performance but these constituents often do not agree, their values and interests conflict.
  - E.g. The board of trustees of a museum may pursue their primary goal of appealing to the diverse public through the collection and exhibitions of the highest quality art. But other stakeholders of the museum such as the local community and the government officials might be more interested in having the museum present exhibitions aimed at children. Religious leaders may be considered about whether the art is in their view socially and morally acceptable.
- Resolving the conflicts and differences between constituents requires unique decision-making mechanisms.

### Goal conflict in Government NFP Organisations

- Conflict is also inevitable in government NFP organisations because these organisations are directed from a number of sources- the executive, judicial and legislative branches and possibly also from various levels of governments- some federal and state.
- Managers of these organisations face external pressure because the press and public in democratic societies have access to considerable information.
- Some NFP employers even face re-election pressures and need to please campaign donors and the public at large.
- This diffusion of direction and potential conflict greatly complicates the job of management generally and the goal congruence in management controls specifically. It creates goal complexity at worst and also triggers conflict and confusion.
  - E.g. Law enforcement government agencies have to respond to the laws quickly and to rulings made by all levels of legislatures. Their funding and consequent accountability may also be to multiple authorities.

### Addressing Goal Ambiguity

- Without clarity as to what goals should be achieved and how trade-offs among them should be made, it is difficult to judge how well the organisation's control system or how well the management team are performing. That is why goal ambiguity must be addressed to establish an effective control system while reflecting the legal, regulatory, policy and resource environment within which the NFP operates.

### Difficulty to measure performance

- Even if NFP goals are quite clear, these organisations often do not have at their disposal any single, quantitative performance indicator, like the profit and return measurements available to corporations.
- The degree of achievement of the organisation's mission or goals (such as the provision of quality service to its constituents) usually cannot be measured accurately in financial terms.
  - E.g. If a hospital's goal is to save lives or cure the ill, how is this success to be judged? By the time to attend a patient brought to the emergency ward or by the survival rates of patients? Or measures of prevention rather than merely curing? How about the cost?  
  
You cannot adequately measure performance in this NFP situation. And one focus can be compromised in favour of another.
- Without a small set of quantifiable performance indicators, the task of management becomes difficult to:
  - Measure organisational performance in achieving the overall goal
  - Difficult to use results controls (including performance-based incentives) at a broader organisational level.
  - Analyse the benefits of alternative courses of action.
  - Decentralise the organisation and hold entity managers accountable for specific areas that relate exactly to the organisation's overriding goal.
- Increasing use of performance measures in public service organisations and disseminating data to general public has also been growing.
  - The goal of these initiatives is to supplement the traditional input focused measures such as expenditures and staffing levels, with results-oriented measures such as output, quality and timeliness, which would improve governmental efficiency and effectiveness by increasing public managers' accountability.

### Balanced Scorecards in NFPs

- The Balanced Scorecard has also been successfully adapted for use by not-for-profit and public sector organisations.
- While the top line financial objectives of for-profit organisations are replaced by mission-related objectives, the process of identifying relevant stakeholder, internal process and resource measures serves much the same purpose.

### Budgets in NFPs

- In non-profit organizations, the planning processes may **be less focused on capital funds, although capital is often a major constraint for them as well**, forcing them to consider trade-offs among various programs and **designate available funds** annually in their operating budget to well-chosen **courses of action that help further their charitable objectives**.

### External Scrutiny

- Most NFP's do not directly serve or do not have to answer to a group with ultimate authority, like a shareholder group. They do have to answer to a number of external constituencies.
- The constituencies (donors, government entities, alumni, society at large to an extent etc.) often make up the not-for-profit organization's governing body.
- **These external constituencies are very demanding.**
  - **This is because most NFP's are established to provide valuable social service and as a consequence they are often held to a higher standard.**
- Performance reports can provide valuable information that helps the constituents make informed choices (such as which school to send their children to, which hospital to entrust their health with, which charity to donate their money to).

- High societal expectations lead to high demands for accountability. If an organisation is perceived not to be performing effectively, donations can be withheld, and managers and boards of trustees can be forced out of office. Government regulators can shut the organisation down or place restrictions on them.
- Sometimes intense external scrutiny can also shape some decision-making processes, including management control related processes. Planning and budgeting processes are likely to be more important and more time consuming because external parties must be heard and their concerns must be accommodated.
  - Management and employee compensation in NFPs is often subject to considerable political pressure.

### Legal Constraints

- NFPs have to be compliant with a lot of legal and political pressures.
- Compliance with legal constraints calls for **tight action controls** and increases control costs.
- The **provision of incentives may not be feasible**.

### Employee Characteristics in NFP organisations

- Employees of NFP's often have some characteristics that distinguish them from those in For-Profit organisations.
  - The size of compensation packages of employees in NFP organisations are not competitive with those offered in for-profit organisations. This causes personnel control issues because it diminishes employee quality and causes employee retention issues. In this regard, NFPs are not as well developed as for-profits because they are limited in the types of personnel they attract and manage to retain.
  - Most important to hire good, capable people and make them accountable for organizational goals.
- Members of NFP boards are sometimes selected not based on merit or qualification but because of factors like being a large donor to the organization (may lack necessary qualification for the role).
- NFP trustees are paid little or nothing for their services, so they may be less committed to or more easily distracted from their tasks.
- On the other hand, NFP organisations often attract employees who are highly committed to the organizational goals.
  - Such employees may find it more intrinsically rewarding to pursue the NFP organisation's goals (e.g., shelter for homeless) compared to creating shareholder value in a dispassionate sense.
  - When NFP employees are attracted by the idealism of the NFP and can be retained, their high commitment minimises the other personnel control problems like lack of direction and lack of motivation. **Control can then be easily achieved through personnel and cultural controls.**