Management Control Theory

Topics

- Basic concepts
- Organisational control
- Performance standards
- Levels of control
- Control systems
- Control structures
- Typologies of control

Key learning system questions

7 MNO
Basic concepts

**Definition**

**Control** – the ability to direct the financial and operating policies of an entity to gain economic benefits from its activities

**Management control** – all of the processes used by managers, to ensure that organisational goals are achieved and procedures adhered to, and that the organisation responds appropriately to changes in its environment

**Control environment** – the overall attitude, awareness and actions of directors and management regarding internal controls and their importance to the entity ... [it] encompasses the management style, and corporate culture and values shared by all employees. It provides a background against which the various other controls are operated

**Definition**

**Control procedures** – those policies and procedures in addition to the control environment which are established to achieve the entity's specific objectives

**Controllability principle** – individuals should only be held accountable for the results they can control
The cybernetic control process involves four conditions:

- The existence of an objective which is desired
- A means of measuring process outputs in terms of this objective
- The ability to predict the effect of potential control actions
- The ability to take actions to reduce deviations from the objective

In the cybernetic system, variations between targets and actual achievements are detected and result in corrective action, either through feedback or feed-forward processes.

**Feedback control** is the measurement of differences between planned and actual outputs achieved, and the modification of subsequent action and/or plans to achieve future required results.

**Feed-forward control** is the process of forecasting differences between actual and planned outcomes, and the implementation of action, before the event, to avoid such differences.
Performance standards

Five major standards against which (financial or non-financial) performance can be compared:

- Previous time periods
- Similar organisations
- Estimates of future organisational performance before the event
- Estimates of what might have been achieved after the event
- The performance necessary to achieve defined goals
Levels of control

Definition

**Strategic control** – control exerted by the board and chief executive

**Management control** – control exerted by middle managers

**Operational control** – control exerted at the supervisory level

Study tip

Make sure that you have lots of examples to illustrate the levels of control

Watch out!

You can apply this model to lots of practical situations. Make sure that you practise doing this

Diagram of a control system
Control structures

Organisations operate through a variety of organisational forms. The form of structure that is adopted will determine the type of control exercised over operational management

- Functional
- Divisionalised
- Matrix
- Network

Divisional structures may be

- **Cost centres**: which are responsible for controlling costs
- **Profit centres**: which are responsible for achieving profit targets
- **Investment centres**: which are responsible for achieving an adequate return on the capital invested in the division

Study tip

You might be asked to recommend a change of structure to improve control
Typologies of control

Cybernetic controls include
- Routine
- Expert
- Trial-and-error
Learning takes place here through feedback and feed-forward

Non-cybernetic controls include
- Intuition
- Judgement
- Power and politics
Learning does not take place as objectives are ambiguous, outputs are not measurable and the effects of intervention are unknown

Control is not limited to accounting or financial controls, but includes a wide range of non-financial controls such as performance measures; human resource controls such as recruitment, training, supervision and culture; as well as non-cybernetic controls

Study tip
Remember that control is not limited to accounting!