

# The Evolution of Internal / Managerial Control and its Impact on the Organization's Management

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## *Abstract*

*The term of cluster as economic agglomeration became in time an obsessive concept for politicians, consultancy organizations, business associations and companies, in general. It is seen as an instrument that guarantees the economic success at local and regional level, one of the solutions to sustain cohesion.*

*We know that clusters connect people and organizations, their activities are interdependent and intertwined. Even so, there are voices that criticize clusters and the approach of Michael Porter who launched the term in the early 90's. Given this we search for answers about what is a cluster and why should the industrial policy focus on it? What determines organizations to gather in a cluster? Is there a typology of clusters? At the end we make some observations about clusters in Romania and their potential influence on the economic development.*

**Keywords:** *cluster, organizations, strategy, internal control, management*

**JEL classification:** M00, M10

The current article was prepared having as main objective to adjust the public institutions in Romania, especially their managers, to better understand the concept of the internal control and the specific approaches used to establish an efficient management for the organization. On the other hand, we hope our argumentation, intended to present an historical evolution of the internal control as a management function, will enforce the professional standards in this area of expertise.

According to the provisions of Law no. 234 / 7<sup>th</sup> of December 2010, modifying and completing The Government Ordinance no. 119/1999 regarding the internal control and the financial preventive control and the Provisions of the Minister of Public Finance Order no. 1.649 from 17<sup>th</sup> of February 2011 modifying and completing the Provisions of the Minister of Public Finance Order no. 946/2005 Approving the internal control code, in public institutions in our country, the top manager is the main actor responsible with establishing, within the organization he/she manages, an efficient control structure, able to perform this task which cannot be delegated to other management function and, finally, to determine results achievement with permanent collective effort. Other managers, each of them situated on different hierarchic levels, will perform the control function within its own structure. Therefore, we can speak about a hierarchy of the internal control, each unit having the responsibility to help the superior ones in such a way

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that all are working together for a sound development, ensuring the achievement of management's mission, its existence.

This article presents concepts and approaches, various information, knowledge and premises helpful in a high degree, at least for the beginning, for all managers, because our paper suggests possible creative actions. Anyway, the complexity of the controlling process, as it is described below, should not, of course, determine an inhibition of the manager or, even worse, the renouncement of the responsibility of what we call *controlling*. We hope that, on the contrary, the concepts bellow, and the suggested approaches will produce concrete solutions and, finally, a more adequate representation of the managerial control function.

Before starting our intercession, we consider necessary to make a short review of some important definitions related to the function of control, which you will find bellow:

- *"...to adjust the organization's activities in such a way that characteristics of (significant, n.n.) predetermined performances are being maintained within acceptable limits. Without this adjustment, the organization has no clues on the quality of its performances considering its pre-established scope. Acting like a "steersman", controlling ensures the evolution of the organization on a pre-determined route (Griffin, 2002)*

- *"...a process (organizational n.n.) of adjustment, establishing standards dictated by the necessities of fulfilling the scope of the organization, a process of comparing the actual performances with the standards and applying corrective measures, when needed (Robins & DeCenzo, 2001)*

- *"...monitoring the activity to ensure these are running according to the plans, and also correcting significant deviations (Robins & DeCenzo, 2001)*

- *"...assessing how the initial plans have been fulfilled (DuBrin, 2000)*

- *"...the entire ex-ante and ex-post evaluation actions of the organization's results, links of the organization and each employee, identification of deviations from the objectives, norms, regulations and standards initially established and generating causes, and also taking corrective actions to eliminate deviations, by maintain the organization's balance. (Zorleţan, et al, 2005)*

- *"...a systematic effort of the manager to compare performances with pre-established standards, plans or objectives, in such a way to determine in what degree the results are respecting the standards, if corrective measures are needed and if resources have been utilized in an efficient and effective manner to fulfill the results (Mockler, 1970)*

By these definitions various approaches are projected to define internal control as the main attribute for the management. Considering all of them, they are defining a complex and dynamic organizational process. Generally, the wording "internal / managerial control" means to systemically and permanently examine / check / assess an activity / situation etc. following its evolution and apply corrective measures if needed. In the same time, it means a continuous monitoring and finally establishing if the situation has been controlled and risks avoided. The internal / managerial controlling process represents an internal structure of the

organization helping us to understand the current situation, objective reality and, generally to correct deficiencies, dysfunctions and any error.

In our opinion, internal / managerial controlling process is defined by responsibilities, activities and approaches of the managerial team, directly controlled by the top manager, to assess / measure results<sup>2</sup>, and compare the performances with pre-established standards / objectives, identification and elimination of any negative deviation, integrating positive deviations, and finally obtaining the adjustment of the entire organizational system considering its fundamental scope. Internal control represents a monitoring process and permanent adjustment of the entire system considering its fundamental scope and an increase of the general efficiency<sup>3</sup>.

O relative recent phasing (Barley & Kunda, 2003), projected in such a way to enhance the USA reality, identifies, starting with 1870, five big “*ages of the managerial control*”. These ages, represents chronological steps marking the historical evolution itself and also how it grow-up. Management and control, in general, are different by signification given by the social actors to specific concepts and approaches. Considering this milestone, we are registering a fluctuation of the managerial control.

Having in view the above-mentioned model and taking into account the social and economic evolution in our country, in author’s view, the content of the managerial control function has registered a series of oscillations and significant particularities. We are hereby presenting large periods of time in which the control has revealed a certain social practice and also particularities reported to two important factors: efficiency maximization of competitiveness, on one hand, and focus on socio-economic factors, on the other hand.

- **The Age of Industrial Revolution** [1870-1900; 30 years]

In this period, the managerial control is subordinated to its main objective of attracting and shaping a specialized work force, capable and responsible, thus diminishing the fluctuation of personnel ensuring loyalty of the employees. The dominant behavior was represented by the exaggerated sense of ownership of the employer, most of them coming from the countryside and the poor neighborhoods in urban area. After a long period of wild exploitation, the employers had manifested an excessive preoccupation related to material and working conditions of employees. From their own resources, some companies have built libraries, churches, parks, gymnasia, social houses, social clubs they improved the working conditions, being non-hygienically and dangerous, they promoted religious and educational programs and established benefits and bonus schemes for their employees, measures unseen by that time.

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<sup>2</sup> By wording “*organization’s results*” we understand not only the performance of the system but also those obtained by each component unit or each employee.

<sup>3</sup> The capacity of the organization to manage a specific problem and give a rapid feed-back to its clients expectations.

In Romania at the end of 19<sup>th</sup> Century, being mainly rural and agricultural, the managerial control was performed in special state institutions and “daughters” of foreign companies, banks and distribution networks functioning by the rules established by the “mother” company. Modernization of the economic Romanian system at that time meant to massively import means and techniques to apply the managerial control function, and also an alignment to the tendencies in that period.

- **The Age of Scientific Management** [1900-1925; 25 years]

In contrast with the ownership approach from the industrial revolution period, the scientific management founded by Frederick W. Taylor had as main objective to increase competitiveness and productivity to identify the best combination of procedures for creating a product. Scientific management was created and built up based on three premises: a) scientific and controlled study of work to register a significant increase of efficiency; b) the employees are being considered fully rational, stimulated by material advantages, promotion, increase of salary etc.; c) employees are motivated first of all by money. Building on these ideas, Taylor introduced, by that time, a case by case scheme of payments to motivate the workers exclusively on quantitative criteria based on concrete, measurable results. Surprisingly, Taylor was not appreciating the ownership concept, accepted in the industrial revolution period. He often said that *„...a worker with self-esteem doesn't want to receive things; each man wants to earn them by their own efforts.”* consequently, managerial control focused on strict monitoring and verification of the quantitative elements ensuring work efficiency.

Romania, at the beginning of the century, has known a significant development of its extractive industry and soil exploitation, transport and commerce. Work organization and control function, in accordance with managerial concepts at that time, it's an imposed reality by the foreign companies established on our territory. The principles of scientific management, elaborated by Taylor in 1911, were applied by us, especially in oil industry where certain “daughter” companies were acting having “mother” company in the USA. Controlling tasks allocation was, consequently, respecting these principles.

- **The Age of Human Relationships** [1925-1955; 30 years]

Compared with the focus on the efficiency of control in the scientific management period, the approach in this period named “human relationships” was starting from the premise that, for the employee, social interactions and the need to belong to a group are more important than material advantages. Consequently, instead of paying the employees for working more, this approach considered that employees can be motivated if their supervisors will treat them with respect, if groups of employees in a certain area would participate to decision-making process and if jobs would be projected in such a way not to restrict social and professional interaction, associations etc. In many ways, this approach looks like industrial

revolution period, though there can be noticed an essential difference given by the fact that in this period controlling was constantly improving and stabilizing the working force of the company, while, in the age of human resources, the main scope is to improve the organizational and relationships environment.

Although history presents many cases of how abusive the internal control was used, especially in mining sector, inter-war Romania registered a reconciliation of the subordinating relations, a careful approach of the relationship with the employee. After war, controlling relations had a punitive side imposed by the communist regime preoccupied, at least at its beginning, to transform the managerial control into a repressive instrument.

- **The Age of Rationalized Systems** [1955-1980; 25 years]

In contrast with the previous period which was placing the theory related to the employee in the center of the control philosophy, systems rationalizations or, in other words, systemic approach, was completely ignoring the employee in its search for principles and functions generally applicable which would help the organization to function as a whole. Using idea from the electrical engineering and computers, the systemic approach was looking for the best ways of planning, organizing, coordinating and controlling of organization performances. Managers were concentrating their activity on inputs, outputs, processes and organizational relationships and less socio-human aspects. Training the supervisors was not important because in this theory, the entire management system of the organization, and not only supervisors, are determining the success and the failure.

In the communist regime, the controlling system in Romania was characterized by constant increase of productivity, avoiding wasting of resources and also rationalizing the economic system. Therefore, the scientific management of that time was excessively focused on control, everything being subordinated to a centralized planning, rigid and dictatorial.

- **The Age of Organizational Culture and Quality** [1980-2005; 25 years]

Finally, compared with the useless, too philosophical approach of the rationalized systems, the internal control was oscillating, again, in the opposite direction, highlighting two paradigms: organizational culture and quality. Instead of focusing on efficiency/profit or subunits of the organization as parts of a larger system, managers and companies had maintain the internal control with ideals, values and common actions of the organization's personnel. The interest moved from resources and products towards satisfaction and motivation of employees, team working, mobilizing values and charismatic vision with morale precepts. The main scope of this approach was for the employees to represent their organization, being dedicated to realize its services and products with high quality, thus employed for the general good. The entire philosophy in this period was build up

on the belief that inspired by this vision which is reflecting in the organization's fundamental, employees and managers would work harder, being more loyal to the company, its clients and specific social environment.

For Romania, the first half of this period was an extension of the previous one focused on repressive tendencies related to internal control. Starting with 1990, significant transformation took place related to restructuring and reorientation of socio-economic environment. The alignment to the Euro-Atlantic management practices brought a continuous modernization of the internal control process regardless the size of the organization. Especially, decentralized control was followed and the ownership approach was eliminated.

### Comments

Over the last decade we noticed some particularities helping us to conclude that the age of organizational culture and quality is already history. The accelerated transition to the knowledge economy<sup>4</sup> offers to the managerial control a generous and favorable area to develop specialized techniques and instruments. Thus, in this context, we noticed a reconsideration of the relation between the internal classic control<sup>5</sup>, focused mainly on the area of financial and economic activity and the internal control based on holistic approach focused on examining more indicators and "invisible" elements – information/knowledge/abilities/skills and managerial qualifications.

The main development direction we refer to is given by the quantitative assessment /analysis of the quality processes and specific levels of performances, in such a way to rapidly realize an efficient correction of deviations and finally to adjust the organizational system of the public institution as a hole. In these conditions, as a continuation of the above mentioned periods, we can appreciate we already are in a new age of the managerial control focused on specialized information and qualified abilities.

The specialized literature of the last decades is highlighting by "*managerial controlling*" the entire approaches and practices used (by the people having management responsibilities) to balance the entity and put it on a predetermined route. Obviously, the vision we refer to is originated in the systemic-holistic approach and starts from the belief that the organization<sup>6</sup> needs a mechanism, an internal regulatory system identifying fast any deviation / dysfunction / weaknesses<sup>7</sup> and is consistently directing the hole to the "result" (fundamental scope mentioned in constitutive deeds, strategies, policies, plans etc).

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<sup>4</sup> "Products" and intensive-intellectual activities.

<sup>5</sup> Classic internal control is mainly focused on investigating and testing tangible elements, strictly economic.

<sup>6</sup> Public institution, in case of this article, represented as a cybernetic system.

<sup>7</sup> Real/effective (in case of ex-ante control, *feedback control*) and/or probable (in case of ex-post, preventive control, *feed-forward control*)

In this context, the managerial team leading the public institution<sup>8</sup> is in fact the “pilot” of a cybernetic system as that one above mentioned. By its decisions and actions and mostly through the internal control system<sup>9</sup>, specially created within the organization, the management observes the system’s entropy and acts consequently to maintain it with acceptable limits. The efficient functioning of the public institution is directly linked with the informational entropy of the institutional system and it’s optimizing itself towards a distinct value given by the maximized efficiency /effectiveness/competitiveness.

Similar, the internal control process may lead, within the controlled structure, to chaos, meaning a plus of entropy. The main causes generating such an inadequate situation, with unwanted consequences for the organization and its functions, are: a) uncorrelated objectives with controlling actions; b) lack of knowledge, abilities and skills of the controller; c) quality / quantity of the processed information related to identification and applicability of the corrective measures.

### Conclusions

A careful observation of the above mentioned periods, help us concluding that, historically, the theory of the managerial control are phased out in large cycles 25-30 years, moving between approaches focused from maximizing the efficiency (the Age of Scientific Management and the Rationalized Systems one) to approaches focused on employees (the Age of Industrial Revolution, of the Human Relationships and the one of Organizational Culture and Quality).

As a continuation of this conclusion, we can think of a new age of internal control characterized by a group of premises (standards imposed by regulations) helping us to assess and decide upon the internal managerial control within an organization and its specific actions. As direct applicability, we will try to conceptually design this new period, which we will named “a standards” one and we consider it’s already undergoing together with the issuance of the *Minister of Public Finance Order no. 946 / 2005 approving “Internal Controlling Code, including management and control standards for the public institutions” to develop managerial controlling system.*

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<sup>8</sup> We should have in mind exclusively the area of applicability for the internal control, as it is defined in Law no. 500 from 11<sup>th</sup> of July 2002 regarding public finances. According to art. 1, point 30 by public institution we understand: “... Parliament (Senate, Deputies Chambers, n.n.), Presidential Administration, ministries, other specialized institutions of the public administration, public authorities, public institutions, their subordinated institutions, regardless their financing scheme”.

<sup>9</sup> The two wordings “internal control” and “managerial control” are used in this paper having the same meaning.

- **The Age of the Internal / Managerial Controlling Standards**  
[2005-present]

Following in-depth analysis made in the '90, the concept of internal control has been modified in a significant way. We found new constrains (controlling environment, risks assessment, monitoring, self-evaluation etc.) which finally can be found in the internal control standards. Controlling becomes a concept for the study of complex sciences and, from this perspective, its role as the main responsibility of a manager is reconsidered within the entire process of guiding the organization towards its fundamental and specific scope.

The main constrain revealed within this period is that the manager proves he /she is capable of undertaking the internal control only if presenting proves he/she respects the standards. An important signification is given to the issuance of the internal procedure establishing how the activities are conducted and how they contribute towards achieving its specific scope.

In this new perspective, the managerial responsibility defines a juridical relation obliging the task fulfillment by the manager of the public institution meaning to effectively manage, within some internal and external constrains and in accordance with law provisions, efficiently achieve the results, to communicate and fulfill managerial obligations in accordance with juridical liability. Middle level managers' responsibility derives from the top management of the public institution for all five components of the internal / managerial control within public institution: controlling environment, performance and risk management, information and communication, control, audit and evaluation.

In our country, *Law no. 234 / 7th of December 2010 modifying and completing The Government Ordinance no. 119/1999 regarding the internal control and the financial preventive control*<sup>10</sup> establishes competences and responsibilities of the main decisional actors in public sector management and public patrimony administration. Thus, *Law no. 234/2010* mentions that *Ordinance no. 119/1999 regarding the internal control and the financial preventive control*, has been modified and completed with provisions establishing that to each financial situation of a budgetary year a report will be attached regarding the internal / managerial control. This is an exclusive responsibility of the top manager, firmly highlighting, his/hers obligation related to organizing and controlling according to specific standards. If the top manager doesn't fulfill this obligation of preparing the annual report of the controlling system this will bring penalties, according to the law.

In accordance with normative above-mentioned Order no. 1649 / 2011 was issued modifying and completing Minister of Public Finance Order no. 946/ 2005 approving "Internal Controlling Code, including management and control standards for the public institutions" to develop managerial controlling system. Details were given for the legal framework related to instructions for preparing,

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<sup>10</sup> Published in the Official Journal of Romania no. 831 / 13<sup>th</sup> of December 2010.

approving and submitting the annual report<sup>11</sup> of the top manager regarding the internal / managerial control system and annual / quarterly factsheets regarding the stage of the controlling system implementation. The date for submission is established by normative.

Reporting represents the official form proving that the top manager is taking the managerial responsibility of controlling.

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8. \* *Government Ordinance no. 119/1999 regarding the internal control and the financial preventive control*
9. \* *Minister of Public Finance Order no. 946/ 2005 approving “Internal Controlling Code, including management and control standards for the public institutions” to develop managerial controlling system*
10. \* *Minister of Public Finance Order no. 1.649 from 17th of February 2011 modifying and completing the Provisions of the Minister of Public Finance Order no. 946/2005 Approving the internal control code*

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<sup>11</sup> The first annual report on internal / managerial control of the public entity was prepared at the closing date of the financial year 2011.