THE FINANCIAL MANAGERIAL CONTROL PROCESS WITHIN THE COMPANY

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Abstract: *In an uncertain and volatile environment, organizations must adapt to the conditions and respond appropriately to its challenges in their favor. The goal of any company is to achieve performance and create value. But, the progress of an organization is measured by the continuous comparison of the results obtained with the targets provided in the strategy, plans and programs. This is where managerial control comes in. This work is aiming to answer the question: Why is the process of managerial control useful? For this purpose, the managerial control process in general and the financial control process are presented. The main techniques applied in financial managerial control are specified, insisting on budgetary, cost and inventory control. It is also proposed a framework for any managerial control process.*

Keywords: *managerial control process, financial control techniques, budget control, costs, inventory*

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1. Introduction

The goal of any company is to achieve performance and create value in competition on the market, based on competitive advantage. The internal sources of competitive advantage generally refer to new ways of approaching the business that exist or can be created within the

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organization, to technical aspects regarding new ideas, and generally to all aspects within the organization that can create an advantage compared to competition (Negulescu, 2020). But, the progress of an organization is measured by the continuous comparison of the results obtained with the targets provided in the strategy, plans and programs. This is where managerial control comes in.

Managerial control is the process by which a business can be managed, based on progress evaluations and the needs that employees must have met in order to meet production expectations. It is heavily dependent upon the standardization of processes or the regulation of outputs such that management can easily compare expected workflow to real-time workflow and adjust processes as needed. It also involves examining past processes, evaluating present processes, and designing future processes in order to create a streamlined, efficient workflow that standardizes outputs (Conklin & Grimsley, 2022).

Managerial control, although it is carried out with the support of other people with different functions within the company or the support of internal auditors, is dynamic and decentralized. It is usually carried out on the basis of procedures and rules, based on the established objectives, plans and programs, as well as the results obtained, with the aim of creating value for the company.

The main control systems in organization management are: production control, budget control, cost control and stock control, which are quantitative systems, or personnel efficiency control, as a qualitative system.

The paper wants to illustrate the necessity of the managerial control process in any company. The research is fundamental, and the research methodology is based on the study of references, direct observation and own opinions.

2. Managerial control process

Management control is based on a process of setting objectives, planning, budgeting, implementing, monitoring projects, analyzing results, and taking corrective actions. The purpose of management control is to create greater coherence within the organization and enhance goal congruence (Löning et al., 2016).

An effective management control system must have characteristics that align with the organization's goals and objectives. Although MCS differs from organization to organization depending on their goals, nature of business, and management styles, the following characteristics help curate a better MCS system (Vaidya, 2023):

- *Alignment*. The MCS must align with the organization's larger scheme of things. It must fit the organization's structure, be congruent with the objectives and goals, and help the decision-making process.
- *Rewards*. Management control techniques must motivate employees across departments and stature to work towards their individual and organizational goals through regular incentives and rewards.
- *Decision-Making*. The MCS must be able to process data and provide the managers with helpful information to make decisions and facilitate improvements in processes and daily activities within the organization.
- *Measurability*. The system's main objective is to provide data points that help the organization achieve optimal efficiency levels concerning its goals. Therefore, ensuring that the metrics in contention for measuring the performance are measurable in real terms is essential.
- *Communication*. When a variation from the goals set for a particular employee or a department is detected, the system needs to communicate to the assessor about the divergence from the set goals.

The following are the steps involved in the control process (Keup, 2021; Byjus, 2023; open.lib.umn.edu; Merchant, 1982):

- Establishing standards and methods or ways to measure performance.
- Measuring actual performance.
- Determining if the performance matches with the standard.
- Taking corrective action and re-evaluating the standard.

More specifically, the control process includes the steps shown in fig. 1.

Briefly,

1. Based on the company's strategic objectives, the management issues plans and programs.
2. In order to achieve an effective control, work procedures or standards are created.
3. Measurable, quantitative and/or qualitative indicators are established.
4. Following the execution of the stipulated works, the progress or performance is measured based on the results obtained.
5. The results obtained are compared with the established indicators.
6. Next is the analysis of the deviations.
7. Following the decision, the necessary corrective measures are taken.
8. Finally, the feedback of the established corrective measures can lead to the resumption of the process.

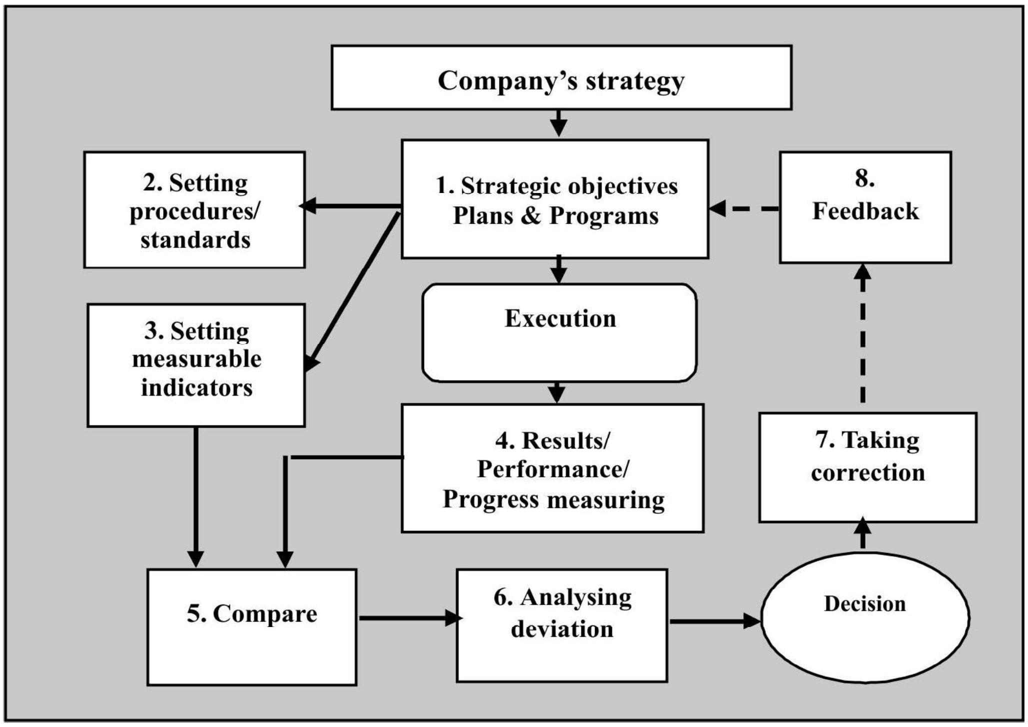

Figure 1. The process of managerial control

(Author's concept)

It's important that managers monitor and control the process from start to finish. That includes not only the controlling process, but any actions planned to resolve the deviation or reset the standards. An understanding of the controlling process shows if plans are being met and, if not, what actions need to take place in order for them to be met (Keup, 2021).

Corrective measures are simpler and immediate, such as the accidental lack of a material resource that can be purchased, a financial or human resource that can be reallocated, or more complicated and long-lasting, such as obtaining financing or modifying some technological operations.

The controlling function does not end by taking corrective action as it is a continuous process. After suggesting the corrective measure a feedback report is prepared. Feedback refers to list of reasons for deviations of plans or for inefficiency in overall working of organization; along with reasons the corrective measures are also specified in the feedback report and feedback acts as a base to establish the standard for next year and controlling process again starts from the first step (Mbaknol, 2023).

3. Control in financial management

The implementation of financial plans without adequate control and feed-back does not ensure the efficiency of financial management activities.

The controlling process in business management is when managers set, measure and refine their business operations and manage cost control. By using a controlling process, a company can navigate changes to the supply chain, customer demand and other variables that impact a company's livelihood (Keup, 2021).

3.1. Techniques applied to financial control

Some of the techniques are: Personal Observation; Budgetary Control; Break-even Analysis; Ratio Analysis; Cost Control; Internal Audit;

Statistical Reports; Management Audit; Return on Investment and Others (Sharma, 2023).

1. *Personal Observation.* Personal observation of the actual performance of the subordinates at the workplace is the most effective, direct and oldest method of control. The managers need to hold discussion with the persons whose work is being controlled and they should watch the actual operations.

2. *Budgetary Control.* Budgetary Control is the process of using budgets for comparing the actual performance with the corresponding budget performance in order to find out the deviations, and to remove the deviations by either adjusting the budget estimates or correcting the causes of deviations.

A budget is a highly useful tool for controlling the day-to-day operations of the enterprise. It provides a standard by which actual performance can be evaluated to find out the deviations from the planned results. This information enables the managers to take corrective action for bringing the actual results in conformity with the plans. Budgetary control is an effective and widely used control technique.

3. *Break-even Analysis.* Break-even Analysis is an important technique of cost control. It is an analysis of the inter-relationships among the cost of production, volume of production and the amount of profits.

4. *Ratio Analysis.* A Ratio is an arithmetical relationship between two figures. 'Ratio Analysis' is a study of ratios between various items or groups in the financial statement of an organization. With the help of such analysis, the efficiency of financial performance of an enterprise can be judged. It measures the financial condition, profitability and efficiency of the enterprise.

This analysis is an important technique to exercise control over the departments of an enterprise. Some important examples of Ratio Analysis are the analysis of Liquidity Ratio, Leverage Ratio, Turnover Ratio, Profitability Ratio, Valuation Ratio, etc.

5. *Cost Control.* Cost Control is an important technique for financial controlling process. The technique of cost control involves the

determination of the standard in respect of each item of cost, ascertainment of the actual costs regarding those items, detection of variations in order to determine the responsibility, cause, extent and cost of each variance, and then taking necessary action to ensure that the current costs conform to the standard costs in the future.

Control over costs can be effectively exercised not in total but in the various components or elements of the total cost of any job. Therefore, first of all, it is necessary to control each element of the total cost.

6. *Internal Audit.* Internal Audit is an effective technique of financial and managerial control. It means the independent process of verifying and evaluating the accounting, financial and other functions of the business organization. Internal Audit is carried out by the managers themselves or by the special staff appointed for this purpose.

7. *Statistical Reports.* The analysis of Statistical Reports is a very important tool of control. Often quantitative control is exercised on the basis of analysis of the statistical reports prepared by different managers or higher authorities of an organization.

In such reports, they provide various information in respect of the accomplishment of work productivity, effectiveness and efficiency of the subordinates, deviations of performance from the standards, and the possible reasons for the deviations of the work or responsibilities allocated to different employees of the company.

8. *Management Audit.* Management Audit is an overall and scientific evaluation of the quality of management. It is an independent and critical examination of the entire management process. It is a systematic search and appraisal of the efficiency and effectiveness of the managers of an enterprise. It locates the deficiencies in the performance of management functions.

Therefore, management audit is a comprehensive and constructive review of the performance of the management team of an organization.

9. *Return on Investment.* Return on Investment (ROI) is a useful tool of controlling overall performance of an enterprise. It is also called 'Return

on Capital Employed' (ROCE). The basic aspect of this technique is that profit is taken not as an absolute figure but is considered in relation to the invested capital.

Rate of return is calculated by dividing the net profits by the total amount of investment. It can be computed in respect of historical data so as to reveal the rate of return realised, or it may be applied to budgeted data to give a projected rate of return.

10. *Network Techniques.* Network Techniques are being widely utilised as control systems. In such technique a project or programme is broken down into small activities which are arranged in a technological sequence.

Various activities should be accomplished according to the sequence. The time limit for each activity is determined.

A network diagram is then drawn in order to present the inter-dependence and inter-relationships among all the operations involved in the project.

3.2. Budget Control Process

Control in financial management represents the feedback obtained from the comparison of the performances obtained against the plan or the planned budget in order to measure the efficiency of the use of the resources used to achieve the managerial objectives.

Budgetary control starts as soon as the budget has been approved, as the expenses incurred and the incomes obtained are monitored in financial terms, i.e., the differences obtained compared to the plan or budget are analyzed in order to decide on corrective actions.

Accountability in the control system is designed through the organizational structure of the organization, through which the people at each level report to the people at the higher level. The tool used is the budget control report which represents "the most important vehicle of the feedback process and which ensures maximum effectiveness" because "actions bring benefits while information only produces costs

(Lucey, 2000) because, through the budget control report, the necessary corrective actions are decided.

The role of budgets is to serve in planning activities, forecasting the future of the organization, allocating resources, measuring activity results and performances, controlling the use of financial funds. Here we find the functions of finance discussed in the first chapter: allocation, distribution and control of financial funds.

The advantages of budgeting can be formulated in a few ideas, as follows:

- It provides a framework for planning, i.e., for managers to think about the future, to identify the organization's objectives and to establish the sources and the level of financial sources used to achieve the objectives;
- It provides a framework for financial activity: the forecast of cash flow, operational situations and the balance sheet or the patrimonial situation;
- Constitutes a tool for evaluating the efficiency and effectiveness of actions and operations;
- Provides continuous feed-back on how the actions are suited or not to the objectives and on how to distinguish controllable changes, which are the responsibility of managers, from uncontrollable ones, which are related to changes in the remote external environment;
- Encourages responsibility and increases motivation at all managerial levels.

The budgets can be: fixed, flexible and continuous.

The fixed (static) budget is designed to remain unchanged even if the volume of activity changes. This type of budget is not useful because forecasted income and expenses rarely match actual activity.

The flexible budget is designed to change in accordance with the variation in the volume of activity. Fixed costs are not affected by the variation in activity, but variable costs increase or decrease depending on the variation in production and sales. In this case, the actual and planned costs are calculated according to the volume of activity. This system allows a significant comparison between the two types of costs: planned and real (effective). Changes to the budget are made after the activity has been completed and are monitored (monthly, quarterly, half-yearly). The flexible budget can be useful in controlling the performance of the activity, especially the costs and performances.

The continuous budget takes into account simultaneous variations and changes affecting a wide range of activities. The budget can be modified whenever there is a variation, a change in activities, based on the argument that the budget represents the manager's horizon.

The budget is a managerial tool used in the management, control and evaluation of financial performance.

Managerial budgetary control as a system includes the following subsystems (Garrity, 2000):

- Planning: what should happen in a future period of time.
- Reality: what actually happens.
- Comparison: reality is compared with the plan to establish the differences.
- Validation: differences are evaluated and explained.
- Action: corrective measures are identified and these corrections are practically applied.

However, the use of the managerial control process presented in fig.1 is also valid in financial managerial control.

The budget provides, as have shown, a periodic feed-back on the performance of the various activities, the organization and its managers. By comparing what is actually happening with what is in the plan, managers not only evaluate their performance, but can assess deviations from the plan and take timely corrective action. Where the system does not signal any change to the plan, it means that it is "by exception" management. Deviations of actual facts from the plan sometimes represent positive aspects, that is, things are going better than we planned, or negative aspects, which mean that things are going wrong and we must immediately apply corrective measures.

Financial statements and budget control reports can be influenced by a number of factors, such as:

- different accepted or imposed accounting concepts, conventions or standards;
- different methods applied to determine the value of stocks at the end of the financial year, to inventory, to calculate depreciation, others;
- fiscal and legislative regulations;
- personal conception of the managers;
- facts (real-life events and their impact on financial statements).

As a rule, the variations recorded in income and expenses are considered satisfactory if they are located in a certain "control band", having an upper and a lower limit, called "control limits". Control limits are established by estimation or statistical analysis. The estimate is based on experience and judgment and it is generally considered that a wattage of ±5% is not significant.

Statistical analysis through probability tests is based on the normal distribution to determine whether the variations between the budget and the achievements arise from chance or from controllable causes. If it is assumed that the budget allocation is the arithmetic mean of the population, the level of variation can have the values from table 1 (Lucey, 2000).

Table 1
Level of control limits

Variation	**Control limits**
5%	Mean ± standard deviation 1.96
2%	Mean ± standard deviation 2.33
1%	Mean ± standard deviation 2.57
0,2%	Mean ± standard deviation 3.09

Source: Lucey, 2000

If, for example, from the historical records the standard deviation is 110 euros, and the budget allocation is at an average cost of 3300 euros, then the 5% control limit is on average ± 1.96 or 3300 ± 110 euros.

Although statistical analysis seems to be a rigorous method, in practice it is possible that the distribution of values is not valid or the calculations are difficult to perform.

3.3. Cost control

In an organisation are many activities that are covered by indirect costs. These are necessary to have an efficient management and thus to create value for the organization. But indirect costs, like inventory, physical assets and other resources must be controlled and maintained within optimal limits. Too high expenses lead to the waste of financial funds, and too little expenses lead to the impossibility of providing resources for the processes of transforming inputs into outputs.

A planning and control system is also the budget-based activity through which the organization's activities are identified, the factors that cause costs are determined, and then costs are collected for analysis and improvement decisions.

'Responsibility Accounting' is the technique of accounting in which the performance of various employees is evaluated by ascertaining how far they have implemented the pre-determined targets set for the departments, units, sections, or divisions for which they are responsible (Sharma, 2023). The use of responsibility accounting focuses attention on management by objective rather than management by domination. Each employee is responsible for his area of operation and for effective control. It is necessary to be known what the costs should be and what the costs were. Thus, in responsibility accounting, costs are allocated to responsibility centres instead of products.

A responsibility centre is an organizational unit such as department, division or section headed by a responsible person. The head is responsible for reaching the target set for the centre. The costs incurred by a responsibility centre are divided into two categories: Controllable costs, and Uncontrollable costs. Costs are accumulated and reported according to the classification. The head of a responsibility centre is responsible directly for the controllable costs of this centre.

There are three types of responsibility centres stated as follows:

1. *Investment Centres*, where the head of this centre is responsible not only for costs and profits but also for the effective use of assets. The investment made in each centre is separately calculated and the return on investment is applied as the basis of evaluating the performance of the centre. It is the ultimate extension of responsibility.
2. *Cost Centres*. Most of the departments and sections have cost centres. In a cost centre the targets are fixed in terms of costs. The performance of cost centres is evaluated by making a comparison between the actual expenses and the budgeted costs. In cost centres, the control system measures only the costs incurred by responsibility centres; no attempt is made to measure the value of their outputs.
3. *Profit Centres*. In a profit centre the targets are set in terms of profits. The performance of this centre is evaluated by comparing the profits actually earned with the target profit. This is done by preparing the departmental profit and loss account.

3.4. Inventory control

Inventory control is carried out at least annually during the asset inventory. Since, in many organizations, there are thousands of raw materials, materials and products that make up the inventory, periodic control is usually carried out by the Pareto method or the 80:20 rule, which means that 80% of the stock value means 20% of the stock components.

Inventory are intended to ensure the rapid satisfaction of demand for production or for the market (finished products) and to absorb seasonal fluctuations. But these are associated with the costs of obtaining, storage and with the losses for inventory without movement, damaged or no longer needed. Therefore, inventory control comes to identify sources of unnecessary costs that can be reduced or eliminated.

In order to achieve efficient management of inventory, the adoption of the latest technologies is a great solution. Using new technology is like a superpower that enhances your businesses capabilities (Ramachandra, 2022). By comparing the resources used and the products or services produced, appropriate financial decisions can be made. The purpose of management is to increase the value of the organization and financial management supports decision-making by providing data, information and financial analysis.

In support of the control of the organization's management and financial management come the specific activities of internal financial control and external financial audit.

By permanently controlling the creation and use of financial funds, managers can increase the value of the organization. Therefore, financial managerial control is a vital tool in the life of an organization.

Conclusions

The control ensures the feed-back necessary for managerial decision-making by taking into account the deviations from the objectives planned through budgets in order to increase the value of the organization.

Therefore, the control function should not be misunderstood as the last function of management. It is a function that brings the management cycle back to the planning function. Thus, the control function acts as a tool that helps to find that the actual performance deviates from the standards and also finds the cause of the deviations and attempts to take corrective measures based on them (Negulescu, 2022).

At the same time, managerial control ensures "Simplifying supervision within an organization, delineating the specific responsibilities of supervisors and the specific responsibilities of workers, as well as how these sets of responsibilities overlap. Ensuring quality of outcomes as well as efficiency in achieving outcomes". (Conklin & Grimsley, 2022).

It is essential for the process of Management control to be present at all levels and in all functions with two main goals:

- To allow each manager to control his management unit in order plan and program means, stages and monitor performance;
- To allow each manager to present the results he has obtained, the decisions he has taken, the objective towards which he is heading (Sundharavadivel, 2018).

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