

Designing rules with justice in mind

Natàlia Cugueró-Escofet and Josep M. Rosanas argue that management control systems based on just principles are what lead to optimal business results.

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Decisions taken by executives in the banking sector are coming under close scrutiny in the wake of the global financial meltdown. Were the rules of the game the problem, or was it the behavior of the people who were supposed to follow them?

To generate meaningful debate and identify a path forward for companies, Natàlia Cugueró-Escofet and [Josep M. Rosanas](#) of IESE look at the vital role that Management Control Systems (MCS) play in business today, how they may impact organizational behavior and their relationship with organizational justice.

They argue that formal MCS must be designed with justice in mind, but just as critical is the behavior of the managers using them.

Formal justice

Formal justice, as articulated by the official rules of a company, has a major impact on organizations. When managers perceive company rules to be just, they tend to react positively.

Such rules help align the company's goals with the individual goals of employees. Assessment procedures need to be consistent, so that people are clear about when and how they are going to be judged and rewarded.

The just design of MCS distributes resources and responsibilities according to rules that are explicitly established ahead of time. Managers are evaluated on functions over which they

have some degree of control, and a minimum reward is received by all participants.

Finally, just MCS include ways of addressing injustices, as well as avenues for improving the systems.

Informal justice

Beyond the formal rules, MCS must also be guided by informal justice. Since rules cannot be created for every possible situation, employees' informal understanding and application of justice in all decision making becomes vital.

In other words, MCS will always be affected by the subjectivity of the people who use them.

As such, it's not enough just to include a set of justice requirements in the design of MCS.

Degrees of goal congruence

In designing and using MCS, there are four possible combinations, which lead to very different outcomes.

- A just design interwoven with just use of the system leads to maximum goal congruence.
- An unjust design combined with just use leads to occasional goal congruence.
- A just design combined with unjust use leads to perverse goal congruence.
- An unjust design combined with unjust use leads to minimum goal congruence.

In the ideal scenario — where just design is used in a just way — both formal and informal justice are at work. This sets up optimal alignment of employee behavior and organizational goals.

When there is maximum goal congruence, managers apply existing rules proactively and consistently. They instinctively analyze circumstances at all times and check every decision to ensure that the system design makes sense and leads to just outcomes.

When fairness is perceived to be lacking, people can petition the manager, who, being just-minded, may consider changing certain aspects of the system.

When justice is present in both design and decision making, people are motivated to make the greatest possible effort to cooperate with their peers and managers to achieve corporate goals.

They see their own objectives as part of a greater goal, which is to be achieved through the joint efforts of everyone in the organization.

System/use mismatches

When there is an unjust system combined with just use — that is, occasional goal congruence — managers who act justly can actually transform the system. This can eventually lead to maximum goal congruence.

Take, for example, the MCS of a newly launched company. Its MCS would typically be rudimentary and incomplete. It may be that the systems are designed to assign bonuses in ways that work well for the sales department, but offer zero incentives for people in other departments who support the sales force.

To remedy this situation, a manager could apply one or both of two measures:

- Adopt reparation policies.
- Implement incentive schemes for support staff, so that they are also evaluated and rewarded based on the support they provide.

In this case, informal justice would spur improvements in the design of MCS.

When a design is just and the system is used unjustly, dysfunctional learning occurs. This can lead managers to demand changes in the system itself — for example, stricter rules, which are usually harder to adhere to.

What's more, when there are too many rules to follow, people tend to overlook those that they don't consider to be important.

Research shows that when people think they are being treated unfairly, their first reaction is to blame the design of MCS. This often triggers changes in MCS, making them more rigid. Many times, these new rules actually worsen the level of justice.

Reaching the highest level

To achieve the highest level of goal congruence and, consequently, superior business performance, the people who work in the organization must clearly focus on the just use of MCS.

If the current systems are perceived to be just, do not simply adopt more rules. In addition, if systems are used justly, MCS will become more just in their design as they evolve over time.

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