A COMPARISON OF EFFECTIVENESS FOR CENTRALIZED AND DECENTRALIZED BUSINESS DECISION MAKING

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ABSTRACT

There has been and will always be an on-going battle to determine which decision making style best fits a business. It is up to the individual business to determine which style best fits their work environment. Centralized and decentralized decision making are two of the most well-known forms businesses and corporations consider when determining the most precise decision style. Both styles offer advantages and disadvantages, while a hybrid model allows decision makers to choose advantages of both. There may not be a precise model to follow, but yet there is always a style that fits a business environment perfectly.

KEYWORDS: Environment, Centralized, Decentralized, Precise, Advantages, Disadvantages and Hybrid

INTRODUCTION

A Comparison of Effectiveness for Centralized and Decentralized Business Decision Making

Businesses are always faced with many challenges and obstacles. Many of these challenges are derived from a common concept of decision making. The idea of decision making is due to the amount of choices a business is confronted with. However, the main idea is to make the best intellectual decision, which in return creates for an easier managed workforce and a higher rate of profit. There are many different decision making styles a business can choose from, many of which have different aspects and benefits. Therefore, from the beginning, a business has decisions of which decision making style best fits their work environment.

Two of the most common decision making styles include centralized and decentralized decision making. While both have degrees of success and failure, centralized is typically used most often. Aspects such as efficiency, control, and profitability should be evaluated using both styles before choosing which one performs best for an individual business or corporation. It is vital that a business observes both positive and negative side effects to ensure their decision is well based and can ensure them the highest level of success. “There has been an ever going battle on which organizational structure is the most effective and profitable in today’s business world… centralized, decentralized, or hybrid” (Seeds & Khade, 2008, p. 99). Therefore, a comparison of effectiveness for centralized and decentralized decision making should be evaluated.

Centralized Decision Making

Centralized decision making can be defined as, “The degree to which decision-making authority is kept at top levels of management” (Seeds & Khade, 2008, p. 99). In essence the top level managers are the only individuals that are given the authority to make crucial decisions within the business. This style of decision making has been the most
commonly used practice when compared to the decentralized style. An example would be a manager of a retail business deciding which sales tactics would be more beneficial, rather than a sales clerk deciding the more beneficial tactics.

**Advantages of Centralized Decision Making**

There are many side effects that are related to a centralized decision making style, some of which are great advantages to a business. The most common advantage found with a centralized style is cost efficiency. Top level managers can cut straight to the chase, determine what problems need to be solved and which solutions are most appropriate. Within businesses there are often project managers. “Centralized project managers report to a centralized project management organization (PMO). A centralized PMO is defined as an organization to which project managers report and from which they receive direction, guidance, and oversight” (Curlee 2008, p. 83). This allows project managers to communicate with an organization as a whole, in which they can then evaluate their decisions, ensuring cost effectiveness in a timely fashion.

Seeds and Khade (2008, p. 100) noticed other advantages which include simplified reporting, accuracy in reporting, ability to easily align employee objectives with corporate objectives, and standardization of content. Centralized decision making also comes with reduced conflict. When one person or small groups of individuals are responsible for making decisions, companies often encounter less conflict. A larger group of decision makers often yields more ideas and opportunities, which can lead to more conflict. More precise and quicker execution also becomes another advantage.

There is also a level of control that is developed with fewer decision makers. “Reduction in number of administrators” evaluated by Seeds & Khade (2008, p. 101) proves the point of less conflict and the advantage of fewer paid employees which can also lead to cost savings. Top level managers are typically entitled more control to make decisions over lower level employees.

**Disadvantages of Centralized Decision Making**

Although there are many advantages to a centralized decision making style, there are also many disadvantages. One of the most common disadvantages is the resistance or the caution of change. When top level managers become comfortable with their level of command and control, it often becomes challenging for them to see the viewpoints of other employees; therefore, alternate decisions often become ignored. Changes or amendments to a businesses operating system can be rather stressful and complicated for all employees. Along with a caution of change comes the idea of less creativity. When individuals feel more empowered, a coward mindset may be created, causing lower level employees to hold back their ideas.

Commitment is another struggle involved when a company incorporates a centralized system. After top level managers have held a position for a long period of time, they become the only go-to individuals for results and innovation. “There’s a tendency to be insensitive to your user’s needs, particularly those in locations remote for the centralized function” is a statement made by Allan B. Deering, Vice President-MIS, *Pepisco* (Deering 1987, p. 39). Contradicting the advantage of quick response times mentioned earlier, centralized systems can also have time delayed decisions and actions. Information established with lower level employees that need to reach top managers may take extensive amounts of time before it is ever resolved. Those decisions must follow a chain of command or hierarchy system which can be a hamper to a business.
Decentralized Decision Making

Decentralized decision making can be defined as, “The degree to which decision making authority is pushed down to lower levels of the firm” (Seeds & Khade, 2008, p. 99). In essence lower level managers or employees are responsible for identifying and resolving decisions. This style has become a newer trend of decision making styles for business more recently. For example, a factory worker has noticed machine troubles and realizes it needs repair or replacement; they then have the authority to make a decision of which action is best for the business.

Advantages of Decentralized Decision Making

Just as centralized systems have advantages, so does decentralized systems. “It makes it more effective and more capable of doing its own tasks” (Drucker 1974, p. 301). Drucker is stating that individuals that have the authority to make decisions without going through the levels of hierarchy are capable of making decisions that are more effective. Therefore, decisions can be made more quickly, saving time and money, which can yield a higher rate of profit.

It makes management more effective by enabling it to focus on the tasks which management needs to perform and to relieve itself of those tasks which management need not perform, does poorly, and spends too much time on if loaded down with them (Drucker, 1974, p. 302).

In essence, Drucker is evaluating the idea that top level managers have their plates full enough, make irrational decision due to their lack of knowing situations firsthand, or simply do not make effective decisions properly. This ultimately relieves the heavy burdens of top level managers, making their jobs much simpler.

Seeds and Khade (2008, p. 101) concluded other advantages include, “Increased control at the local level, ability to manage more content, and the ability to add spot training instantly when needed.” A decentralized systems also gives the lower level employees a sense of empowerment or authority, which can often lead to better work ethics and task accomplishment. One of the biggest advantages is simply the daily hands-on tasks of lower level employees who are more familiar with business procedures and can promptly identify objects that need more attention.

Disadvantages of Decentralized Decision Making

One of the most hazardous conditions of the decentralized style is the concept of human error. Any individual is prone to make mistakes. However, if decisions are reviewed by other employees, errors will become less evident. Decentralized systems typically work best when implemented in environments that change rapidly. If environments remain consistent, there is no need for continuous, and such precise management.

Top level managers often have a mental set-back when implementing a decentralized approach. Considering they commonly make the majority of decisions, they are then more like a second resource. This simply causes conflict with employees, which can be difficult to resolve.

The Hybrid Model

A common saying is, “the best of both worlds”. That is the idea behind the hybrid model of centralized and decentralized decision making. Many businesses possess the hybrid form where decisions that need to be made by top level managers are kept by top level managers and where decision that need to be made by lower level managers are kept by lower level managers. Time and money savings can be essentially doubled considering decisions can be made quickly, effectively, and collectively.
Determining the Best Approach

As stated previously, one of the first decisions a business encounters, is what style of decision making works best for them. Although two of the primary choices are centralized or decentralized, there can also be a hybrid form, which collaborates options of both. At other times it may also change for short periods of time, depending on the work environment.

“Although organizations can deal with corporate communications using either a centralized or decentralized approach for general purposes, when it comes to a crisis, the approach must be completely centralized” (Argenti, 1994, p. 180). Argent is stating the most important decisions during a crisis should come from top level managers. This can allow them to make more precise decisions at a quicker rate, which can most importantly save a company.

When a business determines which approach to implement, there are many aspects to review and consider before making a final decision. However, Deering states, “There’s no right answer. It’s which approach works best in your specific environment” (Deering, 1987, p. 39).

Time Based Approach

Many businesses make decisions based on time. If time is essential and decisions need to be made quickly at the front line, a decentralized approach would work best. Employees can quickly evaluate situations and determine the best decision. If time is not essential, top level managers can make decisions accordingly, giving them the benefit of decision efficiency.

Efficiency Based Approach

A major aspect of decision making is its efficiency. It is crucial that businesses make the correct decisions the first time to prevent the time delay of making the same decision again. Both top level managers and lower level managers can make efficient decisions based on their work styles. Therefore, the final decisions can be made by top level managers.

Size Based Approach

A business must also include an evaluation of their operating size. If a business is fairly large, a more decentralized approach would enable them to have more control. A small business however may not benefit as much using the decentralized style, but can make precise decisions with a small management organization.

Implementing Change

Once a business decides which style best fits their needs, it is vital that all employees understand their authority level and which decisions they can make. Before making changes, there must be a realization that change is needed (Seeds & Khade 2008, p. 103). A current television show, Undercover Boss, shows individuals how this works. A top level manager, usually the CEO, goes undercover to secretly investigate how their business is operating. The individual can see the actions made on the front line of business and determine which operating styles work best. They can then evaluate their research and implement the change to make their business more efficient. It is vital that top level managers understand every aspect of a business.
A follow-up to change is also vital for a business to perform. Change and variation within a business takes time, patience, and information results. If there are no positive effects created with change, another change may be needed.

**Study Results**

Many studies have been conducted with the attempt to determine which operating style will work best. Jan Zabojnik developed a test comparing centralized and decentralized decision makings. It was found that a system of decentralization would yield similar results, considering the workforce and constraint of the employee was the same. This would be a comparison between the top level manager and the lower level. Other incentives which may affect a change would be pay differences, such as wages, bonuses, and promotions.

Zabojnik sums up the conclusion by ensuring the reader that centralization is the more profitable choice. This is based on conclusions concerning employee’s pay wages are similar in both situations (Zabojnik 2002, pp. 1-21).

Various studies have also been conducted to determine differences in trainings or managers in both decision making styles. Wanda Curlee conducted a test of just that. Statistical analysis from the survey conducted, proved there were differences in training styles received by project managers. Statistical results repeatedly showed more extrusive training for managers involved with a centralized style. This was necessary for relations with other cultural corporations and the compliance of their business. (Curlee 2008, pp. 87-88)

According to Seeds and Khade (2008, p. 102) the percentages of companies that implement centralized, decentralized, or a hybrid model are all close. Approximately 31% have discovered a hybrid model, gaining benefits of both centralized and decentralized styles. Business containing the standard centralized style equates to 31% also. Considering decentralization is becoming a newer style of decision making, 38% of businesses have chosen that to be their new style. These close range percentages prove a consistency to the idea of each business implementing styles that best fit their organization.

**Current Examples of Implementation**

Considering centralized decision making was once the “social-norm” many businesses have experimented and completely evolved into a more decentralized system. Many automobile companies have reevaluated their process of decision making, and determined a decentralized approach is simply the best. General Motors was one of the first to implement this change (Seeds & Khade, 2008, p. 102).

Both styles have their advantages and disadvantages. “Centralized operations benefit from economies of scale, better utilization, and flexibility. However, decentralized plants may have lower logistics costs and are more responsive to the dedicated assembly plant” (Seeds & Khade 2008, p. 102). In this situation there must be a determination to verify if easier operating styles with a centralized style is more beneficial than decentralized operations containing less inventory and quicker feedback.

Other corporations, such as Intel, have discovered a change to decentralization is not efficient. Many technological companies derived the conclusion a decentralized style best fits the needs of their consumers. However, with rising levels of new technology phases and new products, the time phase of decision making for Intel was much too long. The time it would take for front line employees and research teams to develop new ideas and make decisions was hampering their profit margins. Therefore, Intel reshaped and refined their company to a complete centralized style.
Other businesses are simply guided in one direction based on consumer business. General Electric for example is a vast company. Containing many sub-companies, it is more difficult for a CEO based in headquarters to make decisions for the consumer-based field. A decentralized style is the best option to implement. Individual managers must report statistics to top level managers to ensure efficient time control and precise decisions.

Analysis

Decisions are constantly being made by individuals and businesses. For those who withstand high expectations, the best decision is often more than one or two options. As for a business or corporation, there exist many styles of decision making. Centralized and decentralized are simply two of the most common classifications.

The majority of decisions an individual or individuals make are not straight-forward. All decisions come with effects. Some effects can be prosperous, while others can be detrimental. With hopes of making all prosperous decisions, it is essential to know the effects of all decisions available before choosing a single one.

When a business is deciding whether to implement a centralized or decentralized structure, time and cost efficiencies are the top aspects to consider. Without understanding how a business operates, decision making is rather useless. Without understanding which style will best suit a business is even more useless.

Both centralized and decentralized decision making styles offer great opportunities for success and profitability. Centralized styles should be implemented more often where top level managers should be held accountable for decision making. Decentralized styles should be implemented when front line employees and lower level managers have a better understanding of the business, which entitles them to make more decisions.

Considering the centralized method has been implemented most, many businesses are conscious of its benefits. With a centralized style, decisions can be made more efficiently. Top level managers are aware of how the business operates and are capable of determining actions that will improve the overall success. There is a level of reduced conflict and reduced decision options allocated, which can lead top level managers straight to the chase and make conscious decisions.

Decentralized styles have become an innovative way to steer away from the common centralized styles. Benefits regarding decentralized styles include quick response time, increased control at the local level, and reduced pressure on top level managers. All of which can also make a business more profitable.

CONCLUSIONS

Considering the facts of past results from businesses implementing either a centralized or decentralized structure, there are many advantages and disadvantages to both. A hybrid model has also allowed businesses to implement parts of both styles in order to receive advantages of both and reducing the disadvantages of one or the other. Once a corporation has evaluated which style works best for them, they can then implement that style and reevaluate their success. If there are no significant advantages, a different style may be necessary. All in all, a business’s decision can be determined by Allan Deering’s quote, ‘There’s no right answer. It’s which approach works best in your specific environment’ (Deering, 1987, p. 39).
REFERENCES


AUTHORS DETAIL

Adam Long is an MBA student at Lincoln Memorial University, Harrogate, Tennessee, where he also completed his undergraduate study of business and professional golf management. He held an internship with Walmart as a field management intern. He also has an extensive background in golf facility operations and turf-grass management. During his time in undergrad, he was a member of LMU’s men’s golf team, residential life staff, and participated in other various extracurricular activities while graduating with *cum laude* honors. He plans to become educated and certified in production methods including six sigma, lean manufacturing, and more.

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