

## Centralization and Decentralization

Another highly important issue in organizing is the extent to which authority is centralized, or its opposite, decentralized, in a formal organization structure. In management, centralization refers to concentration of authority and decentralization dispersion of authority. However, both these terms are used to give various connotations. These words are used in the context of administrative processes, physical and geographical location, various functions being performed, or degree of delegation of authority. When these terms are used

in the context of physical or geographical location, physical or geographical decentralization refers to dispersion of an organization's operations throughout the country. The functional decentralization refers to dispersion of organizational functions into separate autonomous units, for example, production, marketing, finance, etc. However, both these classifications of centralization or decentralization are merely descriptive and not analytical. Therefore, the terms are used with certain prefixes like geographical decentralization or functional decentralization. It is the degree of delegation of authority that conveys the meaning of centralization or decentralization in management, though in this case too, people prefer that these terms should be used along with 'of authority' to make them more clear and explicit such as 'centralization of authority' or 'decentralization of authority'.

When centralization and decentralization are used in the context of degree of authority at various levels and associated management practices, they denote different degrees of delegation of authority. Thus, centralization refers to the reservation of authority at the top level of the organization and decentralization refers to systematic delegation of authority in the organization. However, there can neither be absolute centralization nor there can be absolute decentralization. The concepts of centralization and decentralization are two extreme points in the matter of distribution of authority in the organization. In between these two extreme points, there may be continuum of authority distribution.

### Delegation and Decentralization

Delegation and decentralization should not be confused because of the tendency of using two terms interchangeably. Though these terms are closely related, decentralization is much more comprehensive than delegation. Thus, both these terms should be used differently. The major difference between delegation and decentralization may be identified in two ways: first, decentralization is used to mean several types of dispersal other than of authority also; second, even in the context of authority, the terms denote different. Table 11.1 presents difference between delegation and decentralization.

**TABLE 11.1: Difference between delegation and decentralization**

Basis	Delegation	Decentralization
1. Status	Process of authorizing subordinates	Result of widespread delegation
2. Nature	Compulsory as minimum authority delegation being must	Optional, depends on organizational policy
3. Purpose	To reduce burden of superiors	Giving autonomy to organizational personnel
4. Freedom of action	Less freedom to subordinates	More freedom to subordinates

### Factors Determining Degree of Decentralization

A basic question that arises while designing the organization structure is: how much to decentralize the authority? Managers cannot ordinarily be for or against decentralization of authority. They may prefer to delegate authority, or they may like to make all decisions. Although the temperament of individual managers affects the extent of authority delegation, other factors also affect it. Most of these factors may be beyond the control of individual managers. Such factors are of the following types:

**1. Size of Organization.** Decentralization depends on the size of the organization. The larger the size of an organization, the more urgent is the need for decentralization. In a large



organization, more decisions are to be made at more places. In such cases, it becomes difficult to coordinate them. The complexities of the large organization may require major issues to be passed down the line for discussion. Managers at various levels are to be consulted. This process may take sufficiently long time resulting in slow decision making. Slow decision making may be quite costly to the organization. Therefore, to minimize the cost, authority should be decentralized whenever feasible.

**2. History of the Organization.** Decentralization of authority depends on the way the organization has been built up over the period of time. Normally, those organizations which expand from within or expand under the direction of the owner-founder show a marked tendency to keep authority centralized. This is the reason why organizations belonging to many industrial houses have been designed on centralized basis. On the other hand, organizations that represent amalgamations and consolidations are likely to show a definite tendency to retain decentralized authority specially if the acquired unit is operating profitably. Moreover, the management process and pattern of acquired organization, once independent one, cannot be changed immediately so as to centralize the authority. Therefore, at least for some time, the acquired unit will enjoy considerable autonomy.

**3. Management Philosophy.** The management philosophy of top-level managers has considerable influence on the extent to which authority is decentralized. In fact, decentralization is a kind of management philosophy to regulate organizational process including decision making. In many cases, top managers may see decentralization as a way of organizational life that takes advantage of the innate desire of people to create, to be free, or to have status. They may find in it a means to harness the desired freedom to economic efficiency. On the other hand, many top managers may keep authority with them not merely to gratify a desire for their status or power but because they simply cannot give up activities and authorities they enjoyed before they reached the top or before the organization expanded from a small one.

**4. Availability of Managers.** Availability of managers directly affects the degree of decentralization because exercise of authority requires competence on the part of those who exercise authority. If better quality managers are available, there is more chance for decentralization because of two reasons. *First*, these managers can handle the problems of decentralized units effectively. *Second*, such managers have higher need for degree of autonomy which is possible in decentralized structures only. Moreover, decentralization also works as training ground for managers which increases the ability of good managers.

**5. Pattern of Planning.** Planning is usually the most crucial management function in thinking about decentralization. Other functions of management are also important but assigning those activities to managers at various levels typically depends on how planning duties have been allocated and the extent to which planning activities have been undertaken. Allocation of planning activities may be subject-wise and type of plan-wise. In the organization having carefully-drawn standing plans, the chance for decentralization is high because managers can make decisions within the context of those plans without referring the matters under decisions upward. Similarly, if they have been made party to the planning process, other functions which are to be performed within the context of planning process, can be easily decentralized.

**6. Control Techniques.** Development and use of control techniques affect the degree of decentralization by ensuring whether the performance at various levels and points of the



organization is in line with planning. Higher the degree of development and use of control techniques, better is the prospect for decentralization. In fact, improvements in statistical devices, accounting control and other techniques have helped make possible the current trend towards decentralization. In the absence of adequate control techniques, either there is less chance for decentralization or it may not work properly.

**7. Decentralized Activities.** In many cases, decentralization of authority becomes necessary because there is decentralization based on other factors like economies of division of labour, the opportunities for using physical facilities at various locations, and the nature of work. For example, the activities of banking, insurance, and transport organizations have to be decentralized. Although this kind of decentralization may be geographic or physical in nature, it influences the decentralization of authority. In fact, some organizations with diverse locations may form local board of directors. For example, State Bank of India operates on the basis of local board of directors with each zone having its own board of directors.

**8. Rate of Change in Organization.** The rate of change in the organization also affects the degree to which authority may be decentralized. If the business of the organization is fast developing and it is facing the problems of expansion, there is more chance that authority will be decentralized because in this case, top managers will have to share disproportionate decision making and consequently overburdened. This problem can be overcome by delegating authority at the lower levels. As against this, in old, well-established, or slow-moving organizations, there is a natural tendency to centralize authority because few major decisions are made and, in most cases, decisions are programmed requiring insignificant amount of analysis and time.

**9. Environmental Influences.** Besides the various factors discussed so far which are mostly internal to the organization, there are environmental influences also which determine the degree of decentralization. Among the most important environmental forces are the government regulations over the private business and leave very little scope to the use of discretionary power of the manager. For example, business covered by administered prices requires less time of manager's in determining the price structure and sometimes even distribution pattern. Thus, even marketing functions throughout the country may be centralized. Moreover, since top management itself does not have authority over these aspects, there is no question of its delegation.

### **Rationale of Centralization**

Centralization, as discussed earlier, is the systematic and consistent reservation of authority at central points within the organization. This results in a number of benefits in the organization:

1. Centralization provides opportunity for personal leadership.
2. It facilitates integration of efforts.
3. Quick decisions are possible; hence emergencies can be handled very easily.
4. It makes communication and control easier in the organization.
5. It helps in reducing wastage of efforts by avoiding duplication.
6. There is uniformity in actions throughout the organization and, thus, coordination can be achieved easily.

Centralization is quite suitable for smaller organizations, organizations producing single or homogeneous products, and operating in limited geographical areas. However, when



organizations grow in size and diversify, the benefits of centralization turn into limitations which affect the operational efficiency of the organizations. In such organizations, decision making becomes quite complex but at the same time, faster decision making is required. This is not possible in centralization. Therefore, its alternative, that is decentralization, is preferable.

### **Rationale of Decentralization**

Decentralization has become the prevailing philosophy for organizing activities on the part of large organizations. Experience shows that many organizations which were centralized and working efficiently at one point of time have adopted decentralization because they were not able to cope up with the situation under the old system. Decentralization offers the following benefits:

1. It reduces burden of the top management so that it can focus more attention on strategic management.
2. It facilitates growth and diversification in the organization.
3. It is a good philosophy to motivate managers.
4. It encourages development of managers by providing them opportunities to shoulder more responsibility.
5. It emphasizes horizontal growth of the organization thereby reducing the number of management levels and increasing the span of management.
6. It pinpoints more accurately on the results to be achieved by each unit of the organization by making various units autonomous.

Decentralization is useful basically to large organizations with multiple products or operating in different geographical locations. Further, if the organization is growing rapidly and working in dynamic environment, decentralization is the best philosophy to achieve positive results. However, it does not mean that decentralization offers all positive things as compared to centralization. In fact, there are many problems in decentralization. Some of the major problems of decentralization are of the following nature:

1. If not followed properly, decentralization will create chaos in the organization in the absence of proper control.
2. It tends to increase costs by making most units autonomous for facilities.
3. In decentralized structure, there is more need for good managers. Unless these managers are available, decentralization cannot be effective.
4. Decentralization requires high degree of self-motivation and self-control because of autonomy given to managers.

These problems, however, are not inherent to decentralization but emerge because it is not followed properly. Looking into the role of decentralization for managing large and diversified organizations which are to be more in number in modern society, some efforts should be made to make decentralization effective.

### **Making Decentralization Effective**

Whether to decentralize or not depends on various factors described earlier. However, when organization chooses for decentralization to take its benefits, it has to make some efforts to reap its advantages. Following are some measures which make decentralization more effective: