MultiScience - XXXIII. microCAD International Multidisciplinary Scientific Conference
University of Miskolc, 23-24 May, 2019, ISBN 978-963-358-177-3

HOW CAN WE ADAPT THE BALANCE SCORCARD TO THE NEEDS OF SOCIAL ENTERPRISES?

Sándor Bozsik[1], Judit Szemán[2], Zoltán Musinszki[3]
Ph. D, associate professor, Ph. D, associate professor, Ph. D, associate professor
University of Miskolc, Faculty of Economics

Abstract
This paper focuses how can we measure build up the management control system of a social enterprises in Central-Europe. This paper focuses the applicability of the traditional Balanced Scorecard system to the special needs of a Social Enterprises. The paper argues that the former adaptations are not considering the Central-European specialities, so it suggests extending the BSC system with new segment – how the social enterprises fit to the requirements of the grantor and regulator public institutions.

THE DEVELOPMENT OF TRADITIONAL MANAGEMENT PERFORMANCE SYSTEM TO THE BALANCED SCORECARD

The management information system collects the data from the accounting system, so the most important source of data is the annual report of a company. The annual reports should meet strict legal criteria, and the only publicly available information about the financial performance of a company. The data are comparable with the data of other enterprises and the valuation is more or less objective. The core part of the annual report is the financial statements – especially the balance sheet and the income statement.

"Financial statements are a structured representation of the financial position and financial performance of an entity. The objective of general-purpose financial statements is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. Financial statements also show the results of management's stewardship of the resources entrusted to it. To meet this objective, financial statements provide information about an entity's:

1. assets;
2. liabilities;
3. equity;
4. income and expenses, including gains and losses;
5. other changes in equity; and
6. cash flows.

This information, along with other information in the notes, assists users of financial statements in predicting the entity's future cash flows and, in particular, their timing and certainty." [1]

The International Accounting Standard 1: Presentation of Financial Statements sets out the requirements for the components of financial statements as follows:

1. balance sheet,
2. income statement,

DOI: 10.26649/musci.2019.066

3. statement of changes in equity
4. cash flow statement,
5. notes (comprising a summary of significant accounting policies and other explanatory notes). [1, 8. par.]

Balance sheet is a statement of financial position at the end of a period (end of the business year) in terms of assets and financing (liabilities and ownership equity). The income statement presents the results at the end of a period of activity. It presents information on the profit and loss and other comprehensive income. Statement of changes in equity, analysis of other comprehensive income and statement of cash flows are also required by the IAS 1 standard.

From the financial statements a multitude of indicators can be formed. The traditional financial indicators provide information about the property, financial and profitability state. They can give a view about:

1. the structure of the assets and the liabilities,
2. the effectiveness of the assets,
3. the amount of the debt,
4. the liquidity,
5. the profitability relative to the various projection bases.

During the analysis of the balance sheet we can draw conclusions about the property and financial state of the enterprise, and from the cash- flow about its financial state. [2]

In addition to individual financial indicators, we can also use indicator systems. One of the most popular indicator systems is the Du Pont system. It is based on the idea that not profit –- as an absolute indicator –- is in the centre, but the Return on Investment (ROI) – as a relative value. The top indicator of the system is the ROI that is definable as the ratio of the net outcome and the net asset value. The strength of the ROI that it is not an individual indicator, but an indicator system whose elements carry important information for the decision maker. This indicator can be further divided into two indicators: the profit margin and the turnover rate of the assets to the revenue. These two indicators can be further distributed by the outcome, cost, asset and liability data are the responsibility of the leader of a given decentralised unit.

The financial statements' data are typically aggregated data. These highly summarized data give an overall picture of the company's management. They help us to see the problems, and to know where to look for the source of the problems, but it does not give answers for the causes of problems. We tend to ask questions in the analysis of financial statements, rather than to formulate answers. However, there is a big problem. Only financial indicators can be calculated from the financial statements. The traditional financial indicators applied as the benchmark of the enterprises cannot provide appropriate information to the management for the following reasons:

1. The traditional financial indicators inform about the companies' past achievement; they do not have connection with the future.
2. They are unsuitable for the prevention of problems, namely they take into account the effects of the organizational actions and consumer choices that have already occurred.

3. They are short- term in approach, and therefore cannot serve the aims of the company strategy.
4. They are not diagnostic featured: they show the problems but cannot point out the root cause.
5. Due to being set in terms of money, they cannot be used for displaying qualitative factors, although the achievement of an enterprise consists of both quantitative and qualitative elements connected to the performance of the tasks assigned by the company. [3]

Despite the criticism of the use of traditional financial indicators enjoy a great popularity. Their advantages are the simplicity, the availabilities and the cheapness However, their application based on the literatures' recommendation have dangers. [4]

Nowadays the economic environment of companies has significantly changed: the former permanence was replaced by variability, marketing has come into the focus of operation instead of production, and the knowledge-focused approach has appeared beside the capital-centered approach. [5]

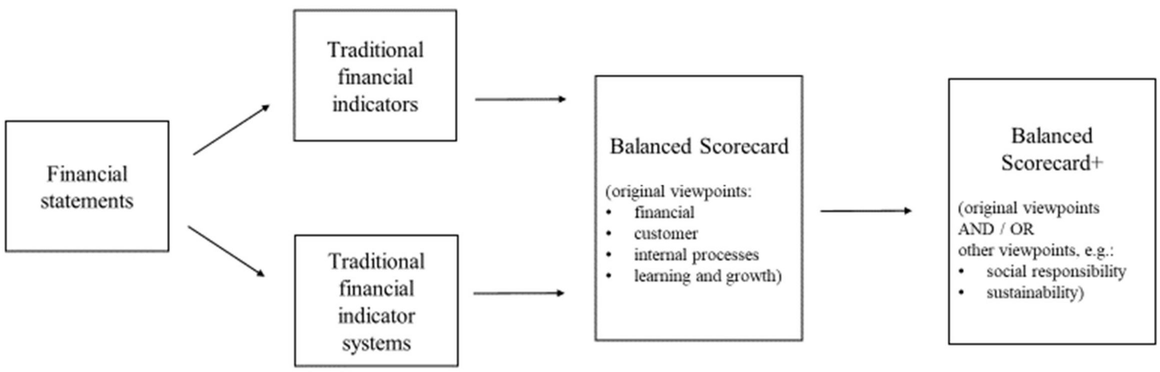

Fig. 1
From financial indicators to balanced scorecard [own editing]

In today's highly competitive environment the financial indicators alone are not able to give direction for the future; typically, they can give a view about some actions of the past, and so are retrospective, post factum indicators. In recognition of the changes, Robert S. Kaplan and David P. Norton developed a balanced, strategy-based indicator system. Both financial and non- financial indicators need to be reflected in the benchmark. The balance between them has to be created and they have to be united in a complex indicator system. This is achieved by the Balanced Scorecard (BSC). The viewpoints of the basic model (financial, customer, internal processes, learning and growth) are looking for answers for four questions:

1. What are the expectations of the stakeholders?
2. What kind of achievement is expected by the customers?
3. In which processes is it necessary to provide outstanding performance?
4. How may the change and developmental ability be maintained in the future? [6]

However, the basic model was not regarded as a definite model by the model creators. Over the last two decades different types of the basic model have been revealed taking different factors into consideration. The number of viewpoints has expanded:

1. the supplier,
2. the future,
3. social responsibility and
4. sustainability has become independent viewpoints. [7][8][9][10]

PERFORMANCE MANAGEMENT OF SOCIAL ENTERPRISES

To defining and classifying the concept of social enterprises is not an easy thing. The task is difficult due to the great variety of objectives, legal forms, organisational types, activities of social enterprises. To work out our definition, the overview of previous research findings is required. [11]

However, the economic role of the social enterprises is not negligible. By the European Commission, the social economy includes 2 million enterprises which means 10 % of all European businesses and employs over 11 million employees, the 6 % of EU working population in 2011. [12]

But the problem of a very general definition, that it does not tell us to much about the origin, the nature of objectives, the governance form, the funding of this organisations, consequently, gives small help to understand the deep nature of social enterprises.

A lot of paper attempted to create more specific definitions. Some of these terms are the followings:

Social purpose businesses which primarily reinvest surpluses in the business or community rather than generating profits for shareholders or owners.

The definition narrows the concept of SE to the social business but excludes those enterprises which runs public services but out of state direct control.

The social enterprises (later abbreviated by SE) have got a wide and deep literature but have not a clear and unique definition. The lowest common denominator of the definitions is “organisations which trade to achieve their social objectives”, or similar [13]

Due to the mixed nature and high variety of social enterprises the Balanced Scorecard (later BSC) method seems to be the most applicable performance management tool. The Balanced Scorecard is very flexible to tailor-made any individual organisations. Unfortunately, the literature is relatively poor relating to, how to use the BSC in non-profit organisation and especially in SEs.

Manville made a BSC system non-profit small and medium sized enterprise (SME). [14]. He noted that the motivation for adopting the scorecard were both internal and external due to the heavily regulated nature of the organisation. If these enterprises want to access public funds, they should meet the data request of public authorities.

Another approach worked out a full implementation of Balanced Scorecard system to the non-profit organisations. The article’s methodology used Risk Management, Quality Assurance and Information Technology, areas that contribute considerably to the successful implementation of the Balanced Scorecard. [15]

By Meadows et al. the target of the organisation should be identified to meet the riskiest areas of running a SE. They identified four risky or problematical areas. They are the following:

1. Weak organisational capacity which covers the lack of financial control over the budget and profit, lack of a proper HR systems, due to the poor quality of workers and HR staffs, and the weak governance due to agency and free-rider problems.
2. Poor financial performance due to lack of proper reserves, due to the dependency of public funds and the low level of profitability.
3. Poor service/product development including lack of expertise, market intelligence and limited distribution channels.
4. Inability to evidence the added social value is the consequence of the former three points.

The elements of BSC system should reflect these risk factors. The Business Model element examines the poor service/product development, the Financial Return element meet the challenge of poor financial performance, the Organisational Development focuses the problem of weak organisational capacity, whereas the Social Return element measures the progress to improve the added social value. [16]

The key indicators are grouped inside the model by the term to achieve them. The structure is represented by Figure 2.

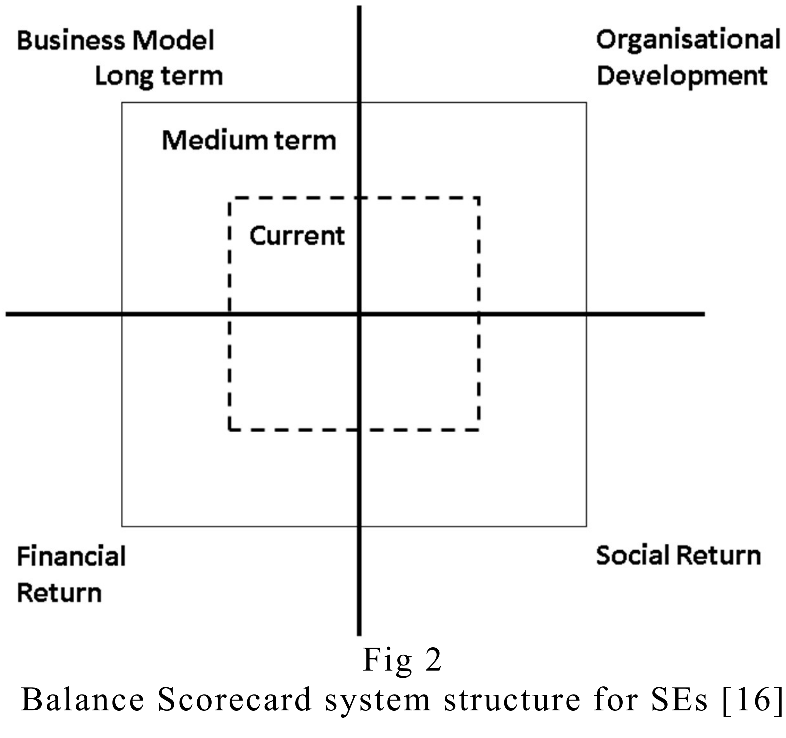

Fig 2
Balance Scorecard system structure for SEs [16]

Sommers gave three basic modification to the classical balanced scorecard model, developing the Social Enterprise Balanced Scorecard (SEBC). He replaced the financial perspective with social goals as a target area; the financial perspective is extended to express environmental and social sustainability too; and some stakeholder groups were added to the customer perspective, separating those who pay for a service (donors, grant funders) from those who consume it (employees, beneficiaries and the wider community). [17]

Bull’s paper analysed the results of 30 pilot social enterprises utilizing the BSC system. The paper concluded that highlighting both strengths and areas where greater support may be required would be a great help for these enterprises. (Bull 2006)

He stated that the SEs general strengths by his investigation is the learning perspective. (i.e. training and development, participative decision-making and personal development cultures) The other strong area is the vision and strategy creation ability.

The weaknesses are the low level of management system from the accounting to the quality standards. The reason is the shortage of resources like financial literacy, professional skills and moral hazard.

Bull also modified the original BSC model to SEs by modifying the four perspectives into: multi-bottom line (dealing with synthetic assessment of financial, environmental and social results), stakeholders’ environment, internal activities (related to structure, communication, quality, etc.), and learning organization (dealing with training and knowledge management). [18]

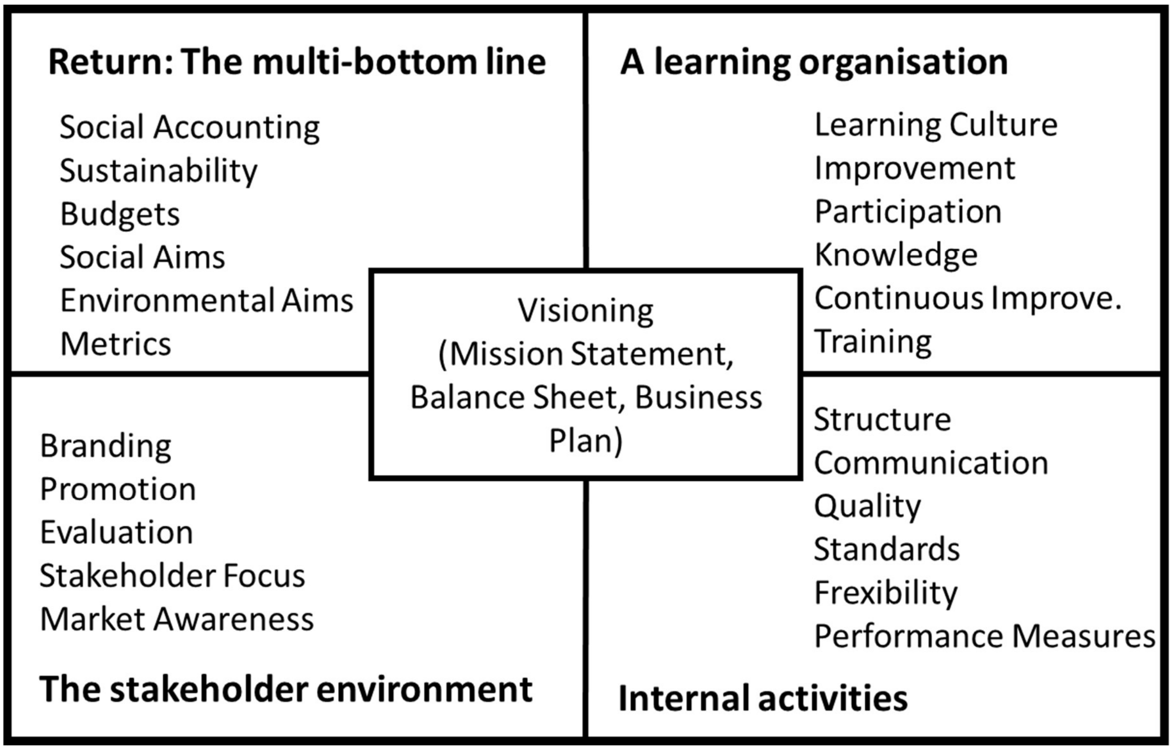

Fig.3
The Balance Model and Topic Areas [18]

BALANCED SCORECARD MODEL OF SOCIAL ENTERPRISES

We choose the classic Bull-model as a basis to create our own BSC model. The financial accountability is an important part and key issue for every enterprise, so we only slightly modified the left upper segment. However, we replace the environmental aims to financial and environmental solvency.

One of the missions of the social enterprises is to help their member to develop and improve the important labour market abilities. Since in the learning organization perspective we inserted new aspects which emphasize the improvement of the competitiveness of the labour force.

The internal activities strive to enhance the efficiency of operations. We plan here only one modification. How can the social enterprise develop the members' relevant labour market abilities?

The stakeholder environment was dramatically restructured. Instead of it we place the requirements of the grantor and regulator public institutions. Most of the social enterprises depends of public funds, so the enterprises should meet the criteria of the state and European funds.

The available state funds can be numerous. Especially in the agriculture and country development there are several opportunities. [19]

The request of the donor public organisation can be various. They often prescribe the number of employees or members, the length of their employment, they can limit the amount of payable transfers. In addition to the circumstances of employment they can order numerous data service about the activity of the social enterprises, determine the major accounting and taxation policy rules, the structure and content of financial reports, they can require financial budget.

Public institutions can act as an external control over the business of social enterprises.

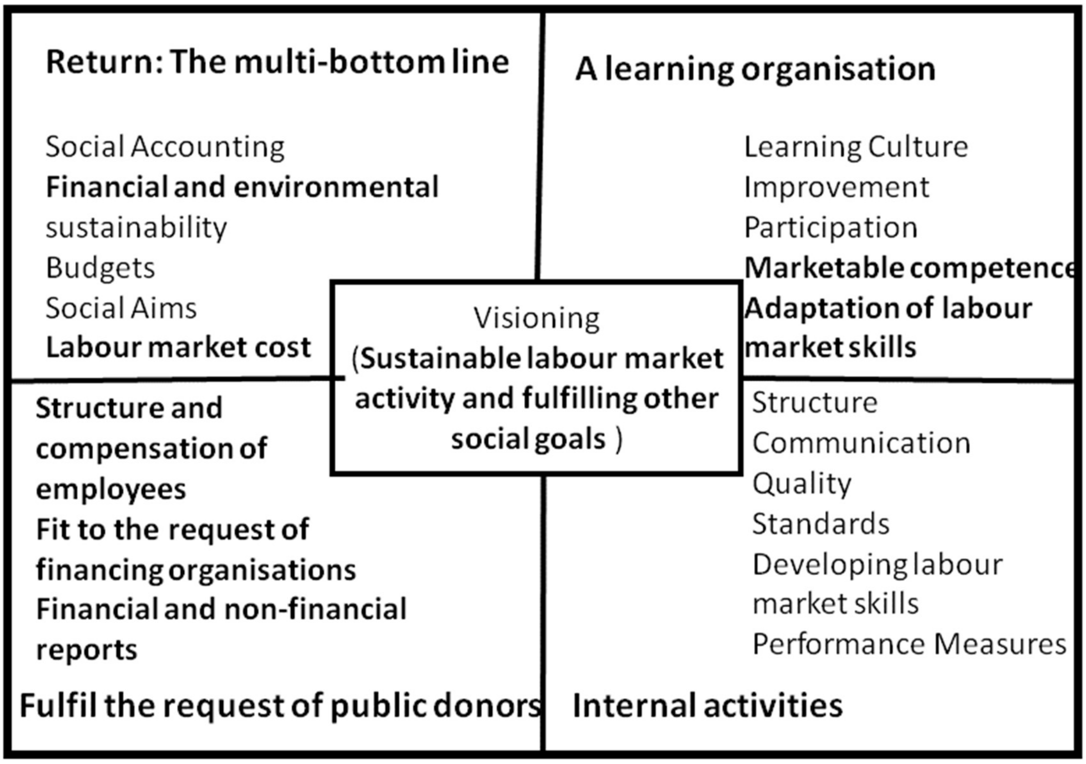

Fig.4
The Balance Model and Topic Areas [own edition]

Acknowledgement

This research was supported by the project no. EFOP-3.6.2-16-2017-00007, titled Aspects on the development of intelligent, sustainable and inclusive society: social, technological, innovation networks in employment and digital economy. The project has been supported by the European Union, co-financed by the European Social Fund and the budget of Hungary.references.

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