

## Influence of Characteristics of the Organizational Structure of Management on Level and Structure of Transactional Costs of Firm

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### Abstract

Efficiency of goal achievement of the organization, implementation its strategy, efficiency of interaction with the external environment is in many respects determined by the correct creation of an organizational structure of management. Main goal of existence of an organizational structure of management is ensuring sustainable development of the organization. Achievement of this purpose is carried out by means of improvement of ways of interaction of the organization with the external environment, and also interactions of elements in the organization. Exact feature of management- based organizational has great influence on structure of transactional costs of that organization. High transactional costs reduce efficiency of functioning of the organization. It is possible to increase efficiency of organization activity by management of transactional expenses. Classification of transactional costs is given in this work, the main characteristics of an organizational structure of management are considered too. The analysis of influence of the following factors: level of formalization of an organizational structure of management, extent of centralization of an organizational structure of management, number of hierarchical levels of management, number of hierarchical levels of management, number of functional divisions, control range on the transactional costs was completed.

**Keywords:** Organizational structure of management; Transactional costs; Centralization; Decentralization; Control range.



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### 1. Introduction

An important purpose of an organizational structure of management is its capability to adapt to changes in external and internal environment of the organization with the minimum expenses, including transactional costs.

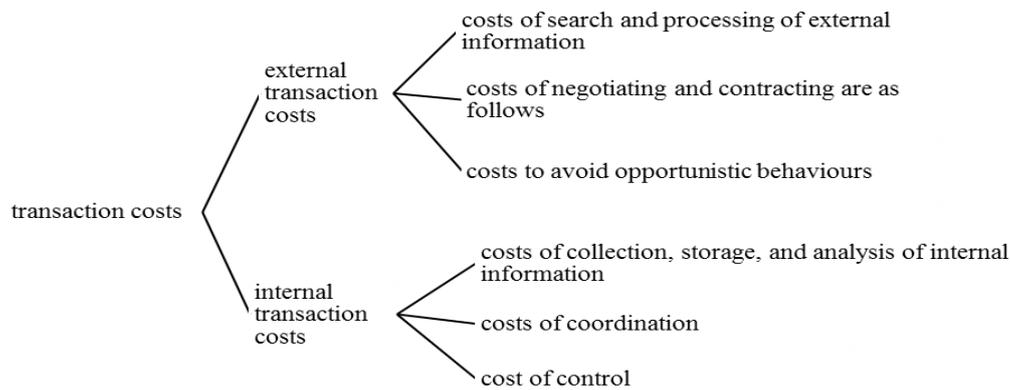
Investigated questions of the theory of transactional costs Coase (1937); Stigler (1961); Arrow (1969); Alchian and Demsetz (1972); Barzel (1982); Williamson (1985); North (1987); Jones and Hill (1988); Eggertsson *et al.* (1990); Nicholson (1992).

Various factors exert impact on the size of transactional costs. In this work we will consider influence of characteristics of an organizational structure of management on the level of transactional costs.

### 2. Methods

#### 2.1. Classification of Transactional Costs

It is offered the following classification of transactional costs of the organization (fig. 1).

**Fig. 1.** Types of transactional costs.

In detail this approach of classification of expenses is opened in work «Analysis of the transaction cost in modern conditions».

## 2.2. Characteristics of Organizational Structure of Management

It is possible to carry to the main characteristics of an organizational structure of management: extent of formalization of structure, extent of centralization of structure, number of levels of management and regulation of controllability. Let's consider these and some other characteristics of an organizational structure slightly in more detail.

### 2.2.1. Level of Formalization of an Organizational Structure of Management

When designing, in case of efficiency analysis of an organizational structure of management it is necessary to consider the level of formalization of structure. Formalization of a management structure has positive and negative consequences for organization activity. Let's consider at first the positive moments.

1. Formalization of procedures allows the organization to function accurately, helps to avoid the conflicts between employees, to increase performing discipline. It is reached thanks to what each employee well represents as in what sequence each of participants of production process shall make.

2. The formalized activity allows to reveal and eliminate defects of the existing structure of management by an exception of duplication of functions, definitions of missing or unnecessary functions.

3. Transfer of the formalized information is carried out easier, than at oral speech, the risk of her distortion decreases.

But formalization has also negative consequences.

1. A large number of instructions, bureaucracy result in rigidity of structure. The structure becomes nonflexible, hardly adapts under changes of the external environment of the organization.

2. Formalization of procedures leads to the fact that the personnel first of all aim to perform instructions, but not to improve results of results of organization activity.

### 2.2.2. Extent of Centralization of an Organizational Structure of Management

In practice completely centralized or decentralized organizations don't meet. Any organization can be called centralized or decentralized only in comparison with other organizations or in comparison with itself, but during other periods of time.

For determination of comparative extent of centralization of the organization it is necessary to consider the following its characteristics.

For definition of comparative extent of centralization of the organization it is necessary to consider the following her characteristics.

1. The number of the decisions made at the subordinate levels of management. The more the number of those decisions which are made by subordinate heads the is higher extent of decentralization.

2. Importance of the decisions made at the subordinate levels. In the decentralized organization heads of an average and lower link can make the decisions connected with costs big material and a manpower or change of activity of the organization.

3. Consequences of the decisions made at the subordinate levels. If heads of the lower and average link can make the decisions affecting more than one function, then the organization can be considered as decentralized.

4. Extent of control of work of subordinates. In strongly decentralized organization performance appraisal of subordinates becomes on the basis of final indicators, in centralized actions planning of subordinates is performed.

The centralized structure has the of benefits and shortcomings. It is possible to allocate two main benefits of centralization.

1. The organization with the centralized structure is capable to mobilize in shorter terms the resources for the solution of complex challenges. It occurs because exactly in the centralized structure it is simpler to achieve the coordinated work of a large number of subsystems.

2. In the centralized structure less time for reaction in response to influences of external factors is spent. It is connected with the fact that in the centralized structure less time for coordination of decisions is spent

Also one big shortcoming has the centralized structures. As in the centralized system everything depends on harmonious work of one head, such system can be unreliable. The fact that even temporary absence, leaving or failures in work of the head can lead to negative consequences for system in general is a cause of unreliability. It means that in this case normal functioning of the organization depends on abilities, health and whims of one person.

Level of centralization and formalization exert a great influence on structure of transactional costs of the organization.

We will consider changing of internal transactional costs under the influence of change of extent of centralization and formalization of structure.

**Fig-2.** Dependence of transactional costs of collection, storage and analysis of internal information on the level of centralization and formalization.

<b>High centralization</b>	<b>From averages to high</b>	<b>Averages</b>
Low centralization	High	The averages seeking for growth
	Low formalization	High formalization

**Fig-3.** Dependence of transactional costs of coordination on the level of centralization and formalization.

<b>High centralization</b>	<b>Averages</b>	<b>High</b>
Low centralization	From low to averages	Low
	Low formalization	High formalization

**Fig-4.** Dependence of transactional costs of control on the level of centralization and formalization

<b>High centralization</b>	<b>Averages</b>	<b>High</b>
Low centralization	From low to averages	Low
	Low formalization	High formalization

Let's consider a case when the organizational structure of management is characterized by the low level of centralization and low level of formalization. It is characteristic, for example, of the project organizations. In this case costs of collection, storage and the analysis of internal information will be high as the relevant information gathers under each project. Growth of these expenses is caused also by the fact that in such structure a lot of time for handling of internal information, decision making, the choice of alternatives leaves. Transactional costs of coordination in such structure can also be high as quite often there are problems in case of establishment of tasks and job sharing in time. A lot of time for coordination in decision making process can leave. Transactional costs of control are within the limits from low to averages.

In case of high centralization of low formalization it is possible to review an example of the small, just created organization. In that case transactional costs of collection, storage and analysis of internal information will have the size from averages to high. In this structure losses from incorrect decision making as all decisions are made solely by the boss that in increases probability of mistakes are possible. Transactional costs of coordination in such structure are low as the structure has the small sizes and low branching of internal communications. Costs of control have average size and include generally development costs of estimative indicators for measurement of deposits of workers.

In case of low centralization and high formalization it is possible to consider, for example, educational and medical institutions. In such organizations of costs of collection, storage and analysis of internal information there will be averages aiming at growth as in addition to the control exercised by professionals, other control methods are almost absent. From - high extent of decentralization there is a duplication of information by different services that leads to growth of transactional costs. Leads process of forming and storage of a set of reports, orders, instructions to growth of transactional costs. Transactional costs of coordination in such structure rather high that it is caused by big extent of formalization. Control costs is small, but can aim at growth since organization members considerably independently control work process, and it gives the chance of opportunistic behavior.

Let's consider structure highly centralized, and also highly formalized. An example of such organization is the company occupied with mass production of products. Transactional costs of collection, storage and analysis of internal information in this case have average size. They consist generally of expenses on forming of instructions, provisions, reports. Let's consider transactional costs of coordination. They have the average sizes because high extent of standardization allows to simplify coordination in very branched structure and to lower these expenses. On the other hand, a lot of time for finishing orders, decrees, formal rules and procedures to contractors because of complexity of structure can leave that leads to growth of transactional costs. Transactional costs of control in such structure are high.

### **2.2.3. Number of Hierarchical Levels of Management**

Very large number of levels in the organization badly affects system of communications as when passing information through each level there is its misstatement, efficiency of communication, so and management process decreases. It leads to growth of transactional costs of coordination.

### **2.2.4. Number of Functional Divisions. The Number of Functional Divisions Can Change Under the Influence of the Following Factors**

1. Grouping shouldn't lead to the head's overload a large number of subordinates. It means that it shall be observed by the control range. If the range of control isn't observed, it leads to growth of transactional costs of coordination.
2. Integration of uniform works can give economy of means thanks to expansion of scales of production.
3. Grouping shall provide coordination of works and reduce coordination problems.
4. The most important works require top-level attention therefore they need to be grouped at top levels of management.

### **2.2.5. Control Range. Range Of Control Is an Admissible Number of the Performers Subordinated To One Head**

Excessive increase in number of subordinates leads to growth of managerial obligations of the head that reduces control over work of subordinates. On the other hand, excessive narrowing of the range of control can lead to increase in number of hierarchical levels that will lead to coordination complication. Big decrease in the range of control can lead also to increase in number of heads in the organization and to increase in administrative costs.

Small range of control conducts to the fact that the head has an opportunity to support continuous contacts with subordinates, to exchange with them necessary information, to operate with higher quality them. But in this case there is a danger that the head will excessively interpose in the matter of subordinates and to limit their freedom of behavior. It also leads to flexibility loss, deprives of workers of an opportunity to prove creatively and initiatively.

In case of the big range of control the head can be overloaded with coordination of the current work of subordinates and not solve strategic problems.

Establishment of the range of control in each case shall be performed taking into account features of the entity (an enterprise scale, complexity of products, amount and type of production), and also specifics of work of heads at the different levels of management.

## **3. Offers**

Badly structured organizational structure of management can lead to a large number of the conflicts as in the organization, and also to complicate processes of interaction of the organization with the external environment. It can mean incorrectly organized communications, incorrectly distributed powers. The inefficient organizational structure of management leads to mistakes in coordination, to inefficiency of decision making process, to the conflicts for spheres of influence, etc. It also leads to excessive increase in transactional costs that finally leads to decrease in efficiency of functioning of the organization in general.

## **4. Results**

The size and structure of internal transactional costs to a large extent depends on characteristics of an organizational structure of management. Changing these characteristics, it is possible to achieve reducing transactional costs. But at the same time it is necessary to consider the next moments:

- 1) in case of change of characteristics of an organizational structure of management transactional costs of one type can decrease, but increase transactional costs of other type;
- 2) some types of activity cause the necessity of use of organizational structures of a certain type that exerts a great influence on characteristics of an organizational structure of management and the size of transactional costs.

For example, to increase in the sizes of firm there is an increase in transactional costs and decrease in organizational effectiveness. It is possible to solve this problem having constructed divisional structure or having increased standardization and formalization of an organizational structure of management.

## **5. Discussion**

To increase organizational effectiveness, reducing transactional costs it is necessary identification and elimination of unprofitable transaction or optimization of transactional costs. These actions are resulted by adjustment of an organizational structure of management.

Decrease in transactional costs allows not only to reduce product cost, but also to increase efficiency of business processes in the organization. Studying of level and structure of transactional costs allows to analyse organization activity and to reveal sources of a large number of the problems arising in the course of activities.

## **6. Conclusions**

In this article it is attempt to analyze the different aspects of transaction in order to identify the extraneous cost of that and eliminate unprofitable expense that led to reaching an optimized cost. Various aspects has come in through this analysis to attain the best method of management. The investigation revealed that by decreasing the cost

of transactional cost not only there will be a decline in the price of the products but also a noticeable increase in the efficiency of organization created to manage the business will be achieved.

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