

**BUSINESS AND NON-PROFIT  
ORGANIZATIONS FACING INCREASED  
COMPETITION AND GROWING  
CUSTOMERS' DEMANDS**

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# CONTENTS

Introduction .....	7
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## I. BUSINESS AND NON-PROFIT ORGANIZATIONS AS THE OBJECT OF RESEARCH

1. The Communication of Non-Profit Organizations with Their Stakeholders in the Light of the Direct Research <b>Wioletta Kwak</b> .....	11
2. The Social Engagement as a Source of Innovation <b>Grzegorz Baran, Janusz Bąk</b> .....	23
3. The Transformation of Culture in Modern Forms of Organization on the Example of Virtual Organizations <b>Barbara Czarnecka, Piotr Czarnecki</b> .....	35
4. Selected Aspects of Performing the Personnel Function in Small Food Service Enterprises <b>Katarzyna Okuniewicz</b> .....	57
5. Analyzing Business Model Components Using the Sensitivity Model <b>Anna Ujwary-Gil, Marina Candi</b> .....	71
6. Multicriterial Evaluation of Applying Japanese Management Concepts, Methods and Techniques <b>Mateusz Podobiński</b> .....	85
7. Labor Quality in an Enterprise as a Subject of Research <b>Mariusz Wyrostek</b> .....	97

## II. MODERN TOOLS FOR BUSINESS AND NON-PROFIT ORGANIZATIONS MANAGEMENT

1. A Method of Estimating the Determinant of Enterprise Competitiveness <b>Olaf Flak</b> .....	113
2. The Principles of Implementing Early Recognition Systems in an Organization <b>Janusz Bąk, Grzegorz Baran</b> .....	129
3. Stakeholder Management as an Effective Tool for Project Success <b>Martyna J. Książek</b> .....	141
4. New Public Management as a Response to Expectations of the Society Towards the Civil Service <b>Mariola Wiater</b> .....	157

5.	Evolution of Lean Management Concept and Evaluation of Experience in its Application <b>Krzysztof Drabek</b> .....	169
6.	Applying Selected Models of Change Management in Non-Profit Organizations <b>Paweł Korczak</b> .....	183
7.	Commercialization as an Appropriate Approach to the Process of Restructuring Hospitals in Poland <b>Bartłomiej Kaszyk</b> .....	195

### III. BUSINESS AND NON-PROFIT ORGANIZATIONS – GLOBAL AND REGIONAL ASPECTS

1.	Activities of National Parks as a Source of Revenue for Their Communes. Case Study of Babia Góra National Park <b>Bernadetta Zawilińska, Wojciech Strzelczyk</b> .....	211
2.	Possibilities of Using Public Relations Instruments By a Public Organization on the Example of the Office of Town and Commune of Głuchołazy <b>Marcin Flieger</b> .....	227
3.	Small Training Services Enterprises in Knowledge-Based Economy- an Attempt at Identification of the Main Trends and Modifications <b>Iwona Małgorzata Kutzner</b> .....	245
4.	The Impact of Tourism on the Socio-Cultural Environment in the Gorce National Park and its Vicinity <b>Małgorzata Luberda</b> .....	261
5.	The Analysis of the Development Strategies of Selected Local Government Units, Including Types of Communes <b>Emilia Norkowska</b> .....	277
6.	Managing the Competitiveness of Regions <b>Karolina Olejniczak</b> .....	293
7.	The Problem of Securing Interests of Persons with Disabilities in Accordance with Provisions of the Convention on the Rights of Persons with Disabilities <b>Monika Trętko</b> .....	307

### IV. FINANCIAL ASPECTS OF ORGANIZATIONAL MANAGEMENT

1.	The Application of the Event Study to the Analysis of the Public Information Impact on the Corporate Bond Prices <b>Anna Rybka</b> .....	323
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2.	Non-Returnable and Returnable Instruments of European Union's Public Aid for Entrepreneurs <b>Ludmiła Kryskova</b> .....	341
3.	The Effectiveness of the Leniency Program in Combating Cartel Agreements in Poland <b>Jerzy Choroszczak</b> .....	359
4.	Pre-Sale of Flats as a Method to Limit Market Risk <b>Marcin Sitek</b> .....	373
5.	The Development and Importance of Small and Medium Enterprises in the Polish Economy During the Economic Slowdown <b>Anna Nijakowska-Augustyn</b> .....	387
6.	Strategic and Financial Drivers of Business Value Creation <b>Iwona Zaręba</b> .....	403



## INTRODUCTION

We are happy to present the next volume of this regularly published scientific monograph. The 13th volume brings an analysis of current phenomena and processes taking place in business and non-profit organizations. It points at new conditions in which organizations are established and then function. It also provides an attempt at explaining what determines the way organizations function in a dynamic market. The book also analyzes strategies applied by the surveyed organizations in order to achieve and maintain competitive advantage in the world of increased competition and growing customers' demands. The book is divided into the following thematic sections which constitute the construction base of this monograph: business and non-profit organizations as the object of research, modern tools for business and non-profit organizations management, business and non-profit organizations – global and regional aspects, and finally financial aspects of organizational management.

In the first section, the authors analyze the issue of communication of non-profit organizations with their stakeholders. This part presents the addressees of promotional activities, forms of contacting various groups of interest as well as instruments and scope of marketing communication activities undertaken by organizations. They examine transformation and development of culture in the context of virtual organizations, social engagement understood as a source

of innovativeness, or work quality in the context of a resource theory of an enterprise. The next part, devoted to tools used by organizations, proposes an interesting theory of the so-called competitiveness integrated model, and the current status of research of the company competitiveness barometer, definition and algorithms for estimating the determinant of enterprise competitiveness. Moreover, it brings an analysis of the implementation of the early warning system in an organization, stakeholders' management and the implementation of the concept of new public management aimed at increasing social expectations as exemplified by the strategy of human resources management of the civil service and other internal documents. The third section brings considerations of global and regional aspects of organization's functions. It analyzes, among other aspects, such issues as: the impact of Polish national parks on their respective communes' own revenue, possibilities of using public relations instruments by a public organization, identification of the main trends related to the small services enterprises or problems of tourism in terms of its relationship with the social as well as cultural environment.

The final section of the monograph presents financial aspects related to organizational management. We would like to draw your attention to an article on the event study and its application in research on corporate debt market. The empirical part of this article brings an analysis of how prices of instruments quoted on Polish Catalyst market react to selected events concerning the economic situation of the issuing company. The reader should also find it interesting to read about the development of SMEs in Polish economy during the slow-down period.

We would like to thank all the authors for very interesting articles and their contribution to this edition. We also thank the reviewers for their valuable and insightful comments. We hope that the texts included in this volume will arouse readers', scientists' and practitioners' curiosity.

**Adam Nalepka, Anna Ujwary-Gil**



**I.**  
**BUSINESS AND NON-PROFIT**  
**ORGANIZATIONS AS THE OBJECTS**  
**OF RESEARCH**



# THE COMMUNICATIONS OF NON-PROFIT ORGANIZATIONS WITH THEIR STAKEHOLDERS IN THE LIGHT OF THE DIRECT RESEARCH<sup>1</sup>

**Wioletta Kwak<sup>2</sup>**

## **Abstract**

*The paper is devoted to the issue of communication of non-profit organizations with their stakeholders. It presents the addressees of promotional activities, forms of contacting various groups of interest as well as instruments and scope of marketing communication activities undertaken by organizations. The paper is based on the conducted direct research. Proper communication with the environment is vital for non-profit organizations functioning in the market. The surveyed entities used various forms of contacting their stakeholders, both direct and indirect ones. Particular instruments of marketing communication have been used to different extent by the organizations.*

**Keywords:** *non-business organization, non-profit organization, stakeholder, communication, marketing communication, promotion.*

## **1. Introduction**

The paper aims at presenting the means of communication used by non-profit organizations (NPO) with various groups of stakeholders<sup>3</sup>. The paper focuses on recipients of promotional activities, forms of contact with the environment and the instruments and scope of marketing communication activities performed by the surveyed entities.

The paper presents the selected results of both quantitative and qualitative direct research conducted in 2009<sup>4</sup>. The research covered non-governmental organizations operating in the area of social security. The choice of the organizations operating in the above-mentioned field was determined by their

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1 Publication financed from scientific funds in 2008-2010 as a research project No. 2571/B/H03/2008/34.

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3 Stakeholders are individuals being in a relationship with a given entity of their own will or forced to it (*Leksykon zarządzania*, 2004, p. 151). These are entities interested in the functioning of an organization, bearing certain risk related to its functioning (Polskie Forum Corporate Governance. Retrieved from [http://www.pfcg.org.pl/article/12760\\_Interesariusz\\_ang\\_\\_stakeholder.htm](http://www.pfcg.org.pl/article/12760_Interesariusz_ang__stakeholder.htm)).

4 The whole research project concerned the role of marketing strategies in creating value for stakeholders of non-profit organizations in Poland.

role in the society. All entities participating in quantitative research were public benefit organizations (PBO). The possession of a PBO status was seen as evidence of a wider scope of activities of an organization. Quantitative research, conducted by means of a questionnaire, covered three Polish provinces: Małopolska, Podkarpacie and Silesia. Particular organizations from provinces of Małopolska and Silesia were randomly selected<sup>5</sup>. On the other hand, in Podkarpacie, due to a smaller number of registered entities, all PBOs operating in this area were asked to participate in the survey. The quantitative research was conducted on 269 entities altogether. However, the analysis took into account the questionnaires of 253 organizations, as others did not meet formal requirements. The qualitative research consisted in the case study analysis of 10 purposefully selected organizations from the province of Małopolska. It was assumed that these should be the entities with significant achievements in their activity, serving as models for other entities to follow. The research used the technique of an in-depth interview, the analysis of material offered by the surveyed entities and the information published on the Internet.

## **2. NPO stakeholders as recipients of promotional activities**

It is not only service recipients and donors who are recipients of NPO promotional activities. When designing a system of marketing communication, we must take into consideration other entities as well (Wiktor, 2003, p. 326). Non-profit organizations function in a definite environment and provide value to various groups of stakeholders. The nature of the addressees of an organization's activities affects the applied marketing communication strategy (Czarnecki, 2012, p. 233).

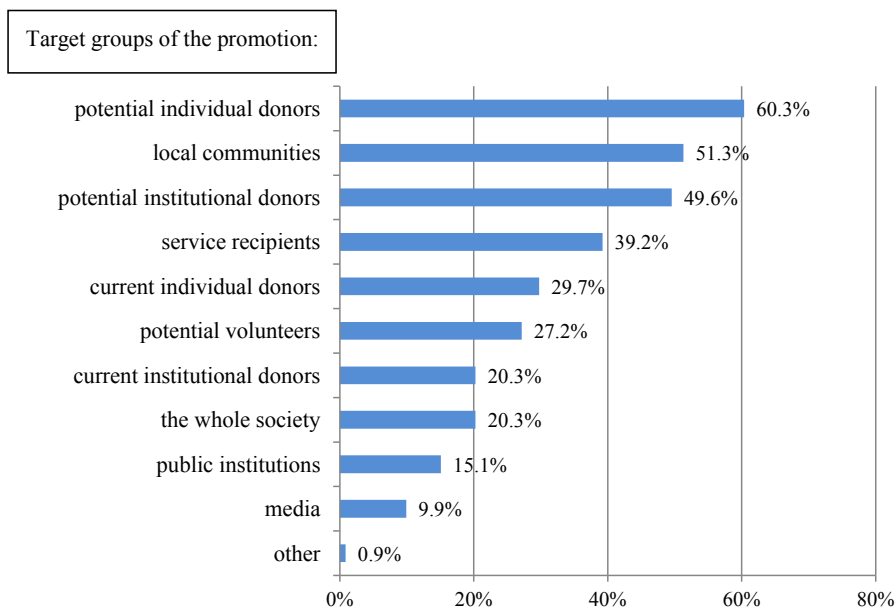
The promotional policy may take up the so-called narrow or wide form. In case of a narrow form of promotion, communication of an organization is addressed to a narrower group of recipients than potential clients – to people shaping opinions about an offer or influencing the decision-making process. On the other hand, a wide form of promotion is directed at a broad group of addressees. In this case, apart from the present and potential clients and donors, the addressees of promotional campaigns are also potential intermediaries, local communities and other interest groups (Wiktor, 2003, pp. 326-327). Non-profit organizations, depending on their needs and resources they possess, use both the former and the latter form of promotion.

The most important addressees of promotional activities of the surveyed entities (quantitative research) were potential donors and local communities

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<sup>5</sup> The sampling frame was an all-Poland base of non-governmental organizations: [bazy.ngo.pl](http://bazy.ngo.pl)

(Figure 1). NPOs, however, directed their promotional activities also to other interest groups.



**Figure 1.** Target groups of promotional activities conducted by non-profit organizations (quantitative research, N=232)

The subjects covered with the research were also asked to rank particular groups of stakeholders taking into account their significance for the organization. The answers obtained in this way allowed me to state that the most significant interest groups for the surveyed NPOs (quantitative research) were: local communities, service recipients and their family and friends. Further places in the ranking were occupied by: donors, the whole society, volunteers and public institutions. The least important interest groups for the surveyed entities, as seen in respondents' declarations, turned out to be employees (in case of associations also organization members) and media. Also the organizations selected for qualitative research were asked to rank their stakeholders. Service recipients, their family and friends and local communities also frequently came on the top of the rankings. 6 out of 8 entities (which created the ranking of significance of particular groups of interest) ranked service recipients on the first place and their family and friends on the second.

### 3. Forms of communication with stakeholders

The surveyed non-profit organizations used numerous forms of contact to communicate with their stakeholders (direct and indirect, traditional and using latest technologies). The most frequent ways of contacting most recipients were ‘face to face’ and telephone conversations (Table 1). The organizations also often contacted service recipients, their family and friends and volunteers by means of group meetings. Donors were often reached via post and the Internet. The Internet was also used by a considerable group of organizations to contact the media. Public institutions, apart from being contacted via direct and phone conversations, were also often reached through the post. Local communities were most frequently contacted via available mass media. In contacts with employees, obviously ‘face to face’ communication prevailed.

**Table 1.** Forms of contacting various groups of stakeholders by non-profit organizations (quantitative research)

	Phone calls	‘Face to face’ conversations	Group meetings	Symposiums, lectures, conferences	Mass media	Internet	Post	No contact
Service recipients (N=220)	49.5%	70.5%	42.3%	15.5%	17.3%	31.4%	26.4%	3.6%
Family and friends of service recipients (N=212)	48.6%	54.7%	38.2%	8.5%	13.7%	24.1%	17.9%	12.7%
Individual donors (N=230)	40.4%	68.3%	17.0%	5.7%	27.8%	37.0%	36.5%	1.3%
Institutional donors (N=227)	46.3%	58.6%	10.6%	11.9%	26.0%	36.1%	38.3%	3.1%
Public institutions (N=214)	49.5%	60.3%	8.9%	15.9%	17.3%	31.3%	40.2%	5.1%
Local communities (N=210)	14.8%	28.6%	29.0%	16.7%	49.0%	33.3%	18.1%	5.2%
Media (N=208)	51.4%	45.2%	4.8%	9.6%	20.2%	39.4%	24.5%	13.5%
Employees (N=171)	34.5%	68.4%	32.7%	12.3%	5.8%	24.6%	12.9%	22.8%
Volunteers (N=211)	44.1%	80.1%	46.9%	15.6%	12.3%	32.2%	21.3%	6.6%

The choice of a proper form of communication with reference to a specific group of addressees is of vital importance. An inappropriately selected form of contact may account for the fact that the communication will not reach a particular addressee or the message they receive will be incomplete. (Michalski, 2007, pp. 302-303).

#### **4. The instruments and scope of promotional activities of NPOs**

Organizations use various instruments and tools to communicate with the environment. Particular instruments of marketing communication may be used separately, however, in order to obtain quicker and lasting effects, it is justifiable to combine them and to use some of them together (Sztucki, 1996, p. 202). The composition of promotion should be adjusted to the goals of a given organization as well as to the situation this organization is in (Michalski, 2007, p. 314).

Building positive image was vital for the surveyed non-profit organizations. L of the entities (quantitative research) performed regular activities in this area (Table 2). Over half of the respondents declared that they often or very often undertook activities aiming at creating positive image<sup>6</sup>. Huge significance of an organization's image in the society was confirmed by the respondents reaction to the following statement: "The organization does not attach significance to its image in the society". 85% of organizations did not agree with this statement (34.6% totally disagreed while 39.5% disagreed). The expressed opinions were affected by subjective evaluation of a financial situation (grouping variable "evaluation of financial situation", Chi-square = 13.941, df=4, Asymptotic significance = 0.007 < 0.05). Individuals which evaluated their financial situation as very good, more often than the others "totally disagreed" with the statement that "The organization does not attach significance to its image in the society". The expressed opinions were not influenced, however, by: the size of the city in which the registered office of the organization was located, the province or the geographical scope of its operations<sup>7</sup>. The significance of the non-profit organizations' image in the society was also emphasized by individuals taking part in the qualitative research. It should be emphasized that taking care of the most favorable image is particularly important for a non-profit organization, as it relies on external support and image is essential in accomplishing its goals and its mission

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6 Other research conducted by Klond and Jawor Association shows that 54% of Polish foundations and associations performed activities "related to promotion and creation of the organization's image" (Herbst and Przewlocka, 2011, p. 140. Retrieved from [http://civicpedia.ngo.pl/files/civicpedia.pl/public/raporty/podstawowefakty\\_2010.pdf](http://civicpedia.ngo.pl/files/civicpedia.pl/public/raporty/podstawowefakty_2010.pdf).

7 Kruskal-Wallis test: grouping variable "size of the city" (Chi-square = 5.045, df=5, Asymptotic significance = 0.410), grouping variable "province" (Chi-square = 2.975, df=2, Asymptotic significance = 0.226), grouping variable "geographical area of operation" (Chi-square = 1.481, df=3, Asymptotic significance = 0.687).

(Krzyżanowska, 2000, p. 117; Szymańska, 2004, p. 338). Building a positive image is a long-term process (Howaniec, 2005, p. 27), requiring constant and well thought-out activities (Kotnis-Górka, 2011, p. 82).

**Table 2.** Promotion methods used by non-profit organizations (in %, quantitative research)

	Regularly	Very frequently	Frequently	Seldom	Hardly ever	Never
Advertising in mass media (newspapers, radio, TV) (N=239)	4.6	10.9	18.8	29.3	20.9	15.5
Additional promotion (coupons, contests, shows, lotteries, gadgets, calendars, Christmas cards, etc.) (N=237)	3.4	7.6	22.4	26.6	18.1	21.9
Creating positive image of an organization (N=243)	25.1	16.5	36.6	12.3	6.2	2.3
Personal promotion (direct contact with addressees of organization's activities) (N=241)	29	29.5	28.6	7.1	4.1	1.7
Advertising in the Internet (www pages, sponsored links, blogs, advertising banners, etc.) (N=237)	22.8	11.4	12.7	18.6	16.9	17.7

Non-profit organizations may also use advertising in mass media. It allows them, for example, to repeat the messages many times and to direct them at a wide range of addressees at the same time (Kall, 2002, p. 18; Michalski, 2007, p. 323). A serious constraint encountered by non-profit organizations which would like to advertise in mass media are costs. Mass media advertisements (press, radio, TV) was regularly used only by 5% of the surveyed respondents (quantitative research). It was frequently or very frequently used by almost 30% of organizations. On the other hand, over 15% of the respondents never used this promotion method. Advertising in the Internet was never used by nearly 18% of organizations, while 23% of entities declared their regular presence online. The use of the Internet is “a vital feature of all contemporary marketing communication systems” (Iwankiewicz-Rak, 2011, p. 72). The Internet gives



non-profit organizations a lot of new possibilities of communication. It is a relatively cheap and interactive medium (Kotler, 2005, p. 612), characterized by constant access and offering a possibility of reaching remote places with the message. Undoubtedly, non-profit organizations will intensify the use of this medium.

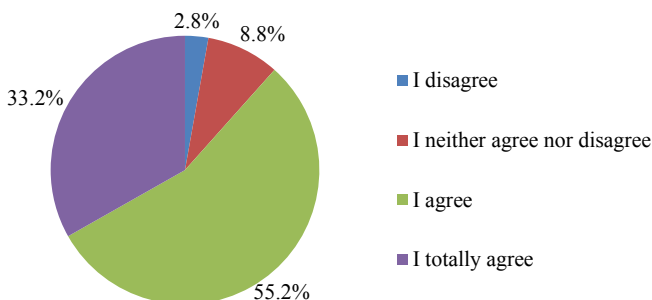
Personal promotion was an instrument of marketing communication intensely used by the surveyed respondents. It was used regularly by 29% of organizations, while 58.1% used it frequently and very frequently. Direct contact with addressees of activities is particularly important for non-profit organizations due to the nature of their offer – namely service (Iwankiewicz-Rak, 1997, p. 125; Krzyżanowska, 2000, p. 116). Personal promotion tasks refer to all employees contacting the surrounding environment of a an organization (Wiktor, 2006, p. 129, 131-132), representatives of the board, volunteers and organization members. Direct forms of communication may serve the purpose of attracting various groups of stakeholders, such as service recipients, donors, volunteers (Iwankiewicz-Rak, 1997, pp. 125-126).

Non-profit organizations may also use the tools of auxiliary (supplementary) promotion in their marketing communication process. They form “additional, unusual stimuli” (Wiktor, 2006 p. 199), enriching the organization’s offer (Huczek, 2003, p. 103; Wiktor, 2006, p.199) and contributing to attracting various groups of stakeholders (Iwankiewicz-Rak, 1997, pp. 124-125). The use of additional promotion instruments brings quick but short-term effects (Wiktor, 2006, p. 201). We should also remember that we should not use them too often, as they will cease to be exceptional (Huczek, 2003, p. 103; Wiktor, 2006, p. 201). Additional promotion tools (such as calendars, Christmas cards, lotteries) were frequently or very frequently used by 30% of the surveyed entities. Among other ways of promotion, the respondents often mentioned special events, radio programs, radio and press interviews, information in media on performed activities, performances, shows, exhibitions, leaflets, posters, announcements made in church, conversations, internal marketing.

According to 88.4% of the surveyed people, non-profit organizations should conduct intense promotional activities (Figure 2). Only 2.8% of the respondents had a different opinion on this issue. Opinions on the legitimacy of intense promotional activities performed by non-profit organizations did not depend on subjective evaluation of financial situation, province, size of

the city in which the organization's registered office is located or geographical scope of operations<sup>8</sup>.

Non-profit organizations should conduct intense promotional activities



**Figure 2.** Opinions on the legitimacy of intense promotional activities undertaken by non-profit organizations (quantitative research, N=250)

Promotion messages should emphasize “desirable, exceptional and reliable” benefits (Doyle, 2003, p. 355) for the stakeholders of non-profit entities. Organizations participating in the qualitative research indicated the most emphasized aspects in promotion communication. They are presented in Table 3.

<sup>8</sup> Kruskal-Wallis test: grouping variable “evaluation of financial situation” (Chi-square = 1.108, df=4, Asymptotic significance = 0.893), grouping variable “province” (Chi-square = 1.829, df=2, Asymptotic significance = 0.401), grouping variable “size of the city” (Chi-square = 4.021, df=5, Asymptotic significance = 0.546), grouping variable “geographical scope of activities” (Chi-square = 1.244, df=3, Asymptotic significance = 0.743).

**Table 3.** Basic features stressed in promotion communication of non-profit organizations (qualitative research)

Name of the organization	In promotion communication we emphasize most ...
Urszula Smok Foundation “Donate Life” Register of Bone Marrow Donors	“idea of bone marrow donation”
“Blessed Sister Bernardyna Jabłońska Hospice”	“our own mission”
Anna Dymna Foundation “In Spite of Everything”	“information on the purpose of collecting resources (and that it can be checked at any time)”
Association of the Sick People’s Friends, St. Lazarus Hospice	“information on the care – that it is professional, for everybody who needs it and that it is for free”
Association of Parents and Guardians of Disabled Children “Give a Chance”	“complexity, professionalism”
“Arka” Specialist Counselling and Helpline	“usefulness and effectiveness”
Caritas of Cracow Arch-Diocese	“our own mission”
Association for the People in Need “Sursum Corda”	“effects of our work, results of our activities”

Non-profit organizations should emphasize in their promotion messages the domain of their activities, which was achieved by the surveyed units. They informed about their mission, goals and other vital aspects related to their operations. “Sursum Corda” Association placed the emphasis on information in promotion messages on the effects of their activities. Anna Dymna Foundation “In Spite of Everything” stressed the purpose of collecting the resources, informing of the possibility of verifying the information provided. It seems important, as it may ensure donors that their support was used properly (the resources were appropriated in line with their purpose).

## 5. Conclusion

The communication system in non-profit organizations aims not only at convincing people to use the offer, but also to attract resources for an organization’s activity, attracting people to work for it, building trust of public opinion (Iwankiewicz-Rak, 1995, p. 4). The communication strategy of non-profit organizations should cover then various groups of stakeholders – both external and internal ones (Bruhn, 2005, s. 384). In contacts with their stakeholders organizations can use various instruments. Communication may be traditional and with the application of the latest technologies.

Non-profit organizations must be able to communicate with their stakeholders in an efficient and effective way. It should be emphasized that a one-way activity is insufficient. What is really needed is a dialogue between

organizations and stakeholders, covering information and persuasion activities and feedback between communication recipients and senders (Wiktor, 2006, pp. 41-42). In this context it seems important to cover not only organizations but their stakeholders as well with the research. Such research could, inter alia, indicate the forms of contact preferred by particular groups of stakeholders or the most effective instruments of marketing communication.

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# THE SOCIAL ENGAGEMENT AS A SOURCE OF INNOVATION

**Grzegorz Baran<sup>1</sup>, Janusz Bąk<sup>2</sup>**

## **Abstract**

*Innovation, innovation economy, innovation management are all crucial issues in both theory and practice of management. The purpose of this paper is to provide mechanisms for the use of corporate community involvement in public affairs as a source of innovation for both business organizations and in relation to ways of solving social problems and pursuing public purposes. The use of business engagement in social affairs as a source and inspiration for innovation and the mechanisms of responsible use of that business engagement by community and public organizations were analyzed. Companies have discovered that social problems have their economic side and the involvement in solving the problems of the public sector can strongly stimulate their own business processes. The new paradigm for innovation grows in the field of cooperation between private business and public interest, generating positive and permanent changes for both sides. There is a strong need for the cause social responsiveness and increased social sensitivity, not only on the side of the business but also in public organizations.*

**Keywords:** *innovation, change, social responsibility, cause social responsiveness, social engagement.*

## **1. Introduction**

A significant part of the debate on management practice and sciences has been dominated recently by such terms as innovation, innovative economy, innovation management. Not only nowadays but presumably always creativity and innovation have been the crucial factor in building a competitive advantage by individual companies and a society as a whole. Creativity and innovation have been always the engine of economic and civilization acceleration.

Innovation and change are part of everyday life in most contemporary organizations. They are useful for the society and the economy, businesses and public institutions. Innovators appear to be those who are able to solve

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the most demanding problems and issues. Thus it is not surprising that a great deal of organizations constantly seek new sources of inspiration for innovative solutions. They build laboratories where they can develop their capabilities, experiment with new technologies, obtain feedback from the first users of the potential products or gain experience in emerging markets.

At the same time, there appear new possibilities of gaining this type of experience in completely unexpected places. Business social engagement is one of such promising areas. Business cooperation with public and social sectors or taking actions to solve specific social problems may be used as new promising sources of innovation. Such involvement allows to gain knowledge about new markets and even create new markets and develop strong and sustainable relationships on them.

In the paper, we attempt to present the mechanisms of corporate involvement in social and public issues as a source of innovation for both business organizations and in terms of solving social problems and pursuing public purposes. We have analyzed how business organizations may use their involvement in social issues as a source of inspiration for innovative solutions. On the other hand, we tried to examine the possibility of responsible use of the business engagement by social and public organizations.

## **2. The increasing need for innovation**

According to P. Drucker, “Innovation and entrepreneurship are thus needed in society as much as in the economy, in public-service institutions as much as in businesses. It is precisely because innovation and entrepreneurship are not ‘root and branch’ but ‘one step at a time’, a product here, a policy there, a public service yonder; because they are not planned but focused on this opportunity and that need; because they are tentative and will disappear if they do not produce the expected and needed results; because, in other words, they are pragmatic rather than dogmatic and modest rather than grandiose—that they promise to keep any society, economy, industry, public service, or business flexible and self-renewing” (Drucker, 1985, p. 254).

The term ‘innovation’ derives from the Latin word ‘*innovatis*’, which means renewal or creating something new. In Polish, innovation is understood as the introduction of something new, a newly introduced thing, a novelty or a reform” (Tokarski, 1980, p. 307). Innovation has become the subject of scientific interest during the 1940s and the concept of innovation had been introduced to economic literature by J. A. Schumpeter in 1911. Initially, the issue was considered only in terms of macroeconomic analysis. Primarily, the impact of technological progress on economic development was studied. The



analysis of the determinants of these processes at the microeconomic level appeared later (Bielski, 2000, p. 6).

According to Schumpeter the term innovation included a fairly large range of phenomena: the launch of a completely new product or its variety on the market, the introduction of new production methods that have not yet been proven in the field of industry, opening a new market, gaining a new source of raw materials, the initiation of the new organization of industry (Schumpeter, 1960, p. 104).

Schumpeter believed that innovation had to be related not only to the novelty but also to the first use of the novelty. He did not consider the further diffusion of the novelty as an innovation, but only an imitation. He distinguished also between terms 'innovation' and 'invention'. According to Schumpeter, inventions that have not been put into production are not innovations (Niedzielski and Rychlik, 2006, s. 19). The first theories of innovation were focused on their technical properties and their importance to the economy in which the essential role was played by land, production and capital. The knowledge and information, that are crucial for the contemporary society and economy, were appraised as less important factors (Janasz and Koziół, 2007, p. 13).

With the passage of time, not technological but economic aspects of innovation have turned out to be increasingly important. We should mention here the names of such authors as: P.F. Drucker, Ph. Kotler, R.W. Griffin, M.E. Porter and also Polish authors: S. Marciniak, I. K. Hejduk, W. M. Grudzewski, A. Pomykałski and S. Gomulka (Janasz and Koziół, 2007, p. 15).

According to „*Oslo Manual – Proposed Guidelines for Collecting and Interpreting Technological Innovation Data*”, the crucial problem is proper understanding of the innovation processes and its economic impact. An innovation is the implementation of a new or significantly improved product, process, marketing method, or a new organizational method in business practices, workplace organization or business relations (OECD, 2005). Thus, innovation is any change, provided that it is the novelty at least for the organization applying it.

Drucker (1985) argued that managers have to learn to practice systematic innovation. He claimed that entrepreneurs should not wait until *‘the Muse kisses them’* and gives them a *“bright idea”*. Successful managers go to work and try to create value and to make a contribution. They aim high; the improvement of what already exists and just modifying it is not enough for them. “They try to create new and different values and new and different satisfactions, to convert a ‘material’ into a ‘resource’, or to combine existing resources in a new and more productive configuration” (Drucker, 1985, p. 34).

Gary Hamel and Bill Breen (2008) go further and talk about management as an aging technology in terms of the need for management innovation. According to them, we need to renew the management. In the past half-century we have experienced radical changes in almost every area of life – from technology to geopolitics. Compared to them, the practice of management seems to be developing at a turtle’s pace. A manager of the 1960s, suddenly placed in the former position, would undoubtedly be amazed at the flexibility of logistics chains or all day technical service. However, after the initial shock, he would not have any problem with the management of corporate life. Most management rituals practically do not differ from those before generation or two (Hamel and Breen, 2008, p. 18).

They provide several examples of such innovations: knowledge management in General Electric, new tools for rational capital allocation in DuPont, intangible values management in Procter&Gamble, methods and tools to use abilities and ideas of every employee in Toyota or the construction of Visa as a global virtual consortium (Hamel and Breen, 2008, pp. 38-41)

Thus, the question is how to create a management innovation in terms of public and social problems. We need innovations that would make public and social organizations gain new opportunities to compete, new opportunities for a more rational allocation of resources, new opportunities for cooperation and co-creating value with their stakeholders.

### **3. The role and nature of social responsibility**

Today, companies are constantly searching for new opportunities to compete. It is increasingly difficult to differentiate themselves from competitors only by the offer in the long term. Competitors quickly imitate the changes that have been positively received by the market. Corporate Social Responsibility is one of the possibilities to differentiate themselves in the market today.

Until the First World War the owners and shareholders administered their own businesses and all social activities were dependent on their decision. Since that time there have been significant changes in the perception and understanding of social responsibility by theorists, managers, public servants and public opinion (Rybak, 2004, p. 15).

The concept of corporate social responsibility (CSR) was first formulated in 1899 in “*The Gospel of Wealth*” by the American steel magnate Andrew Carnage (Rybak, 2004, p. 15; Post et al., 1996, pp. 41-43). According to him, CSR is based on the implementation of two principles: charity and stewardship. Both of them are rooted in the Bible. We can then assume that the beginning of the practical implementation of the CSR principles goes back to the early history of society.

Managers should maintain and develop beneficial relationships with all groups that are linked with activities or results of the organization's activities. This idea is in line with the declaration of the director of one of the U.S. companies, who claimed that "every citizen is a stakeholder of the enterprise, no matter whether he shares in it or not, whether he is employed or not, whether he buys its products if he does not. The fact that he lives in American society makes him a stakeholder" (Post et al., 1996, p. 43). This statement, though formulated in relation to American business, is fully adequate to the whole society. Every citizen is part of the state and society, and has the right to the equal access to all its goods.

According to A. B. Carroll and A. K. Buchholtz: „The concept of business responsibility that prevailed in the United States during most of our history was fashioned after the traditional, or classical, economic model. Adam Smith's concept of 'invisible hand' was its major point of departure. The classical view held that a society could best determine its needs and wants through the marketplace. (...) Thus, the 'invisible hand' of the market transforms self-interest into societal interest" (Carroll and Buchholtz, 2003, p. 31).

In the classical economic model no additional external impact is required in order to protect the public interest. Business organizations work for the benefit of society by taking care of their own business. Czy chodziło Ci o: organizacje dbające o własny interes, działają z korzyścią dla społeczeństwa

The invisible hand of the market, claimed by Adam Smith, transforms the self-interest of enterprises in social benefits. Unfortunately, although the market works well in regulating what kind and how many products are needed, it is not able to provide completely honest and ethical operation of enterprises.

According to Drucker, „social responsibility of managers require such proceedings that all being actually in the public interest has become the company's own interest" (Drucker, 1998/1954, p. 418). He understood that "it is (...) clear – though it may sound contradictory – that the more management can use the traditions, values, and beliefs of a society, the more it will accomplish" (Drucker, 1986, p. 20). However, he also understood that managers are responsible for the social impact of its enterprise, stating: "When social responsibilities are being discussed these days, however, the emphasis is quite different. It is on what business should or might *do* to tackle and solve problems of society" (Drucker, 1986, p. 220).

Robert Bauer put it in the similar way: "Corporate social responsibility is seriously considering the impact of the company's actions on society" (Carroll and Buchholtz, 2003, p. 34). Similarly CSR was defined by Davis and Blomstrom: "Social responsibility is the obligation of decision makers to take actions which protect and improve the welfare of society as a whole

along with their own interest” (Carroll and Buchholtz, 2003, p. 35). Trying to resolve what social responsibility is, it clearly comes along as a duty to care for the social welfare, especially if there was a risk that it will be affected by the negative consequences of the business activity.

The most interesting approach to social responsibility, in terms of the paper, was presented in 1971 by the Committee for Economic Development. They used “a ‘three concentric circles’ approach to depicting CSR. The inner circle included basic economic functions – growth, products, jobs. The intermediate circle suggested that the economic functions must be exercised with a sensitive awareness of changing social values and priorities. The outer circle outlined newly emerging and still amorphous responsibilities that business should assume to become more actively involved in improving the social environment” (Carroll, 1991, p. 40). The most useful for our research seems to be the outer circle that represents newly emerging areas of social responsibility and engagement. They are associated with business involvement in improving the social enterprise environment.

#### **4. The search for new sources of innovation**

Nowadays, organizations more or less constantly seek new sources of creativity, inspiration and innovation. Sometimes the influences are completely unexpected. An example is the engagement in cooperation with non-governmental sector or undertaking initiatives to solve significant social problems. In some cases the social engagement is caused by *movement of the heart* but in others it is a component of a business strategy and designed to bring expected benefits. Improving company image, increasing confidence and motivation, raising the level of organizational culture and increasing customer loyalty, which were mentioned in the earlier part of the paper, are the most common business expectations in terms of the social engagement.

We can also observe increasingly more complex motives and forms of the corporate social responsibility development. Some of them are strongly linked with the search for new sources of inspiration and innovation. According to R. M. Kanter: „Winning in business today demands innovation. Companies that innovate reap all the advantages of a first mover. They acquire a deep knowledge of new markets and develop strong relationships within them. Innovators also build a reputation of being able to solve the most challenging problems. That is why corporations spend billions of dollars each year trying to identify opportunities for innovation – unsolved problems or unmet needs, things that don’t fit or don’t work” (Kanter, 2003, p. 190).

To identify these new abilities for innovation, corporations build research and learning laboratories where they can extend their capabilities, experiment

with new technologies and products, get feedback from early users or gain experience working with emerging markets. Today several organizations are looking for such inspirations in completely unexpected places as the social sector, public schools, welfare-to-work programs, the inner city (Kanter, 2003, pp. 190-191).

These companies, according to Kanter, have discovered that social problems are also economic problems, whether it is the problem of finding qualified workers or the search for new markets in neglected parts of cities. „They have learned that applying their energies to solving the chronic problems of the social sector powerfully stimulates their own business development. Today’s better-educated children are tomorrow’s knowledge workers. Lower unemployment in the inner city means higher consumption in the inner city” (Kanter, 2003, p. 191). Kanter calls this phenomenon *a new paradigm for innovation*, which is based on a partnership between private enterprises and public interest that is beneficial for both sides (Kanter, 2003, p. 191).

Porter and Kramer write about creating shared value that means the connections between societal and economic progress (Porter and Kramer, 2011). They said that “it is true that economic and social objectives have long been seen as distinct and often competing. But this is a false dichotomy; it represents an increasingly obsolete perspective in a world of open, knowledge-based competition. Companies do not function in isolation from the society around them. In fact, their ability to compete depends heavily on the circumstances of the locations where they operate” (Porter and Kramer, 2003, p. 32).

According to Kanter, this new paradigm for innovation has long been needed. There are at least two reasons for this. Traditional corporate engagement only scratches the surface, rarely touching the fundamental issues. And second, corporations often just give money, while beneficiaries do not need charity but change and transformation (Kanter, 2003, p. 191).

Financial support and donations as the most typical form of business engagement constitute a barrier to the increased efficiency of business partnerships created to solve the most challenging public problems. Public and social organizations expecting only financial support are losing many potential possibilities of effective and long-term cooperation. An entrepreneur, activated by visible effects of the public cooperation, may want to continue to engage in further projects and motivate others by his example. Limiting the relationship to passive waiting for financial support, it may be difficult to involve donors in projects for the common good.

Treating business as a source of charity is not in the interest of society. It is obviously intelligible that certain social groups, such as the needy, are looking for help in all ways. Notwithstanding, the introduction of comprehensive

solutions for companies' commitment to cooperation should be based on proposals beneficial both from society point of view and the business sector.

Encouraging corporations to actions that will be beneficial for their stakeholders/beneficiaries, but will contribute to the deterioration of the economic situation of the donors as well is not effective in the long term. And it also may contribute to the slowdown of economic growth. It is therefore necessary to consider the creation of comprehensive proposals for the development of business partnership for solving public problems. Such a partnership should be based on professional management and strategy consistent with the social and economic development objectives.

In practice, the above problems are not completely solved. According to the results of comparative studies carried out in Poland, Hungary and Slovakia by Responsible Business Forum (2005)<sup>3</sup>, Polish companies most definitely comment on the absence of proper government policies to encourage investment in activities in the field of social responsibility. They often indicated a lack of legislation, and even the negative impact of government policies on investments in activities of a social nature (in comparison with other countries).

In such areas as education, health, safety, labor market, communication, long-term structural changes are needed. Short-term provisional changes to solve only the current financial problems are not sufficient. What is needed is the partnership with business that can completely transform the approach to solving specific public problems, such as the involvement of local businesses that would fundamentally change the operation of local schools, give new career prospects for their graduates, and even change the entire local environment. Observing differences between learning foreign languages in private language schools and public schools, or communication with patients in private and public health centers, it is clear that such changes are possible and necessary.

The chance is that the local entrepreneurs do not remain indifferent to how public issues are dealt with in their local communities. They begin to understand that social engagement can be a sort of experimental training ground for exploration and testing innovations. Kanter even speaks of a certain evolution of social responsibility into social innovation. (Kanter, 2003, pp. 189-213). Traditionally, opportunities for cooperation with the public and social sectors were perceived very narrowly by business companies. Currently, we observe the increasing business awareness and consequently the higher expectations for the cooperation undertaken. Companies are viewing community needs as opportunities to develop new ideas, present their technologies, solutions and

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<sup>3</sup> The report of the research conducted in the last quarter of 2004 and the first quarter of 2005 on the sample of 154 companies from Poland, 150 from Hungary and 150 from Slovakia, selected from a group of 500 companies with the highest turnover and/or number of employees.

products, find and create new markets, and even create new business solutions. Social business engagement is no longer charity and is increasingly becoming a strategic investment as a testing ground for research and development (Kanter, 2003, pp. 189-190).

The greater public involvement is also required to achieve the success of such a shared value partnership. It is related to social responsibility of public organizations. As long as public organizations pursue only the objectives assigned to them even in the most honest and legal way, it is difficult to talk about their absolute social responsibility. The social responsibility in line with the idea of CSR appears only when they are looking for new solutions and possibilities for action beyond the daily routine duties.

Social responsibility is not charity. Charity is the easiest form of social commitment both for donor and beneficiaries. It is easier for a computer company to give a school new computers than to help change the functioning of the school using these computers to create new prospects for students. The real and fundamental change in this case also requires a significant and active commitment of the school. This additional commitment to public issues and leadership roles adopted by companies in social problem solving may be called CSR2 – *Cause Social Responsiveness*. CSR2 is understood as being sensitive and ready to respond actively to social needs (social cause).

In the designation ‘*Cause Social Responsiveness*’ compared to ‘*Corporate Social Responsibility*’, it is important that the object of responsibility is not a corporation as before but an important social cause. Social responsibility is no longer focused on the organization and its interests but on social problems and solving issues. The use of the term *responsiveness* instead of *responsibility* is equally significant. It shows social responsibility not as a feature of the organization but an activity undertaken in response to a social cause. The use of the term *responsiveness* is to highlight the action-oriented side of social responsibility concept in place of the ideological premises. This greater emphasis on responsiveness has been already proposed in management literature (Carroll and Buchholtz, 2003, p. 46-47). However, the responsiveness was related to the organization, not the social cause.

## **5. Conclusion**

The purpose of the paper was to present the use of mechanisms of social business engagement in public issues as a source of innovation that produces profitable and sustainable change for both sides.

Today and in the past, innovative factors in the development of enterprises and society have been the driving force of economic and civilization acceleration. Innovations are the basis for building competitive advantage and creating new



markets for enterprises. This implies a strong pressure on managers to search for new sources of innovation. It may motivate them to greater involvement and social responsibility. Companies discovered that social problems are also economic problems and they have learned that applying their activities to solving the problems of the social sector may stimulate their own business development.

The new paradigm for innovation grows in the field of cooperation between private business and the public interest, generating beneficial and lasting changes for both parties. Thus, there is the strong need for sustainable response to social problems and the search for new solutions for public purposes. We call it the cause social responsiveness, which requires increased social sensitivity not only from the business but also public organizations.

In such areas as education, health, safety, welfare-to-work programs, social communication, there are necessary fundamental and sustainable changes not only scratching the surface by short-term financial help to solve current budget problems.

We need the business partnerships that would be able to completely transform the today approach to solving crucial public problems. The new paradigm for innovation is the chance that local entrepreneurs will not be indifferent to how they are dealt with public issues in their local communities. Companies begin to comprehend that their social engagement may be used as a kind of experimental training ground for exploration and testing innovations.

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# THE TRANSFORMATION OF CULTURE IN MODERN FORMS OF ORGANIZATION ON THE EXAMPLE OF VIRTUAL ORGANIZATIONS

**Barbara Czarnecka<sup>1</sup>, Piotr Czarnecki<sup>2</sup>**

## **Abstract**

*Nowadays organizations are required to be extremely flexible while maintaining the consistency and integrity of actions, which is a difficult task. What management mechanisms are needed for that? In such circumstances, what is the role of the organizational culture? Does it still remain a kind of a “glue” bonding a company into one piece? What are the patterns of behavior that emerge from a new way of doing business in companies? The purpose of this article is to present the challenges posed by the development of culture in virtual organizations and the identification of potential research directions in this area. We hope that the concepts of culture and related problems presented in this paper prove to be an inexhaustible potential for research on collective behavior patterns and their impact on the functioning of the modern organization.*

**Keywords:** *virtual organization, organizational culture, flexible organization, collective patterns of action.*

## **1. Introduction**

Modern companies undergo another wave of transformation brought by the era of the knowledge economy. Requirements related to the high organizational, financial and resource flexibility and wide use of the Internet for communication change the nature of the relationship between members of the organization from permanent to temporary. Nowadays organizations are required to be extremely flexible while maintaining the consistency and integrity of actions, which is a difficult task. What management mechanisms are needed for that? In such circumstances, what is the role of the organizational culture? Does it still remain a kind of a “glue” bonding a company into one piece? What are the patterns of behavior that emerge from a new way of doing business in

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companies? The purpose of this article is to present the challenges posed by the development of culture in virtual organizations and the identification of potential research directions in this area.

## **2. Directions of changes in the way that organizations operate nowadays**

The environment in which organizations operate has changed significantly over the last 20 years. Under the influence of radical innovation in the area of technology, changes in the political map of the world, new trends and socio-cultural economic shocks, “the walls came down” (i.e. the boundaries which so far divided the various branches of economy, industries, organizations, as well as traditional functional cells within the companies themselves).

Speed and ease of dissemination of new ideas, and the free flow of resources have increased the rate of change in the environment. Due to these changes the environment has become:

- more extensive, due to the processes of globalization and electronic communication,
- more diverse, under the influence of an individualized approach to customers’ needs and narrow product specialization,
- more unstable, as a consequence of rapid innovation and an increasingly shorter product lifecycle, solicited by changing needs and requirements of customers, as well as hyper-competition,
- more complex, because of the growing interdependence of social, demographic, political, economic, technological, and natural processes,
- impossible to predict, even in a relatively short period.

These trends have forced companies to radical, and sometimes even painful, changes leading to leaning the company; such as reengineering, downsizing, outsourcing and general cost reduction. The intervention methods, however, are not a panacea to the problems associated with the company’s competitive advantage and development in turbulent environments.

As researchers argue, reasons for this trouble were: underestimation of intellectual capital as an important source of value, as well as continuous treatment of the organization as an independent unit, competing with other companies in a hostile market environment (in such conditions the company’s interest is in the greatest possible autonomy and not in a closer relationship with other units of the environment; it is so called the paradigm of „an independent organization” (De Wit, Meyer, 2007, p. 238). An increasing awareness of the existence of these obstacles has led the company to make the next step towards greater cooperation and better control of creativity, innovation and knowledge management, and thus greater flexibility and agility. The paradigm shift has resulted in a number of significant modifications in the following

areas: strategic thinking and business models, the role and the importance of leadership, the way of using available resources, the organization of processes, communication, organizational structure and management systems. Table 1 lists the main areas of change in the way the modern organization operates.

**Table 1.** Directions of transformations in the way the organization operates

	<b>Industrial Age Business</b>	<b>Knowledge Age Business</b>
Focus	Bulk – material manufacturing	Design and use of Wtechnology & information
Goal	Commodity & differentiated products Profit/Growth/Control	Innovative products Self-renewal/sustainable enterprise/ innovation
Domain	Regional, local	Global, transnational, metanational
Strategic Orientation	Strategic planning and “fit” Rational strategy Resources and competencies	Strategic emergence and “shaping” strategy “Fuzzy” strategy Capabilities & innovation
Future Change	Predictability, determinism Periodic, steady rate, digestible	Uncertainty, probability, possibility Accelerating, overwhelming, fluctuating
Rules	Linear cause and effect	Nonlinear complex interaction
Game Plan	Long range	Short range probability scenarios
Leader	Manages a strategic plan till its completion	Envisions and suggests possible changes
Power	Centralized decision-making and responsibility	Decentralization Distributed decision-making and responsibility
Challenge	Demand versus capacity to deliver	Demand versus capacity to change
Resources	Material and financial capital	Knowledge and intellectual capital
Knowledge Base	Highly specialized knowledge base resulting in single-skilling	Interdisciplinary knowledge base resulting in multi-skilling
Risk	Moving to quickly – out of control	Moving to slowly – out of the running
Role Of The Managerial Team	Optimization of quality and productivity Application of raw energy Repetitive day-to-day operations Processing of resources & information Separation and specialization of work and organization	Quality= productivity = adaptability and response Application of ideas Quest for innovation Processing of knowledge & capabilities Holistic approach to and integration of work and organization
Process Perspective	Parts interact in a sequence of steps End-to-end efficiency; standardization of the response Hierarchical, linear information flows	Whole emerges from interacting parts Micro-to-micro integrity key; feedback the response Multiple, boundary-less knowledge networking
Organization And Control	Bureaucratic Direction, control Value chain; single organization	Meritocratic Guiding, cohering, focusing Value system; multiple organizations

	<b>Industrial Age Business</b>	<b>Knowledge Age Business</b>
Performance	Shareholder value	Stakeholder value
Measures	Financial performance	Non-financial performance
Key	Organization as a systematic machine	Organization as a systemic organism
Organization's	Organization as a system with clearly	Organization as a amorphous system
Features	set boundaries	with unclear and unstable boundaries
	Independent organization	Embedded organization
	Reactive/sustainability/stability	Anticipative/ flexibility/agility

Source: Own elaboration based on Leibold et. al (2002, pp. 19-20).

Therefore, nowadays organizations are required to: be able to make extremely rapid transformations; be ready for continuous learning and innovation; create networks with other stakeholders in order to survive in the global market; be ready for virtualization – increasing the range of action and allowing better access to resources. And these happen in the context of the continuing technological revolution and changing requirements of the people who become more and more independent, assertive, mobile, with a broad access to knowledge.

New ways of running a business can be embodied in such concepts as: the learning organization (Senge 2000, Morgan 1997), intelligent organization (Śliwa, 2001), organization on the move (Masłyk-Musiał 2003), chronically thawed organization (Weick, Quinn, 1999), organization without borders, N-forms of organization (Schreyögg, Sydow, 2010), embedded organization (De Wit, Mayer, 2007), as well as in structural solutions such as: the project organization, process-based organization, fractal organization, network organization, and virtual organization (Krupski et al. 2005; Brillman 2002; Parker et al., 2009, Warnecke, 1999).

Organizational changes in terms of objectives, technology and organizational structure, along with changes in the way of thinking, attitudes and behavior of the participants of the organization and the creation of new “collective patterns of action”, are all subject to the achievement of the proposed outer and inner flexibility, and will help to improve the coordination of actions.

In the face of such significant changes, the question about the role and direction of the transformation of organizational culture arises again. If we use the theory of organizational equilibrium, culture is an essential tool for regulating the activity of companies in the social internal and external areas, acting as stabilization, integration and coordination, as well as affecting “mental maps” and decisions made by people, by shaping patterns of perception and interpretation of events (Kozłmiński, Obłój, 1989, p. 200-219). Nevertheless, in terms of organizational flexibility the following questions arise:

- Does culture still fulfill the role of a stabilizer within modern, ephemeral forms of organization?
- What cultural patterns emerge from the interactions in such a diverse and uncertain environment and when does it happen?
- Who or what becomes a source of cultural patterns?
- Which of these patterns have a positive impact on the efficiency of the organization and which do not?

Virtual organizations (VO) were selected to help analyze the cultural issues of contemporary companies. This type of organization was chosen due to the main characteristics of such an organization: flexibility, and heterogeneity of members, as well as the nature of electronic communication, which brings about a number of changes and challenges in the social area.

### **3. The characteristics of the virtual organization (VO)**

The term “virtual organization” does not come down to a single, clearly defined organizational form. On the contrary, it includes a number of different configurations and solutions between structural units, where IT tools play an important role in the process of communication and coordination. This means that in order to define the characteristics of virtual organizations we need to use multiple criteria. The following dimensions, which will be used later in the analysis, were extracted from the literature:

- 1) the degree of independence of units included in the VO,
- 2) degree of virtuality, the meaning and scope of the use of IT tools,
- 3) the purpose for which the organization was established and period of cooperation.

#### ***The degree of independence of the units cooperating within the framework of the VO***

Some researchers point out that virtual organizations are, first of all, a variation of the network organization, and this means that VOs consist of separate legally and economically independent entities (K. Zimmiewicz, K. Bleicher, A. Sankowska, M. Wańtuchowicz - after: Stabryła et al. 2009, p. 93). Such a narrow approach would mean, however, that we cannot classify companies where employees are geographically dispersed and cooperate with each other only through electronic communication channels, using IT resources on the Web and offering services exclusively on-line. Therefore, one should assume that virtual organizations may consist of both companies as separate entities (suppliers, customers, clients, suppliers) as well as units that are parts of the same organization, such as virtual project teams, affiliates,

employees performing tasks of teleworking. Single individuals or companies can cooperate in the framework of the VO.

### ***The scope of IT tools***

The use of information systems for internal and external communication is a basic feature of virtual organizations. J. Niemczyk and K. Olejczyk put it as follows: “a virtual organization [...] uses intensively Internet, intranet and extranets to do better what previously was done with traditional methods, and to perform such tasks which were impossible to complete using classical techniques and technologies” (Krupski 2005, p. 112).

The scope of the use of IT tools may vary. This means that both types will be called virtual organization: companies using a mixed system - face to face and electronic contacts (with a predominance of the latter), as well as those organizations that exist only on the Internet, and communication and the flow of knowledge between their departments take place only online. The degree of virtuality, as well as the nature of the concluded contracts, may prove to be an important variable explaining the collective behavior of the members of the VO.

### ***The objective of the action***

Davidow and Malone (1993) define a virtual organization as a whole, which consists of many scattered participants (members), working temporarily in order to gain competitive advantage, operating within the framework of the joint value chain and business processes, supported by modern IT tools (in: Grabowski, Roberts, 1999). This definition indicates the duration and the purpose of the cooperation, as the next, important criteria related to this type of company.

Analyzing potential forms of a virtual organization, Camarinha-Matos and Afsarmanesh (2004) propose the following typology: virtual enterprise, extended enterprise, virtual organization, dynamic virtual organization, professional virtual community and business environment for the virtual organization (VO Breeding Environment) (Camarinha-Matos and Afsarmanesh, 2004, p. 8-9).

- Virtual Enterprise is an example of cooperation of many organizations on the basis of temporary strategic alliances, with companies operating in the same or another industry. They share resources and combine skills thanks to modern technology. The result of an activity of this form of a VO can be a common product or service. It is indicated, however, that the nature of such cooperation is more vulnerable to inequalities in relations and lack of genuine partnership, which results from lack of common objectives in cooperation (companies compete

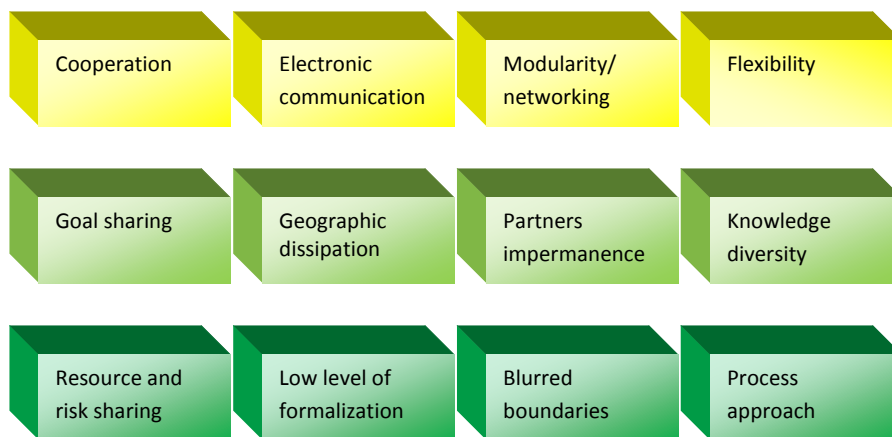


with each other outside the Alliance). Studies indicate that about 70% of virtual alliances end up in a fiasco (Preston-Ortiz 2011).

- Extended Enterprise is a system in which one parent company “expands its boundaries” onto suppliers, for example, by separating the whole physical activity outdoors, keeping only tasks related to design and coordination, and using modern technology for this purpose (e.g. Nike).
- Virtual Organization means, according to these authors, cooperating with all other legally independent entities which are not necessarily geared towards profit, but sharing resources and skills to achieve their mission by offering common products and services, and operating as if they were one organization. As an example, they give municipal companies such as a town hall, a supplier water, a tax office, etc, linked by a computer network (Camarinha-Matos and Afsarmanesh, 2004, p. 9). It should be noted that this is the kind of partnership (peer relationship, having a common purpose), focused on the long term cooperation. It allows flexibility by tailoring customer service processes better, and not necessarily by a large variability of members. In terms of previously described doubts as to the degree of independence of the cooperating units, it can be said that this is a narrower approach to the virtual organization.
- Dynamic Virtual Organization is a variation of the virtual organization of provisional nature, which was set up to achieve a particular purpose, and precisely exists till the end of the life span of the product.
- Professional Virtual Community is a type of virtual community of experts from some areas, who exchange experience or work on projects related to their industry. Among all these virtual organizations, professionals make up a homogeneous group that often uses the same “technical” language and is consistent in terms of patterns of action (professional culture). However, each of the professionals can be a member of another organization at the same time.
- Business Environment for the virtual organization (VO Breeding Environment) is a form of a cluster, which brings together a wide range of institutions, both business units as well as governmental organizations which support them, local non-governmental organizations, banks, etc., in order to increase the potential of the companies in the long run. In the case of market opportunities, companies can quickly create an organizational network and offer products or services. In this case, it is difficult to speak of a “real organization”. Rather, it is a platform that is used for an immediate creation of a network of enterprises, implementing the project together.

Grudzewski, Hejduk, and A. Sankowska and M. Wańtuchowicz also describe different models of the virtual organization in their book. They

indicate that it encompasses the following varieties: virtual image, i.e. electronic business (B2C), developed by the organization as an extension of traditional activities; a variety of types of virtual alliances; virtual team; temporary virtual organization; permanent virtual organization; community of practitioners; inner virtual organization; stable virtual organization; dynamic virtual organization; Network (Web) virtual organization (Grudzewski et al. 2007, p. 169-178). Unfortunately, the great variety of forms the VO can take demonstrates that the virtual organization cannot be included in the framework of a single definition. On the other hand, a variety of models is an interesting and rich in information area of scientific exploration. To sum up, in Figure 1 the main features of virtual organization are shown.



**Figure 1.** The characteristics of virtual organization

Virtualization of organization's activities brings about a number of benefits, but also a lot of challenges. Chances are primarily a result of increase in the company's competitive advantage and responsiveness to emerging market opportunities. And the threats are rooted both in the process of implementation of new solutions, as well as uncertainties posed by the dynamics of the development of this type of structures.

The potential benefits from the implementation of the VO:

- organizational, financial and resource flexibility which enables a rapid response to emerging market opportunities and an individualized offer to customer expectations;
- low cost action by concentrating on core competencies, sharing resources (e.g. technology), sharing risk, shortening the period of preparing deals, the competitiveness of partners in the network;

- innovation - VOs do not only react quickly to changes in the environment, but also create them through innovation;
- access to knowledge resources thanks to cooperation of specialists from many fields and from different parts of the world; openness in sharing information promotes better management of intangible resources;
- greater tolerance for changes resulting from the temporality of the relationship between partners and participation in a variety of projects,
- greater autonomy of workers, although possibly not at all levels and in all fields of activities of organizations, especially those larger ones;
- partnership instead of hierarchy (empowerment), subject to the above,
- better opportunities for developing skills of employees;
- development of cooperation ,
- VOs are a special opportunity for small and micro enterprises, because they facilitate their entry into new markets and access to resources that are not within the reach of financial capability of a single, small company.

The potential risks associated with the VO:

- problems with the coordination and division of tasks– openness and trust between team members do not guarantee a good organization of work; something or someone has to watch over this;
- difficulty with correctly understanding and identifying the purpose of cooperation, because it is not always obvious for all the partners (e.g. cooperation in the process of creation of new products, new technology);
- the appropriate selection of partners/employees; mainly in the context of social skills, reliability and responsibility;
- communication difficulties - electronic communication and cultural diversity of employees/partners may impede the proper understanding of content of the message;
- a paucity of face-to-face relations weakens interpersonal relationships and increases a sense of alienation, greater susceptibility to stress, resulting from high uncertainty and competitiveness;
- high specialization within the value chain raises the risk of losing the remaining competencies by the partner company;
- blurring the boundaries of the organization, resulting in problems with the identification of employees with the organization. It affects not only their integration and loyalty, but also the image of the joint venture in the eyes of customers (Who do I have to deal with as a customer? Who can I contact in case of problems? Who is responsible for the delivered product?);

- problems with loyalty of employees and partners - the lack of a sense of connectedness can encourage risky moves,
- some forms of the VO may lead to more competition than cooperation, for example when choosing specific partners for the implementation of the project, which may exacerbate opportunistic behavior;
- cash flow problems; problems with long-term financial resource planning, particularly for small businesses;
- trouble with the protection of intellectual property.

Modern, very diverse and dynamic work environment imposes a lot of requirements on employees and probably even more on managers. How to reach an agreement on common actions among self-managing and self-organizing mixture of entities? How to build a commitment? According to Charles Handy (1995), virtual organizations need actions based on mutual trust, but it is hard to achieve when employees are treated as workforce, not a valuable resource. VOs are based on information, knowledge and intelligence, which is contained in the minds of employees, but its disclosure also depends on whether employees are attached to the organization. Therefore, it is required to change the contract between employers and employees, from the instrumental to affiliate one.

*“People who think of themselves as members (of the organization – B.Cz, P.C.), have more of an interest in the future of the business and its growth than those who are only its hired help” (Handy, 1995, in: Grabowski, Roberts 1999, p. 711).*

It is difficult to build such ties without identifying oneself with what is being done. It is even harder to create some common basis in such a diverse environment. But maybe Charles Handy was wrong to write these words in 1995? Perhaps, market mechanism among participants of the VO will operate even more strongly than participation and cooperation? To put it in other words: Collaboration? Yes, but “briefly and without undue sentimentality, now you’re a partner/employee, but next time it will be someone else.” How is the analysis of organizational culture going to improve our understanding of what is happening in today’s organizations?

#### **4. Culture and virtual organization**

##### ***Integration perspective***

In a traditional, managerial approach (Schein, 1992, et al.) organizational culture is defined as a set of values specific to a given organization, which determine the perception and the way of thinking of its members. On the basis of values people create norms affecting their behaviours, which can be called “organizational practices”. These standards are the result of joint learning of

organizational participants on how to cope with problems of adaptation to the environment and the internal integration<sup>3</sup>. As a general rule, the practices that perpetuate are the ones that have contributed to the success of the company, and therefore are considered important and worthy of bequeathing to new members of the organisation, thus creating a basic pattern of culture. Since they are repeatedly in use, they are likely to drop out of awareness and become hidden drivers of behaviours (taken for granted assumptions). Culture is therefore a form of collective organizational knowledge that connects and unites members of the organization, and gives meaning to their actions. Values and norms can be equally invented by the group or imposed by the founders, but also enriched and developed by subsequent managers and employees.

Culture manifests itself in various forms of employee behavior, for example in the way of communication, conflict resolution, cooperation, decision making, organizational rituals, as well as in material artifacts like architecture, organization of the premises of the company, employees clothing, logo and other symbols of the company. It means that certain elements of culture can be observed - material and behavioral artifacts, and some remain hidden - basic assumptions, and thus should be deciphered. It is assumed that culture can be consciously shaped by leaders, owners or management. And in this sense, it can be a form of employees' control, through the emphasis on the standards required by management. This mechanism of acculturation is in fact a specific way to educate members of the organization what is right and what is wrong, which can also reduce the costs of coordination and control of labor processes (Czarnecka 2004, pp. 286-287).

The characteristics of culture presented above reflects the so-called integrative approach (perspective), which assumes that the organization should strive for a clear, shared and widespread pattern of desired organizational practices (Martin, 2002, pp. 94-100). Such a model of strong, unified culture was promoted in traditional organizations. It enhanced stability, emphasized the importance of the organizational structure, policies and procedures, awarded behaviors that supported a clearly defined mission, strategy and management actions. In this approach charismatic and self-confident leaders were put in the first place, as a main driving force of the organization.

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<sup>3</sup> The problems of **external adaptation** are related to identifying the purpose of the organization (its mission and vision), i.e.: What kind of products/ services does it want to produce? What kind of needs does it want to satisfy? Who are its customers? On what markets does it want to operate? How should it perform its goals (strategy)? On what basis will the organization shape the relationship with environment? What should be the structure, processes, procedures, systems of control and error detection? The **internal integration issues** are such as: common language and concepts of organizational activity, criteria of belonging to the organization (boundaries of the organization), allocation of rewards and status, nature of authority and relationships (Schein, 1999, pp. 27-48).

On the basis of such culture many companies shaped their identity<sup>4</sup>. It was clear who were their members and what was expected of them, what values they wanted to represent, how they should be perceived by customers. Culture was not only an important transmission belt which strengthened the identification of employees with the organization, but it was also used to build the border<sup>5</sup> between the company and its environment. The integrative approach emphasizes the importance of knowledge and experience gained by the company in the past. Culture is a repository of important skills and strategies that are worth repeating, and participants should use them, reproduce and develop.

The integrative perspective has not lost its significance with the emergence of new types of organizations, but this time the activity of its followers is focused on finding another universal set of cultural patterns which will enable flexibility, rapid adaptation to changes and smooth cooperation within the network. Some researchers suggest a blended type of culture, i.e. a mixture of features of strong and weak culture, which means that in some parts of the organization the patterns should be clear and uniformed, providing stability and predictability, while in others they must be diverse and rich in subcultures, which break schemes and are a source of innovation – but the question is: in what areas and why in these (Grabowski, Roberts 1999, p. 717)?

A slightly different direction is taken by those researchers who are seeking to promote patterns of cultural adaptation based on such values as:

- tolerance of uncertainty
- individualism
- low power distance
- cooperation and partnership
- openness and innovation.

The members of such a culture are required to:

- accept volatility as a permanent element in human life,
- exhibit autonomy in decision-making,
- be highly self-motivated and take responsibility for their own development,
- learn continuously,
- be willing to change patterns of thought and action, to easily establish contacts with customers or partners,

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4 **Organizational identity** refers to how members perceive their organization, what they feel and what they think about it. It is a common interpretation of what is an organization, what distinguishes it from the others, what is its specific nature. Culture shapes the way of identification, but identity can also affect the appearance of some practices and cultural norms.

5 **The boundaries of the group or organization** can be understood in two ways. Firstly, these are the rules that determine who can and who cannot be a member of the group, what distinguishes us from other groups or organizations. This may reflect symbols, such as dress code, manner of speaking, rituals associated with the admission of a new member, etc. Secondly, there are physical elements such as buildings, interior decoration, logos. The boundaries of groups have perpetuated identity. Nonetheless, it should be noted that the boundaries of culture do not have to take only a material form, they can be derived from our mental representations, as well (Hatch, 2002, p.256).

- exhibit openness in exchange of ideas and knowledge, which is based on mutual trust,
- be tolerant to diversity, which in turn requires the rejection of their own cultural patterns.

These requirements mean that certain cultural patterns are useful as long as they allow us to meet organizational roles, specific to a given place and time. When the roles are changing, for example a traditional manager turns into a virtual enterprise manager, the old patterns of behavior have to be replaced by new ones (Sikorski, 2002, pp. 133-137). The clarity of rules and their acceptance by participants as a basic mental scheme has become a mechanism that facilitates integration, adaptation and cooperation between members of the virtual organization. A suggested pattern of behavior should be then reinforced by appropriate institutional arrangements (e.g., personnel policy, structure, style of management).

However, the postulate of high flexibility in the way individuals perceive and respond to the situation is difficult to implement, because it is in contradiction with the theory of social cognition. This theory says that people are not able to easily jump from one pattern of thinking to another, because they have the tendency to simplify incoming information, to look for such data that strengthen once accepted assumptions, as well as the array of other mental limitations that make us *cognitive misers* (Aronson 1995, pp. 151-154). Therefore, it is unrealistic to expect that employees or partners will continually change their behaviors depending on the situation or they reject past experience when making decisions (Schreyogg, Sydow 2010, s.1252-1254). Building a universal, adaptive culture is a bit like requesting a man to write neatly once with a left and once with a right hand.

Also, flexibility is connected with high volatility of business partners, which nevertheless leads to strong competition, and this encourages opportunistic behavior, such as the transmission of incomplete or distorted information, deceiving, cheating, promoting smart and wily, but not necessarily competent people. Table 2 presents a summary of the differences between culture of the traditional and flexible organization, in the context of the integration perspective.

**Table 2.** Patterns of behavior in traditional and flexible organizational cultures

Traditional Organization	Flexible Organization
A reliance on a distinctive hierarchical structure to support the coordination of tasks. Such structures tend to encourage the pursuit of individual interest rather than mutual benefit which stifles creativity and innovation.	Continuous reassessment of tasks and assignments through interactions with others. Organizational performance is improved through a “learning by doing” process.
Roles are clearly defined and the boundaries of responsibility clearly drawn in order to improve efficiency. Task specialization and differentiation may lead to efficiency improvement in the short term but differentiation gives rise to demarcation which in turns inevitably leads to conflict among employees.	A network of authority and control based on expertise and commitment to an overall task rather than on clearly defined roles.
Management is concerned specifically with organizing, planning and controlling. Organizational boundaries must be preserved to retain the power necessary to preserve position and status.	Communication to be much more extensive and open. The communication style that is both lateral and diagonal as well as vertical – organization becomes a network.
Emphasis on a vertical flow of information. Decisions are taken at the top. Individuals within the organization lack a sense of ownership and commitment to organizational objectives.	Greater emphasis on commitment to the organization’s tasks, progress and growth than on obedience and loyalty. Decision making power is placed on individuals who are best positioned to face challenges within the organization. A greater sense of community and ownership. Individuals become stakeholders in the organization.
A high value is attributed to local knowledge, experience and skill. Geographical constraints have an important influence on determining where the organization is located	Contributors scattered throughout the world. Multi-cultural. Large variability of tasks. Flexible employment.
Members of an organization sell their time rather than their competencies and are expected to pledge loyalty to the organization and its management.	High value placed on expertise relevant to the technological and commercial milieu of the organization. Focus organizational resources and competencies on core activities.
Low need to motivate and mobilize for change	Leadership style with emphasis on consultation, interpersonal and group processes. Emphasis is placed on establishing direction, aligning, motivating and inspiring people.
Desirable characteristics of the employees: command execution, individual efficiency, competition with other employees, specialization.	Desirable characteristics of the employees: independence, openness, communication, innovation, ability to work, willingness to share knowledge, cultural intelligence.

Source: Own elaboration based on: Banahan et al. (2004, pp.126-127).



### *Fragmentation perspective*

The radical concept of the temporary and ephemeral organization without borders despises rules that would perpetuate solutions worked out in the past. Procedures, standards, and structures do not deserve attention, because they are archaic in themselves. The hyper-turbulence of environment requires companies to improvise rather than copy historical practices. It is important to create a dynamic potential of the organization, the continuous reconfiguration of knowledge and other resources on the basis of ad-hoc made decisions. Old patterns of behavior and decision making cannot help to solve new problems, so nothing should remain for long in organizational memory. Organizational forgetting is more important than organizational learning and remembering. The same thing applies to the identity and boundaries of the organization, which in highly flexible companies are considered to be barriers to the flow of information and knowledge (Schreyogg, Sydow 2010, pp. 1251-1252).

Such a philosophy of action is perfectly blended with the so-called fragmentation perspective, which assumes that culture is an ambiguous phenomenon, unique and characterized by the presence of many subcultures. However, the boundaries of these subcultures are not fixed and are constantly changing, creating anew in other configurations. That liquidity stems from two assumptions:

- 1) People forming a given organization differ in their individual identity which comes from belonging to multiple groups at work and in their personal lives. This in itself makes their perception of organizational problems entirely dissimilar. It can be said that the identity of individuals is diffused among these groups (*blurred or fuzzy identity*).
- 2) Individuals may identify themselves with different subcultures, depending on the debate. Therefore, subcultures are a temporary coalition, members of the organization participate in it only to solve a particular case, which does not necessarily imply agreement or disagreement on other problems. Nor does it mean that in the future subcultures must have a similar shape. So we can say that agreeing on organizational solutions is an ongoing process of continuous creation and there is not one, stable *modus operandi*. While the traditional approach emphasizes the role of culture as an integrator which provides a consensus on the issues important to the organization, the concept of fragmentation eliminates the notion of a general consensus and common patterns of perception. The problem itself is in the spotlight, not the standard by which it would be solved. Therefore, the boundaries of subcultures are uncertain, fluctuating, blurred, nested and overlapping (Martin, 2002, pp. 104-108, 152, 163-166; Hatch 2002, pp. 231-232).

It also seems that the authors of this concept elegantly omit the obstacle named “limited perception”, assuming that various reference groups equip their members with a variety of ways of interpretation, because each group has to solve different kinds of problems, and distinct issues are important to each of them. This background allows individuals to switch between various interpretations but does it not lead to an intrapersonal conflict?

According to these assumptions, the cooperation between the partners of the VO can take different forms - legal boundaries are not important, it is important that there are no cultural barriers in the form of a distinct identity.

Unfortunately, the fragmentation approach does not provide comfort to managers, because they do not have enough power (influence) to establish some benchmarks of behavior, even in a case such as trust. According to the assumptions, each issue should be settled by a current coalition (a temporary subculture). As in the case of integrative perspective, the question arises: whether the total uncertainty, instead of openness and cooperation will not contribute to the severity of opportunism?

The approach mentioned above deftly describes the diverse world of virtual organizations by explaining how cooperation is possible through constant reconfiguration of partners and self-organization, but it does not allow to answer the following question: what are the sources of failures or successes of the VO and how to operate efficiently in this environment?

### ***Differentiation perspective***

Are patterns of thinking and action disappearing, becoming blurred, because they are too often changed to create a stable pattern? Are the identity, culture and thus the boundaries of the organization still needed for something? Can we imagine the functioning of modern business without borders?

The concept of hyper-liquid organization, however, will remain the realm of myth, because the organization as a social system will always be something other than its surroundings. Blurring the borders would mean that one of these concepts would lose its meaning. G. Schreyögg and J. Sydow argue that:

*“ According to systems theory, the basic relationship of social systems is the interaction with their environment. A differentiation between an organization and its environment implies, at the very least, that organization means something different from environment” (Schreyögg, Sydow, 2010, p. 1253).*

Complexity is one of the factors differentiating these concepts. Environment is always something more complicated than the organization. Social systems are created as a result of the reduction of the complexity of the environment to a level that people can master and control. It is accomplished by constructing and replicating, in the daily manner, the internal world of less complexity.

This process is the basis for determining the identity of the system. Building worlds simpler than setting ones means interpreting events, giving importance to what people experience. On this basis, cognitive maps are formed in our minds. These maps are the basis for understanding the phenomena and events (e.g., what is the competition, what is working together, what is the market, etc.). Thanks to them we can decrypt the incoming information, and even more-detect objects and situations. Organizations, even those operating in the hyper-turbulent environment, cannot exist without referring to past experience. One cannot break up with their own past, since schemes of perception and action are hidden in it. Without them it is impossible to function.

Even if the entire organization is not an important point of reference, a group that an individual belongs to still remains such a point of reference. Most commonly, an individual interacts with other group members, and the group processes shape individual identity, through influencing one's behavior. The fragmentation theory ignores the fact that certain groups may be more important to us than others, and thus more strongly influencing our behavior. The environment we operate in can induce individuals to make forced choices, for example: when my organization is diffused and so really there is no reference group, my attention will be directed more to people outside the company. The question arises: what could this mean for people's behavior in your organization?

The differentiation approach assumes that the organization is a common cultural pattern. However, it is not so uniform or widely spread as according to the integrating approach. Norms and values arising from within the sub-groups' daily routines are a much more important point of reference. Sub-groups identify themselves as separate in relation to the other parts of the organization. They have common problems to solve and they work in their unique way. Groups can be based on functions, management levels, professions, or geographic territory. While building a specific identity, they shape their boundaries at the same time. That is how subcultures are created. They can have different relationships to each other and to the overall organizational values (Hatch, 2002, p. 228-229, Martin s. 101-104). Table 3 illustrates possible relationships between these concepts.

**Table 3.** Linkages between cultural identification, subculture identification, and behavioral outcomes

<b>Identification With The Dominant Organizational Culture</b>	<b>Sub-cultural Identification: Martin and Siehl (1983)</b>	<b>Behavioral Outcome</b>	<b>Research Areas And Sample Studies</b>
High	None	Behavioral consensus around core cultural values	Strong culture o rganizations Deal and Kennedy (1982) Denison and Mishra (1995) Efraty and Wolfe (1988) Peters and Waterman (1982)
High	Enhancing	Behavioral synergy around core cultural values	High-performance teams or “clans” Katzenbach and Smith (1993) Lim (1995) Wilkins and Ouchi (1983)
High	Orthogonal	Situational behavior based on dual influence of organizational and sub-cultural identification	Negotiating multiple identifications Ashforth (1998) Hernes (1997) Pratt (1998) Rousseau (1998)
Low	Orthogonal	Behavioral consensus around core sub-cultural values	Strong geographical, functional, sub-cultural differences Gregory (1983) Jermier et al. (1991) Rentsch (1990)
Low	Countercultural	Behavioral consensus around core sub-cultural values contradictory to overall organizational culture	Cultural resistance and sabotage Alvesson (1993) De Roche (1994) Linstead and Grafton-Small (1992) Robinson and Bennett (1995)

<b>Identification With The Dominant Organizational Culture</b>	<b>Sub-cultural Identification: Martin and Siehl (1983)</b>	<b>Behavioral Outcome</b>	<b>Research Areas And Sample Studies</b>
Low	None	Individualization	Ambiguous or “weak culture” organizations, virtual organizations Cohen (1997) Martin and Meyerson (1988) Smith and Kleiner (1987)

Source: Own elaboration based on: Bligh, Hatch (2011, p. 4).

According to M. Bligh and M. Hatch, analyzing interdependences and processes that occur between the identity of the individual units and identifying with the subculture and organizational values sheds light on the source of a wide variety of behaviors and cultural patterns. Identification with the organization and/or subculture highlights the process in which the individual agrees to seemingly contradictory cultural forces built around certain beliefs, through translating common patterns of thinking into the local language. By accepting, rejecting or modifying individual values, the individual builds the basics of his/her identity as a member of the organization. He/she also contributes to the development of different meanings and cultural varieties within a single company. Interesting research questions that are born in this area are as follows:

- 1) What is the influence of the characteristics of the group on both the process of identifying an individual as well as on the results of the unit?
- 2) What is the strength of the relationship between subcultures and general culture in different work environments?
- 3) What is the impact of a counter-culture on efficiency behaviors in organizations (Bligh, Hatch 2011, p. 41-43)?

The concept of subcultures is based on search for areas of convergence and divergence between the different cultural patterns in place. It seems to be a perfect approach to cultural studies in VOs. In this case a networked culture can be a general pattern, and individual participants may represent subcultures. But, subculture may also be internally differentiated. Although the differentiation approach reflects heterogeneity patterns of action, allowing us to describe cultural differences in virtual organizations, it cannot describe, in a proper way, the dynamics of transformations resulting from the variation of organizational partners. This is perhaps a potential area of future research.

## 5. Conclusion

Culture, understood as a mind programming, is still an important factor in shaping individual and group behavior in organizations. Without culture, one cannot talk about building any form of collective identity. And this process allows us to distinguish the organization from its surroundings. If one asks a question: why do dynamic organizations need culture?, the correct answer is: so that we can still call them “organizations”. However, the way of understanding and analyzing culture in diffused, virtual companies must change. The reference point for such an analysis will no longer be a homogeneous whole, but a heterogeneous group.

We hope that the concepts of culture and related problems presented in this paper prove to be an inexhaustible potential for research on collective behavior patterns and their impact on the functioning of the modern organization. At the same time, the diversity of approaches shows the wide possibilities for the interpretation and description of the phenomenon. Joanne Martin, in her book “Organizational Culture. Mapping the Terrain “ encourages researchers to equal and simultaneous application of all three approaches, to extend the perspective of analysis. Each of the approaches sheds light on other aspects of culture (Martin 2002). At the end we wish to indicate some problems of research which, we believe, are still under discussion.

- 1) If we accept the integration point of view, how do we change the current patterns towards the adaptive culture? What institutional processes should be strengthened?
- 2) What organizational practice, based on the value of adaptive culture, will develop in VOs? What form will it take in different types of virtual organizations?
- 3) How do virtual organizations solve problems of the external adaptation and internal integration? For example, how to negotiate objectives, how to formulate the network level strategy, how to determine control mechanisms, etc. What form does it take in a different types of VOs?
- 4) How will electronic communication influence language, personal relationships, and appropriate perception for members of the VO?
- 5) If we consider the structure of the virtual organization as a cultural artifact, what values, attitudes, and assumptions will emerge under their influence? This is a problem that has already been pointed out in the above parts of the article. Namely, do virtual organizations actually foster collaboration (which is widely postulated), or do they rather strengthen the opportunistic behavior ?
- 6) Who are organizational heroes now, do leaders still remain heroes?
- 7) What are the areas of cultural convergence and divergence in different forms of virtual organizations? What can impact them? How will

they affect the efficiency of behaviors within each subculture and the whole network of partners?

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# SELECTED ASPECTS OF PERFORMING THE PERSONNEL FUNCTION IN SMALL FOOD SERVICE ENTERPRISES

**Katarzyna Okuniewicz<sup>1</sup>**

## **Abstract**

*Performing the personnel function in a small food service enterprise depends largely on how the human is ranked in the organization, as well as on the management staff's approach to forming and exploiting the human potential. This involves creating favorable circumstances to perform this function, which entails examining specific variables (factors) that have an impact on how it is shaped. The study analyzes and assesses selected components of the personnel function in relation to food quality growth in small food service enterprises with use of the results of the empirical research conducted in restaurants located in Lower Silesia. The results obtained from the research were used as the basis for specifying the reality of performing the personnel function in the analyzed food service establishments.*

**Keywords:** *personnel function, personnel policy, food service enterprises, food quality.*

## **1. Introduction**

Food service enterprises are among the oldest forms of economic activity, ones depending on virtually all economic sectors. Such entities operate on the food service market, which is one of the most popular and dynamic market sectors. When considering the dynamics against the changes taking place in the structure of economic entities, what should be seen as a particularly painful issue, especially for continuity of small food service establishments, is first and foremost the necessity to implement stringent legal requirements, including mainly the food law, and hence to respect specific customer's interests with regard to food (e.g. good dish quality). Good dish quality should be identified with such a meal that meets the consumer's expectations in terms of its taste, smell, look and consistency (the so-called "sensory attractiveness"), as well as health properties and health safety (Turlejska, Pelzner, Konecka-Matyjek, Wiśniewska 2003, p. 37). Attentiveness to these qualities is a "measure" in the hands of the personnel, who is highly ranked in the process of shaping food

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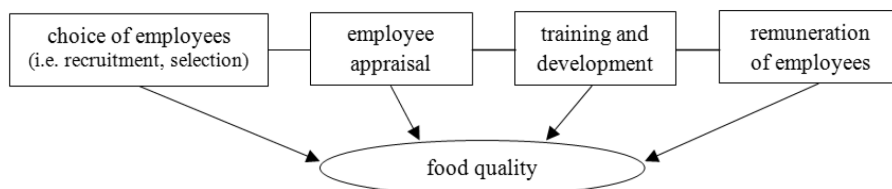
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quality in the entire food chain (i.e. from the primary production to the final consumption) (see more: Wiśniewska, Malinowska 2011, p. 28).

It should be added that quality has numerous layers of meaning, which makes it difficult to define it in an unambiguous manner both in the practice and theory of management (Costin 1999). This results from the fact that quality can be considered both in multifaceted and multidimensional terms, but also in comprehensive terms oriented towards continued improvement of all functions and processes that take place in the enterprise and influence the dish quality (Juran, Godfrey 1993, p. 2.4).

What is also important is the awareness that food quality is shaped not only by people but also as the result of exerting impact on people through, among others, creating favorable circumstances for performing the personnel function, which is one of the organic functions of the enterprise. The function is a set of activities (task areas) which refer to the human and which entail in fact not only recruiting people but also shaping them properly and exploiting them to the fullest (Lichtarski 2000, pp. 237-242). Performing the function should play the fundamental role in the process of shaping food quality. Therefore, it seems to be necessary to strive for recruiting competent employees, that is people who are able to act effectively using their knowledge that is indispensable to perform actions (tasks) related to shaping food quality and who are appointed based on their skills and abilities (Gableta 2006, p.19). What is also significant is the human internal motivation and physical features (e.g. health and appearance).

What seems to be of particular importance is focusing on such generic elements of the function as: choosing, appraising, training, developing and remunerating employees (See: Figure 1). These elements, apart from the fact that they should be performed in a given organisation, must be subject to regulatory (management) activities (Lichtarski 2000, pp. 237-242).



**Figure 1.** Selected elements of the personnel function constituting the object of empirical research

The “instrument” that facilitates performing the personnel function is the high rank of small food service enterprises’ owners with regard to personnel issues. It is them that the approach to people –which manifests itself through

the pursued personnel policy –adopted in a given organization depends on. Decisions concerning this policy reflect a given organization’s human resource management concept, which is a certain philosophy of performing the personnel function, and hence of perceiving employees and general intentions related to them. This policy constitutes a specific signpost in the process of forming a set of actions taken in the area of managing the human potential of food service establishments to facilitate the appropriate formation and exploitation of this potential (Gableta 2006, p. 29). It is also worth noting that entrepreneurs, for example through their attitudes and behaviors, shape a specific organizational culture, which determines the employee attitude to caring for the quality of actions involved in producing high quality dishes.

The study focuses on sixteen micro- and small food service enterprises that employ up to fifty people based on an employment relationship for an indefinite term or civil law contracts. The analyzed economic entities are conventionally called here small food service establishments. Particular attention is given to the leading restaurants on the Lower Silesian market that specialize in national cuisines.

The object of the study is defined as analysis and assessment of performing selected elements of the personnel function in relation to food quality growth in small food service enterprises. Simultaneously, the management staff’s attitude to subordinates is indicated with reference to the pursued personnel policy. This is reflected in the following research question: Does a specified set of principles and guidelines for managing the human potential of the examined enterprises facilitate shaping food quality? It has been considered appropriate to focus on choosing, appraising, training, developing, and remunerating employees. The weaknesses identified within those generic elements of the personnel function are analyzed with regard to attentiveness to food quality.

In order to meet this objective, both literature review and empirical research conducted between 2013 and 2014 are used. The latter were mainly surveys carried out with use of a survey questionnaire, which was developed with own means. They were expanded with in-depth interviews and own observations.

## **2. Considerations of performing the personnel function in small food service enterprises**

The personnel function is always shaped in specific circumstances determined by various variables (factors), which have an impact on its components. Performing this function is influenced by variables connected with decisions and actions taken in food service enterprises and ones that should be directly linked to the elements that form business environment. The factors listed first

are referred to as internal factors, while the ones following them are external factors.

Internal factors should be associated mainly with:

- human resource management system,
- working conditions,
- financial situation of the enterprise (financial standing),
- preferable approach to the human.

External factors are manifested mainly in:

- stringent legislative requirements,
- situation on the labor market.

At this point, it is worth focusing on the human resource management system in small food service enterprises. The system is distinguished by its specificity. The specificity is discussed on the basis of particular features and behaviors which are the same for operating methods of small enterprises. M. Sidor-Rządowska is right to indicate that in small economic entities the system is most frequently (Sidor-Rządowska 2010, pp. 23-25):

- simple – the management staff employ simplified methods, techniques and tools, which is usually accounted for by lack of time, but also appropriate competence necessary to implement more complex human resource management systems,
- centralized – decisions made in these entities, in particular those related to shaping the personnel function, are usually taken by owners themselves. Their reluctance to expand the workforce structure and to delegate responsibility in fear of losing their power and control is manifested here,
- not very formalized – pressure on limiting formal requirements to perform those on which the management staff have no actual influence and which they have to observe subject to sanctions. In small enterprises, significance of other tools is reduced, particularly those which remain within the competence of the management staff, oriented towards shaping the personnel area in enterprises.

It should be added that the scope of functions and tasks performed by employees is very complex in small food service establishments. Particular emphasis is put on the possibility to delegate employees to work on any position.

A relevant determinant of the enterprise's specificity is also its organizational culture, which is a set of fundamental opinions that were developed, invented or adopted in the organization to minimize its problems (Chojnicki, Bałasiewicz 2005, p. 276). Ł. Sułkowski highlights that numerous small economic entities have a hierarchical, but at the same time collectivist, organizational culture based on authority and influence of the owner's family members on the development of the organization (Sułkowski 2005, p. 47).

In such circumstances, what gains in significance is the necessity to create “human-friendly” working conditions with regard to material and social operational aspects that determine the human situation and behaviors in the working process. Therefore, the point is to create conditions which will be fully accepted by employees and which will simultaneously become the basis for addressing their needs and expectations (e.g. flexible forms of working time organization), which will be reflected in appropriate behaviors and hence appropriate quality of the activities taken in the area of food production (Gableta 2003 p. 179).

It is also important to give attention to the financial standing of small food service entities. This is because it may greatly facilitate “investing” in the personnel area of enterprises or reduce these investments. The dominant conviction regarding the practical operation of the discussed enterprises is that proper attentiveness to this area requires certain costs and is therefore unbeneficial. M. Rowińska-Fronczek is right to say that the management staff of enterprises must decide whether they are closer to P.B. Crosby’s convictions (Quality is free! It’s the lack of it that costs!), or lean towards the view that “Quality costs! Projects, investments, training!” (Lichtarski 2003, p. 319).

The actions taken in the personnel area of food service enterprises are largely determined by their preferred approach to people, which manifests itself in the pursued personnel policy. In broader or narrower terms the policy refers to either of the two basic models of this policy, i.e. the sieve model or the human capital model.

A policy based on the sieve model refers to the traditional formula of performing the personnel function based on objective and instrumental treatment of employees called Personnel Management (PM). Preference for this model entails recruiting and retaining employees who are the best in view of the current needs of the enterprise. According to this concept, people who perform their work are treated as one of the “instruments” in the hands of the management staff of food service establishments. In this regard, formalization of the employer-employee relation is desired. As for pursuing the personnel policy in accordance with the human capital model, which draws on the concept of Human Resource Management (HRM), involves a subjective orientation towards the employee, who is assigned the leading role in the enterprise management process. A high rank is attributed to the management staff who are responsible for shaping and exploiting the enterprise’s potential. It is also important to develop employee competence and to invest in their development on a long-term basis, as well as to build their involvement and to stress their participation in decision-making processes (Cierniak-Emerych 2010, pp. 11-31). This participation is reflected in a concept which has been gaining in significance lately and which relates to forming a bundle of key management

practices, i.e. in the so-called High Performance Works Systems (HPWS). Within these systems, a significant rank is assigned to the High Involvement Work Practices (HIWP) concept, which stresses employee autonomy when making specific decisions concerning the work that they perform (Kostera 1999, Cierniak-Emerych 2010, pp. 11-31). In practice, numerous enterprises refer to the sieve model, simultaneously emphasizing elements of the human capital model in the adopted policy.

Problems related to the application and operation of the HRM concept entail to a large extent universalism, willingness to convey the “only right” idea for human resource management. In practice, however, difficulties in its implementation merge (Gableta 2003).

It should be also emphasized that integration with the European Union standards encouraged the contemporary food service entities to verify their previous approach to people and work performed by them. When shaping specific activities concerning the performance of the personnel function, one should at the same time focus on the important, from the perspective of food quality growth, activities connected i.e. with employees taking part in the decision-making process (the so-called employee participation) and investing in their development (See more: Gableta, Cierniak-Emerych 2011).

Employee participation may indicate not only taking part in a specific undertaking but also being its member, sharing something with someone. The issue of participation may also mean allowing the employee to participate in an activity, to assume responsibility, to reap benefits and to incur various costs. Participation understood in these terms indicates also employee share in the process of creating and exercising a specific impact on the operation of the enterprise (Dobrzański 2001, p. 267), inter alia through observing the principles of the Hazard Analysis Critical Control Points (HACCP) system, which is particularly important for product safety and health quality.

HACCP is a system used to identify, evaluate and control hazards relevant for food safety. What gains in importance in such circumstances is creating conditions for cooperation and involvement of people in the process. This means enhancing involvement of all employees, including management staff of food service establishments. This enhancement requires allowing for the competence of the people who have a direct contact with food, providing employees with supervision and training in accordance with the work they perform, as well as ensuring that all employees are aware of their role and responsibility with regard to performing HACCP-related activities. What is meant here is training on hygiene requirements and training on HACCP principles and their application. It is also important to draw on the instructions and procedures which identify employee tasks related to each Critical Control Point (Wiśniewska 2004, pp. 73-91).

Performing the personnel function, and particularly the employees recruitment process should be considered in the context of the situation on the labor market. It is in fact the case of the employer market and the employee market. On the former one, no significant difficulties with availability of employees to perform activities supporting the basic activity of the food service enterprise are noted. It is the employers that dictate employment conditions here and target their offer at the broad labor market to reach the maximum number of candidates. On the latter market, there are, however, certain difficulties in recruiting qualified employees in a given segment (that is, inter alia, the chef). Such persons usually have very high expectations of their employer. This is why it is important to provide them with attractive offers and influencing them to arouse their interest in working in the organization (Ochremiak 2014).

### **3. Realities of performing the personnel function in small food service enterprises – results of empirical research**

The research was conducted between January 2012 and March 2014 in sixteen food service establishments located in the Lower Silesian province. They include restaurants offering a full waiting service and specializing in national cuisines (i.e. Polish, French, Italian and Mediterranean ones). The organizational and legal status of the analyzed enterprises reveals the dominance of the economic entities which are sole entrepreneurs (62%) and partnerships (38%). The questionnaire survey method was used in the research process. The questionnaire was addressed to owners of small food service enterprises. The survey concerned the pursuit of the quality management process in the analyzed organizations. The most relevant questions linked to the examined relation between performing selected elements of the personnel function and activities connected with shaping food quality were selected for the purposes of this study. The survey questionnaire included open- and closed-ended questions. The majority of the closed-ended questions were presented in a tabular form as alternative questions: “yes/no” or a conjunction enabling a multiple choice of answers. The data were collected among a sample that was properly selected from the general population. The research sample was determined through purposeful selection. In order to generate this sample, one hundred and seventeen leading restaurants from the Lower Silesian market were selected. The return rate of the questionnaires equaled 13.7%.

Empirical research on the personal sphere of food service enterprises is a difficult task. It is noticeable that employers neither want to share information nor to verify their own and their employees’ knowledge. Owners of small establishments explain it with their fear of disseminating the results



of the questionnaire survey in spite of anonymity assurance, which does not facilitate conducting research in this area.

Table 1 presents the hierarchy of the values preferred by small food service establishments.

**Table 1.** The main values preferred by small food service establishments\*

No.	Specification	Percentage of answers indicated
1	Improving food quality would not be possible without qualified personnel	26%
2	Bond valuable employees to the enterprise for a long term	19%
3	Take care of the employer's good image on the local labor market	19%
4	Raise the personnel's awareness in terms of food safety	16%
5	Invest in employees	13%
6	Minimize labor costs	6%

\*Respondents could choose multiple answers, which is why the total does not equal 100.

As it can be seen, the personnel role in shaping quality is becoming more and more significant. This is proved by the management staff's statements that rank employees high in the process of improving food quality (26%). Nineteen percent of the management staff indicate that their efforts made to employ good personnel are usually linked to certain activities oriented towards supporting the process of developing the employer's positive image on the local market, which is reflected in the so-called personnel marketing. What is noticeable against this background is the concern declared by the management staff of food service establishments about bonding their key employees, i.e. the so-called core employees (i.a. chef, manager), with the enterprise (19%). At the same time, raising the personnel's awareness of food safety (16%) and investing in their development (13%) is becoming increasingly more significant. In such organizations, no attention is given to minimization of labor costs (6%). It should be also added that the statements recorded in these areas are in fact declaratory.

Seeking an answer to the question: "Does a specified set of principles and guidelines for managing the human potential of the examined enterprises facilitate shaping food quality?" was accompanied by investigating the aforementioned components of this function, such as recruiting, selecting, appraising, training, developing and remunerating employees. It is noticeable that the recruitment process in small food service establishments is carried out by owners themselves (88% of the indicated answers) or a person who is highly ranked by the owner in the process of appointing competent employees,



that is the chef (12%). The management staff are not willing to outsource tasks concerned with verifying personnel needs.

The results of the research indicate that the necessity to fill a new position in a small enterprise usually involves placing an announcement in the media (31%), mainly in online recruitment services and daily press (See Table 2).

**Table 2.** Which recruitment tools are applied in your enterprise to fill a vacancy when necessary?\*

No.	Specification	Percentage of indicated answers
1	Announcements in the media	31%
2	Personal contact	28%
3	Recommendations from employees	22%
4	Announcements at workplace	14%
5	Job assistance	6%

\*Respondents could choose multiple answers, which is why the total does not equal 100.

Simultaneously, free interviews with owners of small food service establishments reveal that these tools are used mainly for filling the position of the chef (i.e. due to his or her leading role in the quality shaping process). Therefore, the person to take this position is chosen more carefully. What is important here is the candidate's experience (measured by years of work and employment in renowned restaurants), culinary knowledge and skills, and ability to implement quality systems, as well as:

- self-organization competence (i.e. independence, time management, perfectionism, decision-making capacity, stress resistance),
- interpersonal competence (interpersonal communication, teamwork).

It should be also added that when it is necessary to fill non-core positions (e.g. a cook, serving staff), small enterprises use mainly personal contact (28%) and recommendations from employees (22%). These persons are employed even without any qualifications, and their skills are tested on the job, with careful execution of adaptation programs for new employees through extension of coaching. These employees are expected to present attitudes such as honesty, trust, subordination, as well as work involvement, ethical conduct and independence.

Table 3 presents selection tools applied in small food service establishments.

**Table 3.** Which selection tools are applied in your enterprise to choose the best candidate?\*

No.	Specification	Percentage of indicated answers
1	Job interview	34%
2	Analysis of documents (CV, covering letter)	26%
3	Work samples	26%
4	Knowledge tests	6%
5	Recommendations from others	6%
6	I do not apply any selection methods	3%

\*Respondents could choose multiple answers, which is why the total does not equal 100.

According to the management staff, an efficient tool that facilitates making decisions on employing the most competent employee is job interview (34% of answers indicated by the respondents) (See Table 3). Owners of a few of the researched enterprises, bearing in mind the significance of the human capital growth in the context of performing tasks connected with shaping food quality, included the direct involvement of the chef (12%) in the staff recruitment process. In the case of small enterprises, it is sometimes the case that no selection techniques are taken into account –owners employ anyone who wishes to work in their enterprise.

Employee appraisal is also among important elements of the personnel function. Appraisal facilitates identification of the desired attitudes, behaviors and performance, which foster improving the quality of the activities taken in the area of food production. They are applied in 94% of the analyzed food service establishments, mainly in the form of non-formalized appraisal, which is an element of employees' everyday work. A special emphasis is put on the informal appraisal performed by the owner (83%), appraisal meeting (12%) and appraisal by colleagues (3%).

Table 4 presents the major criteria for employee appraisal in the analyzed food service establishments.

**Table 4.** Which criteria are taken into account in your enterprise when appraising employees?\*

No.	Specification	% of answers
1	Accepting the values observed in the enterprise (involvement, diligence, perseverance and regularity, order)	25%
2	Quality of work (precision, careful implementation of the adopted procedures)	24%
4	Ability to work unsupervised and uncontrolled by superiors	14%
5	Interpersonal communication	10%
6	Compliance with hygiene requirements	10%

No.	Specification	% of answers
7	Ability to use the working time (minimizing losses, inter alia, of energy, materials, time)	10%
8	Ability to make decisions at work	8%

\*Respondents could choose multiple answers, which is why the total does not equal 100.

Due to employees giving much attention to executing specific food quality characteristics, the greatest significance is attributed to behavioral criteria, which refer to specific employee behaviors (i.e. involvement, regularity in performing activities (tasks), maintaining order in the workplace) (25%), and to effectiveness criteria (i.e. work quality) (24%).

Table 5 presents the main reasons for employee appraisal in small food service establishments.

**Table 5.** Do you appraise your employees in order to\*:

No.	Specification	Percentage of indicated answers
1	Increase their remuneration	30%
2	Know whom to dismiss	22%
3	Increase their motivation	22%
4	Encourage them to take care of shaping food quality	15%
5	Decrease their remuneration	7%
6	Know whom to train	4%

\*Respondents could choose multiple answers, which is why the total does not equal 100.

At the same time, 56% of the management staff declare that the appraisal approach applied in their enterprises entails activating employees to take actions in the quality area. Emphasis is put also on stimulating them to take actions exceeding the adopted standards through increasing attentiveness to good working ambience (30% of the indicated answers), using bonuses and allowances (22%), increasing employee remuneration (18%), ensuring employee development (13%), praising and recognizing (11%), and employing for an indefinite term (4%).

The interviews conducted with the enterprises' owners reveal that they do not attach much weight to the issue of recognizing employee expectations and preferences regarding their training or development. There are still considerable reserves in this area. It is worth bearing in mind that triggering them is not facilitated by the owners' fear of the risk involved in the first considerable "investment in a human". According to employers, taking relevant actions is too costly and comes down to organizing the training required by the law.

Therefore, a high rank is assigned to training which is related to implementing HACCP principles and which is oriented towards developing employee involvement in improving food quality, particularly food safety (88%). In these entities, much emphasis is put also on the on the job training run by the chef (coach) (88%), which consists in uncovering their potential, supporting their development and stimulating them to work “better” on a given position. Lower rank is assigned to external training (i.e. specialist courses), where only the best employees are delegated (44%). What is important is also job rotation, which consists in deploying employees anywhere in the enterprise (38%).

#### **4. Conclusion**

The operation methods of small food service enterprises show a mixed personnel policy model, which constitutes rather a non-intentional and unconscious compilation of the sieve and human capital models. Combining different behavior-related principles and guidelines for the personnel requires in particular taking into account two fundamental employee groups, i.e.:

- core employees (i.e. chefs), who are chosen more carefully, with associating the features of their potential with the features facilitating attentiveness to food quality in the spirit of the sieve model. After employing a person, emphasis is put on shaping his or her potential through investing in his or her development, including proper exploitation in the context of quality growth.
- non-core employees, i.e. cooks in relation to whom the constant “delaying tactics” can be seen (Stabryła 1996, p. 24). It is noticeable that there are employees recruited through “contacts”, which reduces the costs involved in recruiting them. It is remarkable that these persons are usually employed without any analysis of their qualifications and their skills are tested on the job. If the employee does not turn out to be successful “on the spot”, he or she is dismissed or redeployed. The personnel is trained to a limited extent only. Such a method is in fact counter-productive in terms of quality, it does not facilitate food quality growth.

Without questioning the fundamental influence of the employer and core employees on creating added value in the food service enterprise, it should be remembered that the quality culture requires involvement of all internal stakeholders. In the process of caring for food quality, the final result is determined by all its links, including supply. A success or failure usually results in attraction or irreversible loss of the customer-consumer. As the research suggests, it is difficult to attract people with the desired competence profile, even for the so-called peripheral positions (a cook, serving staff). In this respect, a special significance of good working ambience for accepting

the values observed in the examined enterprises and the quality of the work provided there is revealed. This should be borne in mind when expecting that employees will implement the adopted procedures with involvement, regularity and diligence.

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# ANALYZING BUSINESS MODEL COMPONENTS USING THE SENSITIVITY MODEL<sup>1</sup>

**Anna Ujwary-Gil<sup>2</sup>, Marina Candi<sup>3</sup>**

## **Abstract**

*The article deals with the business model and its components as well as the analysis of the relationships between these components using the sensitivity model. For this purpose we define the concept of a business model, paying special attention to its classification and components. Then we discuss the sensitivity model as a practical tool enabling us to define the problem and its elements, to analyze its impact and to explain the possibilities of influence. This research focuses on assessing the relative influence of business model components on each other, thus filling a gap in the literature having to do with the dynamic relationships between business model components.*

**Keywords:** *business model, business model components, sensitivity model, dynamic relationships.*

## **1. Introduction**

Much of the existing research on business models tends to view them as static phenomena that can be mapped (e.g. using the business model canvas proposed by Osterwalder and Pigneur, 2010), yielding depictions of fixed realities. Furthermore, given the prevalence of a component-based approach to business models, the notion that changing the contents of one component will impact other components is largely neglected. This research focuses on assessing the relative influence of business model components on each other, thus filling a gap in the literature having to do with the dynamic relationships between business model components.

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## 2. The business model and its components

In the literature, business models are generally viewed as a tool for describing the economic activities of a company or a vehicle for selling products or performing services. Various authors, in their research and interpretation of business models, point at their variety, especially as far as components of a model are concerned (Morris, et al., 2005), nevertheless, one of common features of the existing taxonomies is the so-called functional aspect directed at creating value for the producer, the customer and a company as a whole (Amit and Zott, 2001; Chesbrough, 2010; Osterwalder, et al., 2005; Teece, 2010).

According to Zott, Amit and Massa (2011) a business model is a new unit of analysis, different from a product, a company, an industry or a network. Although the model focuses on a company, it is wider, as it also comprises its business partners. A vital element of this approach is to explain to both how value is created. Another popular definition of a business model, offered by Johnson and his co-authors (2009) assumes that a business model consists of related elements, that is value propositions for a customer, a profit model, key resources and processes, which all contribute to creating and delivering value.

The multitude of definitions justifies the analysis of business models from determined perspectives, such as economic, operational or strategic ones (Morris et al., 2013). The decomposition of business models then refers to sub-processes related to creating value, profit in time and how a company defines its position in the market, its growth opportunities, choice of customers, or whether it differentiates its offering. Another division contrasts literature on business models from the perspective of e-business activities and strategies and management of innovations and technologies (Zott et al., 2011).

**Table 1.** Six key elements of a business model (Kujala et al., 2010)

Customers: Chesbrough and Rosenbloom (2002), Hedman and Kalling (2003), Magretta (2002), Morris et al. (2005) and Tinnila (2007)
Value proposition for the customer: Chesbrough and Rosenbloom, (2002), Magretta (2002), Morris et al. (2005) and Tinnila (2007)
Competitive strategy: Chesbrough and Rosenbloom (2002), Hedman and Kalling (2003), Morris et al. (2005), Tikkanen et al. (2005) and Siggelkow (2001)
Position in the value network: Chesbrough and Rosenbloom (2002), Hedman and Kalling (2003), Tikkanen et al. (2005) and Tinnila (2007)
Supplier's internal organization and its key capabilities: Normann (2001), Hedman and Kalling (2003), Morris et al. (2005) and Tikkanen et al. (2005)
Logic of revenue generation: Slywotsky et al. (1998), Chesbrough and Rosenbloom (2002), Hedman and Kalling (2003), Magretta (2002), Morris et al. (2005) and Tikkanen et al. (2005) and Tinnila (2007)



Business model components have been classified by a large number of authors. Zott, Amit and Massa (2011), when creating their classification, differentiated first-order and second-order themes among the components of e-business models. In another classification, proposed by Lambert (2012) the main elements of a business model are value proposition, value return, customer, channel, other entities, and value adding processes. Kujala et al. (2010) argue that attention should be paid to six key elements of a business model in project-oriented companies. See Table 1 below.

For the purpose of this analysis a business model is defined as a set of components and relationships between them, and various resources and activities used by an enterprise to generate a value proposition for customers. The configuration of these resources and activities makes up a business model. The taxonomy of adopted business model components includes the following:

*Content (the value proposition)*

*Structure, activities and processes*

*Human capital*

*Partners and channels*

*Customers*

The value proposition (or content) dominates as a key element of a business model next to clients, partners and channels. The above taxonomy also emphasizes human capital, understood as internal human resources, or broadly understood staff (Nielsen, Montemari, 2012). A vital element of a business model is its structure, activities and processes stressing the functional aspect of activities taken in a given business model and the way a company is organized.

### **3. Research question and methodology**

The fundamental research problem was to try to determine how the components of business models influence each other. In answering such a question we have the opportunity to discuss the overall dynamics in business models. Within the concept of a company's business model, we used the sensitivity model (Vester, 2012) in order to identify key components allowing us to control and manage a business model, simultaneously indicating its most important and influential components. The choice of case studies for our research was purposeful. We studied three companies, referred to with the pseudonyms X, Y and Z.

Our goal was not to compare companies and their business models, taking into consideration the differentiated nature of identified components of a business model, although admittedly, such an analysis would be desirable.

However this would require developing research focused on standardizing identified components of business models across multiple cases. In this research we gave our respondents freedom to identify elements which are of key significance in their business model. Table 3 presents the business model components identified by case company respondents.

### *Sensitivity model*

This stage of analysis consists of self-assessment of a company related to identified components of a business model. In order to achieve this, we needed to build a matrix of the levels of influence between the business model components, whose weights will allow us to rank components as influential and less influential in the context of their influence on how a business model functions. Using influence matrixes (Vester, 2012; Ujwary-Gil, 2012) it was possible to determine the strengths of relationship. For the purpose of our research, the assessment was expressed on a three-degree scale, where 0 denotes lack of influence, 1 denotes weak influence and 2 denotes strong influence. Summing up all influences of a given business model component we obtain its active sum, that is the force with which it influences other components, as well as its passive sum – the force with which other components affect it. Using Vester’s model in analyzing influences between particular components of a business model expressed on a three-degree scale, we developed a portfolio matrix of components and determined relationships between components. Table 2 below presents the starting point for the analysis by means of the influence matrix.

**Table 2.** Influences between components of a business model

What influence does x have on y?	Component <sub>1</sub>	Component <sub>2</sub>	Component <sub>3</sub>	Component <sub>4</sub>	Component <sub>5</sub>	Component <sub>n</sub>	Active sum
Component <sub>1</sub>							
Component <sub>2</sub>							
Component <sub>3</sub>							
Component <sub>4</sub>							
Component <sub>5</sub>							
Component <sub>n</sub>							
<b>Passive sum</b>							

The measure of the influence exerted by a particular component on the system (here, a business model) is the so-called active sum determined as a sum of the line devoted to this component. The higher the value of active sum, the greater the influence of the component on other components of the business model. The measure of the influence of the components of business

model on a given component is the so-called passive sum, being the sum of points in a column referring to this factor. The higher the value of passive sum, the greater the influence exerted on the component. Having transferred the scores onto the map of influence intensity, we obtain a portfolio consisting of four groups of components of a business model (Figure 1). The variation ranges of active and passive sums should be plotted onto the co-ordinate system, where the Y-axis represents active sum, whereas the X-axis shows passive sum. Such matrix, in form of a portfolio, allows us to divide particular groups of business model components into:

Active sum (exerting influence)	<p><b>Active components</b> (exerting strong influence, not susceptible to external influence)</p>	<p><b>Critical components</b> (exerting strong influence, susceptible to external influence)</p>
	<p><b>Marginal components</b> (exerting slight influence, not susceptible to external influence)</p>	<p><b>Passive components</b> (exerting slight influence, susceptible to external influence)</p>
	Passive sum (susceptible to influence)	

**Figure 1.** Portfolio of business model components

We are looking at the influence the components of the business model exert on each other, however the business model itself is just the sum of its components. In order to do so we must determine the so-called quotient and product. The quotient is a measure of a relation between the power of influence exerted by a given component on a business model, calculated by multiplying the active sum determined for a given component by 100 and then dividing the result by the passive sum of this component. The product, on the other hand, is a measure of significance that a given component has in a business model. In order to calculate it for a given component, we must multiply its active sum by its passive sum. High value of the product of a particular component informs us that it is significant for the model, and the other way round.

#### 4. Data analysis

Three companies took part in our research, their components (resources and activities) are listed below:

**Table 3.** Taxonomy of business model components

<b>Companies Business model components</b>	<b>X</b>	<b>Y</b>	<b>Z</b>
Content (what is the value proposition)	Product and service sales Direct sales	Design concept	Design Intellectual property
Structure, activities and processes	R&D	Co-creation Used-based research Office Equipment	Personal meetings Project acquisition Emails/telephones
Partners and channels	Personal contacts Investors Non-technical universities Freelancers Technical universities Hardware suppliers	Industry partners Networking Social capital Producers	Other professionals
Customers	Education and public Universities Technical universities	Large businesses City/community	Public sector customers Private sector customers Users
Human capital	Corporate Staff		Human resources

Particular components of a business model were then subjected to evaluation. A vital element of the research was to identify the power of influence exerted by a given component (resource) on other elements in the matrix. The outcomes of influences between business model components, together with calculated scores of active and passive sums as well as their positioning in particular portfolio squares are shown in Tables 4 and 5 below.

Having established the power of influence exerted on particular components, we need to analyze the influence exerted by other components.. In this case we need to focus on the active sum determined as a sum of points from a particular line devoted to a given component. The higher the value of active sum, the stronger the influence exerted by a component on other components.. The measure of the influence exerted by other components on a particular component is the passive sum, calculated as the sum of points in a column corresponding to a particular component. The higher the value of the passive sum, the stronger the influence exerted on it by other components. Table 5 presents a defined matrix of components. In companies X and Z we have not identified any active components. In case of company Y these are producers. In company X the critical components are: R&D, product & service, sales, personal contacts, staff, direct sales, corporate, education & public. For company Y, these are: industry partners, design concept, user-based research, human capital, social capital, co-creation, networking, office, large businesses, city/community, while for company Z: other professionals,

design, public sector customers, human resources. Apart from the fact that these components strongly affect other components, they are also considerably susceptible to influence from other components, which means a risk of uncontrolled feedback. Passive components do not have much influence on other components while being highly susceptible to influence from other components. Our analysis conducted in company X revealed that these are investors, while in company Z they are project acquisition and personal meetings. Characteristic features of marginal components are small influence on other components and low susceptibility to influence from other components. These are: technical university, hardware suppliers, freelancers, universities in company X, equipment in company Y and users, private sector customers, emails/telephone, intellectual property in company Z.

Table 6 presents calculations of the product and the quotient for particular groups of components. The calculations included in the table demonstrate that components of company X, such as technical university, investors, R&D, freelancers, and education & public influence other components more than they are influenced. For company Y these are: to user-based research, networking, large businesses and city/community, while for company Z, components in this group are users, other professional, design, project acquisition and personal meetings. The product is a measure of significance of components for the model.

**Table 4.** Profiles of components forming the active and passive sums

Components of business model	X			Y			Z		
	LJ	HI	PS	LJ	HI	PS	LJ	HI	PS
technical university	5			10			10		
hardware suppliers	1				18			18	
Investors		12	8		18	18		18	18
R&D		16	14		15	13		11	6
product & service sales		18	20		19	21		10	12
personal contacts		13	15		9	10		9	9
Staff		14	14					9	9
Freelancers	10		5		15	18		13	10
direct sales		13	13		15	17		4	10
Corporate		12	16		19	16		4	11
education & public		15	14		11	12		4	7
Universities	10		10		20	16			
					19	15			

X, Y, Z = companies. SA = active sum. SP = passive sum. LJ = low influence. HI = high influence.

**Table 5.** Portfolio of components

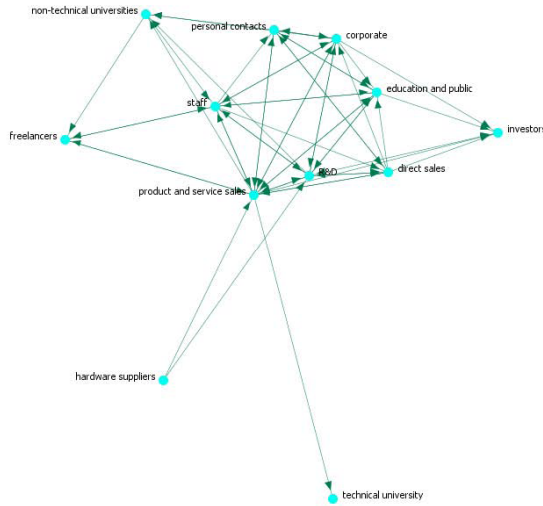
X	Y	Z
<p><b>Active components:</b> R&amp;D, product &amp; service sales, personal contacts, staff, direct sales, corporate, education &amp; public</p>	<p><b>Critical components:</b> industry partners, design concept, user-based research, human capital, social capital, co-creation, networking, large businesses, city/community</p>	<p><b>Critical components:</b> other professionals, design, public sector customers, human resources</p>
<p><b>Marginal components:</b> investors technical university, hardware suppliers, freelancers, universities</p>	<p><b>Active components:</b> producers</p>	<p><b>Active components:</b> users, private sector customers, emails / telephone, intellectual property</p>
<p><b>Passive components:</b> investors</p>	<p><b>Passive components:</b> equipment</p>	<p><b>Passive components:</b> project acquisition, personal meetings</p>

X, Y, Z = companies.





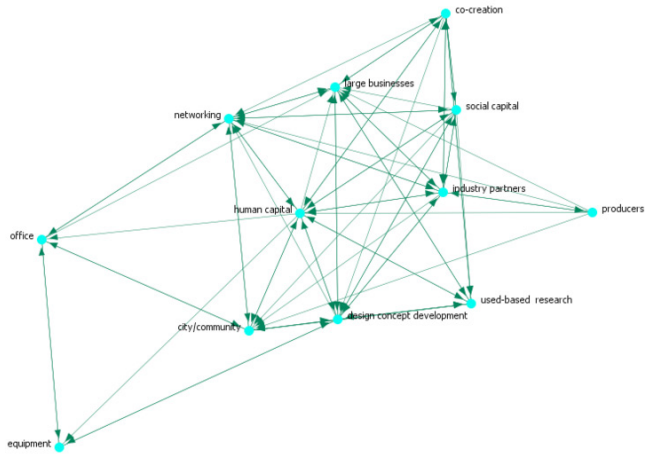
In order to better depict the links between the business model components of particular companies, we used a network of links with strong impact (2.0 weight). The network presentation of the business model components allows us to depict which components influence each other and what the direction of the links is, that is whether they are the so-called out-links or in-links.



**Figure 2.** Visual presentation of the components of company X.

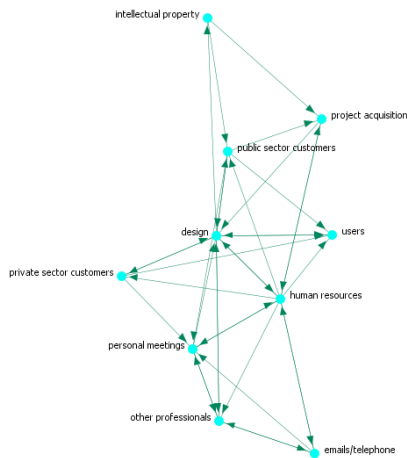
Most components in Figure 2 are characterized by mutual influence. The only exception is that of freelancers, who are mutually linked only with staff, product & service sales and universities. Similarly, hardware does not exert substantial influence on other components, here we notice relations with product & service sales and R&D. On the other hand, technical university strongly influences product & service sales and vice versa.

Visual presentation of the business model components of company Y (Figure 3) shows that the most influential components (strongly affecting others) are: large businesses, networking, industry partners, as well as human capital. Equipment and office are seen as less influential on other components.



**Figure 3.** Visual presentation of the components of company Y

The network of links among the business model components of company Z is characterized by strong influence of design, human resources and personal meetings on other components of the model. Peripheral components (with weaker influence) are intellectual property and emails/telephone (tool).



**Figure 4.** Visual presentation of the components of company Z

## 5. Conclusion

The main purpose of this research was to identify the most influential components of particular business models. The method applied here was to pin-point components, which should be of primary focus to management staff. The ideal, typical control components are those that have the highest and most immediate impact on all other components but are not strongly influenced by other components. In addition, these components should be rather stable, which means that they are not easily changeable by system dynamics but can be controlled by management (Kasztler, Leitner, 2009). From the first perspective it seems that the scores differ. In the sensitivity method in the business model of company X there is no most influential component (the quarter with active components is empty). An influential (but susceptible to external influence) component is product & service sales. Simultaneously, freelancers are the most influential component for the business model (its quotient exceeds 200). The most significant component is product & service sales (360 points). In company Y, the most influential components are producers, city/community and human capital, whereas in company Z private sector customers and design.

It still remains a challenge to measure and manage the dynamics of (non-tangible) resources, to examine how these resources are reciprocally related and how a change in one resource causes changes in another resource, leading to changes in the whole business model of a company. Moreover, an interesting area of research would be an attempt at not assessing the company value but assessing the value of the business model itself. This is an even more daunting task, as one company may have a number of business models (Linder, et al., 2001, Smith et al., 2010, van der Meer, 2007) with different values. The valuation of business models and their dynamics may improve and significantly influence the assessment of the company value.

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# MULTICRITERIAL EVALUATION OF APPLYING JAPANESE MANAGEMENT CONCEPTS, METHODS AND TECHNIQUES

**Mateusz Podobinski<sup>1</sup>**

## **Abstract**

*Japanese management concepts, methods and techniques refer to work organization and improvements to companies' functioning. They appear in numerous Polish companies, especially in the manufacturing ones. Cultural differences are a major impediment in their implementation. Nevertheless, the advantages of using Japanese management concepts, methods and techniques motivate the management to implement them in the company. The author shows research results, which refer to advantages and disadvantages of using Japanese management concepts, methods and techniques in a Polish productive company in Dolnośląskie Province. There still remains the question of which evaluation criteria can be used to assess the use of Japanese management concepts, methods and techniques. The author shows six criteria. The article presents the scoring method of evaluating the Japanese management concepts, methods, techniques, which are based on presented criteria.*

**Keywords:** *Japanese management concepts, methods, techniques, evaluation criteria, scoring method of evaluation*

## **1. Introduction**

Japanese management concepts, methods and techniques are connected with the history of shaping the management system in the Toyota company after WW II. E. Toyota and T. Ohno began to think about the reduction of waste in Ford factories. The process lasted over twenty years (Nogalski, 2010, p. 300). Executive staff of organizations from different countries, acknowledging the success achieved by the discussed car-manufacturing corporation, are deciding to implement the new management tools<sup>2</sup>. However, culture considerations appear to be a big impediment. Culture is a set of norms and values passed down from one generation to another by means of religion, art, literature and other

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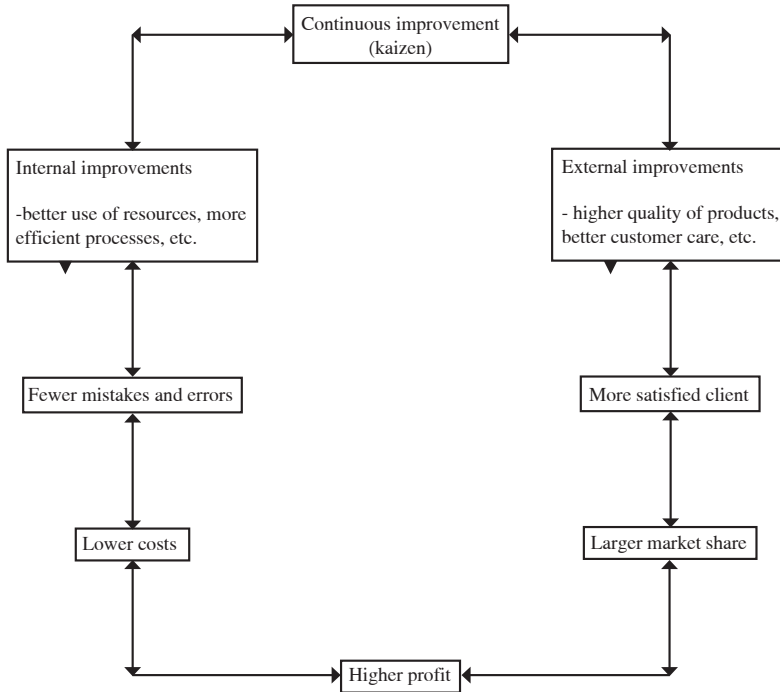
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<sup>2</sup> Management tools include the concept (philosophy), methods, techniques (practices). This division has been presented in: (J. Skalik, G. Belz, 2011, p.104). The term management tools will be used interchangeably with the notions: concepts, methods, techniques.

symbols (Prymon, 2010, pp. 85-87). The Japanese culture has its reflection in the managerial concepts, methods and techniques under discussion. Despite the obstacles, more and more organizations are deciding to implement or improve Japanese management concepts, methods and techniques. It results from the consequences of using the management tools which are mentioned in the second and third point of the article. Recent years have shown a trend to introduce lean management in Polish firms. What is worth pointing out are the evaluation criteria for applying Japanese management tools. The aim of the article is to present selected evaluation criteria for Japanese management concepts, methods and techniques. The author has suggested that the scoring method of evaluation of those criteria should be used. The article consists of six points. First, reasons and results of applying Japanese management concepts, methods and techniques are shown. The next point covers the overview of the six criteria used for evaluating operations, as well as a short characteristic of each. Point number five presents the scoring method of evaluation of Japanese management concepts, methods and techniques based on the criteria shown in the article. The article ends with conclusions and bibliography.

## **2. The reasons for implementing Japanese management concepts, methods and techniques**

Japanese management concepts, methods and techniques refer to organizing and optimizing processes in a company. They are not only used to improve production processes but also the office and service-related ones (Locher, 2012, p. 12). Although they have been known for a long time and they have been the subject of many publications, they are still an important and vital issue. Organizations decide to implement the presented tools for various reasons. Examples may include product quality enhancement, fewer machine failures, fewer faulty products, increase in efficiency. The above are just a few of the effects which can influence an increased company profit by external or internal factors. It is illustrated in figure 1, which refers to the effects of applying the kaizen concept.



**Figure 1.** Effects of using the kaizen concept

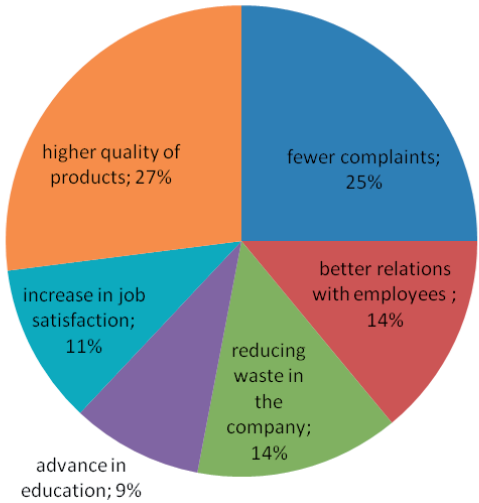
Source: Author's own work based on: Jens et al. (2004), p.47.

Figure 1 refers to the effects of using the kaizen concept. Besides that, the kaizen concept encompasses other methods and techniques, e.g. TQM (Total Quality Management), which constitutes an integral part of kaizen (Stańczyk-Hugiet, et al., 2011, p.118). Thus, the effects shown in Figure 1 may also concern other Japanese management tools. The improvements and their effects result in higher profit. It can be achieved by increased revenue or curbed costs, which is presented in Figure 1. However, is profit maximization the only aim of an organization? Is this the only reason why companies should decide to implement the Japanese management concepts, methods and techniques?

### **3. Aims of an organization and the effects of using Japanese management tools in the light of empirical research**

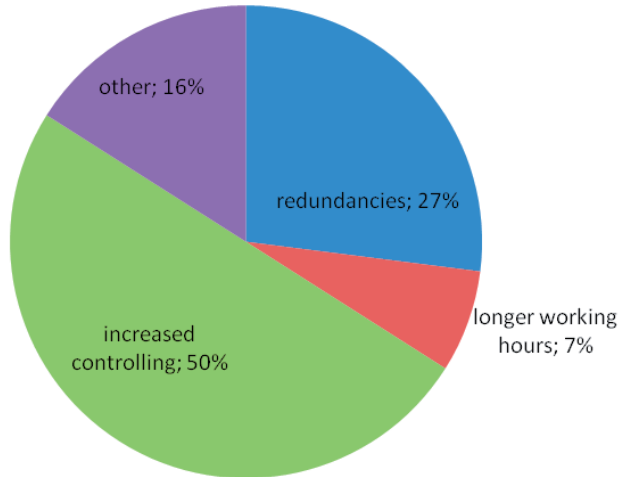
Each organization has its aims. An aim can be defined as a situation which a company is trying to reach. Aims can be divided into strategic, tactical, operational, as well as market-related, social, financial or efficiency ones. The division depends on the criterion applied (Strużyński, 2002, p. 110). According

to the author, however, two fundamental aims can be differentiated, namely: profit maximization and continuity in time. The former is necessary for a company to develop. When companies have higher profits, they can invest more in e.g. machinery, or increase employment or build new production facilities. This, in turn, may lead to increasing market share and cutting costs, examples of which are multiple. The latter aim of each company, as mentioned by the author, is its continuity in time. Organizations may occasionally not report a profit in an accounting year. It may happen that a company has a loss in one or more years. Such a situation may be caused by economic recession or other external factors which a business cannot directly control. However, it does not mean that a company has to go into liquidation, as it can have a profit in the following year. The important issue is to continue operations and survive despite a difficult situation in the market. The above-mentioned aims can be influenced by Japanese management tools. The application of Japanese concepts, methods and techniques forces both positive and negative changes in an organization, which is shown in Figures 2 and 3 presented below.



**Figure 2.** The effect of applying Japanese concepts, methods and techniques in a Polish manufacturing company





**Figure 3.** Negative effect of applying Japanese concepts, methods and techniques in a Polish manufacturing company

The conclusions of the author's research<sup>3</sup> carried out in 2012 in a Polish manufacturing company within the automotive industry indicate that positive effects of applying Japanese management tools include the following: higher quality of products (27%), fewer complaints (25%), better relations with employees (14%), reducing waste (14%), increase in job satisfaction (11%), increase in education (9%). The application of Japanese management concepts, methods and techniques should result in increased commitment of all employees. Therefore the company has witnessed enhanced cooperation between employees (better relations). Continuous improvement causes reduction in waste, which may be effective in terms of better product quality. Enhanced product quality means fewer complaints and higher customer satisfaction, which eventually can improve the company image.

The author's observations and his contacts with lean management coordinators<sup>4</sup> in different Polish organizations prove that not only internal trainings, but also external ones are of big importance. Trainings and workshops are devised to advance the understanding of management tools applied by the companies. As a result, employees increase their knowledge base (advance in

<sup>3</sup> The research method used was a survey carried out with 50 factory workers and office workers on different positions and shifts

<sup>4</sup> Lean management coordinator is a person who is responsible for lean management implementation in a company, aims at creating the right organizational structure supporting lean management and provides an appropriate communication process.

education (9%)), which in turn has an impact on better work performance, and thus on job satisfaction (11%).

However, the same empirical research conducted by the author shows that negative effects of the management concepts, methods and techniques under discussion include the following: increased controlling (50%), staff redundancies (27%), other factors (6%) and longer working hours (7%). Increased controlling results from professional improvement and PDCA cycle. If one wants to improve a process, they need to control its path. Therefore, after detecting failures it is possible to introduce counter-measures in order to increase the efficiency of the process (J. Liker, J. Franz, 2013, p. 59-62). As far as redundancy is concerned, it appears when the implementation of the Japanese management tools is defective. As it is shown in Figure 1, internal improvements are limited by costs. If a process can be done by four employees instead of five because of an improvement, the remaining employee should be moved to another department. He or she should not be laid off in order to reduce costs. It is a mistake in the implementation of Japanese management concepts, methods and techniques.

This is one of the reasons why it is so difficult for many companies to successfully implement the lean management concept. A study from 2007 shows that only 2% of organizations had managed to succeed in implementing the lean concept (Liker, Franz, 2013, p. 43). When staff are being made redundant, they become reluctant to changes because they are afraid of losing their jobs.

#### **4. The criteria for evaluating activities**

In management as an academic subject attempts are being made to determine certain universal criteria which can be used to evaluate activities or results. In his academic textbook, M. Przybyła specified six universal criteria for assessment (Przybyła, 2003, pp. 40-44):

- 1) Teleological
- 2) Praxeological
- 3) Esthetic
- 4) Hedonic
- 5) Economical
- 6) Ethical

Theological criteria consider an activity in terms of achieving its aim or not. They do not take into account any costs which are incurred when the activity is being put in practice. Praxeological criteria focus on such categories as: cleanliness, simplicity, precision. It can be exemplified by the 5S technique involving one's workstation which should be clean, all the necessary things

should be placed in a designated place, etc. Esthetic criteria refer to beauty, i.e. to whether a given product looks good. Hedonic criteria concern having pleasure in doing an activity; whether processes conducted by an employee give them satisfaction, pleasure or joy. Economic criteria are similar to teleological ones. Economic criteria in evaluating an activity or process draw attention to costs and this is the most fundamental difference from teleological criteria. Economic criteria are further divided into economicality and usefulness. Economicality is the relation of useful result to cost utilized for this activity. It should be larger than 1. For instance, let us consider the process of product development. In this process, sales revenue from the product is 10.000 and costs related to the product development are 7000. Let us place it into the formula.

$$E=10000/7000=1.43$$

Clearly, the activity is economical. The other category is that of usefulness. It is the difference between useful result and cost. The result has to be bigger than zero for the activity to be considered useful. Following the previous example, after having placed figures into the formula we obtain:

$$K=10000-7000=3000$$

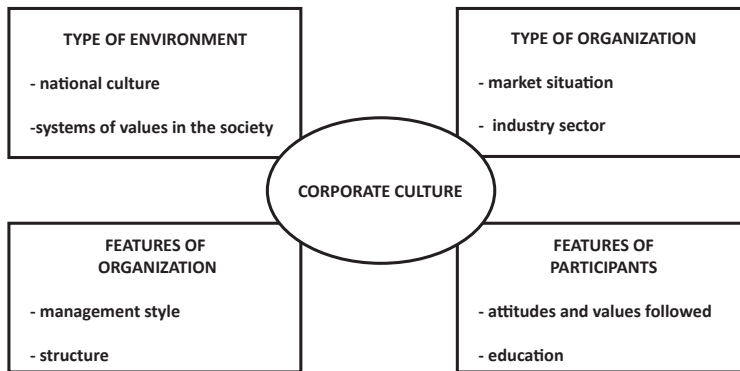
Subsequently:

$$3000>0$$

Hence, the activity is useful.

Economical criteria can be expressed in numerical terms. Therefore, they are mutually comparable (Przybyła, 2003, p. 40-44). Referring to the previous issue of this paper, one of the fundamental aims of a company is profit maximization. Japanese management concepts, methods and techniques streamline processes in an organization, thereby allowing profit to increase. The correlation can also be tested through economical<sup>5</sup> criteria, i.e. economicality and usefulness. Additionally, it is related to the profit and loss account of an organization, where revenue and costs of operational (core) activity are entered. However, there appears a problem in the case of qualitative criteria, which include, inter alia, ethical criteria related to values and norms followed by the people in a given community, country or region (Przybyła, 2003, p. 44). Japanese tools are ‘deeply rooted’ in the national culture, the Japanese one. National culture has an impact on organizational culture, which is shown in Figure 4. Norms and values characteristic for this culture are: collective acting, long-term orientation, self-discipline, improvement, distance of authority, external control (Kraśiński, 2014, pp. 88-90).

<sup>5</sup> Economical criteria are quantitative ones, i.e. they can be expressed with numbers



**Figure 4.** Chosen determinants of corporate culture

Source: Author's own work based on Przybyła (2003), p. 294.

The author's conclusions drawn from observations as well as contacts with persons representing different organizations indicate that companies implementing and using Japanese management concepts, methods and techniques are primarily interested in economical criteria. The remaining criteria, however, are also applied.

### **5. Scoring method of evaluation of applying Japanese management concepts, methods and techniques, on the basis of activities evaluation criteria.**

Japanese management concepts, methods and techniques include, inter alia, lean management, kaizen, Just in Time, Hoshin kanri, Total Quality Management, 5S, Total Productive Maintenance. Particular methods and techniques are part of a concept. For example, the kaizen concept includes: Just in Time, 5S, kanban. Yet, is it possible to use the activity evaluation criteria described in point 4 of this paper for evaluating the application of presented hereby management concepts, methods and techniques? According to the author it is possible, as shown in Table 1.

It is a template table prepared for a production department. It consists of activity evaluation criteria and components characterizing these criteria. The components of the criteria are related to characteristics of the six criteria shown in point 4.6 Particular criteria can be applied to evaluation of management

<sup>6</sup> Teleological criteria consider an activity in terms of its aim. In a production department an aim can be to reduce the retooling time by 10% (a criterion component). Praxeological criteria refer to cleanliness, precision and simplicity of operations. Therefore, cleanliness of workstation can constitute a component of this criterion. Other components are specified in the same manner. The examples are specific for a manufacturing department.

concepts, methods and techniques. The author suggested the scoring method, which differentiates between weights and evaluation referring to particular management concepts, methods and techniques. This method can be used in various company departments applying the management tools under discussion, e.g. in production, logistics, or IT. The weights denote the importance of particular components and criteria, whereas the evaluation indicates the degree to which components have been done in a certain department or the whole company. Both weights and evaluations are multiplied, which gives the score (“total score” position). The maximum score for each component is 15 points. The score for a whole criterion equals the sum of component points in a given criterion divided by the number of components. Owing to this chart, one can see which criterion has the highest score. However, the management should thoroughly analyze the criteria with the lowest scores. It signals which areas need improvements and calls for considering reasons for such a state of affairs. Special attention should be paid to components of weight 3 (the highest) and evaluation 0 (the lowest). This means that the component is a very important one, but inappropriate (or none) means of implementation have been chosen, whereby the needed effects have not been achieved. One example from the table is shortening the time taken for machines instrument turnover by 10%.

**Table 1.** Template table for scoring evaluation of applying Japanese management concepts, methods and techniques for a production department, based on activity evaluation criteria.

Criteria	Components of criteria	Weight (1 to 3)	Evaluation (0 to 5)	Total score
Teleological	Shortening the time taken for retooling machines by 10%.	3	0	4,5 0
	Decreasing the number of faulty elements	3	3	6
	Decreasing the product unit cost by 3%	3	1	3
Praxeological				5
	Clean workplace	1	0	0
	Precision of product workmanship	3	3	9
Esthetic	Simplicity of workmanship	2	3	6
				1
Hedonic	Nice workplace	1	1	1
				9
Economical	Pleasure of doing the job	3	3	9
				4,5
	Economicality	3	2	6
Ethical	Usefulness	3	1	3
				2
	Team (collective) work	1	2	2
	Long-term approach	1	2	2

Components of the criteria used in Table 1 may vary depending on the department and may carry different weights. As mentioned before, it is advisable to pay close attention to those criteria and their components which achieve the lowest score. It is crucial to consider their possible causes and take action to improve or eradicate them, which is the core of Japanese management tools<sup>7</sup>. In the author's opinion, such an evaluation of using Japanese management concepts, methods and techniques in terms of presented criteria is worth being carried out. It is a simple and quick method.

## 7. Conclusion

The aim of this paper has been to present selected evaluation criteria of applying Japanese management concepts, methods and techniques.

The author has provided six criteria which can be used to evaluate the application of Japanese management concepts, methods and techniques. The paper proceeds to discuss the scoring evaluation of Japanese management concepts, methods and techniques. The evaluation consists of six criteria which are further subdivided into criteria components. This method expresses particular criteria in the quantitative way (as points scored). Based on the resulting figure and given weights, one can pinpoint those components of a criterion which needs improving. The type and amount of particular criterion components may differ. It all depends on the company profile and department. Still, the number of criteria applied should remain constant. The method is universal, meaning that it can be applied in various organizations. The activity evaluation criteria can be used for evaluating Japanese management concepts, methods and techniques.

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<sup>7</sup> Kaizen means continuous improvement, while the PDCA cycle (Plan, Do, Check, Act) refers to improving and eradicating of causes.

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# LABOR QUALITY IN AN ENTERPRISE AS A SUBJECT OF RESEARCH

**Mariusz Wyrostek<sup>1</sup>**

**Abstract:**

*Labor which has been evolving together with a human being since the dawn of time very often becomes highly organized, e.g. in form of an enterprise. One of the enterprise theories refers to its resources and the way they are used. Concentrating on these issues, I am enabled to examine the labor quality as a set of skills and competences realized by a human within the organization.*

**Key words:** *resource-based view on enterprises, labor quality.*

## 1. Introduction

During the current phase of business development, the most important stakeholders of each enterprise become its owners and customers. Thanks to the market confrontation of their needs and abilities, new enterprises emerge and function. An enterprise becomes an organization of certain material and non-material resources and skills which allow to achieve common goals with the widely understood labor processes. This way, the enterprise managers and employees join the circle of the stakeholders mentioned above. By bringing their expertise, abilities and skills to the enterprise, they create one of its most important resources – human ones.

Enterprise theories try to explain the nature of resources in various ways. One of the theories deals with the aforementioned resources and processes and with the way they are organized. It seems to be particularly focused on the labor, emphasizing the role and importance of human skills and competences.

The purpose of this study is to consider the labor quality as an important specificity of using the enterprise resources. The reflections shall be used as a starting point for further research and to create a theoretical model of labor quality determinants which in turn shall provide basis for further empirical research.

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## 2. Resource-based view on enterprises

One of the main axes of enterprise development theory is the resource-based view. It indicates that the nature and power of an enterprise lie in the typical, common-sense factors such as the technological potential, human knowledge or management techniques improvement (Noga, 2011, pp. 176-177) – both in the resources and competences of the organization.

The origins of this theory may be detected as early as in the opinions of the economy science precursors. In his review of the economic thought achievements, one of the authors (Kunasz 2006) observes that the notion of resources (production factors) appeared in the classic economists' thought. This author emphasizes that even William Petty enumerated four factors of wealth: labor, land, professional qualifications and other resources which make labor more efficient. He also states that Adam Smith indicated that labor and land are the main production factors together with the capital. David Ricardo in turn, as the aforementioned author notices, in his labor-based view explains the goods value changes with technical progress leading to the labor efficiency increase. Then, he cites Jean-Baptiste Say who rejected some theses of Smith or Ricardo but rated labor, land and capital among the value-making factors. Additionally, he extended the notion of production labor and paid special attention to the role of an entrepreneur of particular organizational and managerial capabilities. Then, he refers to Karl Marx who belied labor was the only source of value increase and treated capital as a particular form of "objectified labor". He also differentiated between labor force and labor. Product value of the former – potential ability to labor (the object of transaction) is determined by the labor period necessary to regenerate it (support of the laborer and his family). He notices that Alfred Marshall, creator of the neoclassical school, increased importance of enterprise. Thanks to it, an entrepreneur makes the production organized correctly by combining the production factors and using the existing conditions. As the referenced author indicates, Joseph Schumpeter treated innovations as combinations of various material elements and human productive force. Innovations understood this way become, by increasing effectiveness of the resources used, a basis for achieving competitive advantage by the enterprise. However, he claims that Edith Penrose avoided the notion of "production factors" and treated enterprises as a unique collection of production resources (Kunasz, 2006, pp. 34-38). Nevertheless, it is assumed that the proper shaping and development of the resource-based view on enterprises took place in the 1980s and 1990s (Lichtarski, 2003, p. 37; Ujwary-Gil, 2009).

The contemporary resource-based view on enterprises is a result of discussions based on three, seemingly different, issues: outstanding

competences, Ricardian economics and enterprise increase. At first, the research on competences dealt with the managers' impact onto the enterprise results and then, through the social competence, they evolved towards the institutional leader. From the Ricardian economics, dealing with but not limited to land management (a perfectly non-flexible factor), a theory of resources as a source of economic rent is drawn. The enterprise increase theory contributes with perceiving the organization as a structure which combines and coordinates the activities of employees, as well as other resources. The production capacities of resources are among the factors which restrict the enterprise increase (Czerniachowicz, 2012, pp. 102-103).

The enterprise efficiency and effectiveness are determined by its resources and the capabilities of using them. *Resources* are, in other words, production factors owned or controlled by an organization; with the use of other resources or skills, they are transformed into final products (Lichtarski, 2003, p. 38). Thus, not only the resources owned by the enterprise count – all other resources which are at its disposal are also important (Czerniachowicz, 2012 p. 102). Resources are classified according to various criteria; the most common classification differentiates between material and non-material resources. It must be emphasized that the very common classification into material and non-material resources, although it helps to achieve good results, it also brings a lot of troubles, too. They arise from ambiguity in classifying various resources and their groups into the two categories. The most extreme example of this seem to be human resources which are assigned to one group or another <sup>2</sup>.

*The skills* are abilities to use resources, that is to deploy and use them so that the enterprise's aims are achieved. These are indirect goods created by the enterprise for more effective use of the resources owned. By frequent links to knowledge, and similarly to it, the skills are of hidden character. Unlike the material resources, skills increase while being used. One of the authors divides skills into competences and key competences. *The Competences* are the skills which relate to the business branch while the *key competences* are those which are of the greatest importance for the company and are decisive for its competitive advantage (Lichtarski, 2003, p. 38). However, from the enterprise's values perspective, its resources make a certain hierarchy. The lowest in the hierarchy are resources.

The above implies that not all the resources are equally important for the competitive results achieved by the enterprise. The resources and skills which are particularly valuable for the enterprise build its key competences. They are of some important distinctive features (Czerniachowicz, 2012 p. 105; Lichtarski, 2003, p. 38-39; Ujwary-Gil, 2009):

<sup>2</sup> Cf. (Kunasz, 2006, p. 40) and (Noga, 2011, p. 177; Ujwary-Gil, 2009).

- strategic value – they allow for making good use of chances and overcoming hazards,
- they are rarely owned by competing businesses – the rarer they are the higher strategic advantage of the enterprise is,
- difficulties with substituting which prevents some resources from being replaced with other ones and this way they remain rare,
- difficulties with imitating and copying which is now a quick and easy way to achieve high profits but this can be prevented by the use of secret resources and competences,
- complementarity – the more the resource is connected with other resources, the more difficult it is to imitate,
- ability to introduce changes which allows to modify and improve the present resources and skills and this way, increase the distance from possible imitators,
- durability understood as a consequence of the features mentioned above, i.e. length of time throughout which the resource support the enterprise in achieving income.

The features mentioned above seem to suit best the non-material resources, as well as skills and competences of the enterprise. This matches the theory analyzed here which emphasizes that material resources are not decisive for the competitive advantage as they are easily imitable and immobile (Hall, 1992, quoted after: Ujwary-Gil, 2009). Thus, these are the non-material resources which are believed to be the main source and power increasing competitiveness of an organization. The characteristics which make them distinguishable include but are not limited to the ability of simultaneous and multiple use, long time of accumulation, increase of value throughout the period of use, carrying out by people (Obłój, 2001, p. 222).

In the resource view, it is indicated that only the enterprises whose managers are able to create unique combinations of material and human resources remain in the market (Noga, 2011, pp.177-178). In this context, people are not a resource itself but rather carriers of resources. This also seems to explain the terminological evolution towards human capital (Ujwary-Gil, 2009) and further, towards intellectual capital of an organization. The conditions necessary for forming key competences and developing human capital in an enterprise are: advantage in innovations and knowledge, unique organizational culture and relatively durable customer relations, both on the buyers' and suppliers' side. In many enterprises, development is equated with development of knowledge making up the intellectual capital contributed to the organization by various stakeholder groups (Noga, 2011, pp. 92-101). An analysis of operation of various enterprises, of various countries and branches, which have been in good condition for over a hundred years, revealed that their common feature is specific approach to the employees. They are treated as the

main source of the enterprise success. These organizations are more likely to sell off fixed assets in reaction to changing market environment than to dismiss employees – their philosophy is to create a community based on the expertise of several generations. It must be noticed that not all the stakeholders bring intellectual capital to the enterprise but only those whose activity contributes to creating new values, bringing measurable market benefits (new products, organizational solutions, quality), (Lichtarski, 2003, pp. 130-131).

The source of competitive advantage is in rare resources and/or skills to use them more effectively. This is a wider look at effectiveness, involving more economical production or better fulfillment of customers' needs. Thus, this refers equally to the effective organization of the operations conducted and processes implemented. Effectiveness results from the diversity of production factors as material and non-material resources, as well as from their complementing each other. With these resources, enterprises provide their customers with added value in form of the aforementioned savings or better fulfillment of their needs (Ujwary-Gil, 2009).

As an enterprise is analyzed from the angle of its resources and competences, this theory is an internal-external approach. In the period preceding increase of interest in this concept, great significance was attached to the surroundings and the relations between the surroundings and the enterprise (Porter's Five Forces Analysis). The resource-based view primarily refers to the internal factors and then analyses external conditions (Czerniachowicz, 2012, p. 102; Kunasz, 2006, p. 38).

The emphasized role of non-material resources, including in particular competences, abilities and skills of people creating an enterprise, draws our attention towards labor characteristic of human capital. Additionally, effectiveness of organization of the processes which create added value make us reflect on their quality. Hence, the following part of this study is going to be devoted to the labor quality issue.

### **3. Issues concerning the quality of labor**

*Quality*, in which representatives of various professions and sciences have been interested in since ancient times, have not been defined explicitly yet. On the contrary, increasing number of authors agree that it is impossible to define it unambiguously and categorically. An etymological origin of this word is Latin *qualitas* introduced in the 1st Century B.C. on the basis of Greek *poiotes* understood as a property or characteristic of an attribute. It is believed that this concept was introduced to the philosophy by Plato to describe a certain degree of perfectness, as an evaluative judgment which is inseparably connected with the user. Aristotle, in turn, recognized quality as “what makes a thing

be a thing”. Hence, from a philosophical perspective, the quality is a feature or a group of features which distinguish a particular object from the others (Skrzypek, 2002, p. 15). Quality is defined in various ways in the management sciences, as well. The variety of definitions extends from the most general and universal to the more detailed ones, referring to particular resources, processes or products and their characteristics<sup>3</sup>. Some of these general expressions take form not so much of scientific definitions as rather literary aphorisms.

Tadeusz Kotarbinski, the creator of praxeology, indicated that the notion of *labor* is very ambiguous which results from the fact that there is no single understanding of it. He defined *labor* as a series of activities characteristic of overcoming difficulties in order to fulfill somebody’s vital needs<sup>4</sup>. He indicated that in various situations different features of labor are emphasized (unpleasant effort, an activity to which someone is devoted, productive character of labour, the opposite of play, forced labor). The above-mentioned necessity to overcome difficulties mentioned creates an enforced situation; thus, a significant feature of labor is its enforcement. Hence, in the praxeological meaning, labor is contrasted with all non-serious activities, not threatened by any enforcement, or with play (Kotarbiński, 1965, pp. 88-91). This is a very general explanation of labor which reflects the praxeological idea of generalizing the efficient operation theory. This way, it is possible to use a very meaning of this concept and to make it detail according to particular conditions and situations. Nevertheless, the definition cited here seems to reflect excellently the nature and fundamental sense of labor which contributes to a human and enables him/her to survive and develop. The enforcing character of labor brings further meaningful results, i.e. the nature of motivation: “The point is that a man/woman would do willingly what he/she must do; that he/she does not do what he/she must only because he/she must do it but that he/she would find pleasure in it and, as a result streamline his/her labor by showing generosity in devoting to it” (Kotarbiński, 1965, p. 231). What is emphasized here is the necessity of an employee engagement (motivation) in the laboring process, which is a condition of the labor streamline. The labor, and in further perspective – the whole enterprise – may remain really efficient only as an effect of constant attention to the efficiency. Thus way, labor still remains one of the basic production factors and the main resource of an enterprise, realized by the employees and managers of various organizational levels.

One of the most outstanding Polish quality scientists defines *the quality of labor* as an extent to which the employee fulfils the requirements and duly performs the laboring process. Requirements on the employee concern

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<sup>3</sup> Cf. (Kolman, 2009; S. Wawak, 2007, p. 212).

<sup>4</sup> That is to perform serious tasks which, if not performed, may bring a threat compared to loss of life, health, means of support, personal freedom, social position, good name, peace of consciousness, joy of living (Kotarbiński, 1965, p. 88).

his/her personal characteristics and qualifications and the requirements concerning the process focus on the production equipment, technology and the environment. The quality of labor understood this way is one of the main constituents of the production quality (Kolman, 2009, sp. 340). Another author, having analyzed many definitions and approaches to the problems of both quality and labor, defines the quality of labor as an extent to which labor is made and its effects influence the laborer, organization, customers and the environment. The labor itself depends on the way the tasks are organized and on the attitude of the laborer (S. Wawak, 2007, p. 219). Such presentation of the labor quality, although restricted with the lack of universality, draws attention to a few important issues. First, he indicates clearly that labor, as well as its quality, remains in close relation to its effects. Then, he emphasizes that labor influences development of an organization, its stakeholders and environment, and the extent of this influence reflects the quality of labor. He indicates the main labor quality determinants which are: the way the task fulfillment is organized and the attitude of people – laborers.

Ambiguity of the labor quality issue seem to result in a way from the aforementioned individual and unique character of each enterprise. This originality of organization relates to the unique method of combining specific resources and competences, which guarantees not only the market success but also leads to further evolution and uniqueness of both the processes and resources. That is why, in order to enable better understanding of the labor quality issue, the following paragraphs shall present some of the most important issues which either reflect the nature of this issue or are significant for its level and understanding.

The three basic production factors mentioned in the first part of this study are often supplemented with a forth one, which is the entrepreneur. This is a person who makes decisions on his/her own, unlike a manager who makes decisions on behalf of the owners. One fact is common for the two: both play the role of a supervisor. Thus, the labor of supervisors and subordinates should be detailed in the labor factor. It must be emphasized that the supervisor does not manage people as such but only the labor they do. This way, it is possible to discuss managing some others' labor – which is the case only for supervisors – and managing one's own labor by a manager or employee. Such management aims at obtaining competitive advantage as an effect of strategic deployment of highly-qualified and engaged employees (T. Wawak, 2002, p. 94-95).

Dealing with the issue of labor quality, it must be stressed that its level is perceived very individually. Various authors use various definition of this quality, depending on the situation context and details, just as it is differently perceived by individual stakeholders of the enterprise. It seems characteristic that the labor quality is not only differently but even contrary assessed, within



the scope of one process, by the employees and their supervisors. This occurs when the supervisors try to achieve labor quality improvement by intimidating employees. To ensure their safety, they are able to work longer or more effectively, or even make less mistakes, which from the employee's point of view seems to prove labor quality improvement. However, the employees' attitude to labour deteriorates, their internal motivation decreases or even ceases and, as a result, they assess their labor quality as highly unsatisfactory (Panek, 2002, p. 241-243). Obviously, such a situation is unfavorable or even destructive for an enterprise, in particular from the resource-based point of view. Nevertheless, by generalization, it can be indicated that unanimity of labor quality assessment made by the employees and their supervisors is of high influence to this quality.

Another issue which conditions and helps to understand the labor quality issue is human resources management<sup>5</sup>. This area of management is responsible for implementation of the personnel strategy, which in turn results from the general enterprise strategy. It consists of several functions whose fulfillment should ensure right human resources. Depending on the business character and branch, as well as on the size of the enterprise, the functions are more or less complex and detailed. Nevertheless, using one author's conclusion, it may be stated that the quality of each function fulfillment influences the quality of labor of the enterprise members (Oleksyn, 2010, p. 370).

The labor quality level depends on several factors resulting from the enterprise itself, its resources, skills and competences. Because labor is inseparably connected with a human, the main groups of its quality determinants relate to the human as a laboring subject. The base is well-trained engaged and well-motivated staff. This staff must be equipped with leading technology, up-to-date machines and devices, as well as good managers. Organization should be based on leadership, delegating authorizations, increasing employees' responsibility and extending their field of operation. Increase of labor quality is possible, in turn, by continuous employee development, expanding knowledge of employees and, as a result, of the whole organization), obtaining extra qualifications and new specializations, which means learning should become a constant element of an employee's life (T. Wawak, 2002, pp. 103-104). Obviously, the above examples do not exhaust the collection of labor quality conditions but only indicate the most important ones, also from the perspective of the resource-based and competence-based view on enterprise. Former reflections may lead the reader to a wrong conviction that all the enterprise characteristics influence the quality of labor positively. This is not the case, of course. Thus, to maintain even minimum balance,

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<sup>5</sup> This is both a very important and extensive issue which, for obvious reasons, shall not be presented here in detail; more information about it can be found in: (Oleksyn, 2010).



some examples of phenomena destructive for the quality of labor should be mentioned. These are, among others, excessive stress at labor or professional burnout. The former is often an effect of excessive or incorrectly selected method of motivating employees, good in intentions but not necessarily in the results. The latter (professional burnout) occurs as an effect of continuous of continuously repeated emotional agitation which, as a result, deprives an employee of his/her ability to labor. This phenomenon is often the reason of not only low quality of labor but also low employees' morale, high absence factor and employment fluctuation (Panek, 2002, pp. 243-246).

Using the above definitions and findings, it is possible to assume that the quality of labor is both the extent to which the requirements on the laborer and labor process are fulfilled, as well as the extent to which it influences development of the organization and its stakeholders. It depends on the qualifications, features and attitudes of the laborer, as well as on the technology used and method of task organization.

In the context of labor quality, the problem of perfectionism is worth mentioning. It happens, particularly in popular thought (and, as a result, in the management practice) that the quality of work is equated with perfectionism. Sometimes this connotation brings very negative effects. Obviously, there are some activities and labors which require perfect performance but usually it is sufficient to make them just well. In all these situations, the required good level should be enough. Otherwise the enterprise (and individual employees, as well) exposes itself to excessive costs resulting from logarithmic increase of time and effort necessary to perform particular labor (Oleksyn, 2010, p. 377).

#### **4. Quality of labor as a component of the enterprise competences**

Even the definitions of labor quality presented above seem to place it in the resource-based and competence-based view on the enterprise. It is indicated that the quality of one of the main production factors, i.e. labor, is decisive for the development of its stakeholders, environment and the enterprise itself. On the other hand, organization of tasks, included in the enterprise competences and skills, becomes the labor quality determinant. Employees' qualifications and attitudes, in turn, treated as the low labor quality factor, are at the same time an important element of human capital – the most important resource of an enterprise.

He perceives the labor quality improvement as a source of profit increase, value added and value of the organization itself. These effects may be achieved by caring about the increase of labor quality of all the organization members, in particular of managers responsible for management quality. This leads to increasingly better use of outlays, both in the aspect of their profitability

and of the quality of products (T. Wawak, 2002, p. 100). Higher profitability translates into cost reduction, which additionally improves their relation to the quality of products offered.

Each enterprise operates to fulfill its stakeholders' needs and increase the value added at the same time. To achieve that, it is necessary to increase production, improve quality, reduce costs, limit delivery times, as well as improve personnel safety and morale. Improvement in these six areas is nothing else but increase of productivity. Increase of productivity is an activity essential for employee development and, as a result, the quality of labor. It must be born in mind that while quality is determined by the customer requirements, reasons for which the customer expectations cannot be fulfilled mainly because of gaps in the labor system and processes. Thus, the role of organization participants is to streamline processes, not only remind employees to labor better (Tkaczyk, Wierzbicki, 2003, pp. 59-67). A recipe for this is continuous taking care of widely-understood quality, in particular labor quality.

A substantial link between the quality of labor and resource-based and competence-based view on enterprise seems to be some of the economic measures used to assess an enterprise operation. For example, productivity or effectiveness must be mentioned here. However, there is a lot of confusion with these notions in the literature. While productivity is popularly treated as a relation of production volume to the outlays incurred for the production, effectiveness is explained in various ways, often contradictory<sup>6</sup>. With its terminological clarity, praxeology may be helpful here.

Practical assessment of an activity seem to determine the quality of labor; at the same time, they are a specific expression of competences accumulated in the enterprise. They concern the product (effect of labor); the laborer; co-operation and the labor itself (the way of laboring and activities) – in its various aspects, such as energy of activity, economy, effectiveness or organization.

Thus, the quality of labor seems to be determined by such product features as, for example, precision, lack of interjections or durability. Precision is the degree of deviation from an intended product feature (the highest precision is when the deviation is the smallest), which makes the product well done – as an effect of successful operation – or not. The product of labor should be free from interjections, faults and defects which proves its purity and purity of the labor itself. Durability concerns the products intended for long-term use (as opposed to the temporarily used) and it is opposite to junk products which are shoddy and break quickly. The aforementioned precision, purity, solidity and durability are owed to such human virtues as reliability, diligence and foresight (as opposite to carelessness and negligence). From the economy perspective

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<sup>6</sup> This is the relationship between the effects obtained and the outlays incurred; as efficiency, effectiveness; as a capability to implement the enterprise strategy and achieve the purposes assumed (Tkaczyk, Wierzbicki, 2003, p. 62).

(which shall be discussed below), people can be divided into lazy ones or diligent and industrious ones. An expert in his/her profession is a person who knows it very well (is able to assess and give advice) while a master has all practical virtues to the highest extent. On the other hand, a bungler is a person who cannot do what he/she does (makes sloppy labor). A positive feature in the field of co-operation is for instance discipline. Now, various aspects of the assessment of the labor itself should be discussed. As far as the energy in undertaking tasks is concerned, using all the resources and force necessary to achieve the planned aim should be appreciated (energy, courage), which is opposite to sluggish pace. Another variant of energy is an initiative, creativity (independent creating of plans and trying to fulfill them) which determine resourceful people and which is opposite to automatism and routine. As the labor progresses, intensity of efforts, patience, perseverance and eagerness are appreciated, contrary to sluggishness and short-time enthusiasm. The aspect of economy requires (at using the resources owned) avoiding wastage, which may be overcome in two ways: by economizing and productivity. Economizing assumes smaller use of resources while productivity also requires the same amount and quality of products – at lower use of resources. Apart from productivity, also efficiency should be mentioned; to labor efficiently means to achieve the same productive effect at lower period of time spent on laboring. Among other usable values of labor, skills, effectiveness and efficiency should be indicated. Skills are understood as dexterity and competence; at the same time, skills are components of efficiency. Efficiency, in turn, is an ordinary condition of the effectiveness of operations<sup>7</sup>. An activity is effective when it results in a planned effect; the opposite of effectiveness is counter-effectiveness and lack of effectiveness is ineffectiveness. Also the symptoms of good labor of organizational character are included in the enterprise competences. The concern merging of activity elements into harmonized wholes. An order is indicated here, understood as of subsequent activities, to make them easier and possible to perform. Equally important value is simplicity (opposite to complexity) of the operation method. What is also emphasized is the necessity of planning and consistency in implementing the plan assumed which should be purposeful, relatively detailed, but not stiff – rather flexible. Finally, it must be added that in relation to good labor each change for better, in all the aspects mentioned above, is a form of streamline (Kotarbiński, 1965, pp. 394-408). This streamline, taking care of constant correcting and improving, seems to be very well incorporated in the problem of quality in an enterprise.

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<sup>7</sup> Effectiveness is sometimes understood in two ways: as all values of practical activities together (detailed assessment: of efficiency, profitability, economy, rationality, etc.) or as each of the good labour values separately (effectiveness is efficiency, effectiveness is profitability, effectiveness is economy, etc.). (Pszczolowski, 1978, p. 227).

The system of activity practical assessment presented here describes and explains the issue of human labor quality to a large extent. On account of that, it can be used as a starting point to build a theoretical model of labor quality determinants. Creation of such a model would give a basis for further analyses and empirical research on the problem of labor quality.

To sum up, it can be stated that while labor itself, understood as one of the production factors or – more precisely – a labor potential personified by human beings – is one of the enterprise resources, the process of labor cannot be equated with the resource. On the other hand, the quality of labor, established to large extent by the practical assessments of activity, seems to express the enterprise competences (which is the way of using the resources) rather than the resources and potential of the enterprise.

## 5. Conclusion

The existence and operation of each enterprise concentrates on fulfilling needs of widely-understood clients and it is possible thanks to possessing suitable resources. One of the main resources of each enterprise, i.e. labor potential, is realized by a human. Qualifications and characteristics of people being the enterprise stakeholders create the human capital which, together with the structure and other resources of the enterprise, realize its competences. To fulfill its competences correctly, an enterprise must coordinate and organize its resources properly, using suitable skills and competences. An inherent element of these processes, providing long-lasting and development of an enterprise, is continuous improvement. This improvement manifests in constant increase of operation effectiveness, which is possible by taking care of suitable quality of resources and processes in the enterprise. All these elements are consolidated within a theory which discerns the enterprise competitive advantage in its resources and competences.

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**II.**  
**MODERN TOOLS FOR BUSINESS**  
**AND NON-PROFIT ORGANIZATIONS**  
**MANAGEMENT**





# A METHOD OF ESTIMATING THE DETERMINANT OF ENTERPRISE COMPETITIVENESS

**Olaf Flak<sup>1</sup>**

## **Abstract**

*The aim of the article is to propose a method for estimating the determinant of enterprise competitiveness, based on the Competitiveness Integrated Model and the Company Competitiveness Barometer. The article presents a description of The Competitiveness Integrated Model, the current status of research of the Company Competitiveness Barometer, definition and algorithms for estimating the determinant of enterprise competitiveness.*

**Keywords:** *competitiveness, competitive potential, strategy of competition, competitive advantage, competitive positioning, determinant of enterprise competitiveness.*

## **1. Introduction**

In the literature on the subject and in everyday business language, competitiveness is used for a lot of different phenomena present in the conduct of the company, sector or whole economy. For many years, the author of this article has been making efforts to sort out the terms associated with the wider concept of enterprise competitiveness and make use of the theoretical approaches, models and methods in a beneficial way for a business practice.

The main objective of the article is to propose a method for estimating the determinant of enterprise competitiveness, based on the Competitiveness Integrated Model (Flak and Głód, 2012, pp. 50-72) and the method of measuring the company's competitiveness which is the Company Competitiveness Barometer (Flak and Głód, 2014 in print; Flak and Głód, 2014, pp. 12-14).

The specific objectives are to present:

- the basis of the Competitiveness Integrated Model and the importance of the concepts included in that model,
- definition of the determinant of enterprise competitiveness and its elements,

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- the use of the Competitiveness Integrated Model until now and the current status of research under the Company Competitiveness Barometer framework,
- algorithms to create a coherent description of the company in the form of a case study, scoring its competitiveness and competitive proximity of the enterprise,
- outline of the research development based on the Company Competitiveness Barometer.

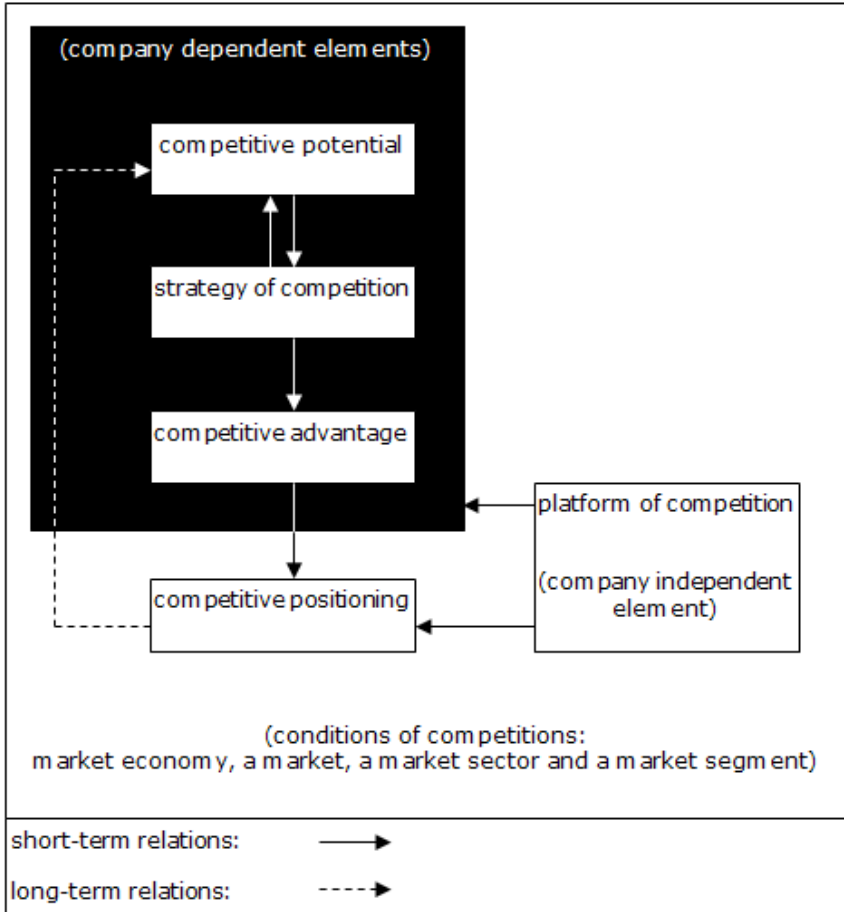
The article has a diagnostic and scheme design aspect. Therefore, the desk research method, presentation of the results of empirical research and the case study were used in the diagnostic dimension. Design issues were based on the prognostic method (Bieniok, 2001, pp. 68-75). Due to the objectives of the article, the research problem and the research hypothesis were not stated in its contents.

## **2. Theoretical basis**

In the literature on the subject, the enterprise competitiveness is defined in many ways. A wide overview of the approaches to this issue and definitions of the terms connected with competitiveness was presented by the authors of the monograph “Competitive ones will survive” (Flak and Głód, 2012, pp. 39-49).

Theoretical basis, which was a starting point for designing the method for estimating the determinant of enterprise competitiveness, and a starting point for the consideration of company’s characteristics that make the company achieve the desired results from the conducted economic activity and be able to compete in the market, is the following definition of competitiveness. “Competitiveness is a multidimensional attribute of the company, resulting from both the internal features and the ability to cope with external circumstances. Competitiveness is relative, that means, there is no absolute scale for measuring competitiveness, (...) competitiveness can be used to describe the mutual relations of enterprises in the market.” (Flak and Głód, 2012, p. 44)

Since the company’s competitiveness is an abstract and general concept, it has some constituent elements which are also elements of the Competitiveness Integrated Model (Flak and Głód, 2014, p. 13). The Competitiveness Integrated Model is shown in Figure 1.



**Figure 1.** The competitiveness integrated model

Source: Flak and Glód (2012, p. 57).

The first element is the competitive potential, signifying the resources that enterprise has or should have to be able to use them to build, maintain and strengthen its competitiveness. These are, in a broad sense, possibilities of the company resulting from its tangible and intangible capital. Competitive potential of the company is at the same time the relative multidimensional concept.

The enterprise uses the competitive potential through its strategy of competition, which is an adopted action program aimed at achieving a competitive advantage towards the entities from the competitive environment (microenvironment), serving the basic objectives of the enterprise. The aforementioned competitive advantage is a company’s ability to deliver the

tangible and intangible assets to the customer via the market. The company's competitive advantage is the relative multidimensional concept.

As a result, the company's competitive positioning is obtained, which is measured by the means of synthetic market and economic results of the enterprise, resulting from the extent of utilization of the enterprise's capacity to compete now and in the future. The competitive positioning of the company is a relative multidimensional concept.

What influences and determines the activity of the company is an environment of the company. In the Competitiveness Integrated Model, the environment is called a platform of competition and denotes a set of characteristics of macro- and microenvironment in which a company operates in a given industry sector. The features of the macro-environment are the same for every company operating in a given sector, while the characteristics of microenvironment may be different for each company in that sector.

The relationships between the model elements and their graphical representation are presented in previous publications of the author (Flak and Głód, 2012; Flak and Głód, 2014). Hypotheses concerning the relationship between the competitive potential and the strategy of competition; as well as the strategy of competition and competitive advantage, were also positively verified in previous publications of the author (Flak and Głód, 2014, pp. 15-16).

### **3. Antecedent use of the competitive model**

The above-described Competitiveness Integrated Model was the basis for development of the concept of an annual survey of competitiveness of Polish companies, namely the Company Competitiveness Barometer (Flak and Głód, 2012, pp. 230-232).

The first edition of the Company Competitiveness Barometer was carried out in 2012 and included over 109 companies. The second edition took place in 2013, with 173 companies taking part in it. Smaller sectorial diversification of the companies and their greater number allowed for statistical verification of the hypotheses on the relationships between the competitive potential, the strategy of competition and competitive advantage – in the Barometer questionnaire only these three elements of the Competitiveness Integrated Model were used. (Flak and Głód, 2014, pp. 15-16).

In the first half of 2014, the third edition of the Company Competitiveness Barometer was held ([www.konkurencyjniprzetrwaja.pl](http://www.konkurencyjniprzetrwaja.pl)). All five elements of the model, which have been operationalized in the form of 45 questions within the Barometer questionnaire, were used: 12 questions about competitive potential, 10 about the strategies of competition, 8 about competitive advantage,

6 about the competitive positioning and 9 about the platform of competition. All questions in the Company Competitiveness Barometer have been closed, single-choice questions.

Due to the volume of this paper, the reader interested in the examined elements of the competitive potential, the strategy of competition and competitive advantage is referred to previous publications of the author (Flak and Głód, 2014, p. 14). Nevertheless, the names of the elements of competitive positioning and the platform of competition used in the Company Competitiveness Barometer, are presented in Table 1.

**Table 1.** Names of the elements of competitive positioning and the platform of competition

<b>Competitive positioning</b>	<b>The platform of competition</b>
ability to settle liabilities when due debt level	risk to the company from companies in developing countries
level of the percentage market share indicator	attitude of Polish customers to the products or services offered by companies in the sector
level of the return on sales indicator	the possibility of use of flexible forms of employment
sales revenue growth	degree of technology preservation used by the company in past 5 years
company's return on equity (own and foreign)	the extent to which the quality of a product or service depends on the quality of supplier's raw materials (intermediates)
	difficulty of company's withdraw from the current sector
	chance that in the next year the customer will begin own production of a product or service
	the extent to which brand awareness influences customers' purchasing decisions
	the degree of similarity of substitutes to the products or services offered by company

In previous research work with the use of the Company Competitiveness Barometer based on The Competitiveness Integrated Model, two operations on data collected from the respondents of the Barometer questionnaire have been used.

The first operation is reduced to recording unaltered responses of the respondents as new records in the database. This allows for later unlimited operations on the recorded data in order to draw up a description of the respondent's company in a form of a case study, as well as perform statistical calculations.

The second operation is used to calculate the level of competitiveness of a subject enterprise in real-time, after completing the Barometer questionnaire by the n+1 respondent, based on the data left by n respondents who answered it earlier. An assessment of a subject enterprise is made by the means of a natural number from a closed interval from 0 to 360 (as results from the number of responses – 36 – on a scale from 0 to 10 points for every answer). Since this is also a part of the method for estimating the determinant of enterprise competitiveness, a detailed description is given below.

The inference based on empirical data in the two above-described ways is sufficient for verification purposes of a part of the hypotheses in the field of enterprise competitiveness (Flak and Głód, 2014, p. 12) and to describe the characteristics of enterprises in popular science form. Therefore, these two types of inference will be used in the method of estimating the determinant of enterprise competitiveness. However, it seems that the distance that separates a given company from the characteristics of the ideal company in the sector (following there is a clarification on whether there may be an ideal company in the sector) can be deduced from the collected data. This mechanism is the third component of the method proposed in this article.

#### **4. Nominal definition of the determinant of enterprise competitiveness**

In this publication, the determinant of enterprise competitiveness is defined as a group of three competing attributes of companies in the market. This group includes:

- description of the characteristics of enterprise's competitive potential, the strategy of competition, competitive advantage, competitive positioning and the platform of competition in a form of a case study (algorithm 1),
- assessment of enterprise competitiveness in a form of a natural number from a closed interval from 0 to 360 points (algorithm 2); where 0 is the lowest value and 360 is the highest competitiveness value (the upper end of the range depends on the number of questions in a research tool, as described below),
- assessment of competitive proximity in the form of a natural number from a closed interval from 100 to 0 (algorithm 3); where 100 is the lowest value and the highest value of competitive proximity is 0.

It should be emphasized that all the above attributes, namely their determination algorithms, are based on following methodological assumptions:

- there is no theoretical model of an answer that is absolutely correct for any sector of economy (the platform of competition) valid for a longer period of time, defining the characteristics of the most competitive enterprises (Flak and Głód, 2012, p. 44),

- comparison of enterprise competitiveness can only take place in a relative way (Olszewska and Piwoni-Krzeszowska, 2004, p. 507)
- characteristics of the most competitive companies in the sector are focused on some of the values of these features, but there is a low probability that companies with extreme traits belong to the most competitive ones in the sector (Bień and Dobiegała-Korona, 1997, pp. 143-144).

The first of the aforementioned assumptions implies that there is no perfect business model which can be compared to other companies in the sector. This limitation makes it necessary to look for other ways to obtain a “pattern”, and a solution is an assessment of the competitive proximity.

## **5. Elements of the determinant of enterprise competitiveness**

The aforementioned elements of the determinant of enterprise competitiveness require their own nominal and operational definitions.

The first and methodically simplest determinant’s element is the description of the company’s characteristics in a form of a case study (algorithm 1). Algorithm 1, used for its presentation, is in fact (nominal definition) a verbal representation of records in the database resulting from the answers given by the respondent about a particular company. To establish it, the data collected (operational definition) have to be interpreted in the database; and their code form translated into a natural language.

The second element of the determinant of enterprise competitiveness is an assessment of the competitiveness of a company in a form of a natural number from a closed interval from 0 to 360 points (algorithm 2). Competitiveness assessment has the following nominal definition: it is a difference between the dominant values of competitiveness components and the values of these elements in the audited company without taking into account the distribution of these values in the plenitude of all surveyed enterprises.

Algorithm 2, used for its calculation and which is also its operational definition has been presented in previous publications by the author on the topic of Company Competitiveness Barometer (Flak and Głód, 2014 in print), but due to the clarity of the following argument, its brief description is presented below.

The fact that the respondents, especially those filling the questionnaire online, expect an immediate result of their actions, prompted the authors of the Barometer to develop an algorithm for calculating the results online, which on the one hand would evaluate a tested company in real time without a pre-defined pattern of competitiveness, and on the other hand would be fair and accurate. Procedure of the algorithm 2 is illustrated in the example in Table 2

**Table 2.** The example of assessing the n+1 respondent’s competitiveness

variable	Question in a questionnaire Possible answers	How is the knowledge about the enterprise collected?				
		complete paper elaborations	unrelated paper documents	complete electronic elaborations	unrelated electronic documents	in employees heads
a	Number of each answer among the n respondents	4	6	5	13	8
b	Contractual value for the number of answers	3,076923	4,615385	3,846154	10	6,153846
c	Number of points given for the answer	0	4,62	0	0	0
x	Answer of the n+1 respondent		x			

Table 2 presents the example of a question, for which the number of answers of n respondents in given categories is indicated by variable a. Assume that n+1 respondent answered in accordance with the “x” (variable x). The maximum number of points that the respondent would receive if their answer was compatible with the most common response (“unrelated electronic documents”), would be 10 (variable b). The variable b, shows the number of points they could get for showing a different answer in proportion to the maximal number of points (10) and the response frequency (described by the variable a, in this case 13 responses). Since n+1 respondent answered “unrelated paper documents”, they scored in approximation 4.62 points out of 10 possible (variable c).

Points for all questions (variable c of all questions) in a research tool can be added and their sum is in the range from 0 to 360 (resulting from the number of responses – 36 – on a scale from 0 to 10 points for each response). It should be emphasized that, in the Company Competitiveness Barometer 2014, 36 components of competitiveness (potential, strategy, advantage and competitive positioning) are assessed. 9 components belonging to the platform are not evaluated (see: Flak and Głód, 2012, pp. 230-232).

Algorithm 2, after new entry for each question in the database, updates the conventional value of points, first by searching for the response’s maximum frequency and giving this answer 10 points, and then allocating to the answer of the n+1 respondent the number of points resulting from the relative frequency of the response (variable b) in the maximal response rate (the maximum value of the variable a). In this way the IT tool “learns” how the following respondents answer and, on this basis, it sets the criteria of awarding points for



the next respondent. It should be emphasized that the evaluation of enterprise's competitiveness is not based on analysis of the frequency of all responses to the question, but on a comparison of the frequency of a response chosen by the respondent (in the example, answer "unrelated paper documents") to a response with a maximal frequency (in the example, the answer "unrelated electronic documents"). Points awarded to the subject company are indicative and subject to measurement error decreasing with an increase of the number of responses recorded in the database.

The third element of the determinant of enterprise competitiveness is an assessment of competitive proximity in a form of a natural number from closed interval from 100 to 0 (algorithm 3). The competitive proximity is nominally defined here as a difference between the dominant values of the components of competitiveness in the overall plenitude of subject enterprises and values of these elements in the analyzed company, taking into account the distribution of these values in the plenitude of surveyed enterprises. The difference in the definition of competitive proximity (algorithm 3) and the above definition of the evaluation of competitiveness (algorithm 2) is worth noting. This difference, in the case of competitive proximity consists in the reference of a distribution of values in the overall plenitude of surveyed enterprises, whereas the assessment of competitiveness does not apply to this distribution.

It should be emphasized that the concept of competitive proximity is based on considerations made in the works of W. Czakon (2010), who wrote that "the category of proximity has a direct or indirect use in explaining the key problems in science of managing. In particular, it contributes to a better understanding of sources of the competitive advantage that are beyond the boundaries of enterprise" (Czakon, 2010, p. 16; Boschma, 2005, p. 61). A similar approach to this category is presented by P. Klimas (2012) in his works. The competitive proximity, however, is a reverse of organizational proximity, which is reflected in an operational definition of the term.

Algorithm 3, used for its calculation and the operational definition, is shown in Table 3 together with an example of a designation of the competitive proximity, for reasons of clarity, for its only one element.

**Table 3.** The example of assessing the n+1 respondent’s competitive proximity

Question in a questionnaire		How is the knowledge about the enterprise collected?				
variable	Possible answers	complete paper elaborations	unrelated paper documents	complete electronic elaborations	unrelated electronic documents	in employees heads
a	Number of each answer among the n respondents	4	6	5	13	8
b	Contractual value for the number of answers	11,11	16,67	13,88	36,11	22,22
c	Number of points given for the answer	0	16,67	0	0	0
x	Answer of the n+1 respondent	x				
y	Competitive proximity for this question	19,44				

Table 3 presents the same question as Table 2. As before, the number of responses of n respondents in each category is indicated by the variable a; n+1 respondent answered in accordance with the sign “x”. The maximum number of points that this respondent could receive if his answer was compatible with the most common response (“unrelated electronic documents”), would be 36.11 (variable b). The variable b indicates how many points they could get for a different answer, proportionally to the maximal number of points (36.11) and frequency of a response (variable a). Since n+1 respondent answered “unrelated paper documents”, they scored approximately 16.67 points. It shall be noted that the sum of all values of the variable b equals 100. In other words, they are the percentages of share of each of them in total response. In this way, the competitive proximity takes into account a distribution of these values in the entire plenitude of the subject companies.

Algorithm 3, after new entry for each question in the database, updates the conventional value of points, first by searching for the maximal frequency of a response, and then allocating the response of n+1 respondent a number of points, resulting from the percentage frequency of a response (variable x) in a maximum frequency of a response. Similarly, as in the case of algorithm 2, the IT tool “learns” how following respondents answer and, on this basis, it sets criteria to award points for the next respondent.

Then, the competitive proximity is calculated as the sum of the variable y (for each question) and compared to the sum of the maximal values of the variable b for all the questions of a research tool. The variable y is the difference between the maximum point value for the number of responses (variable b, in the example 36.11) and the number of points scored for the answer to the

question (variable  $c$ , in the example 16.67). In the above example, the variable  $y$  for the sample question is 19.44.

After dividing a sum of variable  $y$  for all the questions by a sum of the maximum value of the variable  $b$  for all the questions, and multiplying a resulting fraction by 100; a measure for the competitive proximity is obtained, which is a natural number from a closed interval from 100 to 0. Standardization procedure, characterized by the fact that a sum of variable  $y$  is referred to a sum of the maximal values of the variable  $b$ , aims at unifying the range of accepted values for the same numerical interval, regardless of the distribution of responses in the sector. Otherwise, the left side of the interval for two different sectors (greater number - left end of the interval) would vary and depend on the distribution of company's characteristics in the sector. At that time, there would be no possibility of comparing the competitive proximity for companies belonging to different sectors.

A value of 100 indicates the smallest proximity, that is the biggest difference between the characteristics of competitiveness components of the subject  $n+1$  enterprise and all the dominant (most common) features of the  $n$  subject enterprises in the sector. A value of 0 means the greatest proximity, i.e. the smallest difference between the characteristics of the competitiveness components of the subject  $n+1$  enterprise and all the dominant (most common) features of the  $n$  subject enterprises in the sector. In the latter case, the subject enterprise would have all the characteristics such as the dominant characteristics of enterprises in the sector. However, it is a theoretical value, comparable to the concept of infinity in number theory. If so, the enterprise would have "picked up" the dominant features of all enterprises in the sector. This would be an ideal company in terms of business competitiveness (!). The most competitive company would have all the most common characteristics of other companies, but not of one of the existing companies, but the entire plenitude of these companies.

Later in this article, examples of the company's competitive profile designation, based on empirical data collected in the framework of the Company Competitiveness Barometer 2013, are presented. It should be noted that the method of estimating the determinant of enterprise competitiveness, in particular algorithms 2 and 3 described above, is based on the assumption that 36 components of competitiveness (36 evaluated questions about the platform, strategy, competitive advantage and positioning) are assessed. Such action has been implemented only in the framework of the Company Competitiveness Barometer 2014. In 2013 the Barometer contained 30 questions instead of 45, and therefore, in the examples below the limit values of points for the elements of the competitive profile are, as follows:

- assessment of enterprise competitiveness:  $\langle 0; 300 \rangle$ ,

- assessment of competitive proximity: <100; 0> (due to the measurement standardization this interval does not change depending on the number of questions in the research tool).

More information on the results of the Company Competitiveness Barometer 2013 can be found in previous publications of the author (Flak and Głód, 2014, pp. 15-17).

## 6. Examples of the competitive profiles of chosen companies

Table 4 presents the competitive profile of the most competitive Polish company that took part in the Company Competitiveness Barometer 2013. Company belonged to the service sector.

**Table 4.** Competitive profile of the most competitive Polish company of 2013

Elements of competitive profile		Assessment content and value
Case study	Competitive potential	<p>The person representing the company declared that the creditworthiness of the company is high and the level of held share cash in relation to the nature of their business is moderate. Our research shows that in 2013 the most competitive company reached the profit on their core business.</p> <p>Knowledge of business activity is accumulated in complete electronic elaborations. Similarly to the least competitive company, a single employee can introduce small improvements in their work to a limited degree. In addition, constructive conclusions are often drawn within teams or departments from projects or activities that have been successful. Creativity of employees who perform the most critical activities of the company is (only) moderate (!). At the same time, the company documents of realized projects initiatives and production processes (only) in a moderate degree (!).</p> <p>Professional experience of employees, who perform the most critical activities in the company, was high. The extent to which the employee is free to choose how to perform tasks depends on the type of task. In the studied company employees can get to know the company's strategy during meetings with supervisors. The attentive reader will notice that these three characteristics of the competitive potential are identical to the features shown by the least competitive company.</p> <p>Declared deterioration or obsolescence (economical) of existing fixed assets is moderate.</p>
	Strategy of competition	<p>The respondent representing the company declared that in the field of the strategy of competition the subject company has a very dynamic development of marketing skills and shows the care of maintaining the high reputation. Efforts are also made in the field of public relations. However, there is no tendency to employ methods aimed at "slimming" the organization, including lean management.</p> <p>According to the company representative numerous actions to maintain a strong position of the company's brand, such as preparing a trade offer for each of the clients individually and at the same time trying to create own market niches, are taken. The audited company uses modern methods of marketing research in order to reach the right customer target group.</p> <p>Activities that increase the company's competitiveness may include the fact that the test company is looking for more competitive co-operators functioning thanks to the use of outsourcing. At the same time it uses the economy of scale and experience, as well as benchmarking target the search for sources of lowering the costs of production or services.</p>
	Competitive advantage	<p>The main objective of currently used pricing strategy for all products or services altogether is to maximize the total share in the sector or market segment. At the same time the customer can often negotiate the price of these products. The distribution system ensures timely delivery of products of a fairly high level. Sometimes a customer can test the products before buying.</p> <p>All products are warranted (e.g. a free after-purchase service, repair or replacement) and meet, in a fairly high degree, generally accepted criterion of being environmentally-friendly. The company often plans their obsolescence before introducing the product to the market; from 51 to 75 percent of customers are covered by the loyalty program.</p>
Assessment of competitiveness <0; 300>		274 points (very high competitiveness)

Elements of competitive profile	Assessment content and value
Assessment of competitive proximity <100; 0>	4,54 points (very high competitive proximity, company has many dominant features in other companies of the sector)

Table 5 presents the competitive profile of the least competitive Polish company which took part in the Company Competitiveness Barometer 2013. Company belonged to the science and higher education sector.

**Table 5.** Competitive profile of the least competitive Polish company of 2013

Elements of competitive profile	Assessment content and value	
Case study	Competitive potential	<p>The level of held share cash in relation to the nature of their business is low, creditworthiness is equally low. The respondent representing the company declared that it did not generate profit from core business.</p> <p>Knowledge of business is accumulated in unrelated paper documents. To some limited extent, a single employee may make minor improvements in the their work; in addition extremely rarely the constructive conclusions are drawn in teams or divisions after completing projects or activities that have been successful. Respondent rated the creativity of the most critical company's employees as low. In contrast, the company documents the projects, initiatives and production processes to a high extent.</p> <p>Professional experience of the most critical company's employees was very high, and the degree to which the employee is free to choose how to perform tasks depends on the type of task. In the subject company employees can get to know the company's strategy during the meetings with their supervisors.</p> <p>Person participating in the study estimated that deterioration and obsolescence (economical) of existing fixed assets is high.</p>
	Strategy of competition	<p>In terms of the strategy of competition, the subject company has a very dynamic development of marketing skills and shows the care of high reputation. Efforts are also made in the field of public relations. In addition, multiply measures are made to maintain a strong position of the company's commercial brand.</p> <p>However, there is no tendency to employ methods aimed at "slimming" the organization, including lean management. According to a company representative, trade offer is not prepared for the needs of each client individually and at the same time the company is not trying to create own market niches. Subject company does not apply modern methods of marketing research in order to reach the right target group.</p> <p>Activities that increase the company's competitiveness may include the fact that the subject company is looking for more competitive cooperators functioning thanks to the use of outsourcing. At the same time it makes use of economy of scale and experience, but it does not apply benchmarking targeted to search for sources of lowering costs of production or services offered.</p>
	Competitive advantage	<p>The main objective of the current pricing strategy for all products and services altogether, is the survival the difficult times in the market. At the same time, however, the buyer of the company's products may not negotiate the price. The distribution system ensures timely delivery of products or services to a fairly high extent. However, the client does not have the possibility of testing the product or service before purchasing.</p> <p>The company never plans the product life cycle before launching the product. None of its customers is covered with a loyalty program.</p> <p>None of the products are covered by the warranty (e.g. a free after-purchase service, repair or replacement). The company's products meet generally accepted criteria of being environmentally-friendly at a fairly low level. The company never plans the product or service's obsolescence before they are introduced to the market, and none of the customers are covered by the loyalty program.</p>

Elements of competitive profile	Assessment content and value
Assessment of competitiveness <0; 300>	140 points (very low competitiveness)
Assessment of competitive proximity <100; 0>	31,43 points (low competitive proximity, company has few dominant features in other companies of the sector)

## 7. Conclusion

The aforementioned method for estimating the determinant of enterprise competitiveness is a part of a larger scientific intention which is a research project aimed at the diagnosis of enterprise competitiveness in the European Union. In 2014, a pilot study includes countries, such as Poland, Czech Republic, Slovakia, Spain, Finland and Germany. For this purpose, the research tool Barometer24.org has been prepared, which is a development of the presented in the article concept of enterprise competitiveness research. The specific objectives, scope and schedule of this project can be found in other publications by the author (Flak and Głód, 2014, Bratislava, pp. 86-92).

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# THE PRINCIPLES OF IMPLEMENTING EARLY RECOGNITION SYSTEMS IN AN ORGANIZATION

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## **Abstract**

*In the context of the turbulent environment, contemporary organizations have to work out and implement tools enabling them to handle the turbulence, and primarily, to avoid negative consequences of these processes. The tools are related, among others, to obtaining and providing managers, sufficiently in advance, with adequate management information on the environment. Early Recognition Systems (ERS) are a response to such conditions of the organization functioning and the challenge in respect of information support for decision-making processes. Unfortunately, they are mainly of informalized character, dispersed on various levels and in various functional areas of organizations, and very often based on unconscious, habitual actions, and, in consequence, their advancement and effectiveness are low. Based on the main characteristics of early recognition systems, the article presents the framework procedure of systemic solutions in the area of early recognition, which is supposed to enable formally organized activities within this scope.*

**Keywords:** *turbulent environment, management information, early recognition systems, implementation procedure.*

## **1. Introduction**

The contemporary environment is in the constant process of change, which forces organizations that want to maintain and strengthen their competitive position to apply solutions enabling to cope with these changes. Tools which allow to counteract the effects of such changes, also, if not in the first place, allow to avoid them, via their sufficiently early identification. The tasks are related to the implementation of the process of perception and interpretation of changes in the environment to understand them better, but primarily to anticipate its potential, future states. It arises from managers' information needs,

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who, in order to take decisions concerning the future of the organization, have to be equipped with adequate and provided early enough information about the environment (states, changes, trends). The methods and tools enabling the reduction of the uncertainty of decision-making processes and an increase in their effectiveness must lead to obtaining and processing information about the environment faster than the competition and enables better understanding of the conditions of the environment.

Early recognition systems (ERS) are a response to the conditions of the organization functioning in the contemporary environment as outlined above, and challenges within the scope of the informative support for decision-making processes. Research shows that they are mainly of informalized character in organizations, they are dispersed on various levels and in various functional areas of organizations, and quite often they are based on unconscious, habitual actions, and, in consequence, their advancement and effectiveness are low. Based on the main characteristics of early recognition systems, the article presents the framework procedure of systemic solutions in the area of early recognition (ER), which is supposed to enable formally organized activities within this scope.

## **2. The role and the place of early recognition in the organizational system**

Being an open system in the constant codependent relationship with the environment which is turbulent, an organization builds a relation with it, among others, in the strategic management process in which a strategy is an attempt made to take advantage of potential opportunities and threats. Within the framework of this process, organizations have a possibility to identify potential opportunities and threats owing to the observation of the environment and the anticipation of its changes on the basis of the observation of the current signs of the future. As various authors indicate (Watkins, Bazerman, 2003; McGee, 2004; Mercer, 2001), changes are preceded by sent early (weak) signals which are a medium of information about them. By feeding information processes in organizations, they provide knowledge and become a key variable reducing the decision-making uncertainty and increasing an ability of the strategic alignment of the organization's capabilities and the expectations of the environment (Ansoff 1985). An ability to anticipate the shape of the future environment enables the identification of possible strategic options because the information constitutes the basis of decision-making processes and integrates the elements of the strategic management system which secures the future of an organization.

The “early recognition” notion was introduced to the literature in 1980s by Kirsch (Kamas, 1992, p. 24) who indicated that in accordance with the strategic management principles, the observation of an organization’s environment cannot focus only on finding threats and on warning, as it was done within the framework of “early warning”, but it should also serve the recognition of emerging opportunities. At the same time, the observation of the environment cannot be limited only to previously defined areas but it should run comprehensively, including the whole environment. The introduction of the notion of early recognition systems meant the extension of the environment examination tasks by communicating chances, but also going beyond the quantitative identification mechanisms.

We can define the early recognition system as a special type of an information system focused on the anticipation of changes undergoing in the environment of an organization and the reduction of uncertainty related to them, as well as informing top managers about it early enough to make it possible to undertake adequate actions enabling to avoid strategic surprises. The specificity of such a system consists in directing the processes of information processing towards perception and interpretation of weak signals being the symptoms of changes, specified by future opportunities or threats. The system is a tool informatively supporting strategic management (the planning and strategic control systems functioning in organizations) via providing information reducing the uncertainty of decision making situations leading to better alignment of the organization and the environment and by this, guaranteeing the survival and growth of the organization.

When analyzing the literature of the subject, we can identify areas in which ERS are placed and within the scope of which their usefulness for management activities is perceived. The areas are not separable and they should be rather treated as perspectives of looking at ERS in the organization activity structure.

### ***ERS in decision-making processes***

The fundamental and at the same time the broadest area in which ERS are located is the decision-making area. The systems are *de facto* designed to secure the information needs of decision-making processes in the strategic area. On the one hand, they receive (weak) signals from the environment, and on the other hand, they provide information reducing uncertainty in decision-making processes. Their sense boils down to the identification of problems, which translates, for example, into Mintzberg’s decision-making model (identification-development-selection) (Choo, 2006). The need itself is defined as an information need, namely the difference between the information

about the current situation and the expectations which base on experience, trends, benchmarking, or other ways of insight into the current situation.

### ***ERS as a catalyst of learning***

Another area in which we can indicate the usefulness of ERS is the area of organizational interpretation. Such location, at the point of contact between the organization and the environment is compliant with the model of an organization proposed by Daft and Weick (1984).

The problem is perceived in a similar way by Koźmiński (2004, p. 99) who writes that ERS are a source of the situational knowledge generated on the basis of weak signals, which has to be integrated with the problems of the organization against the background of the environment. Associating knowledge having its roots in weak signals with the currently possessed knowledge, bears all traits of a creative process which leads to creating new knowledge. The use of signals in the learning process is, according to Choo (2006, pp. 240-244), an interaction between giving meaning to the signals from the environment, creating knowledge on this basis, and making decisions. In this cycle, constant information flow takes place in such a way that the outlets of one subsystem form a context and provide information feeding another subsystem.

### ***ERS as a tool of risk management***

In risk management, Mitroff and Shrivastava (1987), among others, perceive ERS as a system serving the detection of coming crises and a key element of coping with them effectively. In the model they proposed, the detection stage is identified with ERS which comprises the management information systems, the computer control systems and the systems of scanning the environment, analyzing both the inside and the environment of an organization in the search for coming crises. ERS serves as the protection against them if they are identified early enough, but on the other hand, it can be used to prepare for the battle with it. In turn, Kotler and Caslione (2009) place ERS in the context of the chaotic environment which creates huge opportunities, but at the same time generates a considerable risk, and indicate a necessity to build and develop skills, systems and processes enabling fast recognition of turbulences in the environment, and, what follows, the identification of potential opportunities/threats to avoid critical situations. In their understanding, the system is supposed to serve the recognition of weak signals which will be the basis for risk assessment.

### ***ERS in planning and strategic control***

A particularly significant area is that of planning and strategic control, or more broadly, strategic controlling. ERS is one of the key elements of the strategic management system because it constitutes a tool for recognizing changes in the environment in the form of emerging potential opportunities/threats, and informatively secures its implementation. Gołębiowski (2001, p. 81) claims that: “both strategic planning and strategic control deal with setting the strategic directions in changeable conditions of operation” and indicates the essence of planning and strategic control consisting in the permanent monitoring of external and internal conditionings of operation and the progress in achieving strategic goals, and the implementation of the organization strategy; they are focused on the detection and interpretation of signals about coming changes before they evoke unfavourable consequences and on proper reaction to them in order to increase the level of strategic alignment and a capability of correcting threats and using opportunities. Such an attitude, closely connecting planning and control, by leading to the emergence of controlling which takes over and supports the planning and control process indicates a significant role of ERS in this process (Gołębiowski, 2001, p. 84).

Taking into account the above areas of the ER application and their present state of practical use, one of the basic challenges in the context of the current stage of development is the strive for the institutionalization of this function. The question organizations should ask themselves is not the question whether to systemize activities within the area of ER but how to do it to achieve the best possible effects.

### **3. The basic principles of the early recognition system implementation**

When analyzing the literature and the research by various authors, we can indicate four fundamental principles which concern the ERS design and implementation. According to them, the system:

- should be designed and implemented on the strategic level,
- should be implemented as a formalized system,
- should actively involve the users,
- should be based on the organizational information system (Choo, 1998, pp. 203 -211).

The ERS goals, the areas of its product application, as well as the character of the implemented processes orient it strategically in the sense that the activities are of a long-term, integrative and cross-sectional character, and the future of the organization depends on the effectiveness of its functioning. ER cannot be treated as an insignificant, secondary organizational function that only organizations which are large and rich in resources can afford. In the turbulent conditions of the environment, organizations cannot remain

indifferent to changes in the environment, they have to possess some knowledge about them, and competences related to the early recognition of the changes carried by weak signals become a necessary (at least) condition of maintaining the competitive position. It is particularly important for small and medium-sized organizations which have no reserve resources and a possibility to “get lean” in a crisis situation. For them, encountering a strategic surprise in numerous cases will mean bankruptcy. Small and medium-sized organizations have to rely on their knowledge about the environment and, owing to higher flexibility, win the fight for a competitive position with large organizations because large organizations can amortize the shortage of their knowledge with the possessed resources. Maintaining the dynamic organization-environment balance forces turning the key process securing decisions informatively into strategic activeness. For these reasons, a higher level of management should be a promoter of this system in the whole organization. ERS will be effective only when it acts in a continuous, not an incidental way, and because of this it should be treated as an investment (similarly to research and development) and although on an ongoing basis it consumes resources and generates costs, it can lead to a spectacular success of an organization as a result of recognizing one, specific, ground-breaking change in the environment (earlier than others). The investment should concern both people and the sources of information. Early recognition requires the involvement of all members of the organization, therefore, leadership should be located on the top management levels so that it could possess authority and power enabling the integration and coordination of actions and information flows. The strategic significance of ERS is constituted by the use of the system outlets in making and applying strategic decisions.

Moreover, the implementation of formalized, structured and continuous systems is necessary. Formalization is to ensure the qualities of permanence to ERS, its isolation from other systems and, to some extent, limit the freedom of activity to behaviours which are desired. Non-formalized ERS are just additional activeness to which free time is devoted, and implemented only when it is convergent with the interests of an individual, efforts are doubled and significant information may “escape” as a result of the occurrence of gaps in gathering and processing information. In fact, such an attitude results in the lack of knowledge on how the environment is changing and instead of building competitive advantage it becomes activeness with a vague aim, responsibility and benefits. Formalization should concern an organization of any size. Various authors pay attention to the fact that managers are naturally oriented to the recognition of changes and they only need organizational support enabling an improvement in the processes of gaining, interpreting and integrating information about the environment. A formalized system

means that the information processes base on organizational goals and critical information needs. A continuous system means that in an uninterrupted way information is gathered, networks of contacts and the base of knowledge are built. Obtaining information should be decentralized, and its processing should be centralized, so that it would be possible to integrate information, eliminating its doubling and maximizing effectiveness.

Decision-makers, as the ERS users, cannot be passive but they should actively co-create and co-participate in these systems, not only in the strategic sense mentioned before, but also in the operational sense, starting with the articulation of information needs and the context in which the information will be used, and ending with the generation of feedbacks. The users of the system are the focal point for them, these are their needs that initiate new information cycles, and each person and unit in the organization is a potential valuable detector of information and the source of knowledge. The organization is “flooded” with information from customers, consumers, suppliers, etc., therefore, everyone in the organization has to be aware of the value and significance of the information they obtain every day from the environment, and which they do not usually ponder. They have to be motivated to collect and process information because the lack of involvement on their part will lead to lower effectiveness.

A considerable amount of information needed for early recognition can be possessed by an organization in its resources, but it is usually dispersed information, and the employees possessing it are not usually aware of its importance and value for the organization. Due to that, they do not feel a need to share it. Since the information resources possessed by an organization and competences to obtain it within this scope are dispersed all over the organization, the processes which serve to obtain, process and spread strategic information have to be integrated with the information management processes in the whole organization to enable the implementation of the aforementioned actions in a systematic way. The construction of ERS and the integration with the organization information system should be based on one central point of the convergence of dispersed information in the whole organization (Gilad 1994, p. 170). The integration of the dispersed competences which support obtaining and analyzing weak signals creates a system able to recognize the key changes in the environment.

#### **4. The framework procedure of the early recognition system implementation**

To sum up the deliberations carried out so far, in the context of the tool subject to implementation within the organizational system, we can say the following things about ERS:

- it is an information system implementing information processes related to obtaining, processing and passing information focused on the needs for taking strategic decisions,
- it is a subsystem of the strategic management system, the area of the environment examination in particular, supporting informatively the implementation of the strategic controlling function (planning and strategic control) which facilitates the flexibility and adaptation in the turbulent environment);
- supports actions in the context of identifying opportunities for growth and implementing or redefining strategic goals, as well as provides top managers with information necessary to take more rational strategic decisions;
- on the basis of the identified future opportunities and threats which are communicated through weak signals, it predicts long-term changes in the environment and analyzes their impact on a possibility to implement the organization's bundle of goals;
- people, along with their capabilities of perceiving and interpreting information, are a key subject of ERS;
- the efficiency of functioning depends on the scope of the perception of the environment and the intensity and interpretation of the obtained information.

Taking the above into consideration, as well as the fact that ERS have to be planned and implemented systematically, the implementation of ERS in an organization should be an organized activity. The process of implementing the formalized system should include four major stages (preparation - designing-implementation - exploitation) which consist of partial tasks based on the analysis of the situation, requiring specific decisions to be taken:

- becoming aware of the real goals of activity and their mutual relations - by the management and the team members,
- planning the actions - planning the means and methods of operation adjusted to the goals and the conditions,
- winning and allocating resources - necessary to fulfill the goal or transform the conditions in order to achieve the goal with the possessed resources,
- implementation of the plan - systematic and consistent activities,
- inspection of the implementation - comparing the implementation with the adopted patterns and correcting the activities (Zieleniewski, 1979, p. 203).

The framework implementation procedure presented below (Table 1) is a set of key activities which must be undertaken within the framework of the



organized actions to bring about the effective implementation of ERS in an organization.

The first stage of this process is the preparation stage, the next one is the designing stage, then implementation, and the final one is the exploitation and improvement of the implemented system functioning. The main emphasis should be put on the first two stages, because the key issue to achieve success is its good consideration and preparation of actions (Bieniok, 2004, p. 57).

**Table 1.** The framework procedure of the ERS implementation

Stages	Characteristics
<b>I.</b> Preparation	<ol style="list-style-type: none"> <li>1) Making managers aware of the necessity to implement ERS.</li> <li>2) Defining the main goals of ERS.</li> <li>3) Audit of the ERS currently occurring in the organization.</li> </ol>
<b>II.</b> Designing	<ol style="list-style-type: none"> <li>1) Development of the ERS concept and design intent.</li> <li>2) Designing the ERS architecture.</li> <li>3) Defining methods, resources and budget necessary for the implementation and exploitation of ERS.</li> </ol>
<b>III.</b> Implementation	<ol style="list-style-type: none"> <li>1) Appointment of the ERS implementation team.</li> <li>2) Training the organization members on the essence, principles of functioning and their role in ERS.</li> <li>3) Conducting necessary changes in the organization (structural, process-related ones).</li> <li>4) The launch of ERS.</li> </ol>
<b>IV.</b> Exploitation	<ol style="list-style-type: none"> <li>1) Using information and knowledge generated by the system in the decision-making processes.</li> <li>2) Inspection of the ERS functioning.</li> <li>3) Suggestions of changes and constant improvement of ERS.</li> </ol>

The procedure is initiated by the top management, as a consequence of realizing a need to possess such a system and the will to implement it, according to the principle adopted before that it should be designed and implemented at the strategic level. The realization of these needs becomes a starting point to define the goal for which the ERS will be implemented, the functions it will fulfill and the set of tasks necessary to be performed to achieve the goal. The next stage should be a diagnosis of the present situation within the framework of the current ERS audit which should give an answer to the question about the scope, intensity and effectiveness of the currently implemented activities and should include, among others, the identification of the ERS users and their needs, the identification of the kinds and sources of the currently obtained information. Designing a specific organizational solution

in the form of the formalized system and defining the methods and resources necessary to implement ERS are the actions ending the preparation stage, after which the managers have the awareness of the currently implemented actions and are in the possession of the design of the formalized ERS construction, functioning and the way of implementation. The implementation stage begins with the temporary (until specific effectiveness of functioning is achieved) appointment of the team implementing ERS. The team should have adequate competences, necessary resources and authorization to carry out changes in the structure. At this stage, education and training of the personnel is extremely important, making them aware of the specificity of the system and the character of involvement expected from them. The implementation team introduces changes, assigns responsibilities and launches the first information cycles related to the perception and interpretation of information. The entirety is fastened together by the inspection which concerns the functioning, the way of implementing the tasks and procedures, as well as the internationalized information culture. The results of the inspection become a source of the suggestions for the improvements and this way the whole system is constantly improved.

## 5. Conclusion

The presented framework procedure of implementing and exploiting ERS enables the effective implementation of systematic solutions with reference to the early recognition of changes in the environment, it only requires the adjustment to the specificity of a particular organization. The ERS implementation and keeping it later “on the move” will allow the organization to find the place and the position in the chaotic environment, as well as to keep and improve its competitive position.

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# STAKEHOLDER MANAGEMENT AS AN EFFECTIVE TOOL FOR PROJECT SUCCESS

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## **Abstract**

*This theoretical paper will examine subject literature and will try to analyze how stakeholder management can increase the project success. The article provides background to the topic of stakeholders from the first usage of the term in 1963, supplemented by an analysis of project stakeholder management strategies. The article will provide the reader with insight to how one can increase the success factor of the project with the usage of appropriate stakeholder management tools. This article contributes to the body of literature by detailing about how project stakeholder management influences projects and their success. It is prepared as a response to an increasing role of projects, the influence of different stakeholders on the execution of projects and their own evaluation of project success factors. By analyzing the literature of the concepts and empirical research from 1980s till now, this article will provide the potential project agents (project managers, project teams, etc.) with a better understanding of the role of stakeholders in conducting successful projects. The literature reveals that effective stakeholder management is a critical success factor of projects as they should satisfy the needs of different groups of people in each part of the their lifecycle. The conducted analysis is a foundation for the future research about effective project stakeholder management and a base for additional research.*

**Keywords:** *stakeholders, stakeholder management, project, project management, critical success factors.*

## **1. Introduction**

Even though the field of project management has enjoyed significant interest of researchers, it is still not perceived as important as other fields of management or as a “real” discipline (Kwak and Anbari, 2009). Shenhar and Dvir (2007) have analyzed Harvard Business Review and found out that out of 7000 case studies published in it, only about 2% dealt with projects in general

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and only a few dozen were devoted to project management. In consequence, there are not enough case studies written with an aim to analyze the reasons for project failure thoroughly and in order to have deeper understanding of which factors have negative and which positive influence on projects. However, investigations into project success factors are especially important nowadays as a growing amount of work today is project-based. Projects help organizations achieve their goals and that is why studies into how to manage a project effectively are especially important. As more organizations base their activities on projects, more demand is put on ways of accomplishing a project successfully. Furthermore, stakeholders are not homogeneous; each of them has its own perspective of project success and understanding of the world. Studies show that their knowledge of critical success factors is limited and this shows that more research is needed about this subject, as a popularization of this discipline would benefit the practitioners (Davis, 2001). Project management specialists endeavor to reduce the number of failed projects and one of the directions of research should be stakeholder behavior as each project has various stakeholder groups who can influence the execution of the project at different stages. This article will try to analyze recent empirical research to find out whether and in what way stakeholder management can be an effective tool for increasing project success.

## **2. Who are project stakeholders?**

The word “stakeholder” can be connected with a legal term of a party that is given money or the right to manage a property until the owner is determined, while in business it is understood differently, as a person or a group of individuals, who are affected by the results of an activity. In this way, the stakeholders of an organization are those individuals who are affected, can affect or are interested in an organization, while project stakeholders can be described as those who are involved in some way with the project or who can be influenced by its execution or result.

Stanford Research Institute introduced the term “stakeholder” into the business world in 1963, where it was defined as “those groups without whose support the organization would cease to exist” (Freeman and Reed, 1983, p. 89). In literature, there are two tendencies in describing this term: the broad and the narrow one. An example of the former is by Starik (1994), who actually believes that anything, even a river can be a stakeholder as he defines it as “any natural occurring entity which affects or is affected by organizational performance” (p. 90). On the other hand, there are narrower definitions where stakeholder is usually described as “any identifiable group or individual on which the organization is dependent for its continued survival” (Freeman and

Reed, 1983, p. 91). Regardless of the definition one decides to choose, the most important stakeholders include employees, neighbors, government, clients, community, competitors and other organizations and in some cases even the natural environment and these vary across organizations. When narrowing the concept of stakeholders into only the project ones, the most important usually include the customer, project manager, users of the result of the project, project sponsor or project team and these also differ between projects.

It is usually very hard to predict the reaction of every stakeholder to the result of the project, and because of this they are seen as one of the largest uncertainties in projects. In order to decrease such, stakeholder theory is used to analyze who the stakeholders are and which of them can influence project success, while project stakeholder management is to understand the sources of uncertainty of stakeholders and find a managerial strategy to overcome these.

### **3. Project stakeholder management**

Project stakeholder management is an important part of strategic management theory (Cleland and Ireland, 2007). A lot of research has been done on the importance of project stakeholders as these can have a positive or negative influence on the project and thus it is essential for project teams to be able to maximize the positive influence and minimize any damaging behavior. According to McElroy and Mills (2003, after: Assudani and Kloppenborg, 2010, p. 70), project stakeholder management “is the continuing development of relationships with stakeholders for project success” which means that there is a correlation between one and the other and a skilful project manager should be able to manage them in such way that they would contribute to the project whenever needed.

In order to be able to manage different groups of stakeholders, a thorough analysis of them should be conducted. The most common way of identifying stakeholders of a project is to categorize them into different segments by their different level of influence on the project or involvement/position in the project. These categories can be adapted to the needs of the specific project or a project manager can classify them into general groups as Briner, Hastings and Geddes (1996), who used four groupings in their analysis: client, project managers organization, outside services and invisible stakeholders. Stakeholders can also be divided into groups by their type: project participants (those who actively take part in the project through its lifecycle), communication participants (those who are influenced by the project execution and implementation), and parasitic participants (who have indirect stake in the project) (Nguyen, et al., 2009). According to a very famous division of stakeholders by Pinto (1996), they can be external, so outside of the project (clients, government, ecologists,

competition) or internal, who are within the project organization (project team, the management of the organization doing the project). It is also useful to categorize the stakeholders into primary (or direct) and secondary (indirect) ones. Primary ones are those groups which have some kind of a responsibility in conducting the project while direct are those that directly participate in the execution of the project. Secondary or indirect stakeholders, on the other hand, are those that do not participate in the project directly (similar to parasitic participants).

The project deliverables and outcomes influence stakeholders, while these during the whole project lifecycle influence the project. The most basic project lifecycle is usually divided into four stages: formation, planning, execution, and close-down, and each of them poses different stakeholder management challenges for the team. In the first and second part, the choice of the stakeholders is of critical significance, as it is much more difficult to adapt the project to the needs of stakeholders after it has reached the execution stage. This is why the project manager must identify stakeholders, engage them in the project and establish an initial bond at the beginning of the project lifecycle. At this stage, the stakeholders themselves have the biggest possibility of affecting the goals and execution of the projects, as in general the level of their attributes (urgency, power and legitimacy) is the highest at this stage (Mitchell, et al., 1997). Knowledge about the project should be shared with them while ideas, expectations and goals should be negotiated. During the planning phase, the project manager should create awareness about the project delivery and outcomes and build a relationship with them, putting special attention to key stakeholders. During the execution stage, a follow-up of the stakeholder management should be performed and relations built with any new stakeholders while old ones sustained. During the closing of the project, disengaging activities should be held with the project stakeholders. This is where the project manager must verify that all the stakeholders that are engaged in the spreading the result of the project understand their roles, as these will be the individuals who will distribute the benefits of the project.

In order to effectively manage stakeholders, the project team should be aware of the exact tasks and targets of each stage of the project lifecycle as well as understand the nature of the clients' organization and the regulatory framework of all project related assignments. Goals and general planning of the project should be executed with keeping different stakeholder objectives in mind. Sutterfield, Friday-Stroud and Shivers-Blackwell, (2006) have developed a nine-step framework which shows the cyclical pattern of stakeholder management which can be seen on Figure 1.





**Figure 1.** Project stakeholder management strategy framework

Source: Sutterfield, J.S. et al. (2006), p. 33.

The figure above illustrates the nine steps of project stakeholder management from identifying the mission and vision through the feedback. It shows that even steps such as “Identify Project Vision & Mission” or “Conduct Project SWOT Analysis” which at a first glance do not seem connected with stakeholders do have some influence on stakeholder management. With the use of this framework, project managers can assess each stakeholder together with situational aspects and in this way decrease the risk of conflict while increasing the benefits and opportunities set by different stakeholder groups.

#### **4. Project critical success factors: an emergence of stakeholder power**

The topic of project success has been receiving scholarly attention for the past thirty years and throughout this time it has matured greatly. Back then, studies about this topic were generally quantitative, based on simple formulas, while it was believed that it could be measured against an objective set of criteria. In 1970s, researchers assessed whether the project was accomplished during the implementation stage and according to Freeman and Beale (1992,) success was mostly based on the performance of individuals that took part in the project

measured in subjective and objective methods. This is why most literature of that time suggests that the foundation of project success was achieving the technical aspects of the implementation, not soft skills like, for example, communication with the customer of the project (Jugdev and Muller, 2005). It was only in 1980s and 1990s that the researchers started examining the customers' viewpoint instead of just the technical aspects as a measurement of project success (Pinto and Slevin, 1988). Nevertheless, in general, it was believed that the main stakeholders influencing project success were the manager and the team while other stakeholders were neglected (Anderson, et al., 2004).

Researchers today realize the complexity of the term with at least five interrelated dimensions: technical, economic, behavioral, business and strategic. Even in our times, one set of criteria that a project must achieve to be called "successful" does not exist but the 21<sup>st</sup> century did bring new ideas into science about what project success is. Now it is believed that it is determined by short-term project lifecycle rather than strategic goals of the organization while it is attributable to the project owner and sponsor. Future studies on what factors can increase project success as per stakeholder perceptions will provide more insight into this topic, but at the current stage a successful project can be described as "realization of the strategic objectives of the client organization, satisfaction of end users and satisfaction of other stakeholders" (Ika, 2009; after: Assudani and Kloppenborg, 2010, p. 67).

Pinto and Slevin (1987) have attempted to categorize main project success factors, some of which do have elements of stakeholder management, which include:

- project mission defined;
- support from top management;
- detailed schedule and plans;
- consultation with client and his acceptance;
- suitable team members;
- technical expertise;
- monitoring of the project;
- on-time communication with main players;
- the skill to deal with unexpected situations within the project.

It is not easy to say that every project that is finished within the time frame, within scope and budget is a successful one, there are examples where projects have met this criteria but were failures when, for example, the project product does not solve a problem it was meant to. This is why there should also be a distinction between a successful project process and its product (intended level of client satisfaction reached, whether it benefits the end user, whether it allows better competing with competitors, gaining a new market

share, ability to use an upcoming opportunity). This is why nowadays project success is broken into three dimensions: process (meeting budget, scope and time requirements), product (benefits for the end user, meeting client needs) and organizational success (business and strategic benefits). Shenhar and Dvir (2007) believe a project can be successful when it fulfills five criteria: efficiency, impact on the team (team satisfaction, building new skills, motivation, etc.), customer impact, business success and preparation for the future. This means that two of these criteria can only be accomplished with the use of effective stakeholder management. Westerveld (2003) developed this thought and concluded that project success is only measured by stakeholders: by client appreciation, project team, users, contractors and any other interested parties. Furthermore, project can reach different levels of success and thus can be seen as a pyramid. Firstly, meeting the project goal and client expectations is at the bottom of the pyramid as this is the main criterion which must be met for the project to be called successful. Then the second level is finishing the project on time, within budget and scope. The next level of project success is meeting internal organizational criteria while at the top and hardest to achieve is observing external relations.

Turner (2004) set up four main criteria for a project to be called a successful one, all of which include project stakeholders: the criteria of the success of the project should be agreed upon with stakeholders before and during the project lifecycle, there should be active collaboration between the project manager and sponsor, the project manager should be given the right to take action when unforeseen circumstances appear, while the project owner should monitor the performance aspect of the project. According to Nguyen, Skitmore, and Kwok Wai Wong (2009) accomplishing a project is based on satisfying stakeholders as “the success of the project depends very much on fulfilling their needs and expectations” (p. 1129).

Project success can also be evaluated according to different stakeholder perceptions. One stakeholder group may perceive a project as a successful one while another as a failure. Such a situation happens, for example, in infrastructure projects, where ecologists may have a different view upon it as opposed to the future users. The same happens when project managers see it as success because it was finished within the estimated period, scope and budget while the end users may not find the project beneficial. Managers of the organization in which a project takes place may see success as the amount of profits the project brings, while the technical team may see success as the functionality and innovativeness of the product. This is why one of the reasons stakeholder management should be used as a tool to increase the chance of project success is by understanding how each stakeholder perceives success and tries to satisfy his or her expectations.

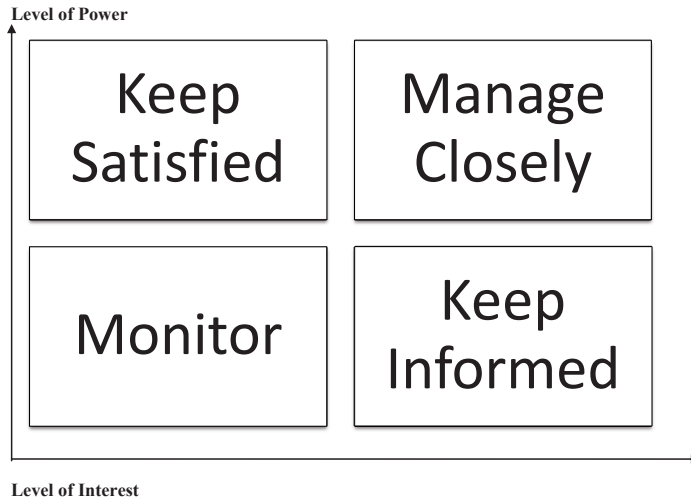
There are a number of factors by which stakeholders influence the project. One of the most widely known is the “power” influence. Dahl (1957, after: Mitchell, et al., 1997, p. 865) explains power as “a relationship among social actors in which one social actor, A, can get another social actor, B, to do something that B would not otherwise have done” and this definition fits also into the notion of stakeholder power. Project stakeholders can possess three types of power: positional, resource and expert. The next factor is legitimacy, which is seen as a prerequisite for a successful transaction with different stakeholders. It is conceived as “a generalized perception or assumption that the actions of an entity are desirable, proper or appropriate within some socially constructed system of norms, values, beliefs and definitions” (Suchman, 1995, p. 574). In short, legitimacy is a reflection of contractual relations, as well as legal and moral rights in the bond between the project and the stakeholders. The third factor is urgency and with this attribute stakeholder groups may put pressure on the project team to take some emergency action. Urgency is the level at which the stakeholder calls for instant attention. They use this feature when their feelings are so strong they decide to act. The next is the proximity factor or the amount to which the stakeholder is involved in the project. It is advisable to rate the proximity of each stakeholder – from stakeholders which are directly involved in everyday life of the project to ones that are distant from the project. The relationship between the project and the stakeholder is often driven by vested interest, as stakeholders could have such for a number of reasons such as: political, environmental, opportunism, etc. These factors are very important to project success as there can be stakeholders which are in the case of proximity very far from the project but have large power to influence the project.

In this way, in order to maximize the possibility of project success, project managers must categorize stakeholders in order to develop beforehand the responses to the possible actions of each stakeholder group. Much research has been done on the possible ways of calculating the influence of stakeholders on projects to enable teams to manage them more successfully. Nguyen (et. al, 2009) have set up an equation to calculate stakeholder impact:

$$I = P + L + U + K + D$$

Stakeholder impact in this theory is equal to the sum of stakeholder power (P), legitimacy (L), urgency (U), level of knowledge (K) and the degree of proximity (D).

One technique of managing stakeholders is shown in Figure 2 where the relationship between the project team and the different groups of stakeholders is mentioned according to their power and interest levels.



**Figure 2.** Power and interest grid for stakeholder management

This figure shows that on the one extreme, the project team should monitor stakeholders that are low in both interest and power but on the other side, those groups with high power and interest should be managed closely. The other stakeholder groups should not be neglected, either. Project managers must keep the interested stakeholders continually informed about the proceedings of the project while those individuals with a high level of power but uninterested in the project itself should be satisfied in order for them not to influence the project negatively.

Table 1 specifies critical success/failure factors for different stakeholder groups from empirical research with ones that involve stakeholder management distinguished in bold.

**Table 1.** Project success and failure factors for the project stakeholders

Project Stakeholders	Success and Failure Factors
<b>Investor or owner</b>	Clear and accepted purpose Specific plan <b>Open communications</b> <b>Stakeholder endorsement</b> Project execution cost <b>Interested owner</b> (Jacobson and Choi, 2008)
<b>Project executive or project sponsor</b>	<b>Open communications</b> <b>Political support</b> (Jacobson and Choi, 2008)

<b>Project Stakeholders</b>	<b>Success and Failure Factors</b>
<b>Consumers</b>	Clear specifications <b>Open communications</b> Acceptance (Pinto and Slevin, 1988)
<b>Operators/users</b>	Clear specifications <b>Commitment</b> <b>Open communications</b> (Jacobson and Choi, 2008)
<b>Project manager and project team</b>	Clear and accepted purpose Specific plans <b>Commitment</b> <b>Open communications</b> <b>Respect and trust</b> <b>Collaboration</b> <b>Political support</b> Expert advice and review Risk awareness Clear roles and responsibilities Leadership style (Pinto and Slevin, 1988)
<b>Senior supplier (design and/or management)</b>	<b>Open communications</b> Risk awareness <b>Respect and trust</b> <b>Collaboration</b> (Jacobson and Choi, 2008)
<b>Other suppliers (goods, materials, works, or services)</b>	<b>Commitment</b> <b>Open communications</b> <b>Respect and trust</b> <b>Collaboration</b> (Jacobson and Choi, 2008)
<b>Public</b>	Transparency Accountability <b>Community outreach</b> <b>Political support</b> (Jacobson and Choi, 2008)

Source: Turner, R. and Zolin, R. (2012).

Based on the information provided in the table above, the following stakeholder management factors lead to project success, whereas the lack of them could cause project failure:

- open communications
- stakeholder endorsement
- interested owner
- commitment
- respect and trust
- collaboration
- political support
- community outreach.

Furthermore, some of the other factors are actually a result of ineffective or lacking stakeholder management such as risk awareness or clear and accepted purpose.

In order to have a successful project, project managers should also analyze the attitude of different stakeholder groups. In this way, the project team knows in advance which groups will have a positive and which negative influence on the project and consequently prepare yourself for the attacks and try to maximize the positive support. McElroy and Mills (2000) have categorized stakeholder attitudes into five groups: active opposition, passive opposition, no commitment, passive support and active support. Many studies, such as Bourne (2006) or Milosevic (2004) show that the success of a project is partly based on the identification of stakeholders, understanding their needs, creating mutual relationships with them, and preparing and exploiting resources to satisfy their needs. In order to keep the project on track, project teams must identify all stakeholders, create relations, fulfill the expectations of the most important groups, and communicate with the stakeholders in an effective way. If these points are not introduced into the project, the likeliness of project failure increases greatly. A permanent identification and prioritization of stakeholders throughout the project lifecycle is considered as good practice. At many instances, it is only possible to judge whether the project is successful or not, only after a few months or even years after it has been completed, thus project managers to ensure project success, must already manage stakeholders during the project to be able to identify what these individuals will consider as success in the future.

Many researchers have underlined the importance of stakeholder management and how this has become an essential soft skill for a successful project manager (Crawford, 2005; Winter, Smith, Morris and Ciemil, 2006). As previously noted the maximization of the positive influence of stakeholders and minimizing the negative is a way of enhancing the project success rate. Three recent empirical studies on this subject have proven that involving stakeholders into the project is one of the factors causing project success (Chan and Chan, 2004; Dainty et al., 2003; Wang and Huang, 2006).

Monitoring stakeholders can allow the project team to detect a hidden stakeholder, which, if ignored, can have a disastrous influence on the project. The sooner such stakeholder is identified, the sooner a plan can be made to manage such individual or group. Furthermore, separate stakeholder groups have distinct interests and power during the different stages of project lifecycle. With the tools of project stakeholder management, these can be properly treated and their actions reacted to. Jugdev and Muller (2005) argue that one of the success factors of projects is to agree upon the success criteria with the stakeholders a few times during the project lifecycle while a collaborating relationship should be built between the different stakeholder groups and the project manager. Ika (2009) believes that the success of a project is multidimensional, uncertain and reliant on stakeholders. Studies show that

project success is clearly tied to effectively communicating and managing relationships with the various stakeholders of the project (Assudani, 2010).

Stakeholder management can even reduce paperwork and thus project time and success rate as the usage of communication tools between participants leads to a better coordination of the project which as described above is one of project success factors. There are many other habits, which are part of effective stakeholder management, such as proper use of charters and communication plans or soft skills of project manager to be able to build relations with stakeholders such as the ability to motivate, empower or to resolve conflict.

In order to have successful projects, leaders must remember that stakeholders nowadays have the biggest ever amount of knowledge due to an easy access and spread of information. In this way, the more information the stakeholder groups possess, the more ultimate influence they have on the project. McElroy and Mills (2000) have underlined that this knowledge can range from total ignorance to full awareness of the project. Stakeholders can gain information about the projects from hearsay and gossip rather than true validated information. Thus, in order to have a successful project, it is essential to be sure that truthful information is spread about the project and any misleading information leakages must be avoided.

Based on extensive research, Beringer, Jonas and Kock (2013) have proven that stakeholder management is even a critical success factor in project portfolio management. Moreover, Lycett Rassau and Danson (2004) have demonstrated that stakeholder management is the basis also for program management. Furthermore, there is strong evidence in literature that there is a connection between effective stakeholder management and the performance of a project (Donaldson and Preston, 1995). By definition, a project should also reach acceptable ethical and sustainability levels to be considered successful and ignoring individuals who are influenced by it can be considered as a failure to reach such project targets.

One of the main benefits of project stakeholder management is decreased risk. If the project team is able to identify stakeholders and analyze their needs and expectations, this will enable the team to predict any action from these individuals aimed negatively at the project and have a plan not to allow it to happen. When such risks appear in a project, like when Złote Tarasy construction was stopped halfway through the project because of protest of a co-called “Friendly City” association, it is possible to say that the team made an inadequate analysis of how their decisions can affect the interests of others. Insufficient communication with the stakeholders of the impact of the project leads to conflict and disputes and possibly slowing the project down. Especially in large infrastructural/real estate projects where the change in landscape is quite large, some people will be resistant to such change because



they have been accustomed to the way it was previously. Based on an analysis of the extensive body of literature Mohan and Paila (2013) concluded that the two essential ingredients of reaching project success are: high performance teams as well as effective stakeholder management. On the other hand, the lack of or ineffective stakeholder management can lead to delays and/or going over budget because of controversies or disputes.

## **5. Conclusion**

To sum up, judging on some definitions of the term project as a temporary partnership of stakeholders coming together to create something new, stakeholder management is not only a critical success factor for project success but an inevitable part of any project. In the most recent edition of Project Management Body of Knowledge Guide, one of the project management methodologies, a whole new 10<sup>th</sup> knowledge area was added about stakeholder management which shows that more emphasis than ever is put to this subject. Even though there have been many studies done on project success, there is still no one unified criteria which a project must meet in order to be considered successful, which makes it harder to analyze stakeholder management as a success factor. In the past, it seemed that a project was successful when it reached cost, quality, scope and budget limits, but even so there are many examples where the project has not met those but still is considered as a success whereas some projects met all three but still but left the client unsatisfied. An example of the first is the Sydney Opera project, which was finished with an 8 year delay while costs have greatly exceeded the initial budget. The building, however, met other success factors and today not only serves as an opera but it is one of the main attractions and symbols of the city.

It is evident, though, that stakeholder identification and prioritization as well as building relationships with the stakeholders are the essentials of effective project management and thus, achieving project success. There is no doubt that effective dealing with stakeholders is essential to projects as it is them who need to be satisfied and who possess power and influence and thus largely shape the planning and result of the project. Based on the findings of this article it is possible to agree with Bourne and Walker (2005) who have argued that “the ability to understand the often hidden power and influence of various stakeholders is a critical skill for successful project managers. Without attention to needs and expectations of a diverse range of stakeholders, a project will probably not be regarded as successful, even if the project manager was able to stay within the original time, budget and scope” (p. 650). There is still, however, the need for further research on the topic of stakeholder management as a way of tackling possible project failure problems as, for example, no

study has still been done on trying to find a relationship between stakeholder responsibilities and cost overrun.

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# NEW PUBLIC MANAGEMENT AS A RESPONSE TO EXPECTATIONS OF THE SOCIETY TOWARDS THE CIVIL SERVICE

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## **Abstract**

*The high dynamics and complexity of the changes in the environment are making it necessary to implement continuous changes in different areas of the activity of modern organizations. Changes also occur in the functioning of the civil service and, according to the concept of New Public Management, they concern the implementation of management methods and techniques used in the private sector. An important factor determining the changes implemented are the expectations of the society. The article presents an implementation of the concept of New Public Management aimed at increasing social expectations as exemplified by the Strategy of Human Resources Management of the Civil Service and other internal documents.*

**Keywords:** *civil service, customer orientation, New Public Management, Human Resource Management*

## **1. Introduction**

Since the creation of public administration, the issue of its role, organization and the scope of authority and responsibilities have been widely discussed around the world. Throughout history, as a result of political changes, public administration has been subject to numerous transformations (Zawicki, 2011, p. 16). These changes in public administration are expressed e.g. by the concept of New Public Management (NPM) established at the turn of the 1990s, whose main idea is the implementation of business management methods and techniques used in the private sector to the activities in the public one (Hood, 1995, p. 97, as cited in: Ochnio, 2012).

Regardless of the changes being made, performing a menial role towards the society shall be the factor constituting the rise and functioning of the public administration (Zawicki, 2011, p. 16), which is what civil servants in particular have been appointed for.

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H. Izdebski indicates that the functioning of modern public administration is not possible without a bureaucratic system, which is part of the civil service (Izdebski, 2007). According to the Constitution of the Republic of Poland, the Civil Corps was established “in order to ensure a professional, diligent, impartial and politically neutral discharge of the State’s obligations” (Article 153 item 1 of the Constitution of the Republic of Poland, 1997). The task of the civil service in Poland is to create a modern state, to improve the efficiency and effectiveness of its organs and to ensure the citizens’ satisfaction ([http://dsc.kprm.gov.pl/sites/default/files/sluzba\\_cywilnapodstawowe\\_informacje\\_v\\_6\\_06\\_2013.pdf](http://dsc.kprm.gov.pl/sites/default/files/sluzba_cywilnapodstawowe_informacje_v_6_06_2013.pdf), access: 3.5.2014). The functioning of the civil service in Poland is regulated by the Act on the Civil Service of 21 November 2008, under which the corps of civil servants is composed of employees under a contract of employment and civil servants employed by an appointment in the government (Article 3, Law on Civil Service, 2008).

The purpose of this article is to propose ways to implement the reform of New Public Management, with particular emphasis on the postulate of customer orientation in the Polish civil service in the area of human resources management. The implementation of this objective will be made through:

- Presentation, based on the literature, of the assumptions of New Public Management associated with the change in the expectations of society and the controversy surrounding its practice;
- Implementation, indication of NPM components implemented in the civil service by analyzing source materials: information from the website of the civil service and internal documents, i.e. Strategia Zarządzania Zasobami Ludzkimi Służby Cywilnej, Zarządzanie w służbie cywilnej – poradnik praktyczny, Vademecum pracownika, documents of the Department of the Civil Service of the Office of the Prime Minister etc. References to the assumptions of the New Public Management implemented in the civil service were also recognized in the Law on Civil Service of 21 November 2008 and the Constitution of the Republic of Poland.

Given the theme of the conference, it was intensely sought to reveal aspects related to the implementation of one of the assumptions of the concept of New Public Management – the postulate of customer orientation. Therefore, it was assumed that the requirements of customer orientation were dominating in the concept of NPM, which lies at the source of their creation.

## **2. The increase in the expectations of the society as a basis of the concept of New Public Management**

The origin of the concept of New Public Management was the ineffectiveness of traditional, hierarchical and highly formalized Weberian administration and processes, which began to occur in the economies of Western countries in the second half of the twentieth century. This period was accompanied by a rapid development of the mass media, and phenomena such as the intensification of competition, the growth of political consciousness of citizens and universal access to information witnessed in the growth of expectations of the society towards the public administration. The result of these developments was the growing participation of citizens in the exercise of public power by creating social organizations and associations in Western Europe. In these countries, societies were also critical of the size of the public sector (Hausner, 2002, p. 48-62, as cited in: Ochnio, 2012) and the concept of state intervention by J.M. Keynes and related high levels of public spending, accompanied by an increase in employment in the public administration (Musialik, 2011, p. 496, as cited in: Ochnio, 2012). In response to the impact of economic, social, political and technological factors, the implementation of the NPM reform was launched (Larbi, 1999).

New Public Management reforms in various countries were carried out in a different manner. The first reforms were implemented in 1979 by the government of Margaret Thatcher in Great Britain. The concept was later realized in Australia and New Zealand in the 1980s, and since the early 1990s – also in the United States (Dunsire, 1995, p. 17, as cited in: Supernat, 2004). The driving force behind the implementation of the concept of New Public Management in the United States was striving to improve the functioning of the public sector as a result of the public criticism towards the organization of public administration expressed in studies (Osborne and Gaebler, 1992, as cited in: Supernat, 2004).

B. Kudrycka indicates that “substantially all Western European countries have implemented (for better or worse) the principles of New Public Management, [and thus] it seems imminent and unavoidable that these principles will be implemented in Poland” (Kudrycka, 2001, p. 405, as cited in: Supernat, 2004). References to the assumptions of the NPM concept can be found in the Polish government documents (National Development Plan 2007-2013, as cited in: Ochnio, 2012). In Poland, in the spirit of the New Public Management e.g. local government reform was carried out in 1999 (Ochnio, 2012). Currently, the concept of New Public Management has an equally strong impact on the operation of the Polish civil service, as evidenced by the analysis carried out using internal documents of the Ministry of Defense.



### **3. Implementation of components of NPM as exemplified by the document Strategy of Human Resources Management of the Civil Service and other internal documents**

The empirical research performed in the Ministry of Defense in 2009 and an analysis of internal documents, including the Strategy of Human Resources Management of the Civil Service, showed that in the civil service of this institution, a broad spectrum of components of NPM was implemented. The methods of implementation of values characteristic of the concept of New Public Management in the civil service in the Polish Ministry of Defense in the political and organizational dimension can be considered as follows:

- The postulate of separation of politics and administration was included in the Law on Civil Service of 21 November 2008. Article 1 of the Act indicates that the Civil Service shall be established in order to “ensure a professional, fair, impartial and politically neutral discharge of the State” (Civil Service Act, 2008). The function of the Civil Service is to enable the proper functioning of the administrative apparatus of the state, regardless of the political situation and changes of governments (<http://dsc.kprm.gov.pl/system-sluzby-cywilnej>, access: 28.04.2014);
- Improving public services, the results of which should include actual changes in people’s lives, unlike the previously advocated “production of services” (Supernat, 2004) and to reduce their cost and optimize the use of human, material and financial resources (Hood, 1995, p. 496, as cited in: Ochnio, 2012). The Polish civil realization of this demand took to improve the quality, efficiency and effectiveness of public service delivery through the development of desirable attitudes and behaviors of participants of the organization using the Strategy of Human Resource Management. One of the values of the civil service is “to be effective and creative, to provide a quality service and effectively use available resources” (Zarządzanie w Służbie Cywilnej – poradnik praktyczny, 2002, p. 3). The primary duties of a member of the civil service, beyond the respect for the Constitution and legal standards and care for the interests of the state include reasonable disposition of public funds, competent, independent, efficient and planned implementation of tasks (Węglowska, 2007, p. 108). This reflects the orientation of the effectiveness of actions taken. Improving the quality and efficiency of work processes to serve the human resource management, periodic assessment (Potyrało, 2007, p. 96) and training (e.g. adaptive training – the employee’s manual *Vademecum pracownika*, which allows for building model attitudes and standards in internal and external customer service – called “professional civil service”);



- The priority of the customer whose needs must be identified and addressed. The foundations of this approach were created in 1936 by the administration theorist Marshall Dimock, who saw that “consumer satisfaction is equally the task of public administration and business” (Lynn, 1996, p. 86, as cited in: Supernat, 2004). In the Polish civil service, this demand has found a wide application ranging from identifying customer needs, training office staff and customer satisfaction research. One of the measures is to announce to the public via the office’s website, what desirable employee features are, such as: competence, integrity and friendliness to the customer of the state office (<http://dsc.kprm.gov.pl/system-sluzby-cywilnej>, access: 28.04.2014). An interesting direction in responding to the needs of customers is the provision of public services electronically, through the so-called virtual administration, which in the Polish civil service includes the following stages: online information and one-way communication. The first of these stages involves the possibility of obtaining information about the office on its website, and the way interaction is to provide access to official forms on the website of the office. The next stages of electronic services include two-way interaction and transaction making (Zawicki, 2011, p 65);
- The focus on results has been used in the civil service in the area of personnel policy through the use of an integrated system of employee evaluation. To enable to use of this tool, evaluation criteria are determined, referring to expected results and affecting remunerations (Zawicki, 2011 p. 50, 65, 66). It should be pointed out that the remuneration system comprising of the base salary, a special bonus and a bonus for long term service (Article 90 item 1 of the Law on Civil Service) does not correspond to the assumptions of NPM assuming that the salary should depend on economic indicators (Ochnio, 2012);
- The limitation of the hierarchy is made by flattening organizational structures and reducing the management levels (Zawicki, 2011, p. 67). In the civil service it is associated with improved quality, efficiency and effectiveness of public services. It is indicated that the provision of a quality service for the government and society, along with reducing bureaucracy, is to contribute to the improvement of the Polish position in Europe and the world;
- The use of methods and techniques of strategic planning and management. An example is the formulation of mission: “Serving the citizens, we effectively perform the tasks of the state. We act professionally, fairly, impartially and politically neutrally,” and the vision of the civil service: “the Civil service enjoying social trust guarantees that the key actions for the functioning of the state

- are made” ([www.niepelnosprawni.gov.pl/.../sluzba\\_cywilna\\_w\\_polsce\\_0.pdf](http://www.niepelnosprawni.gov.pl/.../sluzba_cywilna_w_polsce_0.pdf), access: 5.05.2014);
- Directing in a managerial way: the powers of the Directors-General in offices are inherent in the assumptions of the concept of New Public Management, covering coordination of the work of offices, delegating tasks to employees and exercising care over their relevant training (Pryciak, 2011, pp. 102, 105-108). Providing competent leadership and effective management, along with an appropriate delegation of tasks at all levels of the civil service belong to its fundamental values (Zarządzanie w Służbie Cywilnej - Poradnik praktyczny, 2002, p. 3). The independence of qualification procedures and a high level of civil servants competences are also the aim of the National School of Public Administration (Ochnio, 2012);
  - The flexible personnel management, including the use of organizational solutions used in the private sector, includes:
  - The abandonment of the career system (promotions awarded by decision of the leaders, conditioned by seniority and special achievements) to a positional system (establishing the employment relationship on the basis of competitions announced for a position) (Hausner, 2002, p. 50, 51, 67, as cited in: Ochnio, 2012). The principles of recruitment to the civil service in Poland are “openness and competitiveness” (Article 6, Law on Civil Service, 2008). Openness refers to universality, transparency and equality in applying for employment in the civil service, along with the need to ensure proper recruitment procedures (such as an obligation to publish a notice of the call and its result, prepare a protocol and the selection of such a candidate who is the best guarantee for successful execution of their future tasks). The competitiveness of recruitment is expected to provide uniform principles, methods, tools, evaluation criteria, and immutability of the requirements specified in a vacancy notice. In addition, recruitment to the civil service should be characterized by independent persons engaged in recruitment, along with objectivity and the promptness of the action taken. Efficient, objective and fair recruitment process in the civil service is to enable the proper performance of the tasks of the state outlined by the constitutional vision of the civil service and to contribute to the creation of a positive image of the civil service, thus fostering a bond between citizens and the state, based on trust in the rightness of the actions of the state (<http://dsc.kprm.gov.pl/nabor-do-sluzby-cywilnej>, access: 29.04.2014);
  - Dropping the consideration of formal powers in favor of increasing the importance of experience, along with hard and soft competences (Kwiatkowski, 2011, p. 51). This is confirmed by the use of the Assessment Center method in the recruitment for strategic positions

in the civil service, which is to assess the level of competence accepted as necessary for a particular job. The development of practical skills is realized by carrying out central training aimed at producing team skills and disseminate the highest, uniform labor standards (Strategia Zarządzania Zasobami Ludzkimi Służby Cywilnej. Służba cywilna profesjonalisci w służbie obywatelom, 2006, p. 6). Implementation of the idea of empowerment, conducive to teamwork and allowing employees of public administration to take on initiative and express creativity in order to better meet the needs of consumers and achieve better results (Supernat, 2004).

- Assessing activity in the civil service in particular is aimed to ensure the adequacy of employee qualifications for the positions occupied through the use of the Thomas International Method, which consists of the Personal Profile Analysis (PPA) and the job profile analysis (Professiogram/Psychogram). Also a computer system (SZOCK) is used which allows one to check the level of competence development of employees. Competency assessment is based on a “competency test” and a “self-test” (Potyrało, 2007, p. 99);
- Promoting ethical behavior through the creation of standards defining ethical behavior of civil servants, codes of ethics and codes of conduct (Ordinance No. 70 of the Prime Minister of 6 October 2011 on the guidelines for compliance with the rules of the civil service and on the ethical principles of the civil service); providing training in this area and ensuring proper working conditions, influencing the attitudes of civil servants;
- Changes in organizational culture. The organizational culture of the public administration should be characterized by flexibility, reducing hierarchies, innovation, problem solving and entrepreneurship, and, therefore, by solutions that are appropriate for adhocracy, which is the opposite of bureaucracy (Waterman, 1992; Handy, 1996, as cited in: Supernat, 2004). It is pointed out that, as in other countries, the civil service culture is a bureaucratic and legislative culture, which must be changed to keep pace with the rest of Europe (Strategia Zarządzania Zasobami Ludzkimi Służby Cywilnej. Służba cywilna profesjonalisci w służbie obywatelom, 2006, p. 6).

#### **4. Controversies concerning the postulate of customer orientation**

The concept of New Public Management and the practice of its implementation raise concerns and reservations among many researchers. The biggest objection of the experts in this field is raised by the demand of the public administration to be determined by the needs of consumers. The researchers suggest that citizens in the society cannot be equated with consumers, since

their participation in politics is not only to maximize individual interests, but also to solve common problems (Supernat, 2004). The use of market-based solutions to meet the needs of the society in which the market is not a perfect mechanism for allocation of resources, results in the limited possibilities of application of managerial approaches in the public sector (Jeżowski, 2002, pp. 14-15, as cited in: Krynicka 2006). Doubts also arise in terms of whether administration should be more accountable to the customers or to the entire public, and whether, as in business, they should diversify the customers according to their importance or treat them equally? These doubts make it necessary to refine the idea of customer orientation and define the limits of consumer proactive public administration (Supernat, 2004).

The reservations of critics of the New Public Management also apply to the postulate of using, by the public administration, of management methods and techniques normally used in business. This could lead to the recognition of certain expectations of citizens (preserving a historical site or landscape) as ineffective, uneconomical or impractical (Box, 1999, p. 55, as cited in: Supernat, 2004). There arises a risk of other values than effectiveness and efficiency being dominated or omitted by public authorities, and rising of behavior contrary to the ideal and values of the public service. In this context, it becomes important to isolate elements of the public sector and public service that should not be viewed and managed from a market perspective (Supernat, 2004).

According to B.G. Peters, the concept of New Public Management does not provide citizens with an equal access to public services. This is due to the varying quality of public services arising as a result of decentralization of public service delivery (Peters, 2001, pp. 305, 330-331, as cited in: Ochnio, 2012). There is also a contradiction between the postulate of homogeneity of public services and risk diversification for the decentralization of their provision (Supernat, 2004).

In the practice of public management, in addition a difficulty of ensuring the accountability of public officials in terms of decentralization and deregulation may occur, due to the fact that resource management efficiency can lead to a failure to set targets, which becomes a manifestation of irresponsibility (Supernat, 2004).

## **5. Conclusion**

The concept of New Public Management was founded as a response to the failure of the public sector and trends and phenomena taking place in the economies of Western countries, including the increase of importance of the political awareness of citizens (Hausner, 2002, p. 55, as cited in: Ochnio, 2012). As a result of these developments, the expectations of the public

towards the state administration have increased (Musialik, 2011, p. 496, as cited in: Ochnio, 2012), which resulted in making the reforms seen today to be characteristic of the concept of NPM.

The assumptions of the concept of New Public Management raise concerns among many researchers. They are associated, among others, with the legitimacy of implementation of standards used in the private sector in the public one, and with the possibilities of public administration operating based on the postulate of customer orientation. Despite these doubts, the concept of New Public Management has been reflected in a series of reforms being implemented in the Polish public administration as well. Today, many assumptions of the New Public Management can be seen in the functioning of the civil service in the country.

The Strategy of Human Resources Management of the Civil Service includes the following strategic priorities: “conscious leadership; the effectiveness and efficiency of operation; continuous improvement of the image of the civil service; motivating and rewarding employees according to transparent rules; recruiting and retaining the best employees; planned training and development; coping with change; effective internal communication.” The priority of conscious leadership means that the involvement of leaders is considered to be decisive to ensure the highest quality of service at all levels of management, particularly at the highest one. The efficient delivery of services to the public and the state requires an optimal use of resources through the use of modern technology, methods of work and proper planning. Improving the image of the civil service is done, among others, through regular communication with the public, showing respect and providing a high quality of service, which all affect public confidence in the State. The key to ensure proper customer service is to improve the process of recruitment and selection, providing opportunities for development, a transparent system of promotion, fair evaluation and remuneration (Human Resource Management Strategy for the Civil Service, 2006, pp. 7-27). All of these priorities closely fit the assumptions of the concept of NPM, with its particularly pronounced demand for customer orientation.

The literature highlights the lack of clear results of the implementation of the New Public Management in Western European countries (Supernat, 2005). The researchers suggest that the implementation of the NMP components in the countries of Central-Eastern Europe should be tailored to the specific circumstances, due to the continuous development of the civil society and the rapid implementation of the processes of democratization after 1989. (Peters, p. 332, as cited in: Ochnio, 2012). The direction for further research could include determining a degree of compatibility between the assumptions of NPM and the Polish national culture.

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# EVOLUTION OF LEAN MANAGEMENT CONCEPT AND EVALUATION OF EXPERIENCE IN ITS APPLICATION

**Krzysztof Drabek<sup>1</sup>**

## **Abstract**

*The purpose of this article is to explain what lean management concept is and to evaluate its effectiveness from different points of view. The article attempts at evaluating the effect of using lean management, not only referring to economic impacts but also to other criteria. It also includes an analysis of hazards that may result from implementing the concept and in particular from its improper implementation. The author also points out gaps in the studies concerning lean management.*

**Keywords:** *Japanese methods, manufacturing management, lean management, lean manufacturing.*

## **1. Introduction**

Lean management is a relatively new concept, however, introduced by global business giants it shows that it brings the desired results and introduces new quality into the field of management. Expansion of the area of management causes creation of newer and newer Lean concepts. It allows a company to increase profits, reduce costs and be considered as a modern company. On the other hand, there are plenty of opponents of the discussed concept, as for example Gendo and Korschak, who criticize it. In the article the author tries to explain the lean management concept with reference to its beginnings and rules it is based on. The main purpose of the article is to study the consequences of lean management implementation in companies. The first part concentrates on origins of the lean concept as well as on rules of its application. The next part analyses positive and negative effects of implementing Lean concept and identifies risks that may occur during its implementation. The article ends with conclusions and indication for further research directions.

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## 2. The origin and the concept of lean management

Lean management is a concept connected with economical management of the organisation. It belongs to the family of newer concepts of small organisations management and it has found application in many branches of industry in the world, including: automotive, aircraft, food processing industry or in administration. Lean management concept comes from lean thinking philosophy that was introduced to management dictionary by Womack, Jones and Roos<sup>2</sup>, scientists from Massachusetts Institute of Technology. They were the first ones to use the term “lean production” (Lisiecka and Burka, 2011, p. 19). The first attempt to organise production as a set of subsequent operations were made in 1855 in Colt factory in Hartford, Connecticut. In 1915 Henry Ford fully implemented the term of “flowing productivity” (Jones, 2007, p. 73). Production in Ford factory in Highland Park was organised in such a way that each machine producing car parts was forming an element of one single flowing manufacturing process. Thus within a few minutes a finished product was created from rough casting. Lean management term is intrinsically linked with Toyota company, where the beginnings of conscious implementation of this concept may be found. Source of management system of TPS (Toyota Production System) dates back to 1890, when Sakichi Toyoda designed and patented a handloom. A partially automated handloom greatly improved performance of the employees and quality of products. However, Toyoda was still improving the handlooms and as a result he managed to design highly reliable, automatic looms, whose power source was combustion engine. Special attention should be given to an automatic stop system of the loom in case of a breakdown, e.g. thread break. It is the described mechanism that is treated as a starting point of Toyota Production System. In the 1930s the founders of Toyota, Sakichi Toyoda and his son Kiichiro, taking their inspiration from Ford issues, were working on their own version of flowing productivity in the automotive sector. As a result of these works they defined two frameworks that the TPS concept was based on (Lisiecka and Burka, 2011, p. 19):

- immediate stop of the line when defective product is noticed; in order to prevent damaged parts from getting into further stages of production (Jidoka rule),
- using pull system assuming that only such amount of parts should be created as it is needed for current production (defined as just-in-time). Later one more framework was added to the above that targeted distribution of work in a mixed production flow (defined as Heijunka).

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<sup>2</sup> Authors of „lean production” term, representatives of Massachusetts Institute of Technology (MIT), whose book is regarded as a peak in discussion over the reasons of Japanese car companies success on American market (Zimmiewicz, 2000).

This led to achieving production of different goods in small batches by means of simple tools described in technological description of manufacturing process. Toyota has progressed steadily and it has finally become the largest car manufacturer all over the world that encouraged other manufacturers to use its solutions. Lean production is a general version of the TPS system applied not only during production process but also in the whole Toyota business system, including product development, coordination of suppliers and relationship with customers. For many years Toyota Production System was unnoticed in management theory and practice. Probably the main reason of that was the fact that it was not formally documented until 1965. The first signs of interest in Toyota Production System appeared in connection with the first fuel crisis. In 1990 Womack, Jones and Roos, after many discussions about differences between American and Japanese automotive industry, published a book titled “The Machine that changed the World”. This book describes the phenomenon of Japanese car production system that proved to be a base of numerous “lean” systems and concepts. Currently Lean concept has evolved into different areas, e.g. lean office, lean and green, lean in healthcare, lean administration or lean accounting (Lisiecka and Burka 2011, pp. 22-24). Lean concept is successfully applied in banking, where each element of the customer service process is lean and improved despite the fact that in most cases full elimination of waste in this sector is not possible (Chlebicki and Siciak 2011, pp. 70-72). Lean management is also used during restructuring of companies (Nalepka, 1997; Kozłowski and Zakrzewska Bielawska, 2005; Bartusik and Cabula, 2006), including any changes in company regarding in particular changes of organisational structure and management process, working processes organisation or production and line issues (Marona 2005).

The essence of this method while restructuring large companies (e.g. state-owned enterprise, state enterprises) is continuous, slow but thorough leaning of a company as well as avoiding and preventing any waste (Bitkowska, Wojcik and Kolterman 2010, p. 115). Lean management term concerns the whole system of business, organising and management of product development, operations, suppliers, relationships with customers and general enterprise, which needs less human effort, less space, less capital, less materials, less time for goods production and services with fewer defects in order to meet the customers’ requirements in a more precise way in comparison to traditional management system. Lean management concept is based on a number of assumptions. The most important of them are described by K. Bartusik (2000, p. 96):

- combining high performance with quality of production,
- integration of tasks and functions,

- shortening of ways of information flow by making organisational structures flat,
- introducing far-reaching changes in the scope of business (the scope of changes may include the structure of property, methods of organisation and management, professional training, shaping the employees attitudes, organisational culture, etc.),
- reaching higher productivity and quality of work with less time, money and work,
- decentralisation of responsibilities and competences in connection with decentralisation of information system and self-control,
- arranging small organisational units working according to team structure,
- flexibility of organisational structure,
- creating appropriate atmosphere in organisation,
- continuous learning and improving of the organisation as well as its employees.

Lean management successfully used by different kinds of companies is characterised mainly by team work and it is the fundamental condition of this concept (Bartusik, 2000, p. 97). Collaborative decisions of all team members account for the fact that each of them is jointly responsible for company operations. Work in groups that are appropriately organised, e.g. by exchanging task between team members, allows each of the member to familiarize with and perform all kind of team operations. Another characteristic feature of Lean Management is application of quality control (Total Quality Control) modelled on Japanese concept ensuring that errors committed during assembly are eliminated (it is typical for production companies), error sources are searched at the place of their creation and the quality is differentiated and continuously improved according to the criteria defined by the customer. TQC is one of the most important issues connected with lean management, which is underlined by one of its originator, Taiichi Ohno. He said that production control system (kanban<sup>3</sup>) will not work in the areas where TQC does not work properly. Quality control has fundamental importance (Shimokawa and Fujimoto, 2009, p. 69).

Next feature of lean management is market based production, which means that the producers concentrate on regular customers, who are systematically “researched” in order to get information about current market trends. Collected information is taken into account while planning development of new products. Owing to this, the manufacturer has current information about requirements of the market and the customer gets products according to their specific expectations. The basis is direct cooperation

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<sup>3</sup> **Kanban** is a Japanese word that means sheet (board), ticket or sign. It is a tool for managing of material production flow of similar to Toyota production management type(Liker 2004)

between sellers and manufacturers. *Direct contact with suppliers* is one of the main characteristics of the Japanese concept as well. It is worth drawing the reader's attention to the method of carrying out research and implementation studies using *Simultaneous Engineering*. The concept of this approach is simultaneous involvement of all departments taking part in a new process of product development starting from the earliest stages, cooperating with each other and covering particular stages. In this approach, each operation is started with information coming from the previous operation and thanks to that the time needed for development and costs are reduced and quality improvement is achieved (Minguela-Rata, 2011, p. 81). Thanks to using *Simultaneous Engineering* there are some benefits like: parallel development of products and means of production, early market determination of crucial features of a new product, including into the new product development process development potential of the manufacturers of means of production and suppliers of these means (Bartusik 2000, p. 97). The next feature is *relating to flatness of the organisational structures (decentralisation) and delegating power of decision to the lower structures*. One type of decentralisation is delegation of powers that means authorising subordinates to make certain decisions, perform particular operations and devolution of responsibilities in matters belonging to the principal's competences.

Decentralisation of decisions brings several benefits, such as:

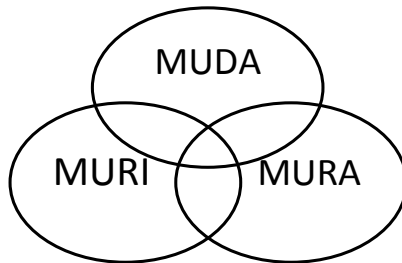
- greater flexibility in the context of market requirements,
- better knowledge of recipients and current transactions,
- greater efficiency in development and in implementation of innovations,
- better motivation of employees thanks to awareness of one's scope of activities and influence on company development.

Other features of *Lean Management*, which are also important, are (Lisiecka and Burka, 2011, p. 21]: *strong customer focus, constant improvement in the scope of kaizen<sup>4</sup>, use of continuous flow of materials or market orientation to producing goods in small batches*. The concept of *Lean Management* is very broad and includes all aspects of company functionality. For its proper implementation and functioning, new solutions must be accepted by the whole organisation (Trenker, 2011, p. 388). Managers and employees of Toyota use Muda term when they talk about any types of waste and are trying to eliminate it. There are two other "M" functioning in Toyota corporation and, despite the fact that they are slightly different, they are as important as the previous and the function as a whole in the form of "3M" (Figure 1). A document "The

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<sup>4</sup> **Kaizen** is a philosophy of striving for perfection and maintaining it everyday during production (it originates from Toyota production system) (Liker, 2004).

Toyota Way” refers to “3M”, that is **Muda**, **Muri** and **Mura** (Liker, 2004, p. 88).



**Figure 1.** Muda, Muri, Mura as a whole in 3M concept.

Source: Self-study based on Liker, K. J. (2004. pp. 114-115).

- **Muda**- in other words: waste, especially all activities that need labour input instead of creating value.
- **Mura** in Japanese means irregularity. It occurs when work of operator, machine or material flow is interrupted.
- **Muri** in Japanese means an excessive burden of employees, machines and processes. A signal denoting *muri* is exhaustion of employees, strange machine noises, etc.

In practice, implementation of the *Lean Management* assumptions is allowed by expanded collection of techniques and tools defined as *Lean Toolbox* in literature (Bicheno and Holweg, 2008). The most popular Toolbox tools are: 5S, Just-in-time, Kanban, SMED, Poka Yoke, TPM, Heijunka, Six Sigma, Jidoka (Bicheno and Holweg, 2008; Faron, 2011).

## **2. Efficiency and evaluation of *Lean Management***

There are many books describing activities that must be taken during implementation of the *Lean Management* concept but the realization of this concept requires a lot of time and work. It is a long process that needs consistency and outlay of appropriate means. Understanding of the need for change is also very important. This need must be understood both by management level and by employees who are lower in company hierarchy. However, it should be remembered that the discussed concept is only one of many concepts which may be chosen for implementation in the company. The choice of a proper method is dictated by both conditions in a company and effects that one wants to reach. *Lean Management* is chosen mainly as a concept that determines reduction of costs in a company. In order to check

this condition there is a need to test efficiency of lean management. Not only economical results of implementing this concept should be analysed but also other aspects.

In Poland, a relatively small amount of research on efficiency of *Lean Management* is conducted on a large scale in comparison to foreign analyses. Among the Polish thesis on efficiency of *Lean Management* studies of such authors like: Piasecka-Głuszak (2013), Nogalski, Szreder, Walentynowicz (2005), Walentynowicz (2013), Czerska (2009) may be highlighted. In order to analyse the efficiency of *Lean Management* the results of some studies were compared (Table 1).

**Table 1.** Comparison of the studies regarding *Lean Management* effectiveness

Source and remarks	Effects of Lean Management implementation
Nogalski B., Walentynowicz P. (2011) (In: Faron 2011)	<ul style="list-style-type: none"> <li>- reducing production area,</li> <li>- limiting the costs of production tooling even by half,</li> <li>- reducing production cycle by 40% on average,</li> <li>- reducing the number of defects by more than a half,</li> <li>- reducing the time of set-up by 40%,</li> <li>- reducing the need for staff by 30%,</li> <li>- ensuring much greater variety of goods,</li> <li>- getting significantly higher level of customer service.</li> </ul>
Czerska J. (2009)	<ul style="list-style-type: none"> <li>- growth of labour productivity by 180%,</li> <li>- growth of added value by 100%,</li> <li>- growth of sales by 200%,</li> <li>- growth of material rotation by 186%.</li> </ul>
Haus B. (2006)  (Studies conducted in 1994 on over 150 German companies)	<ul style="list-style-type: none"> <li>- reducing inventory, which leads to decreasing of involved capital by 40%,</li> <li>- shortening the time of adjusting the devices by 40%,</li> <li>- shortening the production cycle on average by 37%,</li> <li>- increasing productivity (within 2 years) by 35%,</li> <li>- reducing the need for staff (within 2 years) by 30%,</li> <li>- reducing absences from work due to a sickness to less than 3 %,</li> <li>- reducing the number of damaged products from 2,5% to 0,4%.</li> </ul>
Walentynowicz P. (2013)  (Studies conducted on 20 production companies in Poland over the period 2008-2011)	<ul style="list-style-type: none"> <li>- reducing inventory,</li> <li>- reducing the costs of manufacturing,</li> <li>- shortening the production time,</li> <li>- increasing the speed of reaction to market needs,</li> <li>- increasing the quality of products,</li> <li>- increasing staff motivation</li> <li>- growth of labour productivity,</li> <li>- positive impact on organisational culture,</li> <li>- increasing economic and financial effectiveness.</li> </ul>

Source and remarks	Effects of Lean Management implementation
Bożek M., Handzelewicz A. (2012)  (Studies conducted on American companies after II World War concerning employees training within the scope of one of the <i>Lean Management</i> tools)	- 86% of the surveyed companies noticed increasing of productivity by at least 25%, - 100% of them reduced time for employees training minimum by 25%, - 55% of them reduced the number of deficiencies by at least 25%, - 100% of them improved customer satisfaction by at least 25%.
Faron A. (2011)  (Studies conducted by S. Sussmann and P. Kraus in 1994 carried out on 500 big German concerns)	- increasing competitive ability thanks to reducing the costs, - reduction of wastefulness and higher quality, - growth of labour productivity, - flattening of hierarchy, - shortening time for making decisions, - paying special attention to customer needs and requests, - increasing staff satisfaction thanks to better communication between supervisors and subordinates, - better motivation of employees and their identification with company success.
Zarzycka E., Michalak M. (2013)  (Case study conducted in international company providing accounting services, where a tool from the scope of Lean Accounting has been introduced)	- the quantity of processed data decreased by 70%, - time needed for closing account books and for preparing reports was shortened by 40%, - overall production efficiency increased by 30%, - the costs of financial reporting decreased by 25%, - lower litigation expenses and transaction costs, - shorter and less labour-intensive processes, - less time for generating information (reports).

The above results show that *Lean Management* has beneficial effect on the situation of both manufacturing and service companies. The benefits are impressive and in these results there are no negative effects. However, we may wonder why relatively few companies still introduce this concept in their activities. Lean management brings many economic benefits but the consequence of its implementation may be e.g. social costs that are usually omitted. Survey evidence shows that lean organisations have weaknesses, the same as other management concepts and only some elements are timeless and they may induce positive effects for company (Haus, 2006, pp. 47-48). Some of the positive results may also be connected with risks that may not always be predicted by leadership. As Haus (2006) points out:

- reducing of inventory needs careful examination of the production process, so there is no need to stop the production cycle due to lack of materials or there is no delay in shipping the products to a customer,



- shortening the time of adjusting the devices is usually connected with the need to replace equipment currently used by new machines. Another option is to reprogram the entire production cycle so the analysed process of moving devices will not be required very often,
- reduction of production cycle means transition from a linear organisation to a parallel one so it needs modernisation of production line, purchasing new machines and devices and it is often connected with increasing production scale to cover financial commitments resulting from creating new production network,
- reducing the need for staff is, on one hand, a positive aspect because it allows saving financial resources by an organisation, however, it is not as simple anymore as it requires some time and it is negatively perceived by the society.

Bağçor (2012, p. 284), however, lists some mistakes during implementation of *lean manufacturing* (that refers to the entire concept *Lean* as well) that may also result in unintended negative effects:

- *not understanding Lean philosophy* - *Lean Management* is a process of continuous improvement, not single counter-measure,
- *wrong approach of leadership* - crucial issue is involvement of the entire management staff and defining a direction in which an organisation and all employees are heading,
- *economic profits* - achieving the profits is not the main reason for implementing new management system but it is a consequence,
- *results* – it is essential to obtain results immediately, however, if targets were wrongly defined (which is very likely) it can lead to a lack of confidence to the entire *Lean* system,
- *introduction* - starting and spreading *Lean* rules without having a well-trained employee in the organisation hierarchy,
- *finishing* - *Lean Management* is not a simple operation, it is a journey that never ends - kaizen.

The results of implementing *Lean Management* are dependable on both organisation and employees as well as on surroundings. Special focus must be put on leadership that has a strong influence on taken actions. In literature on the subject the objection is raised that lean organisation is only combination of other management methods and as a concept it is not modern and innovative (Zimniewicz, 2009). It can be also stated that many changes are difficult to introduce, which causes significant costs. Therefore, in the world of science there are critical opinions regarding management of *Lean* type. According to Zimniewicz (2009, pp. 47-50) the people who raised objections against *Lean Management* concept were Genso and Korschak. They entered into a sharp polemic with Womack, et al. stating that “*Lean Management has no scientific basis and it is a product of imagination*” and that “*Lean Management is not the basis of Japanese success but certain expression without keynote*”. Other

authors also spoke rather negatively about *Lean* concept (Zimmiewicz, 2000, 2009; Faron, 2011). That criticism of *Lean Management* may be also relevant to employees' behaviour, delegation of tasks and decentralisation of decisions, or even flat organisational structure. It is worth adding, however, that those critical objections were not raised against customer focus and delivery of high-quality products and services. In the *Lean* concept it is emphasized that an employee is a self-reliant, innovative person, who carries great responsibility. However, this does not apply because in fact employees perform their activities imitatively and there is no time for being innovative and creative. Tasks performed by employees are also an element that denies the idea of *Lean Management* assuming decentralisation of decisions. In a lean organisation, a director or a manager should promote the development of each employee, who has greater independence in action and larger scope of decision making. This independence should improve employees' motivation. In the fact there are often situations when an employee is encumbered with too many tasks and in the same time he must spend more time on performing them, without any additional payment for this work. Greater scope of duties means greater accountability for additional tasks. Therefore, increased responsibilities lead to fatigue, irritation and annoyance instead of motivating (Zimmiewicz, 2000, p. 475). This may result in negligence of performed tasks and in the consequence it may influence the quality of produced goods or offered services. To avoid this, very strong work standardisation with an accurate job description developed in organisations. Also improvement proposals, including kaizen, leading to constant improvement, must be reported to supervisors, who have to decide whether to implement them or not. Another aspect that may be treated as a risk during implementing *Lean* concept is cultural barrier. Despite the fact that there are opinions assuming that at the level of philosophy cultural barriers are not important in Polish companies there is reluctance to introduce changes (Kraśiński, 2014, p. 98).

The reaction of employees to changes in Polish companies is well presented by two quotations mentioned by Kraśiński (2014, p. 98): "*You must raise our salary; otherwise, we do not want to perform any additional tasks!*", "*It is good as it is. We do not have any problems!*". It should be pointed out that the same author at the same time pays attention to the fact that "*unwillingness to reject the status quo and continuous search for improvement may be explained in the best way by cultural barriers on which in theory people do not have any effect. However, taking into account successful cooperation within many Polish-Japanese projects and others in which Polish cooperate with representatives of foreign countries it may be stated that the reason for not taking over the Japanese philosophy of management is laziness, which due to cultural barriers (in a general sense) and certain stereotypes connected*

*with Japan may be easily hidden and justified*". However, regardless of the type of reasons of employees' unwillingness to changes they may impede introduction of *Lean* concept in a company and limit its efficiency.

#### **4. Conclusion**

Since the 1980s, when literature on the subject began to draw more attention to *Lean Management* concept, this method has been constantly developing and it has become popular almost in every branch. The study results in most cases highlight positive effects of the method. It is successfully used not only in production but also in management or accounting. The question arises, however, if all results of "*lean*" company were studied in an exact way?

Most of the authors study production and sales increase or costs reduction, whereas costs, both economic and social, of *Lean Management* implementation are not presented. A long period of time has to elapse to adequately prepare managerial staff and employees or to modify or exchange production lines in a proper way. Employees at all levels are required to be more responsible and to undertake additional duties, which constitute additional pressure for them. It would be interesting to study whether increasing responsibilities, as the result of lean management introduction, has any influence on increasing employees' salary. The studies usually do not include opinions of employees of the lowest level, who perform most of duties in an organisation. Moral issues of such an action on the company may also raise doubts.

Therefore, it is important to conduct studies among employees of the lowest level in the scope of *Lean* concept awareness as well as consequences of its implementation. *Lean* concept is a relatively new method so the results examined over a long period of time may differ from the results reported just after its application. This can be based on experiences of Toyota company that has been analysed and described for many years but no other company has reached such spectacular effects as Toyota. However, Toyota success cannot be treated the same as the success of *Lean Management* all over the world. It is difficult to notice in scientific literature studies regarding companies' persistence in applying *Lean Management*. There is therefore a need for verification of how companies using lean management cope over a long period of time and whether it was a single action of improving results or, as *Lean Management* concept assumes, organisation's consistent policy of moving towards constant improvement of the processes and striving for excellence.

It follows from the above considerations that Lean Management implementation is undoubtedly the method that effectively influences cost reduction, that is why it is so readily chosen by companies. The results of the study dominated by economical results arouse companies interest in this

method, however, they do not show other, not fully investigated, effects of its implementation. It should be pointed out that information and conclusions presented above rather indicate a problem and their aim is to show complexity and specificity of *Lean Management* concept. They also indicate a need for further development within this scope.

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# APPLYING SELECTED MODELS OF CHANGE MANAGEMENT IN NON-PROFIT ORGANIZATIONS

***Paweł Korczak***<sup>1</sup>

## **Abstract**

*Change management is very important these days. An organization's market share and development are based on change. A company that cannot manage change will probably not survive in the market. Due to different characteristics between non-profit and for-profit management it is not recommended to directly adopt management techniques and methods to the third sector organizations. The article focuses on presenting popular change models from commercial organizations and assessing their use in non-profit organizations, and offers an explanation why they cannot be used in the original form.*

**Keywords:** *change management, change, change model, non-profit organization, NGO, third sector.*

## **1. Introduction**

Studying scientific literature and statistical data, we can conclude that the NGO sector is experiencing significant bloom, which has been particularly visible in the last few years. Research carried out in Poland by the Central Statistical Office in 2014 shows that in the period 1997-2012, the number of active associations, foundations, social, religious bodies, self-government organizations, professional and employers increased almost threefold. In 2012, the number of non-profit organizations was 83.5 thousand, revenues amounted to PLN 23.9 billion, the average full-time employment was 128.4 thousand. Compared to 1997, these values were respectively 27.4 thousand, 8.1 billion PLN and 81.2 thousand. A significant increase in the number of NGOs (Non-Governmental Organizations) has intensified competition in the third sector. This forces organizations to search for and implement modern management solutions (Zielinska 2011, p.96). Although profit and public management approaches offer important insights into how to manage nonprofit organizations, they still fail to provide a more contextual and comprehensive

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approach. Models are needed to fully account for the fact that non-profit organizations are multitudes of different organizational components (Anheier 2005 p. 246).

This article deals with change management. An important dimension of this phenomenon gives an increasing pace of change and the associated determination in achieving the basic objectives of the organization – survival and development. In the 21<sup>st</sup> century, we are dealing with the pressure of implementing changes; in order to remain competitive on the market, organizations cannot limit themselves only to creating conditions providing stable functioning. They must take a risk of changing (Osbert and Pocięcha 2010, p.149). Taking also into consideration the limited number of publications concerning managing the change in non-profit organizations on the Polish market, the goal of this paper is to present selected characteristics of non-profit organizations, which should be taken into account when designing a change management model strictly for non-profit organizations. The differences are also presented between the three sectors in the economy, the characteristics of the third sector in terms of characteristics distinguishing these entities on the market and identifying key characteristics that should be taken into account when applying models to NGOs. Then I will describe selected models of change management and identify their disadvantages that prevent their use in the non-profit sector in the form in which they are used in commercial organizations.

## **2. Characteristics of the third sector from a point of view of the specificity of the management**

In a market economy, we can distinguish three different areas of activity, called sectors. The first sector – contains enterprises, the second – institutions of central and local government and the third sector – NGOs. These are the organizations which form voluntary associations, existing outside the domain of the government (Żyro 2006, p.182).

In the literature we can find many terms used to define the non-profit sector, also used in this study. According to Kietlińska (1995, p.29) there are, *inter alia*: civic organizations, non-governmental organizations, non-profit oriented organizations, voluntary sector, independent, charitable, philanthropic, third sector, non-governmental sector.

Table 1 shows fundamental differences between non-profit organizations and organizations of the first and second sector (Kozuch 2005, p.15):



**Table 1.** Fundamentals of non-profit organizations (public and private) and commercial entities

<b>Constitutive features</b>	<b>Commercial organizations</b>	<b>Public organizations</b>	<b>Non-governmental organizations</b>
Conditions of operation	Entrepreneurship activities in the interest of the owners, meeting the needs of customers, as a condition to remain on the market; the provision of goods and services according to market criteria	Justice and social solidarity, equal opportunities for development of individuals and groups; representation of the needs and interests of the majority; objectification and business continuity, avoiding bias, neutrality	Selflessness, charity, mercy, charity, acting on behalf of minorities; voluntary, spontaneity, improvisation, community meanings, intuition and expression of personality
Priorities	Competition for customers in order to achieve profit to develop, or at least stay on the market; action consistent with the law; care and external and internal customers, if it translates into achieving (or increase) profit	The implementation of social policy embedded in the existing canons of political and legal; standard needs and expectations; institutionalization of meeting needs; donor activity - passive recipient	The guard values, voluntary action, entrepreneurship, social participation, partnership, advocacy, people in need; individualization, selectivity needs, decentralization, de-institutionalization, subsidiarity in the process of meeting needs, particularism; self-help, mutual aid and self-reliance
The mandate of the organization	Legal empowerment depends on the type of ownership and legal form, the Commercial Code, single decisions, resolutions of statutory bodies, regulations	Constitutionally empowered bodies and institutions of the State; legislation: codes, regulations, instructions	The statutes and rules of procedure; resolutions, decisions of statutory bodies, such as councils and boards.
Recipient of services	A stranger - the customer comes first, the counterpart; soliciting customer satisfaction and loyalty, as instruments of creating profit	A stranger - the consumer, the customer, controlled warmth, distance, perspective institutional relations with the recipient	Our man; emotional closeness, multidimensional interactions and the identification of the operator
Responsibility	To the owners	to the electorate	To recipients of action

Source: Kozuch (2005).

The summary of fundamental assumptions of non-governmental organizations, compared to commercial enterprises and government organizations shows that the non-profit sector has different performance characteristics. The differences are evident in every aspect concerning the conditions of action, the priorities of the organization, recipients of services or responsibility.

According to Anheier (2005, p. 246), among the key facets that must be applied to the nonprofit organization in management field are:

- A holistic concept of the organization that emphasizes the relationship between it and its environment, the diversity of orientations within and outside it, and the complexity of demands put upon it.
- A normative dimension of management that includes not only economic aspects, but also the importance of values and the impact of politics, as exemplified by the value guardian and advocacy roles of nonprofits
- A strategic–developmental dimension that sees organizations as an evolving system encountering problems and opportunities that frequently involve fundamental dilemmas for management
- An operative dimension that deals with the everyday functioning of the organization, such as administration and accounting, personnel and service delivery

Peter Drucker (1995, p.226) pointed to the different specificity in the management of non-profit organizations:

- Non-governmental organizations exist in order to „do good”, which means that they can treat their mission as moral absolutes, and not as an economic activity that is subject to the account inputs and outputs. Their activities cannot be oriented to generate higher profits, because „doing good” is something „the best”. If the said „good” cannot be achieved, it means only that efforts should be redoubled.
- NGOs are dependent on a number of „voters”, as opposed to companies offering their products / services on the market for profit. The most important „voter” is the customer and his satisfaction.
- Non-governmental organizations base their activities on the budget, and not on performance fee (budget revenues come from the taxpayer, the donor). The success of the institution is measured by the size of the budget rather than obtained results. Getting rid of certain activities often deprives the organization of position and prestige. They cannot admit to failure or, worse, to the fact that a goal has been achieved. This applies particularly to institutions financed from the state budget or local area.

Also, Hudson (1997, p.54) lists several typical characteristics of non-profit organizations, determining the difference in the management of non-governmental entities

- Weak link between providing funds and users of services; in private sector providers offer customers goods and services for which they pay the market price, in the public sector authorities provide public services, and voters vote for the government to guarantee the best social system of taxation, in the third sector (NGOs), donors finance projects by organizations from the sector (link between funders and beneficiaries is the weakest here).
- Difficult to precisely define the objectives, such as improving health, raising the level of education, environment, spiritual development, etc.
- Complex organizational structures resulting from the need to balance the interests of different groups of „stakeholders” who often form the management board.
- Focus on cultivating values, because of their disregard, quickly weakens the morale and staff motivation or causes endless discussions.

Highlighted features specific to the operation of non-profit organizations indicate the need to distinguish management methods between sectors. Effective application of management models depends on the modification of the methods in such a way as to take account of the characteristics (specificity) of a non-profit organization. Particular emphasis is placed on the core values that support activities on convincing „voters” to company’s social mission. The NGO sector is very different from the other sectors and it is not possible or desirable, to transfer directly models and techniques to these entities. The characteristics presented by Drucker and Hudson should be taken into account, when designing and carrying tools onto the ground of non-profit organizations.

### **3. Criticism of commercial models of change management from the point of view of the application in third sector organizations**

In today’s complex and unpredictable world, change has become inevitable. Undoubtedly, it is affected by the rapid development of new technologies, which in turn shortens product life cycle. The product life cycle is becoming shorter and shorter, customers more frequently demand new products and the strategies of the organization must be adjusted quickly. All this means that organizations do not have enough time to change, and too slow adaptation to market activities may result in loss of competitive advantage. In order to keep pace with the changes required by the market, the organization should continually improve the process of change (Albrecht and Sack 2000, p.4). Another reason why change management is needed nowadays is globalization. The world has become one giant market, with few barriers to the exchange of goods, services or information. The process of change has to face new challenges. Today’s organizations need to implement process changes in their

branches, located often around the world. There is no simple answer to the question of how the process of change should be implemented in a global manner. Employees that are working and developing in different organizational cultures may need a different approach to the management of change (Albrecht and Sack 2000, p.4).

The subject of change management has seen many models proposed by researchers. Many of them have common foundations and present similar ideas. In this article, two selected models will be presented: Kurt Lewin's 3 stage model - the first change model, widely cited in scientific publications, constituting a base for further models and John Kotter's 8 step model, based on academic and business experience, popular and widely used in organizations around the world.

### ***Kurt Lewin's 3 stage change model***

The approach to Kurt Lewin's change management is well-known and often used by management practitioners today (Cameron and Green 2004, p.96). Lewin was one of the first theorists who studied the knowledge of the action, learning and change. Lewin's change model consists of three steps: unfreeze, change, and refreeze.

#### ***Unfreeze***

This phase of change is built on the theory that human behavior is established by past observational learning and cultural influences. Change requires adding new forces for change or removal of some of the existing factors that are at play in perpetuating the behavior.

#### ***Change***

Once there is sufficient dissatisfaction with the current conditions and a real desire to make some change exists, it is necessary to identify exactly what needs to be changed. Three possible impacts from processing new information are: words take on new or expanded meaning, concepts are interpreted within a broader context, and there is an adjustment in the scale used in evaluating new input.

#### ***Refreeze***

Refreezing is the final stage where new behavior becomes habitual, by strengthening new patterns using formal and informal mechanisms.

Lewin's model has significant flaws that prevent its effective use in nonprofit organization. Below the most significant ones are presented:

- Lewin's model lacks of flexibility

It is perceived as a model basically lacking the flexibility required to fit with the currently dominating constant, and sometimes even chaotic, process of change requiring, as such, a great deal of flexibility. The final stage of the process should not end up on a rigid, hard state but that it should, instead, conclude leaving the organization in a sort of soft / open state which could be constantly shaped accordingly as needed.

- The assumption that the organization when carrying the changes is stable

Non-profit organizations function in a constant struggle for the realization of approved projects, as part of the mission. The budget is collected from people who want to support the objectives of the activity. NGOs almost always operate under a limited budget and under pressure to meet its goals, so the assumption of instability of action should be fundamental to the assumptions of the model change management.

- Not including politics and power in organization

To maintain activity, NGOs must honor their commitments to various stakeholder groups. Stakeholders may be permanent employees, volunteers and organizations who want to meet specific goals. Not taking them into account in the plan of change can be a major obstacle to its effective completion.

- The model is used to achieve specific objectives

The objectives of the activities of non-profit organizations are often not precisely defined. NGOs have a mission that is realized by conducting various activities. Lewin's model is designed to achieve clearly defined objectives, does not take into account the possibility of the mission, which may consist of a variety of non-identical goals.

### ***John Kotter's 8 step change model***

It was first published in 1995, in the form of an article in the journal Harvard Business Review. Next year, assumptions of the model were enhanced with a lot of new information. The model is based on personal experiences gained in the academic work and business world. The model consists of eight consecutive steps (Kotter, 1995, p. 59):

#### ***Establish a sense of urgency***

If a change is to be effected, it should be carried through as quickly as possible to avoid a loss of impetus. A lack of urgency can lead to a scenario in which the change is perceived by those affected as 'death by a thousand cuts'

#### ***Form a powerful guiding coalition***

Change cannot be successfully implemented by one person, irrespective of their position in the organization. Even a chief executive on their own cannot make a change happen: a change initiative needs to be driven from the top of the organization but it must take the people with it.

### ***Create a vision***

Every change project, by definition, involves delivering a vision. Clearly, however, some projects will be more complex than others. For complex change projects (step and major change initiatives), it will be necessary to develop a strategy to explain how the vision will be delivered.

### ***Communicate the vision***

Change Champions will typically support the Change Manager in communicating the change vision. In successful change initiatives, the initial communication of the change vision is likely to have come from the head of the organization personally.

### ***Empower others to act on the vision***

Similar in some respects to the creation of a guiding coalition, this stage is about engagement with the people who are affected by the proposed change. It is true in most change initiatives that the people who are closest to the problem are best placed to find solutions to that problem.

### ***Plan for and create short-term wins***

One of the single most characteristics of organizations that are successful in implementing change is their ability to maintain momentum. In most cases, this is achieved by a well-considered strategy which seeks to deliver early success –short-term wins.

### ***Consolidate improvements and keep the momentum for change moving***

This has a link to the importance of generating short-term wins. Early and frequent success will encourage and enable more innovation and change; indeed, staff will be significantly more positive about change where they see how the change has delivered a benefit and feel that they have and can influence future change.

### ***Institutionalize the new approaches***

This is critical to organizations that want to be creative and innovative. While there is no guarantee that a particular methodology or approach to change that

has worked well in the past will be effective in the future, it makes sense to try to do more of what has worked previously.

8 step Kotter's change model also should not be used in non-profit organizations in its original shape. It has the following flaws:

- Top-down management

Objectives imposed by the board of management and lack of consultation among employees. In organizations where staff employees and volunteers are the main driving force, opinions and advice from the volunteers and basic employees should be seen as valuable and should be taken into consideration when planning changes.

- Needs of individuals recede into the background

Kotter does not mention about needs of individuals in his change management model. As similar to "top-down" management, organization non-profit should, when processing the change, take into consideration needs of individuals and try to take them into account during process change.

- Once the process of change starts, it is hard to change its direction.

Non-profit organizations, in order to satisfy various stakeholder groups must be able to frequently change its courses of action. The multistage Kotter's model, is not conducive to the speed and shape of the final in the course of the changes.

- The process of change takes too much time

In today's rapidly changing world companies must operate in the volatile and demanding market. Kotter's multistage change model, is not conducive to the introduction of rapid change, and does not allow to form process in the late stages. It is not able to move from one change to another in required fast pace.

#### **4. Conclusion**

It is not advisable to transfer directly change management models from commercial or government organizations to the third sector. The third sector and entities functioning within it are different so methods and management techniques should be accordingly adapted to their specific characteristics. Lewin's and Kotter's change models presented here do not take into account the specifics of the management and operation of non-profit organizations. The subject of the article has not been fully discussed and the author plans to continue the work and to develop a new model of change management that will contain all specific characteristics and issues that must be applied in change model for non-profit organizations.

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# COMMERCIALIZATION AS AN APPROPRIATE APPROACH TO THE PROCESS OF RESTRUCTURING HOSPITALS IN POLAND

**Bartłomiej Kaszyk<sup>1</sup>**

## **Abstract**

*While Polish health system has been suffering from underfunding for over 20 years, Polish hospitals have faced chronic debt. The situation indicates that necessary action must be taken to transform the hospitals in terms of financial and organizational issues. Current law and organizational structure of Polish hospitals have many flaws and are not coherent with the turbulent environment in which the hospitals operate. Moreover, managers running hospitals under the structure of SPZOZ, do not have any incentive to enhance the functioning of their hospitals, and this contributes to poor managing of the companies. What is more, managers do not have clear information which management structure they should choose to be able to normalize the situation in the hospitals as they are attacked by two extreme groups having different remedies for the hospitals' problems.*

**Keywords:** *transformation of hospitals, commercialization, health care, management, Polish hospitals, capital companies.*

## **1. Introduction**

Niall Ferguson, one of the most brilliant contemporary intellectuals, in his recent book entitled “The West and the Rest”, identifies six factors that have given advantage for the West over other civilizations and cultures: private competition, dynamic development of science, private ownership, consumption, work ethics and medicine (Ferguson, 2013). There is no doubt that Poland, after the collapse of Soviet regime in 1989, faced a very difficult task to begin and develop the relative advantages mentioned above. Undoubtedly, the introduction of free market rules in Poland has had significant influence on every area of Poles' lives. Ownership transformation, related to the collapse of the state monopoly, has influenced the intensification of private activities that launched the competition. This process has allowed Poland to increase the

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number of new technologies necessary for dynamic growth. The development of free market rules has prompted the growth of new areas of science and fostered significant improvement of the existing ones. Moreover, a new term - work ethics, virtually unknown before 1989, now appears in a dictionary of every company. After the era of socialism, Poland has followed the global trends that developed countries represent. In Poland, the mentality of people has been changed towards consumerism society which is connected with natural transition of every economy from industrial to postindustrial economy. According to Philip Kotler's definition (Kotler, Bowen, Makens, 2009), the postindustrial society in addition to having access to food, accommodation, basic utility services and access to a minimum level of education, is characterized by the need of broad and unfettered access to health care.

Health is the dearest value to a man. Health was the cause of creating the phenomena of Welfare State in the II Reich (Deutsche Reich). Social insurance programs, introduced in 1880 were the first in the world and have become an example for other countries to organize a public help as foundation of creating a modern Welfare State (Palmera, 2012). Otto von Bismarck, Chancellor of the Reich, introduced then pension, accident insurance, medical care and unemployment insurance. These steps changed definitely the perception of health in Europe. Individual approach was replaced by a collectivist attitude, which entrusts health protection to the state. Poland is not an exception and also there the case of health care was left to public institutions which led us eventually to disposing the idea of fraternal societies so widely popular in XIX century in Great Britain. The phenomena of Welfare state dismissed the notion of generating smaller communities focusing on specific industries guilds on the principle of mutual help. Having expanded successively the Bismarck's idea, societies in Europe have created a number of new institutions in different spheres of life, including health issues.

It is well known that depending on the quality of the institutions, people feel safe and satisfied with medical services or not. The most important institution which is responsible for caring about health of the society and is the closest to a patient is hospital. People express their opinions about health care system basically judging the quality of medical services that hospitals provide. According to a survey conducted by TNS Polska (<http://www.stefczyk.info/wiadomosci/gospodarka/coraz-wiecej-polakow-zle-ocenia-sluzbezdrowia>, access: 7.03.2014) at the beginning of 2014, almost 4 out of 5 respondents (79%) are not satisfied with the current health care system in Poland. Only 18% of respondents evaluate the system positively and meager 1% of the surveyed are very satisfied with the health services in Poland. Unfortunately, the case of Polish health system and hospitals are still issues that are not solved. That indicates that despite the fact that many free market rules have been developed

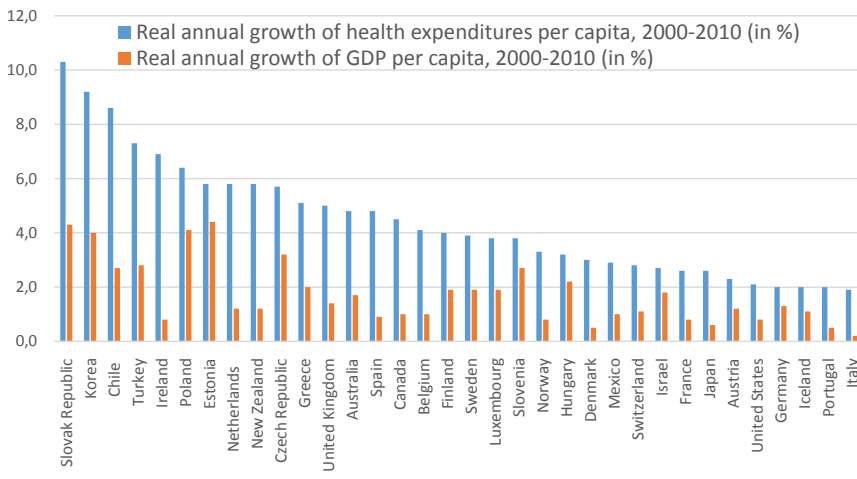
in Poland since 1989, medical care is a neglected topic in the political debate in Poland.

Nowadays, a big discussion is being undertaken in Poland. Its focus is: whether Polish hospitals should be commercialized or they should stay under the ownership construction of SPZOZ (independent public health care company). However, in the very important discussion on the creation of health care system, many misunderstandings are visible. The purpose of the article is primarily to indicate to the authorities of Polish provinces, managers of hospitals, politicians and people who are interested in the subject that necessary steps in terms of transformation of Polish hospitals have to be taken, since such institutions as SPZOZ do not function properly. They would be more effective if they functioned as capital companies.

The aim of this article is to demonstrate that transformation of SPZOZ to a capital company is an appropriate approach that managers should follow. This is a solution proposed by the Ministry of Health and after the changes in law in 2009 it is a normalized process, adapted to hospitals' needs. In the article many misunderstandings related to commercialization of hospitals are explained and clear advantages of commercialization are revealed to help managers choose a necessary path for overall restructuring. The article presents a commercialization process as the first and necessary step of Polish hospitals' restructuring.

## **2. Development of the health sector in Poland**

In the last decades, in developed countries a fast development of health care sector can be observed. In many cases the dynamics of the growth is still faster than the dynamics of GDP growth. In Poland in the years 2000-2010, annual expenditures on health care have grown on average by 6.4% a year. Taking into consideration the list of countries included in the OECD survey, it was a remarkable result for Poland, which was beaten only by Slovakia, South Korea, Chile, Turkey and Ireland, which is indicated in Figure 1.

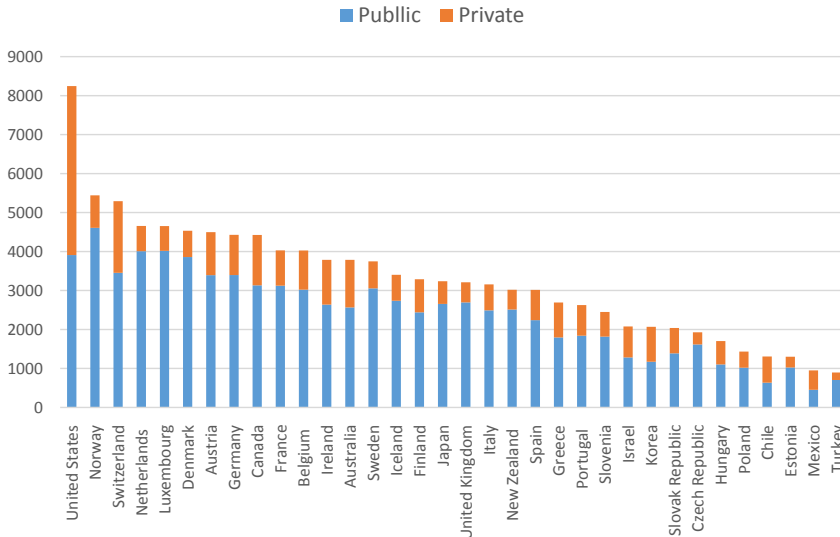


**Figure 1.** The growth of health expenditure compared to GDP growth (per capita) in 2000-2010

Source: own elaboration based on OECD Health Statistics (2014) and World Bank Indicators (2014).

In all countries represented in Figure 1, expenditures on health system grow faster than GDP per capita which is the consequence of the fact that medical care has the features of a luxury good (elasticity above 1), meaning that spending on medical services grows faster than revenues (Skorupska, 2012, p. 16).

The amount of expenditures that is transferred to health system depends heavily on the development level of a particular country, which is measured by its GDP. However how the system would be financed in terms of private or public sources depends on social policy run by a government. Figure 2 presents the level of public and private expenditures on health (in USD and according to PPP) in 2010.



**Figure 2.** Public and private expenditure per capita for medical services in selected countries in 2010 in USD using purchasing power parity

Source: own elaboration based on OECD Health Statistics (2014) and World Bank Indicators (2014).

The lower level of expenditures on health care in Poland in comparison to its GDP and other countries, together with coexisting dynamic growth of the spending, indicates a big development potential of health care in Poland. Despite its intensive development, Polish health care system, whose dynamic growth is significantly faster than average growth among OECD countries, is not well-organized and its most important institutions - hospitals, still suffer from lack of organized structures and huge financial debt.

### 3. Problems of Polish hospitals

The lack of effectiveness of Polish hospitals is indicated by many experts as the biggest problem of Polish health system. Hospitals, due to their size, nature and scope of current activities, generate massive liabilities which generally exceed the funds which the hospitals obtain from NFZ (National Health System). The situation leads to the creation of huge debts for hospitals. The chronic problem of Polish hospitals is revealed by the fact that despite many attempts of debt reduction financed by the Ministry of Health (which according to the Ministry cost approximately 20 billion PLN so far), the situation has not improved. Even though the hospitals received the financial help, it was often not connected with overall restructuring of their functioning, and in the

long run the problem with the finance appeared again. Polish hospitals have suffered from financial debt for many years and according to the Ministry of Health data in the second quarter of 2014 the value of total liabilities reached PLN 10 030.3 million (Ministry of Finance, 2014). The disastrous financial situation often forces directors of the hospitals to incorporate drastic savings and even close entire medical departments.

Besides financial problems, managers and owners of hospitals have to act in the turbulent political environment, which is populated by people with contradictory views on health care structure, some opt for liberalism, others for socialism. The problem makes the managers confused - they do not know what steps they should take to solve the upcoming and current problems. Thomas Sowell is an American economist, associated with the Austrian school of economics, who a quarter century ago pointed at a very interesting phenomenon (Balcerowicz, 2012). As he discovered, it often happens that in various disputes nowadays, the same people could be found on the opposite sides of particular disputes. These disputes are on a variety of issues including political, economic, cultural, social, military and health issues. Following the observation of Sowell and public debate on the health care system in Poland, it is hard to disagree with Sowell's observation. During the reform of the health system in 1999, people representing a conservative wing objected to the idea of giving hospitals the status of independent institutions under the power of provinces, which was supposed to be the step taken into the direction of introducing a competition between hospitals (sic!). The same people placed themselves on the same side of a dispute during the next reform of health system in 2003 which involved the introduction of one payer to the system - NFZ instead of healthcare funds (kasy chorych). This step was also attacked by conservatives, who criticized the decision as a step towards implementing free market dogmas in the health system. Because of these numerous disputes, many health reforms were not completed properly. This is a fact but it cannot be an excuse for authorities that bear responsibility for the current turbulent situation in the health care system in Poland. In addition, many populists afraid of free market, development and changes are in opposition to organizational changes of the hospital system proposed by the Ministry of Health. The so-called 'Plan B' enables hospitals in Poland to transform directly their organizational structure from SPZOZ to one of the forms of capital company: limited liability company or joint-stock company. The group of people who were opposing the two previous reforms in 1999 and 2003 are also in opposition now. When the situation of hospitals in Poland needs urgent changes, they rise theses which are not empirically proven (for example that automatically, after commercialization, hospitals would become



privatized) which destabilizes the process of transformation of hospital and misinforms managers about which path they should take to run the hospitals.

The system under which hospitals operate (which is based on contracts with one payer - NFZ) forced a strong competition among them and revealed a need for effective management of the limited financial resources. Nowadays, hospitals have to adapt to the new situation; functioning in the free market environment instead of the system based on public transfers. At the system level as well as in the sphere of realities of law in Poland, the optimal solution to introduce normality of functioning of hospitals and adapt to the changes appearing in micro and macro environment is to transform hospitals in the light of 'Act on Medical Activity' (*Ustawa o działalności leczniczej*) from 2011. In the wake of the Act from August 30, 1996 the process of transforming hospitals can be called commercialization and because of accepting in 2011 a program called 'Support of local government units in action to stabilize the health system' ('Plan B') by The Council of Ministers, for the first time, the process of organizational and legal changes in hospitals can be called 'transformation' (before 2011 the hospitals, which opted to be a capital company, first had to declare bankruptcy and then they could create the new structure). The transformation process was run by the majority of primary health care institutions in Poland (usually they were also privatized) but the vast majority of hospitals still acts as SPZOZ - an old fashioned construction, which does not allow hospitals for effective reorganization and effective functioning.

#### **4. The meaning of Polish hospitals' commercialization**

Understanding the concept of commercialization seems to be a key factor in Polish reality in order to understand correctly the process of transforming one company into a capital company. The term 'commercialization of hospitals' has negative connotation among the Poles after the social regime experience. First, commercialization in Poland is identified with privatization which causes strong social resistance and the wording itself is used as a component of political war. The social fear of commercialization enhances dark vision of long queues for free treatments, different quality of medical services for patients and payable hospital services. These concerns are at least exaggerated, which is clearly indicated by an example of non-public hospitals (NZOZ) that offer medical services faster than the public ones where patients have to wait for a particular examination for many months. The social dislike of the term 'commercialization' can be compared to the fear of the Poles of the term 'liberalism' or free market in the 90s. At the time when the government noticed that the market transformation paralyzed many Polish brains, they

used other words as synonyms for ‘free market’, for example ‘western-type economy’. The similar situation can be seen nowadays when the government instead of using the term ‘commercialization’ uses a word ‘transformation’ to make the process acceptable by the Poles.

Opponents of commercialization indicate that the process is equal to privatization, which means that the patients would eventually have to pay for medical services and owners of the hospitals would only look at the financial statement and not at the well being of patients, or alternatively they will promptly transform the hospitals into plastic surgery entities. In this article, the author clearly emphasizes that these fears are not justified in the light of the concept of creation of commercialized companies presented in the act from August 30, 1996. There is a clear distinction between privatization and commercialization and these two terms cannot be treated as synonyms. Commercialization in opposition to privatization does not mean changes in the ownership structure but changes in law and organizational structure of hospitals which are subject to the changes. Therefore the process of commercialization of hospitals should be interpreted as transformation leading to changes in the structure of SPZOZ into capital companies. It is necessary to point out that according to Act on Medical Activity (*ustawa o działalności leczniczej*) a public authority retains full control over the new medical company created by the transformation of a hospital (Dercz and Rek, 2012). It means that public authorities still own 100% of shares and the ownership structure is not changed. The rules of law do not contain legal constraints which prevent hospitals from further possible privatization by selling some or all shares of a company by the local authority. Some restriction concerning forbidding privatization of hospitals is imposed only on clinical hospitals and is included in art. 6 paragraph 7 of Act on Medical Activities, according to which the value of shares belonging to clinical hospitals cannot be less than 51% of share capital of a commercialized hospital. It should be noted that rules of law indicate only the possibility of transforming SPZOZ into a capital company: limited liability or joint stock company. Therefore there is no possibility to transform hospitals into limited partnership. The ability to transform SPZOZs to a limited partnership or limited joint-stock company might begin the creation of a net of commercialized and connected hospitals - such model exists among trade networks<sup>2</sup>. However the most important clarification is that one cannot mislead commercialization with privatization as commercialization of hospitals should be interpreted

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2 Shopping networks coordinated by an organizer, necessary for the functioning of hospitals, would allow managers of hospitals to receive better condition of contracts with suppliers. Concentrated network management in the hands of a single entity should also lead to formulation of a joint strategy for the entire network and taking steps to rebuild the structure in order to increase efficiency of functioning both the whole network and the individual hospitals. For example the network can include a combination of weaker companies connected with stronger ones in order to accumulate their resources and create multi-hospitals as institutions able to provide a wide range of medical services (Horosz, 2013, p. 67).

as transformation leading to changes in the structure of SPZOZ into capital companies but not ownership changes. The commercialization of hospitals is an appropriate approach of local authorities and they should notice the new chances for hospitals after the process as well as realize that the old fashioned structure of SPZOZ does not allow hospital to develop and adapt to turbulent environment.

## **5. SPZOZ as a legal form that does not provide incentives for efficient operation of hospitals**

An incentive for every change in a company is always the prospect of achieving better revenue, better effectiveness (Patena, 2011). It seems to be truism but when it comes to Polish SPZOZs it is not so obvious. Not only do the hospitals not observe environment, they do not introduce innovations and organizational changes which could improve their functioning, either. What is the worst, they seem to be indifferent with regard to significant negative financial results that in long term can lead the hospitals to bankruptcy. This irresponsible approach has its origin in the lack of real monitoring body which cares about financial issues of a hospital. The problem also appears when it comes to formulating economic goals of a hospital and responsibility for negative financial results which is a strong premise for commercialization of hospitals.

The monitoring of hospitals by local authorities, which are owners of hospitals and SPZOZs is based on three pillars (Horosz, 2012):

- 1) The first obligation is to present an annual financial statement by the director of SPZOZ to the local authority. The statement is presented annually or under special conditions more often at sessions of the appropriate council. What is worth emphasizing, authorities have no power to give any specific instructions to managers, which causes that the whole process of presenting the financial statements is useless and can be called a courtesy speech instead of being the discussion based on merits and analysis with the solutions for the future. Legislators, having created the structure of SPZOZ, did not include an obligation to accept the financial statement or sanction for managers in the case of rejection of the statement. This construction causes that both managers and owners of hospitals do not take the responsibility for positive result of the institutions as the main incentive does not exist and they are typically satisfied with *status quo*.
- 2) The second pillar, which is statutory responsibility for monitoring how hospitals function, is providing local authorities with the possibility of supervising SPZOZs. According to this possibility, the owner has an obligation to control the hospitals at least once a year. It may be done as a general control or supervision of only one department. If

the control reveals some irregularities, the authorities may inform relevant financial and law institutions about them. As practice shows, these institutions exhibit an unacceptable indulgence during the control. They claim by default that the system of health care in Poland is not perfect and hospitals are not prepared to avoid debt. That irresponsible thinking has led to a significant mismanagement of hospitals that causes multimillion debt in the whole system.

- 3) The third body of monitoring SPZOZs is called social council. The role of the body, contrary to boards of directors of commercial companies, is limited to an advisory body. It is formed and dismissed by the local authorities whose members at the same time are often the part of the body. Social Council has only some consultative power (for example they may express an opinion, accept donations, etc.) and has no tools to make or force changes in SPZOZ. During the presentation of a financial statement, the body gives opinions but cannot approve or disapprove the statement given by a manager. As in the case of the first pillar, the lack of pressure instruments makes that in practice presentation of the financial statement is totally inefficient.

Two acts of law (45b-cm 50 and 60) of Act of ZOZ indicate that hospitals and their managers are responsible for covering costs and liabilities and they have to manage the companies with accordance to the Act of Public Finance. Both acts do not regulate the rules of supervision of hospitals, or real control over planning and executing of a budget. The rules do not indicate who has the power to accept an annual financial statement and it is not written what consequences the managers whose hospitals have negative financial results face. Moreover, it can be read in the acts that whatever the financial result is it does not influence the future funding of the hospitals. According to the legal assumption that local authorities take over the debt of the hospitals, therefore one can say that legislators have allowed managers to grow debt and avoid any consequences. The role of external bodies (local authorities) can be interpreted as the role that is marginalized as the bodies cannot really control the functioning of hospitals or care about their effectiveness. As a result, SPZOZ is deficient, legal creation and in number of scientific research it is called 'legal and formal hybrid' (Perechuda and Kowalewski, 2008). Only commercialization can cause permanent elimination of the dysfunctions, because the first priority should be to provide the directors of hospitals with the responsibility for making decision. It is hard to imagine an effective management system without these components.

## 6. Advantages of commercialization of hospitals

The system solution that eliminates most of the barriers identified in the SPZOZ structure, is the transformation of hospitals into capital companies. It can positively influence the management, and provide access to a range of financial instruments to be of use to hospitals. Understanding the basics benefits of this structure of hospitals is a core element of implementation of overall restructuring of hospitals, commercialization of which is a necessary component.

**Table 1.** The differences between how hospitals function as SPZOZ and as capital companies

SPZOZ	Capital company
<b>Management in hospitals</b>	
Political responsibility, unclear responsibility of management board and owners	Procedures set out in the Code of Commercial Companies, the Board is responsible for the management of property and financial liabilities
Many decisions need a formal approval by local authorities	More freedom and flexibility in a process of decision making
Long-term process of generating of decisions (managers of a hospital and local government, committee of the council, the county council)	The Board makes decisions independently and it is responsible for them
Lack of responsibility for debt and making bad decision in terms of a hospital functioning which is not appropriate for creation of a sound health system	Legal responsibility for debt and making bad decisions
<b>Owner supervision</b>	
Social council - advisory body, participation of representatives who do not take responsibility for the results of a hospital	The Supervisory Board- the main body with legal responsibility. Representatives are collected by substantive approach, legal responsibility
Politicized supervision	Professionalized supervision whose rules are set in the Code of Commercial Companies
The Board and council of local authorities with political responsibility	Meeting of shareholders- body of owners with legal responsibility
<b>Director responsibility</b>	
Political evaluation of functioning	Merit based evaluation from the point of view of assumptions and results
Generally formulated in The Act of ZOZ	Regulated in details by the Code of Commercial Companies

<b>SPZOZ</b>	<b>Capital company</b>
Lack of procedures in terms of financial statement. Rejection of the statement is not equivalent to a director dismissal. Lack of financial instruments to make plans and implementations of necessary steps	Annual statement presented at a meeting and evaluated by board of directors and accepted or rejected by shareholders at a shareholders meeting. Rejection of the statement is equivalent to dismissal of managers
Political responsibility and responsibility in front of commission of public finance discipline	Legal responsibility whose rules are regulated in the Code of Commercial Companies

#### **Finance**

The negative financial result is covered by local authorities	The negative financial result may lead to bankruptcy
Lack of responsibility of director for their decision	Legal responsibility for directors taking decisions
A hospital cannot be liquidated in case of negative financial result	Liabilities exceeding initial capital automatically start bankruptcy procedures
Financial management is carried out on the basis of general rules	Financial management principles and financial statements structure is determined in the Code of Commercial Companies

#### **Employees**

Wage regulations depend on the rules of law and ministerial orders which are not related to efficiency criterion	Transparent wage regulations based on the Code of Labor, wages depend on results
The statutory requirement of consulting a structure of employees with representatives of labor union and the necessity of receiving approval from local authorities for every change on important position	The criterion of the effectiveness of management
Creating a contest for hiring every head of department of a hospitals run in the light of rules of law determined in the Act on ZOZ- social trust is the dominant criterion	Hiring does require a contest - the dominant criterion is efficiency

#### **External financial sources**

Difficulties with clear evaluation of financial statement which causes a problem with access to bank loan, credit	Access to all financial instruments. Evaluation of reliability and effective functioning based on standard procedures
Access to some financial sources of European Union and European Economic Area	Unlimited access to external financial sources and resources of European Union

Source: own study based on advantages of commercialization presented by Kachniarz (2008).

## 7. Conclusion

Thanks to the Act of August 1, 2011, hospitals in Poland received the possibility to transform their structure from old-fashioned SPZOZs to capital companies. Commercialized companies can be managed as businesses under much more stable organizational structure without many misunderstandings associated with SPZOZs. Moreover, the transformation helps hospitals adapt to the turbulent environment they operate within and normalize their internal organizational structure. The question arises whether the transformation is a panacea for all problems of Polish hospitals. It should be clearly pointed out that there is no single solution to solving the problems, but commercialization should be treated as the first step of shifting hospitals to the path of sustainable development. However, the success of the whole restructuring depends on overall approach, which has to be taken by all the sides involved in the process. There is no doubt that qualified management board is crucial in the restructuring process. The managers have to be able to manage a dualistic nature of commercialized hospitals: both as companies offering public medical services and companies acting under roles of free market. That situation requires extraordinary skills and great resilience from the managers. However, the commercialization of hospitals in Poland is a must as it is hard to imagine implications of management, financial, organizational and mentality changes and at the same time keeping SPZOZ structure. Responsible managers of hospitals, seeing all the constraints of SPZOZ, should decide to go for commercialization to secure short and long-term development of their hospitals.

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**III.**  
**BUSINESS AND NON-PROFIT**  
**ORGANIZATIONS – GLOBAL AND**  
**REGIONAL ASPECTS**



# ACTIVITIES OF NATIONAL PARKS AS A SOURCE OF REVENUE FOR THEIR COMMUNES. CASE STUDY OF BABIA GÓRA NATIONAL PARK<sup>1</sup>

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## **Abstract**

*The paper discusses the impact of Polish national parks on their respective communes' own revenue. It presents important changes that were introduced in 2010-2012 in the parks' legal situation and financing. It discusses financial relations between the parks and commune administrations (local government bodies), focusing on the impact of parks on the communes' own revenue. The example of Babia Góra National Park is used to present detailed issues.*

*The impact of national parks on finances of local government bodies depends largely on legal regulations in force, including in particular regulations governing the parks' legal form and funding, as well as those concerning local taxes, tax exemptions and reductions, and compensations of lost revenue for the communes. Local circumstances also play a key role. These include: relative area of the park in a commune, use pattern of protected areas, location of the park's head office, size of real properties and the type and form of their use, number of staff in the park, the park's activities, as well as its social and economic environment.*

**Keywords:** national park, local government, local taxes, own revenue.

## **1. Introduction**

In Poland's well developed system of protected areas, national parks play a key role. They cover areas of outstanding natural value, representing all of Poland's landscape zones. The total area of Poland's 23 national parks is 314.6 ha (1% of the country's area), of which 22.5% is under strict protection. Most national parks were created between 1947 and 1989 as a result of government decisions taken with no regard to the opinion of local communities or the social and economic consequences on the local level. National parks saved areas

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of significant natural value from degradation by rapid development of urban areas, industry and mass tourism infrastructure. At the same time, however, they met with negative reactions from local communities that were subjected to restrictions they often did not understand or accept. Those contradictions have been broadly discussed in literature, with a focus on obstacles hindering local development as a result of introducing legal protection in a given area.

Nowadays, following political and economic transformation that entailed a rejection of central state control and a shift of responsibility to local and regional government levels, as well as a development of market economy, national parks have become important in local economy and their relations with local government entities grew in significance. National parks, in their capacity as employers, land owners, business operators and taxpayers, have direct or indirect impact on their respective communes' financial standing. Those relations are largely influenced by current changes of national parks' legal situation and funding, as national parks have been transformed into State-owned legal persons and acquired far-reaching autonomy in terms of their organisation and funding.

This paper aims at identifying financial relations between national parks and their hosting communes and presenting changes in communes' own revenue from local taxes as a result of transformations of national parks' organisational and legal form in 2010-2012. The example of Babia Góra National Park is used to illustrate specific issues.

As its key objective, the paper seeks to verify the following hypothesis: the change of Polish national parks' organisational and legal form has not resulted in an increase of communes' budgetary revenue raised in local taxes and income tax paid by Babia Góra National Park in 2010-2012.

In the research we analysed the dynamics and structure of revenue from local taxes paid by Babia Góra National Park as a percentage of total revenue from each type of tax in the communes hosting the Park.

## **2. Legal and organisational basis of national parks' in Poland**

Each national park in Poland operates in the public sector and its operation is governed by legal regulations. According to the Act of 16 April 2004 on Nature Conservation, a national park covers an area of not less than 1,000 ha, of particular natural, scientific, social, cultural and educational value, where the totality of nature and landscape assets is protected (*Ustawa...*, 2004a, Article 8). Each of Polish national parks is established, as a State-owned legal

person, by virtue of a separate legal act pursuant to Article 30(1) of the Public Finance Act<sup>4</sup>.

In 2010-2012, legal basis and organisation forms of Polish national parks were modified considerably, which had an impact on the financing of their statutory activities. That evolution was initiated by the adoption of the Public Finance Act on 27 August 2009. One of its provisions excluded the so-called auxiliary holdings, hitherto associated with budgetary entities on the State or commune level, from the list of public finance sector entities (Filipowicz 2012, p. 294-297). In practice, as a result, auxiliary holdings ceased to exist altogether. Until the end of 2010, national parks operated, under the Public Finance Act of 2005 and the Nature Conservation Act of 2004, as State budget entities (*Ustawa...*, 2004a, Article 8 in its wording in force until 31 December 2011), supported by their associated auxiliary holdings, which carried out parts of the parks' statutory activities.

A State budget entity is a public finance sector entity which covers the entirety of its expenditure directly from the State budget and transfers its entire revenue to the State budget. This is known as the “gross-type” settlement of accounts (Borodo 2011, p. 34-35). In order for the national parks to operate legally and efficiently, but purely as public utility entities rather than commercial businesses, part of their statutory activities had to be outsourced to separate entities which could, for instance, collect entrance fees, sell licences, timber, etc. Those entities became known as “auxiliary holdings”. In principle, they covered their expenditure from their own revenue and settled their accounts with the State budget according to the “net-type” method (Etel, Tyniewicki, 2012, p. 185). Specifically, they were required to transfer one-half of their profits to the State budget (*Ustawa...* 2005, Article 26). The use of the other half of the profit was left to the discretion of the national park manager.

Auxiliary holdings associated with State budget entities were designed to operate as quasi-businesses carrying out those activities that could be outsourced. In practice, the outsourcing of activities by national parks was purely formal, which was criticised by the Supreme Audit Office (Babczuk, Krawiec 2009, p. 17).

Auxiliary holdings operated until the end of 2010. Throughout 2011, national parks operated purely as State budget entities. They however struggled in organisation and administration terms. Following the closure of auxiliary holdings, no entity was made responsible for continuing their activities. That was especially relevant as the income of auxiliary holdings had been high enough to largely cover the costs of the parks' conservation effort.

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<sup>4</sup> As of 1 January 2012, Article 8a of the Nature Conservation Act entered into force. According to that Article, each national park in Poland is a State-owned legal person. Until 31 December 2011, national parks were established by virtue of a regulation of the Council of Ministers.

According to the law, the scope of operation of State budget entities is restricted to public utility activities, whereas the auxiliary holdings had carried out tasks far beyond that scope.

2012 saw another change in the national parks' legal situation. Under the new Act of 18 August 2011 amending the Nature Conservation Act and certain other acts (*Ustawa...*, 2011), national parks were transformed from State budget entities into State-owned legal persons (as defined in Article 9(14) of the Public Finance Act of 27 August 2009). That change has allowed the parks to conduct business under the Business Freedom Act of 2 July 2004 (*Ustawa...*, 2004b) and to fund their statutory activity and administrative costs from their own funds and the revenue they raise.

Financial planning arrangements evolved to follow the legal and organisational modifications. In 2010, as national parks still operated as State budget entities with associated auxiliary holdings, each park drew up two financing plans, one for itself and the other for its auxiliary holding (Waryszak 2008, p. 20-22). In 2011, once the auxiliary holdings ceased to exist, national parks sought a new preferable solution to maintain liquidity. Each of them still drew up two financial plans for itself as a State budget entity: one concerned the park's own budgetary resources and the other was made to manage the special purpose reserve provided from the State budget to cover the expenditure on activities that had earlier been performed by the auxiliary holdings. In 2012, once national parks were transformed into State-owned legal persons under the Nature Conservation Act, each of them drew up a single financing plan.

National parks fund their operation from State budget subsidies, own funds (revenue from the park's own activities) and external funds. Significant revenue is raised on sale of services, goods and assets, and lease of property. Some parks raise much of their revenue from entry fees, licences granted, fees for entry of vehicles used by lessees of tourist facilities for their business, and fees for commercial use of the park's helicopter. The park manager may also introduce other fees, such as for commercial use of the park's grounds (e.g. for horse-drawn sled or carriage rides for guests), hosting sport events, shooting of films on location in the park etc. Other sources of own revenue include sale of publications, fees for photography and filming permits as well as permits for certain types of active tourism (rock climbing, bike tourism), fees for campfires, education services, proceeds (or share in proceeds) from coin-operated stationary binoculars or snack machines, rental of bicycles or horse-drawn carriages (Berbeka 1997, p. 61-62; Bołtromiuk 2010, p. 144). A significant part of the parks' own funds is raised from sale of timber, which can be considered a type of side activity. Parks also receive rent from lease of properties. They can also obtain external funds, such as from the National Fund for Environmental Protection and Water Management, the Provincial Fund for

Environmental Protection and Water Management, as well as donations from private commercial sponsors. Until 2012, for institutional reasons, national parks had very limited possibilities to apply for European Union funding. Those limitations were eased thanks to the change of the parks' legal and organisational form.

Those changes were made to introduce a more orderly structure of national and local government economy, including by eliminating the dual type of the parks' legal organisation and increasing transparency of their funding. They should also result in improved economic standing of the parks, due to their broader financial autonomy, including more opportunities to apply for external funding. That should stimulate the parks' managers to seek new funding sources and to use their funds more efficiently.

In relations with their hosting communes, the parks' changed legal status and organisation results in their different standing than before in terms of local taxes. That has required a new interpretation of tax regulations, including in relation to an exemption from corporate income tax (CIT) (a share of proceeds from CIT goes to the communes).

### **3. National parks' impact on the financial standing of their hosting communes**

The significance of Polish national parks in local economy has not been subject of in-depth research and seems to be underestimated. One of the scarce studies on that subject was provided by A. Bołtromiuk, who presented the economic context of Białowieża National Park (Bołtromiuk 2010). The parks' influence is usually perceived as a restriction on the freedom of economic use of their respective areas, which results in social tensions (Królikowska 2007). Perceived benefits usually include promotion of the region among tourists (Zawilińska 2012). In foreign literature, economic significance of national parks is often presented, but their impact on their local surrounding is usually analysed in terms of visitors' spending (studies include: Huhtala 2007; Saayman, Saayman 2006; *Economic benefits of ...* 2009; *Economic Impact of ...* 2011). Tourists' spending is certainly of crucial economic importance in many Polish national parks as well, however most of that spending is not directly linked with the parks' operation.

In Poland, national parks include areas or parts of areas of 119 communes in 48 powiats (districts) in 12 voivodeships (provinces). Most parks cover areas of several communes each (ranging from two communes for Tuchola Forest NP to as many as 14 for Biebrza NP, which is Poland's largest). Communes hosting national parks are predominantly rural: 64% of them are rural-type communes and 26% are combined rural-urban type. Most parks are

located far from major cities (with the exception of Ojców NP, Kampinos NP and Wielkopolska NP) and in areas of relatively low population density (the average population density of communes hosting national parks is 58 persons per km<sup>2</sup>) (Zawilińska 2012).

Local taxes are a source of significant own revenue for communes, allowing them to make decisions independently, largely meet the needs of local community and improve the standard of their services. Local taxes are source of budget revenues for communes only. They include: real property tax, agricultural tax, forest tax, tax on means of transport, tax on inheritances and donations, “tax charter”, tax on civil law transactions and local residents self-taxation. Local taxes that are particularly relevant in the context of national parks’ operation are forest tax, agricultural tax and real property tax. Other taxes are either incidental or unrelated to the national parks’ operation. National parks also benefit from tax exemptions which decrease their respective communes’ revenue. Own revenue of communes related to national parks also include a share in proceeds from corporate income tax that the parks have been subject to since 2012.

A national park is usually the major land user in its hosting communes, being either the largest or one of the largest land users<sup>5</sup>. It therefore provides a significant share of local taxes for its communes. The payment of real property tax and the scope of taxation is regulated by the Local Taxes and Duties Act (*Ustawa...*, 1991, Articles 5 and 6). Real property tax exemptions are particularly relevant for national parks. Under the law, the full exemption covers lands under strict protection, active protection or landscape protection, as well as buildings and structures within national parks, permanently fixed to the ground, that directly serve nature conservation purposes (*Ustawa...* 1991, Article 7). In practice, tax returns submitted by national parks specify land plots, buildings and structures which serve nature conservation purposes. These exclude in particular facilities put up for rent.

In the context of real property tax obligation, auxiliary holdings, associated with State budget entities, could be of relevance in 2010. According to Article 3 of the Local Taxes and Duties Act, under the rules described above, auxiliary holdings were in principle not subject to real property tax. That was because each auxiliary holding, as an entity without legal personality, represented the State Treasury or a relevant local government body and concluded all its civil law transactions on their respective behalf. For that reason, any real properties, buildings or structures were not formally owned by the auxiliary holding but, respectively, by the State Treasury or the local government body. Under the regulations in force until the end of 2010, auxiliary holdings could be

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5 In 10 communes, national park area accounts for more than one-half of the commune area (up to 86% covered by Kampinos NP in Izabelin Commune).



required to pay real property tax only if they were legally appointed perpetual administrators of property (Dolińska-Pierwoła 2007, p. 13-14).

The fact that national parks have been transformed into State-owned legal persons and allowed to conduct business has not in practice changed their situation as regards exemption from real property tax. That is because all lands located on protected areas as well as all buildings and structures serving nature conservation purposes within national parks and nature reserves are exempt from real property tax, irrespective of their owner and the type of the owner's activity.

The said exemption decreases tax revenue of communes hosting national parks, therefore those communes indirectly and partly bear the costs of the parks' operation. Where such tax exemptions and reductions have been introduced to meet objectives of national relevance, the State is legally obliged to fully compensate the communes for their lost revenue (*Opinia...* 2013, p. 6). Such compensations have been expressly provided for in Article 7(4) of the Local Taxes and Duties Act. Under that provision, local government bodies are entitled to a reimbursement of revenue lost due to exemption from real property tax of lands under strict protection, active protection or landscape protection, as well as buildings and structures within national parks and nature reserves, permanently fixed to the ground, that directly serve nature conservation purposes. Detailed procedures of that reimbursement are laid down in Minister of Finance Regulation of 28 May 2007 on the reimbursement of revenue lost by communes due to exemption from real property tax granted to national parks, nature reserves and businesses operating as research and development centres (*Rozporządzenie...*, 2007).

Pursuant to the Regulation, the reimbursement of lost revenue is made on the request of the commune, which must be submitted to the competent voivode (head of province) no later than 31 March of the year following the year for which reimbursement is sought. Upon approval of the request by the voivode, the commune obtains the reimbursement of the lost amount. However, grounds within national parks may also be exempt from real property tax under other provisions of the Local Taxes and Duties Act<sup>6</sup> which do not allow communes to request compensation. It is also worth noting that commune authorities are entitled but not obliged to request compensation. Therefore, they might still lose the revenue on real property tax, for instance if they fail to make the request within the deadline.

National parks are also liable to pay forest tax to their competent local administration. The calculation of that tax is governed by Forest Tax Act of 30 October 2002. As forests account for 61% of the total area of national parks

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<sup>6</sup> Areas exempt from real property tax include e.g. wastelands, ecological areas, or areas covered with trees or shrubs, excluding those under commercial use (Article 7(1)(10)).

in Poland (*Ochrona środowiska* 2012), that tax is significant in the general scale of Polish national parks. Pursuant to the Act, the payable tax amounts are reduced by 50% for protected forests and forests within national parks and nature reserves. Furthermore, forests of a tree stand age of less than 40 years, forests included individually in the national heritage register and ecological areas are exempt from the tax (*Ustawa...* 2002, Article 4).

National parks are also required to pay agricultural tax on lands classified as agricultural lands in the land and building register. The tax is paid according to rates defined in the law. The Act does not provide for an exemption subjective for national parks, as well as any special exemptions in question due to the use of this form of protection (*Ustawa...* 1984). However, in the scale of national parks in general, agricultural tax is not significant. This is because agricultural lands account for small percentage (14%) of national parks' total area. Also, the rate of agricultural tax paid by national parks is usually low as a result of three factors that determine the calculation of reference area for taxation. Those factors are: classification of the host commune to a tax district; determination of land quality class; and determination of the type of agricultural use of the land.

National parks also transfer proceeds from local visitors' tax or health resort visitors' tax to their respective communes. These taxes are collected from individuals who spend more than 24 hours for therapy, tourism, leisure or education in localities which:

- have favourable climate or landscape characteristics and conditions that allow them to receive visitors for the purposes mentioned above;
- are located in areas legally recognised and protected as health resorts.

National parks are required to charge those taxes if they own their own accommodation facilities and provide accommodation to visitors (*Ustawa...* 1991, Article 17).

Local government budgets also receive a share of corporate income tax paid by national parks. In 2010, 2011 and 2012 the share of regional and local administration bodies of all levels in CIT revenue was 22.86% each year; the communes received 6.71% of the total per year (Jastrzębska 2012, p. 111). Legal and organisational status of national parks is highly relevant for their CIT obligations. In 2010 and 2011 national parks, operating as State budget entities, were exempt from CIT (*Ustawa...* 1992, Articles 6 and 27). In 2010, auxiliary holdings were required to pay the CIT. Some of those holdings, e.g. those associated with national parks, could benefit from an exemption laid down in Article 6(2) of the CIT act, provided that they used the amount saved thanks to the exemption on increasing its working capital or financing the investments of the State budget entity up to the value of capital involved in the holding (Musiał 2010, p. 49).

Following national parks' transformation into State-owned legal persons in 2012, controversies emerged concerning the interpretation of CIT regulations. On 20 March 2012, the Head of Tax Chamber in Łódź, acting on behalf of the Minister of Finance and on request of a national park, issued an individual interpretation of the applicability of the exemption laid down in Article 17(1) (4) of the CIT Act, regulating environment protection (in its part concerning the objective of national parks' activities), to national parks. According to that interpretation, national parks, which have nature conservation defined as their main objective in their statutes, are exempt from CIT. This is because nature conservation is understood as a subtype of environment protection. However, that exemption may only be used if the revenue of the park's business is allocated to be spent on its statutory activities. It was also emphasised that the exemption does not depend on the type of revenue (except for the types listed in Article 17(1a) of the CIT Act) but depends strictly on the purpose that the revenue is to be used for<sup>7</sup>. Still, ambiguities in interpreting the said provisions had led some of the national parks to pay CIT in 2012.

Corporate income tax is calculated on the income, i.e. the difference between the revenue raised by the national park (for instance, on sale of timber or collection of various fees mentioned in Section 2) and costs inherent to the national park's operation. Such costs also include the payment of local taxes by the national park, which decrease the park's income and, consequently, the amount of CIT transferred to the communes as their budgetary revenue. For communes, the revenue that they are entitled to as their share in CIT paid by national parks is negligible, as national parks were exempted from CIT in 2010 and 2011 and had a right to be exempt in 2012, as mentioned above (though some parks still paid the CIT in that year due to ambiguous legal regulations). At present, the above mentioned interpretation issued by the Head of the Tax Chamber in Łódź clearly defines the entitlement to CIT exemption.

Each national park, as a business operator, clearly has an impact on the income of local government entities in its area and the local economy in general. The mere fact of establishing a national park, resulting in restrictions in spatial management, also has a significant impact for local economy and often results in the park being perceived by local communities as an obstacle to economic development. It might seem economically much more profitable in the short term (both for the local communities' budgets and broadly for the economy) if the same area could serve other purposes. Those relative benefits would however relate to the direct use value of the area and the revenue resulting therefrom. The balance of benefits and losses would shift upon assuming a longer timeframe and broader perspective, taking into account indirect use

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<sup>7</sup> Individual interpretation no. IPTPB3/423-37/12-2/PM of 20 March 2012.

values, option values and non-use values of the parks (Philips 1998; Famielec 1999, p. 85; Woś 1995, p. 280).

#### 4. Babia Góra National Park as payer of local taxes and its impact on budget revenue of the hosting communes

Babia Góra National Park (BGNP, *Babiogórski Park Narodowy*) is one of Poland's oldest national parks. It was established in 1954 and covers the Babia Góra massif, the highest in the Outer Western Carpathian range (culminating at 1,725 m above sea level). Currently at 3,393.81 ha, it is one of Poland's smallest national parks. In terms of administration divisions, BGNP is located in the southern part of Małopolskie Voivodeship, covering parts of three communes: Zawoja (75.4% of BGNP's area and 19.8% of the commune's area), Lipnica Wielka (24.3% and 12.2%, respectively) and Jabłonka (0.4% and 0.1% respectively); cf. Table 1. The Park is surrounded by a buffer protection zone covering the area of 8,437 ha. Nearly all of BGNP's area (96%) is under the Park's usufruct. Most of the remaining land within the Park's boundaries, located mainly in Zawoja Commune, is owned by land and forest communities.

**Table 1.** Babia Góra National Park's land area in relation to its hosting communes

Commune	Commune area (ha)		BGNP area (ha)				Share of BGNP area in commune area	Share of BGNP forest area in commune's total forest area
	total	of which:	total	of which:	Arable land	Other		
		Forests		Forests			(%)	
Jablonka	21,273	7,068	13	12	0	1	0.1	0.2
Lipnica Wielka	6,736	3,002	826	775	10	42	12.3	25.8
Zawoja	12,878	8,274	2,554	2,454	21	78	19.8	29.7
Total	40,887	18,344	3,392	3,240	31	121	8.3	17.7

Source: data from Central Statistical Office's (GUS) Local Data Bank and BGNP.

Forests dominate in BGNP, covering 95.3% of its area. Most of the remaining area is around the Babia Góra summit, above the upper limits of forests. Despite its small size, the Park is much visited: in 2013 the number of visitors was approximately 80 800, based on the numbers of entry tickets sold (*Analiza działalności...* 2013).

In 2012, BGNP's revenue was PLN 7.25 million, of which 29.1% was a subsidy from the State budget and 47.6% was raised as own revenue. The remainder was obtained under project funded by the European Union and the National Fund for Environmental Protection and Water Management. BGNP

has relatively high financial autonomy, chiefly thanks to high revenue on sale of timber, which accounted for 88.5% of own revenue in 2012.

BGNP's expenditure in 2012 was PLN 5.94 million. Around one-half of that amount (PLN 2.99 million) was spent on salaries and administration costs. A significant portion of the Park's expenses goes to operators located within the hosting communes or, as salaries, to local residents. As a taxpayer, BGNP has direct impact on the financial situation of local government entities. Due to the land use structure within the Park, the forest tax is the most significant element. Forests within BGNP account for as much as 30% of all forests within Zawoja Commune and 26% within Lipnica Wielka Commune (cf. Table 1). Pursuant to the Forest Tax Act of 2002, national parks pay a reduced rate of forest tax, equal to one-half of the normal rate (*Ustawa...* 2002).

Despite that reduction, proceeds from forest tax paid by BGNP accounted for 21% in 2010 and 2011, and 20% in 2012, of Zawoja Commune's total forest tax revenue. In Lipnica Wielka Commune, the corresponding percentage in the same period was between 18% and 19% (cf. Tables 2 and 3). The high increase of the tax amounts in those three years was due to an increase of the tax rate. From the communes' perspective, the protection of forest areas under the National Park and the resulting reduced tax rate causes a significant loss of income and is a source of deficit. However, the forest tax income for communes hosting BGNP would probably be similarly reduced even if the Park did not exist, as the forest areas would most probably enjoy a different type of protection, therefore the reduced tax rate would still apply to them.

As agricultural land covers a minor proportion of BGNP's area, the agricultural tax paid by the Park (only in Zawoja Commune) is negligible for the commune's finance (cf. Tables 2 and 3). On the other hand, real property tax revenue is significant. BGNP owns land, buildings and structures (including the head office, residential buildings, utility buildings, rain shelters), but most of them directly serve nature conservation and are thus exempt from tax. Tax is only paid on facilities not directly serving nature conservation, e.g. buildings put up for rent. In this context, there are disagreements between BGNP and the communes, concerning the calculation of tax due and possible exemptions, as it is difficult to identify clearly whether a building or structure serves the purpose of nature conservation directly or indirectly.

Unlike forest tax reduction, the exemption of national parks from real property tax does not reduce local governments' tax revenue in real terms, as the communes' lost revenue is reimbursed in full upon request by the commune, submitted to the voivode (under Article 7(4) of Local Taxes and Duties Act and the Minister of Finance Regulation of 28 May 2007 on the reimbursement of revenue lost by communes due to exemption from real property tax granted to national parks, nature reserves and businesses operating as research and

development centres). Zawoja Commune obtained such reimbursement in 2010-2012, while Lipnica Wielka Commune has not thus far requested the reimbursement.

**Table 2.** Local taxes due from Babia Góra National Park in 2010-2012

Tax type	Year	Jablonka	Lipnica Wielka	Zawoja	Total tax amount
		(PLN)			
Forest tax	2010	111	11,353	31,402	42,866
	2011	197	13,712	35,518	49,427
	2012	238	15,270	42,106	57,614
Agricultural tax	2010	0	0	132	132
	2011	0	0	146	146
	2012	0	0	287	287
Real property tax	2010	0	371	1,795	2,166
	2011	0	746	2,027	2,773
	2012	0	2,314	6,055	8369
Exemption from real property tax	2010	0	7,050	23,532	30,582
	2011	0	7,050	24,954	32,004
	2012	0	5,745	37,652	43,397

Source: data from BGNP and Lipnica Wielka and Zawoja Commune authorities.

**Table 3.** Proportion of local taxes due from Babia Góra National Park in the tax revenue of communes in 2010-2012.

Tax type	Year	Total revenue of commune under given tax			Proportion of revenue under given tax raised from BGNP in total revenue under that tax*		
		Lipnica Wielka	Zawoja	Total LW+Z**	Lipnica Wielka	Zawoja	Total LW+Z**
		(PLN)			w %		
Forest tax	2010	64,217.8	148,253.5	212,471.3	17.7	21.2	20.1
	2011	71,216.4	168,662.9	239,879.3	19.3	21.1	20.5
	2012	85,810.6	206,395.4	292,206	17.8	20.4	19.6
Agricultural tax	2010	7,839.1	18,404.7	26,243.8	0	0.7	0.5
	2011	19,579.9	20,757.1	40,337	0	0.7	0.4
	2012	39,703.1	40,523.9	80,227	0	0.7	0.4
Real property tax	2010	239,234.5	1,447,478.7	1,686,713.2	3.1	1.8	1.9
	2011	236,427.6	1,755,340.1	1,991,767.7	3.3	1.5	1.7
	2012	262,275.3	1,906,997.1	2,169,272.4	3.1	2.3	2.4

\* For real property tax, the proportion includes the amount paid by BGNP and the amount of the tax exemption.

\*\* LW+Z – the sum of revenue raised under the given tax in the relevant period in the communes Lipnica Wielka and Zawoja and the proportion of the combined amounts paid in tax by BGNP in the communes Lipnica Wielka and Zawoja in the total budget revenue of those communes under the given tax.

Source: data from Central Statistical Office's (GUS) Local Data Bank and BGNP.

In Jabłonka Commune, the only tax paid by BGNP is the forest tax, but its share in the commune's revenue is close to nil due to small areas of BGNP forests in the commune. For that reason, figures for Jabłonka Commune have been omitted in Table 3. In the other two communes, there is a visibly high proportion of forest tax paid by BGNP in the total forest tax revenue. The Park also brings significant income for the communes in its capacity as real property owner (Table 3).

## **5. Conclusion**

National parks play an important role in the local economies and largely affect the revenue level of their respective local government entities. The size and nature of that impact depend both on local circumstances and the legal regulations in force. Local circumstances include in particular: the relative area of the national park within its hosting communes, use structure of protected areas, age of tree stands, location of the park's head office, the types of real properties owned by the park as well as their size and use, number of staff in the park, the types of its activities, as well as the park's social and economic environment (population potential, economic potential, functional structure of the commune's territory). Legal regulations which are relevant for the parks are in particular those governing their legal form and funding arrangements, as well as local taxes, tax reductions and exemptions available, and compensations offered to the communes for their lost revenue.

In terms of national parks' impact on the financial standing of communes, it is mostly negative in communes where the national park covers a significant proportion of the commune's area and includes mostly forests with tree stand older than 40 years. For those areas, the communes only receive one-half of the forest tax amounts that they would be entitled to if the forest was outside national park boundaries (provided that the forest was under protection as a nature reserve or protected forest or was not subject to tax exemption for another reason).

Real property tax payable by national parks also directly affects the communes' finance. National parks have numerous buildings and structures in their usage. Given that most parks are located in rural areas, often sparsely populated and not intensively developed, they probably provide a large proportion of real property tax revenues for their respective communes. Although most buildings and structures used by parks directly serve nature conservation and are therefore exempt from real property tax, the communes may request reimbursement of revenue thus lost from the provincial authorities, so formally they incur no losses.



Another tax of direct relevance for communes' finance is agricultural tax, however few parks contribute significant amounts under that tax. Most Polish national parks predominantly include forests, whereas arable lands, meadows and pastures only account for a minor proportion of their total areas. Furthermore, their classification into categories and tax districts often reduces the tax calculation base.

The changes introduced in national parks' legal form and organisation in 2010-2012 did not directly result in changes to the size of revenue raised by communes from local taxes. Each national park, as a State-owned legal person, is obliged to pay local taxes in the same amounts as if it was a State budget entity. The situation is different for communes' revenue under corporate income tax. National parks are subject to calculate their payable CIT as State-owned legal persons, but due to their statutory activity falling within the scope of environment protection, they are entitled to exemption from that tax.

As far as Babia Góra National Park is specifically concerned, its operation mostly benefits Zawoja Commune, hosting three-quarters of the Park's area, its head office and most of its buildings and structures. BGPN is a significant taxpayer for Zawoja Commune, where most of the Park's staff reside and where most of businesses with the strongest commercial links with the Park have their registered offices. Financial relations of BGPN with Lipnica Wielka Commune are far less strong, as the Park has less of its area in that commune, the Park's head office is located at a significant distance from the commune's boundaries and there are no direct public transport links between Lipnica Wielka and Zawoja. Other villages on the southern side of Babia Góra massif also have weak transport links with Zawoja, which is probably the factor behind the Park's limited significance for Jabłonka Commune. Due to the negligible proportion of BGPN area in the latter commune, the Park's role as a taxpayer in its revenue is marginal.

Among taxes paid by BGPN, the forest tax is the most relevant for the communes of Zawoja and Lipnica Wielka, as it accounts for approx. 20% of those communes' total forest tax revenue. The total nominal value of real property tax paid by the Park (taking also into account the reimbursement that the communes may request, equivalent to the Park's tax exemption) is similar to the amounts raised under forest tax. However, that amount accounts for a minor proportion of the communes' total revenue under real property tax. Interestingly, that proportion is lower in Zawoja Commune than in Lipnica Wielka Commune. That is because the population density is much higher in Zawoja and so is the number of buildings and businesses, which means that the commune's total revenue on real property tax is seven times higher than the corresponding amount in Lipnica Wielka Commune.



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# POSSIBILITIES OF USING PUBLIC RELATIONS INSTRUMENTS BY A PUBLIC ORGANIZATION ON THE EXAMPLE OF THE OFFICE OF TOWN AND COMMUNE OF GŁUCHOŁAZY

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## **Abstract**

*The paper deals with the issues concerning the image management. Measures in this field can and ought to be taken up not only by private companies, but also by organizations of public administration. On the example of the Office of Town and Commune of Głucholazy the author scrutinizes kinds and possibilities of using public relations instruments. As a result, the consistency and efficiency of the image management system in the organization have been evaluated.*

**Keywords:** *image management, public administration, commune, public relations. Instruments.*

## **1. Introduction**

Organizations in public administration are interested in being able to influence the public and, as a result, operate effectively. Adequate image and strong identity are necessary not only to make an organization recognizable, but also to create a positive opinion about it among the society (Flieger, Flieger, 2011). It seems that more and more public organizations start to realize this fact and they become increasingly interested in using array of public relations instruments.

Public relations itself may be defined in various ways, however, one of the most general definitions has been proposed by the World Assembly of Public Relations Associations. According to the assembly, public relations is the art and social science of analyzing trends, predicting their consequences, counseling organizational leaders, and implementing planned programs of action, which will serve both the organization and the public interest. To make it simpler, it can be said that PR is a strategic communication process

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that builds mutually beneficial relationships between organizations and their publics. The aim of these actions is to create and sustain a positive image of an organization or its products (in case of public administration the product is services). The image itself ought to be understood as what people think of an organization, it is a set of impressions which do not necessarily have to reflect reality, in other words - objective assessment (Davis, 2007; Altkorn, 2004). It is created as a reaction to an array of incentives transmitted to a company's clients. The fact that image itself is subjective (Newsom, Scott, Vanslyke, 1989) is an extremely important feature, because it means that image can be influenced and changed, so the public opinion of an organization might be created freely by using appropriate instruments (Flieger, Flieger, 2011).

It appears that public relations instruments are very efficient, a lot of organizations start to realize that focusing on creating a strong, positive image brings considerable benefits in a long term (Flis, 2007). If customers *trust* an organization, they become loyal. In case of local administration, such as the office of commune, positive perception of the region might be a crucial factor which attracts potential inhabitants, tourists or investors (Maćkowska, 2005). If local administration is perceived as professional and helpful, these groups will be eager to become interested in living, visiting or locating their business in the area.

At this point it ought to be emphasized that the nature and identity of public offices differ considerably from private companies. It is enough to consider the foundations of any organization – its mission. Regarding a public administration organization, it focuses at securing safe and decent life conditions for citizens. What is more, *local* administration is expected to solve local problems in an emphatic and ethical way (Knecht, 2006). As a result, the assumptions which constitute the basis of undertaking measures in the field of PR in public organizations are quite different from the motivation of private businesses. Firstly, the hierarchy of objectives differs. In case of communes, the utmost goal is to present what matters the office copes with and, as a result, to build the atmosphere of social acceptance of their actions. However, the level of support and trust does not have any influence on the office's position in the administrative system, whereas in case of private organizations creating an image is just the way to secure financial stability. What is more, public organizations seem to be *obliged* to create image actively, especially in terms of informing about their actions and initiatives, especially that public offices are financed by tax payers. Regarding private companies, getting involved in any measures in the field of image management is once again conditioned by the possibility to increase profits. Thirdly, there is a profound difference regarding the initial public interest of both organizations. There is a strong

tendency among the public to monitor and judge the work of civil servants. In case of private businesses, such initial interest does not exist at all.

Another difference is that because of the statutory foundations public organizations do not have any real competition. Concerning private business, it is quite obvious that the competition is most often strong. Finally, there exists a very important difference concerning the consequences of mistakes in creating image. For the public office, the ultimate result of negative image is only the decrease in level of trust, whereas private companies may even go bankrupt (Giedrojć, 2004; Flieger, Flieger, 2011).

It seems vital to be conscious of the abovementioned differences, for it lets us understand considerably better the circumstances in which public offices operate and conditions which must be taken into account in order to create and manage their image more effectively.

Taking the abovementioned aspects into consideration, the author of the article decided to analyze possibilities of using public relations instruments by a public administration organization. The research has been carried out, together with Katarzyna Batog from General Tadeusz Kościuszko Military Academy of Land Forces, on the example of the Office of Town and Commune of Głuchołazy. As a result, the author made an attempt to determine whether the scrutinized office of commune is able to create a concise system of image management.

In order to achieve this objective, the author has put into scrutiny the documents, both internal and external, which constitute legal foundations for actions in the field of public relations, analyzed symptoms of the commune's public relations activities (both visual and non-visual factors), and carried out an interview with the person who is responsible for creating positive image of the Office of Town and Commune of Głuchołazy by implementing appropriate PR instruments.

## **2. Public relations instruments used by the Office of Town and Commune of Głuchołazy**

Commune of Głuchołazy is a part of Nysa District (in Lower Silesia Province) and it covers the area of 160,7 square kilometers. It has a population of 26000 inhabitants. The Office of Commune of Głuchołazy constitutes a basic unit of a local administration system and its main objective is to organize public life on its territory (Ustawa o samorządzie gminnym [Act on Commune Self-Government], tekst jednolity Dz.U. z 2001 r. Nr 142, poz. 1591; Statut Gminy Głuchołazy [Statute of Głuchołazy Commune], Uchwała nr. 9/60/03 Rady Miejskiej w Głuchołazach z dnia 27 czerwca 2003 r [Resolution of Town Council of 27<sup>th</sup> June 2003]). Concerning the structure of the Office, it consists of

seventeen departments (Zarządzenie nr. 328-Pr.157/08 Burmistrza Głucholaz z dnia 12.06.2008 r [ Resolution of Głucholazy Mayor of 12.06.2008]). The public relations tools used by the commune and analyzed in the paper are: client service, media relations, Corporate Identity, sponsoring, image crisis management, commune's own publications and internal communication.

### *Client service*

Definitely the crucial instrument which is supposed to create a positive image of any organization is the way a client is taken care of by a personnel. At the beginning of the analysis of this instrument it is important to stress that the mayor of Głucholazy town has set the following ultimate objective for all the employees: recognizing and fulfilling all expectations and needs of the Office's clients. What seems especially interesting is the fact that this client has been divided into two categories – an active one and a passive one. The first sort is understood as a person who visits the Office in order to deal with some administrative matters. The latter ought to be perceived as the whole local community, other offices of public administration, cultural and political organizations, all sorts of societies, tourists visiting the commune, local entrepreneurs and also all the people employed in the Office.

There are a few basic elements which constitute a concise system of clients service in the Office of Town and Gmina Głucholazy. First of all, the Office has determined crucial standards regarding the way a client is taken care of:

- the most important people are *clients*,
- clients are not dependant of the Office,
- clients do not disturb the way the Office operates, but they are its crucial goal,
- clients are an *internal* part of the organization, not people from outside,
- each case ought to be treated with proper attention,
- the main objective is to fulfill clients needs,
- clients deserve full attention and kindness from personnel (ISO 9001:2009, <http://www.glucholazy.vel.pl>, access: 12.02.2014).

What is more, the Office has created different ways in which a client is able to contact the organization, has implemented the system of effective dealing with issued complaints and applications, has done regular research on client's satisfaction, and finally implemented methods of continuous improving personnel's skills in the field of client's service. Concerning the latter factor, the mayor of Głucholazy has put into practice the rule of employing only the clerks who fulfill formal demands stated in acts (Ustawa o pracownikach samorządowych z dnia 21 listopada 2008 r., Dz.U.2008.223.1458 [Act on

Territorial Self-Government Staff]). Thus, a clerk should possess appropriate education, skills and work experience. One of the essential conditions of professional service is possessing thorough knowledge in the field of legal regulations and procedures. Each procedure implemented in the Office stems from particular legal regulations and is dedicated to some particular service provided by the Office.

What is extremely important, in order to improve personnel's qualifications, the mayor has created a system thanks to which clerks can take part in trainings, workshops and seminars. The effects of such activities are controlled during systematic evaluation of the quality of their work.

Client service in the Office of Town and Commune of Głucholązy to a vast extent is based on an effective information system between a clerk and a client. In order to build such a concise system the following measures have been taken up:

- clients may have an appointment with the mayor each week on Monday between 12 and 4 pm; they may also send an e-mail directly to the mayor,
- all personnel has been trained to be able to give a client complex information regarding all major aspects of Office's operations, structures and procedures,
- a system of information boards has been created, informing clients about current affairs, e.g. upcoming tenders,
- by the doors to each department there are plates which inform about names of workers, their position, main responsibilities and a person to contact in case of absence,
- the most important and popular documents (forms) have been put on the Office's webpage – they can be downloaded,
- the system of issuing and dealing with complaints and applications has been implemented (Zarządzenie Burmistrza z dnia 28 lutego 2012 r. [Mayor's Resolution of 28<sup>th</sup> February 2012]),
- by using headphones and a microphone connected with a personal computer, a client gains a possibility to contact the Office's Secretary on-line,
- on the webpage of Głucholązy Bulletin of Public Information telephone numbers to all departments of Town Office have been publicized; the Bulletin also allows publicizing other information regarding Office's operations,
- in case there is such a need, the Office publishes brochures which inform clients about Office's operations.

In the context of providing professional service for clients it is important to emphasize that since the year 2010 the Office has been implementing and realizing a so-called Quality Policy, which is based on Quality Management



System (the system stems from the norm PN-EN ISO 9001:2009).<sup>2</sup> As a result, the mayor has accepted Book of Quality, which constitutes a most important document in which all elements of Quality Management System in the Town Office of Głuchołazy are listed and described, including Policy objectives, all quality procedures and processes and relations between them. What is especially important is the fact that all this information is easily available for all employees, who also have been trained in the field of quality issues. In this way the Book of Quality constitutes a base for all units to set appropriate objectives concerning quality.

Thus, crucial goals of Quality Policy include:

- dealing with the administrative matters initiated by clients as fast as it is possible, especially obeying deadlines which are stated in law regulations,
- constant trainings, both internal and external, for personnel, including supporting employees who study at universities,
- constant improvement of communication system, both internal and between the Office and its clients,
- defining management units which are responsible for improving quality of the services provided by the Office,
- securing resources which are needed to make Quality Management System function effectively,
- implementing so-called open information policy for both employees and clients by using IT systems (Polityka Jakości Urzędu Miejskiego w Głuchołazach, <http://www.gluchołazy.vel.pl>, access: 12.02.2014).

In order to monitor if clerks obey the rules and procedures concerning client service stated in Quality Policy, the Office has implemented a mechanism of checking client satisfaction by using a standard survey test for local administration offices, certified by Polish Chamber of Foreign Commerce.<sup>3</sup> Taking part in this program allows the Office of Town and Commune of Głuchołazy to compare client service quality standards with other offices which participate in this undertaking. As a result the Office gains objective, comparable information regarding the standard of service and at the same time sets fundamentals for further improvement in this field.

One of the groups of Office's clients who are especially important and welcome are tourists who come to the region. Service for this group has also been prepared professionally. Within Department of Promotion, Tourism and Sport there exists Tourist Information Center, which is donated by EU funds.

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1 Implemented as a part of the project 'Sprawny Samorząd. Wdrażanie Usprawnień w Zarządzaniu jednostką samorządu terytorialnego w 10 Urzędach Gmin i 2 Starostwach Powiatowych z Terenu Województwa Opolskiego i Śląskiego' (Efficient local government. Implementing rationalizations in management of local administration organizations in 10 Commune Offices and 2 District Offices in Opolskie and Śląskie Provinces).

3 Implemented as a part of the sixth edition of the project 'Badanie Satysfakcji Klienta Urzędu z Wykorzystaniem Jednolitego Treściowo Kwestionariusza Ankietyowego' (Research on a client's satisfaction using a unified questionnaire).



The center operates from the beginning of May to the end of September and it provides service in following fields:

- giving tourist information about the region,
- informing about cultural and sport events,
- informing about regional system of communication,
- selling maps and other publications concerning the region,
- preparing presentations and taking part in fairs and international exhibitions,
- providing press service.

Moreover, in the center it is possible to use a multimedia computer, sponsored by a program realized by Regional Tourism Organization (Centrum Informacji Turystycznej w Głuchołazach, <http://www.glucholazy.pl>, access: 21.02.2014).

### ***Media relations***

Apart from providing professional service for people who visit the Office of Town and Commune of, the second most important tool which is supposed to create positive image of the organization is relations with local media and the way the information about the organization and the region is presented in them. The Office ought to build concise system of information which enables creating a dialog with all the members of the public. Local media constitute one of the channels which seem to play extremely important role in making this process effective.

At the beginning of this analysis it should be stated that in the Office the position of spokesman has not been created. Contact with media is managed directly by the mayor or his deputy or a secretary. In some cases the media is contacted directly by a clerk who works in the department which is responsible for some particular case in question. Most often they are people who work for Department of Promotion, Tourism and Sport, Office of Town Council, Department of Municipal Administration, Investments and Architecture.

The message from the Office is passed on to various journalists from both press, television, radio and the Internet. On the official webpage of the city of Głuchołazy there can be found a list of official media patrons with which the city cooperates. However, the information about the Office is presented also by other media, all of which can be divided into three basic media channels. The first one is the press. It is represented by:

- *Nowa Trybuna Opolska* – newspaper from Opole region, published both in paper version and in the Internet (<http://www.nto.pl>, access: 20.02.2014),
- *Nowiny Nyskie* – regional weekly magazine (<http://www.nowinyńskie.com.pl/>, access: 20.02.2014),

- *Moje Życie Głucholaz* – a biweekly dealing with the matters directly connected with the town and commune of Głucholazy, it constitutes a medium which puts a lot of attention to local matters and the way local government operates.

The next channel is radio and television. The Office cooperates with four local radios, two of which are very much interested in local affairs and which, as a result, often host representatives of local government. They are Radio Głucholazy (<http://glucholazyonline.com.pl>, access: 20.02.2014) and Nysa FM (<http://www.nysa.fm>, access: 20.02.2014). Local matters are also often discussed and commented in a local TV station called TVP Opole ([www.tvp.pl/opole](http://www.tvp.pl/opole), access: 21.02.2014).

The last and at the same time extremely important channel is the Internet. There are a few vital internet portals which are used to initiate and sustain a dialog between the Office and the public, and thus to create a positive image of the organization in question. The first one is [Glucholazy.pl](http://glucholazy.pl), which represents an official service of Town and Commune of Głucholazy. On the page a visitor may find all necessary information concerning:

- City Office itself – structure and management of the Office, contact to all departments, makeup and decisions of City Council, a link to Public Information Bulletin, information regarding the Office's Quality Policy, documents for clients to download,
- the whole commune of Głucholazy – addresses and contacts to all administration, cultural and education institutions, and to all companies and organizations which operate in the city, short history of the city, a list of all historical monuments, attractions, tourist routes, information concerning a bugle-call, a crest and a flag of the city, etc (<http://www.glucholazy.pl>, access: 22.02.2014).

Another portal, [glucholazyonline.pl](http://glucholazyonline.pl), constitutes unofficial service of Town and Commune of Głucholazy. What is especially interesting, apart from commenting the latest local political, cultural and sport events, it has created a chat which is dedicated to enabling local inhabitants to have a conversation with representatives of local political scene and with people working for Town Office. Moreover, the service publishes articles about local events and life in the region, written by inhabitants (<http://www.glucholazyonline.com.pl/>, access 22.02.2014).

Also Public Information Bulletin of the Town and Commune of Głucholazy is an important instrument of building positive image of the organization. The bulletin is run by one of the Office workers and it provides all information concerning the Office which is obligatory for a public organization, including: the Office internal regulations, Commune Status, description of projects financed by European Union funds, strategy and budget of gmina, unit about real estates, tenders and crisis management (Biuletyn Informacji Publicznej

Urzędu Miejskiego w Głucholazach, <http://gmina.glucholazy.sisco.info>, access: 23.02.2014).

Apart from the abovementioned portals, it is also worth to present a service run by a Culture Center in Głucholazy (<http://www.ckglucholazy.pl>, access: 23.02.2014), which publishes detailed information about cultural events. Moreover, on the web pages of Nysa FM radio ([www.nysafm.pl](http://www.nysafm.pl), access: 23.02.2014) and Radio Opole (<http://www.radio.opole.pl/>, access: 23.02.2014) the news about the town and commune of Głucholazy is often published and commented.

Commune of Głucholazy also is a participant of a program financed by EU called '*e-office for Inhabitants of Opole Region*' (<http://www.glucholazy.pl>, access: 23.02.2014). The aim of the project is to build so-called information society in the region by enabling access to public services online. Some of the results of the project are supposed to be: shortening the time of dealing with administrative matters issued by the Office's clients, decreasing the number of visits in the Office, lowering administrative costs.

Apart from commenting daily events, typical information which is broadcast to media by the Office concerns informing public opinion about awards or honorable mentions received by the workers of the organization or citizens, about commune's successful undertakings which are valuable for local community and taking part in charity events or different sorts of fairs, such as MTP Tour Salon Poznań, MTT Glob Katowice, MTT Polagra, MTT Brno.

### ***Corporate identity***

The image of the scrutinized commune requires creating a concise system of visual identification, which should be understood as all signs, graphic elements and colors which are related to the character of commune, together with a concise strategy of using these tools. In case of the Office of Town and Commune of Głucholazy, this system includes following elements:

1) Symbols of commune:

- a crest – the crest of Commune of Głucholazy depicts a black billy goat's head with yellow bent horns, the head turned right, on a white background. A template of the crest is described in the status of Commune (Załącznik nr 2 do Statutu Gminy, <http://gmina.glucholazy.sisco.info>, access: 24.02.2014),
- a flag – official colors of Commune of Głucholazy are presented on a white-and-blue flag, with the crest located on the white part. A template of the flag is described in the status of Commune (Załącznik nr 3 do Statutu Gminy, <http://gmina.glucholazy.sisco.info>, access: 24.02.2014),

- a logotype – it ought to be understood as a graphic form which constitutes an interpretation of the name of commune and which allows unambiguous identification of a town. In case of the Town and Commune of Głucholązy, the logotype consists of only the abovementioned crest.
- 2) Organizational colors – the main colors used in all publications of the Office are blue, white, black and yellow. Prevailing color on the official web page of the city is blue. All the Office's documents must be printed in black.
  - 3) Printed materials – the Office has a set of official templates of documents (application forms) which are used in the process of dealing with clients' matters. Thanks to the fact that they are standardized, it makes it easier and faster for a worker to receive all necessary information. What is important, templates of all application forms which might be useful for a client are available on the web page of the Office. Regarding business cards, official templates are used only by the mayor and his deputy, the rest of office workers use their private cards.
  - 4) Dress code – the workers of the Office are required to be dressed in a classic, esthetic way, in adequate, subdued colors, without excessive decorations.
  - 5) Interior design – subdued colors, places to sit and to fill in documents, the whole building is adapted to the needs of the disabled clients.
  - 6) Plates, sign boards – they constitute a concise system of informing clients where they can find particular department or a person who will deal with their administrative matters. On the outside walls of the building there are boards informing about the character of the organization, inside there are information plates placed next to the doors to each room. Moreover, in the hall there is a big sign board which informs where exactly all departments are situated. This board plays an extremely important role in helping all visitors to find particular room easily and fast, right after they enter the building.
  - 7) Design of promotion gadgets – the Commune of Głucholązy issues a considerable number of various products which are supposed to strengthen commune's image, including: mugs, calendars, maps, t-shirts, emblems, postcards. Naturally all of them present visual elements which are characteristic for the commune – logos, a crest, pictures etc.
  - 8) Means of transportation – the Commune of Głucholązy possesses a few cars, all of which are in white color with the commune's symbols put on them.

### ***Sponsoring***

In case of the Commune of Głucholązy, it stresses the importance of measures which are connected with local tourism. Hence, the commune sponsors numerous cultural and sport events and activities, which make the region more attractive for tourists. Thus, the commune supports events concerning:

- 1) Promotion of healthy life style, organizing leisure activities, development of various interests and hobbies, for instance:
  - Days of Głucholązy – realized together with Czech partner as a trans-border cooperation,
  - Opawskie Mountains Holiday – an event to promote artistic and folk works,
  - Harvest Home,
  - International Tourist Songs Festival,
  - Czech Tourist Songs Festival,
  - International Interdisciplinary Creative Workshops,
  - International Music Workshops.
- 2) Promotion of sport – including events such as chess tournaments (XXIII International Chess Tournament for Opawskie Mountains Cup, <http://www.chessarbiter.com>, access: 12.03.2014; XII Individual Polish Championship in Chess for Uniform Services; VI Polish Championship in Chess for Politicians, [www.glucholazy.pl](http://www.glucholazy.pl), access: 12.03.2014), tennis tournaments (Commune Championship in Table Tennis, [www.glucholazy.pl](http://www.glucholazy.pl), access: 12.03.2014; Głucholązy Tennis Society, <http://www.gtt-glucholazy.pl>, access: 12.03.2014), cycling rallies (XXI Youth Cycling Rally „Witamy Wiosnę”, <http://glucholazyonline.com.pl>, access: 12.03.2014; Skoda Auto Grand Prix MTB – Głucholązy, [www.glucholazy.pl](http://www.glucholazy.pl), access: 12.03.2014; XVI National Cycling Rally „Zdobywamy Pradziada”, [www.victoria-glucholazy.pl](http://www.victoria-glucholazy.pl), access: 12.03.2014; Głucholązy Sports Club Victoria, <http://www.victoria-glucholazy.pl/>, access: 12.03.2014; National Cycling Marathon mini AUDAX, <http://portal.bikeworld.pl/>, access: 12.03.2014; Cykloopawy XC – MTB Głucholązy, <http://www.czasnarower.pl/>, access: 12.03.2014), basketball tournament (X National Girls Basketball Tournament for Mayor of Głucholązy Cup), beach volleyball tournament (VIII Grand Prix of Głucholązy in Beach Volleyball), jogging (III National Street Run for Uniform Services, <http://www.glucholazy.info>, access: 12.03.2014), etc.

### ***Image crisis management***

Image crisis should be understood as some unexpected happening which leads to sudden and substantial deterioration of the way an organization is perceived by the public (Flieger, 2013). For an organization it is absolutely crucial to be able to react very fast and send appropriate message to the public. The information is supposed to decrease indignation and recover positive image

(Mitroff, Pearson, 1998). To be able to do it efficiently, it is necessary for an organization to prepare to a potential crisis in advance by creating a concise system of procedures which are put into practice in case some negative event occurs (Larkin, Regester, 2005).

Regarding the Town Office of Głuchołazy, the research showed that the organization has not prepared adequate procedures in this field. Firstly, all the tasks of a spokesman, who is one of the crucial persons responsible for management during an image crisis, are done by the mayor or his deputy. They are responsible mostly for the process of identifying and analyzing signals and situations which may constitute a potential threat, which results in setting priorities and choosing appropriate strategy, and for realizing the strategy in order to either prevent a crisis situation or minimize its consequences. However, the abovementioned procedures do not include such vital elements as setting a crisis team, moreover, the organization also has not secured any funds which would allow effective implementation of the procedures.

### ***Publications***

It is vital to be aware of the fact that, in order to strengthen image, organizations of public administration can issue various written materials. They constitute a visual element of the message sent to the public. The Office of Głuchołazy is very active in this field, the most important measures include: issuing brochures and leaflets which are supposed to encourage visitors to stop and have a rest in Głuchołazy. This activity is supervised by the Department of Tourism and Physical Activity, which is responsible for all the promotional projects, such as taking part in tourism fairs, organization of promotional events, trainings, conferences, etc (Strategia Rozwoju Turystyki w Gminie Głuchołazy).<sup>4</sup>

Regarding the publications of the Głuchołazy Commune, the most important are the following:

- 1) Brochures presenting what the Office does, tourist attractions in the region, local companies, for instance:
  - ‘Revitalization of Urban Space in the Center of Głuchołazy’ – which describes and presents the results of modernization of those areas, at the same giving a short historical description,<sup>5</sup>
  - ‘Renovation and Adaptation of Destroyed Health Resorts within Polish-Czech Trans-border Cooperation’ – a publication which gives a thorough information about the project, its objectives and results, the history of health resorts in the region,<sup>6</sup>

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4 Implemented as a part of the project ‘Tradycje i perspektywy rozwoju na pograniczu polsko-czeskim w rejonie Głuchołaz i Złatych Hor’ (Tradition and development perspectives on Polish-Czech borderland in the region of Głuchołazy and Zlate Hory), finance by Program Phare CBC JSPF 2001.

5 The project financed within Regional Operational Program for Opolskie Province for 2007-2013.

6 The project financed within Operating Program for Transborder Cooperation 2007-2013 The Czech Republic-Poland.

- ‘On Running Skis Through the Commune of Głucholazy’ - a brochure issued by Department of Promotion and Tourism and Department of Development and Funds, describing the project co-financed by European funds, presenting local ski routes and planned winter events.<sup>7</sup>
- 2) Maps presenting local areas.
- 3) Posters presenting local sport and cultural events.

To sum up, publications of the Commune of Głucholazy focus on promoting tourist advantages of the city and the region, and on presenting in what way the Office absorbs European funds in order to improve quality of life of the inhabitants.

### ***Internal communication***

One of the crucial elements which influence efficiency of client service is the way internal communication processes are organized and managed. The main objective of managing a communication system is to ensure effective channels between all units and departments, sharing information, consulting problems, informing supervisors about dysfunctions (Regulamin Organizacyjny Urzędu Miejskiego w Głucholazach, p. 9). As a result, the organization is able to deal with clients’ matters fast and without mistakes. In this way a positive image of the Office is built and strengthened.

Internal communication processes between workers are supported by following instruments:

- internal and external telephone system - which allows direct, free connections between all units in the Office,
- Intranet system (which is a result of taking part in a EU project),
- e-mail communication – it allows, among the other things, sending all necessary documentation to all units and workers,
- information boards – they inform about current events, organizational changes, etc.,
- reports prepared together by workers from different units,
- monthly meetings with the management – in order to inform workers about plans and upcoming events; it is also a possibility to discuss current problems,
- regular meetings between representatives of different units and departments,
- celebrations (holidays, jubilees),
- exhibitions,
- clubs and societies of workers (Statut Gminy Głucholazy, <http://gmina.glucholazy.sisco.info/>, access: 6.02.2014).

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<sup>7</sup> The project ‘Na Nartach Biegowych po gminie Głucholazy’ co-financed within Rural Development Program for 2007-2013.



Improvement of the internal communication quality, and - as a result – improvement of service provided by the Office, to a large extent was possible thanks to implementation of Quality Management System, which resulted in increase in effectiveness of workers, simplifying recruitments procedures, ensuring clear and concise division of responsibilities between the Office's workers.

### 3. Conclusion

Presented analysis has shown that the Office of Town and Commune of Glucholazy has been able to use various instruments in order to create and manage the way it is perceived by the public. Since the office of commune is obliged to provide service for local community, it seems obvious that the client service becomes the crucial tool in this field. Direct contact between a client and an office worker constitutes this very special moment which mostly determines whether the organization is perceived in a positive way or not. However, it is not the only way to create the image. Of vital significance is also an effective communication system, both internal and external (Storbacka, Lehtinen, 2001; Yeshin, 1998). Thus, the analyzed office made an attempt to cooperate with local media and at the same time tries to build concise system of communication between all office's workers and departments.

Apart from the abovementioned basic instruments, the office in Glucholazy is also active in exploiting other available public relations tools. The organization has an impressive array of promotional publications which cover all important projects and events taking place in the region. These activities are also supported by sponsoring.

What seems especially important, the Office of Town and Commune of Glucholazy has possessed the ability to create concise *visual* concept of the PR message, which is an indispensable element which supports the non-visual content. Thus, the visual system consists of both precisely chosen colors, design of all publications and documents, flags, logos, and the interior design of the building.

However, although the scrutinized organization uses all available public relations instruments, the research enabled to reveal some flaws in the Office's image management system. The biggest problem seems to be the lack of concise procedures regarding image *crisis* management. Despite being conscious of the importance of being well prepared to a potential sudden and dramatic worsening of the way the Office is perceived by the public, very little has been done to create professional system in this field. The Office does not have a full-time spokesman, a crisis team has not been created, there are no adequate funds secured in the budget. As a result, in case real image problems



occur, it may be assumed that the Office will have serious difficulties in dealing with the situation efficiently.

Apart from that issue, it ought to be pointed out that there is a lack of an information desk. Partially, its potential tasks are done by the secretary - its workers are able to direct a client to a right department, inform about the structure and tasks of the Office, register submitted documents. However, these clerks are not always available, because they have also other responsibilities, at the same time in the secretary there are not any written materials (brochures, leaflets) which a client could take advantage of in case a clerk is not able to help.

The last problem is connected with cooperation with local media. Although news and information about the Office appear in all channels of the media regularly, it should be emphasized that in most cases it's the *media* who initiate the contact. The Office itself ought to be definitely more active in this field, trying to make media interested in the projects and events which seem most important from the organization point of view. In this way the Office would have better control of its image.

Nevertheless, it must be stressed that the Office of Town and Commune of Głuchołazy is well-aware of the necessity of creating and managing its image. Its benefits in a long term are undisputed. As a result of focusing on creating satisfaction of its clients, commune of Głuchołazy may count on loyal inhabitants, tourists and investors.

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# SMALL TRAINING SERVICES ENTERPRISES IN KNOWLEDGE-BASED ECONOMY- AN ATTEMPT AT IDENTIFICATION OF THE MAIN TRENDS AND MODIFICATIONS

**Iwona Małgorzata Kutzner<sup>1</sup>**

## **Abstract**

*The processes of globalization, which affect all aspects of social life - economics, politics and culture, also affect the functioning of modern companies. Enterprises, as economic entities, in addition to physical, financial and information resources, have teams of men, which are their biggest strength. Only those of them survive whose resources are based on intellectual assets. The transformations also apply to the organizations themselves, including changing their character, structures and way of human capital management. Furthermore, the role and function of the employee is being reconstructed. This publication presents the results of the empirical research of the author, which constitutes an introduction to the proper and scheduled research process. The aim of the study was to collect information about training services market, entities forming it, the models of these companies, as well as to identify the human capital, which it creates. In addition, it will be an attempt to answer the question whether, or and if so, what is the role of external knowledge worker in small training services enterprise. Also, whether, or and if so, how external knowledge worker affects development of such a company.*

**Keywords:** *globalization, training services market, small enterprise, small training services enterprise, employee, knowledge worker, external knowledge worker, features of external knowledge worker.*

## **1. Introduction**

Globalization is an almost inevitable problem in modern life (Robertson, 1992, p. 409). Globalization processes cover all aspects of modern life affecting the economic, social and cultural development. These processes are reflected in forms the society functions. Historically, they include the following societies: primary, feudal and industrial. And among contemporary

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forms: the post-industrial, global, information, mass, open, consumer, closed. The classic vision of the post-industrial society has been outlined by D. Bell and A. Touraine and supplemented by J. Naisbitt, who defined the following megatrends (Sztompka, 2005, p. 89-90):

- In the economic field there is a change in the dominant sectors, from agricultural to industrial production and from industrial production to services. It consists of a number of different jobs, which are not connected with production. Among them we distinguish: trade, finance, transportation, health care, recreation, research, education, administration and governance.
- In the class structure and stratification hierarchy there is an increase in the size and overall significance of the service sector in society and within its groups of professional and technical employees in the fields of science, research and development, social welfare, education, health, culture, social security system, recreation.
- In the field of technology new intellectual technology flourishes, entailing processing of information rather than raw materials or energy.
- In sustaining the dynamics of the society, the most important impact is exerted by self-perpetuating technological development.
- Knowledge and its acquisition by means of various forms of school education are becoming a central aspect of value systems and dominant issues of everyday life. This is what P. Drucker defines as a knowledge society.

Knowledge-based economy (M. Niklewicz-Pijaczyńska, M. Wachowska, 2012, p.16-17) (KBE) is a type of economy that expands a subject in contrast to the industrial economy and it is based on the following features:

- fundamental resource is widely understood knowledge and information that preceded it, and whose carriers - employees are not treated as a cost, but profitable investment. They also have a decisive role in determining the market value of the company,
- different style of management: it is participatory rather than top-down (command and control)
- the status of the organization does not depend on the scope of authority, but the skills and knowledge: you are worth as much as you know,
- a new dimension of organizational culture based on trust and incentives rewarding creativity and ability to work in a group,
- network organizational structure, in which the main strategy is based on cooperation,
- different incentive system based not only on traditional financial incentives, but also on personal, internal satisfaction,

- development of international companies and new forms of doing business, which contributes to the diffusion of knowledge and the effectiveness of its use,
- a new dimension of relationship with costumers - individualization,
- transformation of the internal and external environment is treated as Drucker's excuse to change, and no longer a threat; while development of the company has no longer linear character, it is often spontaneous,
- difficult to predict, but adequate for the development of the market situation of the entity, the use of modern technology is an indicator of market success and the meaning of existence the company,
- the dominant sector of the economy becomes services, information processing, and use of knowledge, it drastically decreases the importance of industry-related departments and classic production lines,
- management rules are also applied in "non-business" sectors, such as education, administration or health care,
- gain increasingly becomes a means of the task, and not its goal (M. Strojny, No. 10, 2000).

This economy is a network based on mutual relationships. It is a doctrine in which knowledge becomes the engine of socio-economic changes, and consequently a stimulus to economic growth and development of countries. Skilfully prepared or acquired, it becomes a cause of changes in the micro and macro economic. The source of knowledge is a man, and the widely understood associated human capital.

Knowledge-based economy is a model whose key messages have cultural nature because it concerns the human capital. This capital is being built by the family, the environment, and then enriched by the school and the system of standards. Only in the mature form human capital is available in economy (...) (Galar, 2003, p. 308). This capital has a significant impact on economic innovation, institutional transformations, development of modern infrastructure, etc. (K. Makowski (ed.), 2002, p. 181). Modern companies, as economic units, in addition to physical, financial and information resources have teams of men, which are their biggest strength. Gaining competitive advantage depends on their level of education, experience, skills and health. The more valuable to the organization becomes the knowledge worker or external knowledge worker if treated as a strategic resource. M. Juchnowicz (2014, p. 39) claims that strategic resources must be: valuable, rare, difficult to imitate, difficult to substitute, durable, better than the competition's ones, controlled by organization, efficiently organized.

## 2. Knowledge – based economy

In knowledge-based economy intellectual capital acquires growing importance. Product quality or price ceases to be essential. More and more often, in order to gain a competitive advantage, organizations put emphasis on speed, flexibility in decision-making, responding to the environment of the company and developing and maintaining good relationships with customers. In witness whereof, (M. Juchnowicz, 2014, p. 31-32) today in the business environment, as well as within the organization, there have been many new phenomena that have a particular impact on the development of companies. Among them: the next phase of globalization, emergence of new technologies, growing modernity of developing economies, which results in an increase in the level of skills and innovation of employees, urbanization, increased employment in the service sector, aging of the society, as well as new norms and values brought by the new generations entering the labour market. New economy (...) will be based on the use of small businesses, individuals, freelancers, forming virtual communities more flexible, faster in operation than the big corporations (Mrówka, 2012, p. 56).

Intellectual capital consists of: human capital, organizational capital and relational capital. However, the most important are people, their knowledge and those who specialize in actively seeking possibilities and use of knowledge to generate profits in various types of industries: for example: IT, education, e-commerce, health care, financial companies, media, pharmaceutical or high technology (Marcinkowska, 2011, p. 497). According to R. Przybyszewski (2007, p. 22) World Bank says that 2/3 source of wealth of nations are human capital and social capital. People have been the biggest value of companies since 1990s. They are treated as a main resource creating profits now or in the nearest future. Uniqueness, knowledge and competence of employees are difficult to follow by competitors. Human capital also allows companies to gain a long-term competitive advantage (Juchnowicz, 2014, p. 33). In the knowledge-based economy knowledge workers occupy an important place. They are defined as specialized in their profession, they have unique competences, they are well-informed, active and responsible, aware of their role and self-esteem and independent participant of organization.

Nowadays companies are considering the directions of development listed below: (Mikuła, Pietruszka-Ortyl, Potocki, 2007, p. 26–27):

- economic activity around the world, globalization, cost reduction,
- organizational flexibility and the ability to make changes related to market environment and the changing situation,
- flattening structures of companies, networking, fractal organization, virtual organizations, organizations without borders;



- cooperation with external knowledge workers, partnership-oriented actions, outsourcing; to other companies or external knowledge workers;
- building and strengthening of intellectual capital for the individual and organizational level;
- creating systems to facilitate customer relationship management based on new technologies and their effective use.

### **3. Polish training services market**

Polish training services market exists and has been developing since the early nineties of the twentieth century in Poland. In the initial phase, it was only adopting patterns in the field of personnel management from the international companies. Over the years, training industry has gone through various stages of development from dynamic development to recession. Its dynamics depends on European funds. Now this market consists of the following entities according to the Act of 20 April 2004. on employment promotion and labor market institutions, Art. 20 (Official Journal of 2008, No.69, item 415 as amended) and the Regulation of the Minister of Economy and Labour of 27 October 2004 on the register of training institutions (Official Journal of 2004, No. 236, item 2365 as amended). According to the Act, training company is a public and non public entity. Legal and natural persons may establish nonpublic schools and institutions after registration by a local government obliged to supervise the appropriate type of public schools and institutions. Commercial provision of services by these entities and therefore training services has been recognized as an economic activity in the Act on Freedom of Economic Activity. Training services have not been assigned to the so-called regulated activities, such as those which require the fulfillment of specific conditions in specific provisions of the law, as well as any license, permit or consent given by the relevant authority.

An entrepreneur wishing to conduct training activities, pursuant to the Act may be: natural or corporate person, civil law partnership or organization unit not being a corporate person. The entrepreneur, depending on legal form of organization should: a natural person – register in Central Registration and Information on Business, a corporate person, civil law partnership or other organizations – register in National Court Register.

Nowadays, training companies are private, micro and small businesses which operate on local or regional market. In 2010-2013 an observation of development of this market was made, related to changes of size of businesses: the number of micro and small enterprises declined, and the number of large and medium-sized enterprises rose. This trend is confirmed by the analysis of

the range of the training firms and institutions. In 2010-2012, the number of entities operating on local and regional markets decreased, while the number of those who provide services throughout Poland rose. There were no changes in terms of the number of entities of international training: they constitute about 5% of all surveyed institutions and companies. Although the structure of the training market has not changed, there are some indicators proving its development: a growing number of medium and large companies and those that provide their services not only to local and regional markets. Detailed analysis of employment data, including data relating to persons directly involved in the training or consultancy confirms the development of this sector.

Between the years 2010 and 2012 the average employment in the sector increased from 43 to 56 persons, while the average number of trainees increased from 20 to 27. Training sector in Poland is characterized by a high turnover of entities operating in it: there are many new providers on the market, however many entities announce bankruptcy or resign from training activities. As many as 1/3 of enterprises tested in 2012 are relatively new companies: they have been operating on the market no longer than five years. Despite the slight increase of Poles' educational activity, the training sector is increasing steadily as evidenced by the previously mentioned employment growth and observed in subsequent editions of the survey increased turnovers<sup>2</sup>. There is no single definition of an enterprise or a training institution. Depending on the unit, which is preparing to develop / report, they interpret them differently.

Central Statistical Office reports that a training institution is the one that offers training for the unemployed and job seekers. Register of Training Institutions<sup>3</sup> – defines it as one that applies for courses for unemployed and job seekers, financed from public funds. Polish Chamber of Training Companies<sup>4</sup> associates entrepreneurs whose activity is training services. In contrast, the Polish Agency for Enterprise Development defines institutions classified in Polish List of Codes of Business Activities in the area of adult education as for instance: driving and foreign languages schools or companies providing consultancy services in the field of management etc.

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2 Since 2010, the Polish Agency for Enterprise Development, together with the Jagiellonian University (Centre for Evaluation Analysis of Public Policies) have prepared reports on labor market as part of the project Study of Human Capital in Poland. Its general objectives are nation-wide scope, which allows to monitor changes in the labor market. Research in each edition will be conducted according to the uniform methodology, thanks to which results of the research conducted in different years will be comparable. The results will help to plan the development of human capital at the state level, provinces, as well as companies. Based on our research and own observations, the author described the training market at: <http://bkl.parp.gov.pl/raporty-iii-edition-research> [accessed on 05/10/2014].

3 Register of Training Institutions is created up to date by the Regional Labor Offices. The Register of Training Institutions includes, among other information: the name and address of the training institution, names of training staff, premises, its equipment, methods for assessing the quality of training, the number of unemployed and looking for work covered by the training during the last year, information about assistance after completion of the training and subject matter of courses. The Register of Training Institutions is conducted electronically. It is explicit and available on the websites: [www.psz.praca.gov.pl](http://www.psz.praca.gov.pl), [www.ris.praca.gov.pl](http://www.ris.praca.gov.pl), [www.wup.krakow.pl](http://www.wup.krakow.pl).

4 [www.pifs.pl](http://www.pifs.pl). Polish Chamber of Training Services associate entrepreneurs, [accessed on 05/10/2014].

## 4. Empirical research

Empirical research conducted by the author of this publication is the initial stage of the scheduled research process for the purpose of writing a doctoral dissertation. At this stage, the aim was to: prepare research tools and pilot studies, verify the research tools, gather information. Respondents were divided into two groups:

The first group of respondents is:

- owners / persons managing small businesses training services - research sample - 30 people;
- registered in accordance with Polish List of Codes of Business Activities - 85.5Z and 85.6Z - extracurricular education forms and nowhere else classified, from Lower Silesia and Mazowieckie Provinces;
- registered in Polish Chamber of Training Companies (on the date of preparation of the study - 275 subjects);
- registered in Register of Training Institutions (on the date of preparation of the study - about 12200).
- The second group of respondents is:
- External knowledge workers, working with small training services businesses - research sample of 30 people;
- own database of external knowledge workers - 500 people.

Due to the huge body of research collected and numerous aspects of the study, as well as the limitations associated with the volume of publications, information obtained by the author will be presented only in general. The formulated conclusions are primarily used to define a small training services enterprise and external knowledge worker and attempt to answer whether and if so, how external knowledge worker affects the development of small training services enterprise.

The author assumed that a small training services enterprise is:

- a small business employing between 10 and 49 people,
- whose annual turnover does not exceed 10 million Euro,
- whose annual balance does not exceed 10 mln Euro,
- an enterprise registered in accordance with Polish List of Codes Business Activities - 85.5Z and 85.6Z - extracurricular education forms and nowhere else classified,

During the study<sup>5</sup>, which was prepared in late 2013 and 2014, the following information was collected and compiled:

- The characteristics of the organization: type of organization, size, industry, the activities, organizational and legal form.
- identified human capital in terms of: number of employees, the employment structure, the quality of employees' education,

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<sup>5</sup> The method of social research / communications technology / interview questionnaire and observations.

- qualification, age, implementation needs, their job satisfaction, opportunities for growth and self-realization
- The use and development of human capital (implementation of selected methods, techniques and activities that support the use and development of human capital; connection with the implementation of the Human Resource function)

## 5. Results of the study

Preliminary studies aimed at obtaining their goals:

- test the questionnaire to verify its correctness and understanding of the questions. In addition, the author carried out direct talks with the respondents to improve the research tool. The questionnaire will be adjusted at a later stage of research.
- identification of training services market, its operators, structure, making their characteristics; identification of human capital in terms of: number of employees, employment structure, the quality of employees' education, qualifications, age, meeting the needs, their job satisfaction, opportunities for growth and self-realization. Additionally, through direct interviews to obtain information on the following criteria: culture, strategy, methods of operation, dependence on the employee, relationships with people, organizational structure, boundaries of the organization, organizational forms.

In the pilot survey, in the first group of 30 respondents (owners and managers of small training services enterprises) and the second group of respondents (external knowledge workers) who were provided with questionnaires, we obtained 30 replies - 100%. On the basis of the information given by the respondents (the first group of respondents) we can state that the people surveyed identified themselves as owners (co-owners) of companies. All reported that their leading activities are extracurricular education forms and nowhere else classified. Their companies were registered in Lower Silesia and Mazowieckie Provinces, and their activities were conducted within the Polish territory.

Terms of employment: the majority - 25 indications, are companies that employ 10 people, and only 5 of them employ more than 10 people. All respondents declared that they meet the criteria of a small enterprise. Employees employed under contracts of employment work on administrative or office positions or as assistants. External knowledge workers work under civil law contracts. Despite the fact that in accordance with the Labor Code they do not provide work, respondents classify them as employees. External knowledge workers are treated as key "employees" who create the development

of the company. Their competencies<sup>6</sup> are assessed as very high and they are distinguished by many features: they are valuable to the organization, are the personal property of employees (those parts that are somehow hired by organizations to achieve the objectives of the organization) in line with intangibility, observability, effects of ownership, measurement, variability and knowledge. Their psychosocial predisposition and effectively used knowledge comprise a business model of a small training services enterprise. Each element and the success of the business depend on the relationship built between the owner of the company and external knowledge worker. Building relationships is based on partnership and trust. If either party failed to make diligence in a fairly rapid manner that would reflect on the loss of image and reputation of the company in the market.

There are only women employed in administrative and office positions, while external knowledge workers constitute the vast majority of men - nearly 89%. Administration and office workers all have a university degree (Bachelor and Master) - 100%. External knowledge workers, who also completed postgraduate studies, equal 65%, with a PhD 25%, and habilitated PhDs and professors - 10%. External knowledge workers are in 95% self-employed, and in 5% employed under contracts of employment in higher education (research and teaching staff), they are also public administration officials, computer scientists, programmers working for international corporations or coaches. External knowledge workers themselves direct their own careers and they are the owners of sole proprietorships or commercial companies.

In Table 1, data were collected on the characteristics of the surveyed small training services businesses in accordance with the initial assumptions

**Table 1.** Characteristics of surveyed small training services enterprises

Characteristics	The survey sample - 30 people
type of organization	Service, formal, private sector - 30
profile	Service
size	Small businesses – 30
industry	Services – 30
Object of economic activity	Leading - extracurricular education forms and nowhere else classified - 30

<sup>6</sup> Competence is the knowledge, skills, abilities and attitudes of employees, which are used in the work process, are used to implement the strategy of the organization.

Characteristics	The survey sample - 30 people
organizational and legal form	Sole proprietorship- 15
location	Commercial companies, limited liability company - 15 Lower Silesian and Mazowieckie Provinces

Tables 2-5 present the identified intellectual capital in the amount of employment, gender and type of employees, their education and age in small training services companies.

**Table 2.** Identification of human capital in amount of employment in surveyed small training services enterprises

Human capital in the organization	The survey sample - 30 people	
Number of indications	25	5
Number of employees	10 people	Over 10 people

**Table 3.** Identification of human capital in terms of type of employment and gender of the employees in surveyed small training services enterprises

Human capital in the organization	Results	
Gender - External knowledge workers in terms of percentage	Women - 100% of employment in the surveyed enterprises	Men- 0
Gender - External knowledge workers in terms of quantity	Women - 4	Men- 26

**Table 4.** Identification of human capital in terms of education of employees of surveyed small training services enterprises

Human capital in the organization	Results
Full-time employees as a percentage	100% bachelor and master's degree
External knowledge workers as a percentage	65 % master's and postgraduate degree, 25% doctoral and 10% are habilitated doctors or professors

**Table 5.** Identification of human capital in terms of age of the employees of surveyed small training services enterprises

<b>Human capital in the organization</b>	<b>Results</b>
Full-time employees as a percentage	65% under the 35 years of age, 20% to 45 years and 20% above 45 years
External knowledge workers as a percentage	35% under the age of 45 years, 65% over 45 years

Based on all the information obtained, external knowledge worker was defined and its features formulated:

- It is a natural person, who provides services / "work" on the basis of civil law provisions,
- has a unique, advanced and specialized knowledge - a specialist in his field – who shares it non-gratuitously (depending on the scope of contracted work)
- takes care of his self-development, investing in his knowledge, is autonomous, independent, flexible person, easily adapts to the services / tasks set before him to execute / implement, takes care of his intellectual, physical and mental development,
- has exceptional interpersonal skills,
- able to work individually or in a team depending on the nature, complexity of tasks / services to be done, creative, able to think conceptually and use it in his work,
- can perform work / services anywhere, for example using modern IT solutions, internet, videoconferencing or e-learning.

After the preliminary tests and analyzing the results of the questionnaire, the following conclusions (more shown in Table 6) associated with the operation of small training services enterprises were made:

- Culture - positive - impact on the motivation and commitment of employees and external knowledge workers to collaborate, strong - a permanent system, highly competent employees and external knowledge workers, a high degree of commitment, a high degree of tolerance of uncertainty - the setting for the future, perfectly coping with unpredictable situations.
- Organizational structure - network, expressed in many ways leads to cooperation and helps to achieve synergy. The premise of division of labor is knowledge.
- Specialization is based on the personal interests and skills of the external knowledge workers. The structure is flat, and there is no hierarchy. Organizer of the enterprise is a leader within the network. Entitlements of individual units are decentralized, which remains a low level of centralization. The whole structure is flexible and easily adapts to the changing environment of the organization. Observed when more complex to implement services. It uses its

voluntary creation by the participants. Depending on the objectives, great importance is played by information technology.

- Project management - each service performed in the company is treated as a project which has its duration, leader and co-workers. Project team is composed of external knowledge workers, having unique knowledge that can be used for creating proprietary software program dedicated exclusively to the client, preparing management plan for the historic district property or proprietary training program prepared especially for the ordering customer etc.
- Due to the structure of employment (a low proportion of full-time employees to external knowledge workers) work is done in teams created depending on the project and is characterized by volatility of occupied roles in the group, for instance one day someone's a team leader, another – a coworker. In team working we use capabilities and competencies of external knowledge workers and, moreover, an innovative and creative approach to the tasks / projects as well as unusual solving complex tasks. There are no typical managerial positions, lack of formal hierarchy and no formal subordination. In return company is much more consumer oriented. The work is based on building relationships based on partnership and trust. Aspect of cooperation between the training services company and external knowledge worker works out in this type of organizations. External knowledge worker adds value to the organization, even though he is not a part of its shareholders' equity. The existence and development of small training services enterprises depends on the efficiency and involvement of external knowledge worker.

**Table 6.** Traditional organization in contrast to the new models of organization and a proposed model of small training services enterprise

<b>Criterion</b>	<b>Traditional organization</b>	<b>New models of organization</b>	<b>Proposed model of small training services enterprise</b>
1	2	3	4
Culture - a system of values, norms, attitudes, behaviour and thinking	Conducive to the avoidance of uncertainty	High tolerance of uncertainty by the social environment	High tolerance of uncertainty, ease of adaptation to the changing environment, flexibility
Strategy - a characteristic way of achieving the goals of the organization	Passive and reactive	Proactive	Proactive



<b>Criterion</b>	<b>Traditional organization</b>	<b>New models of organization</b>	<b>Proposed model of small training services enterprise</b>
1	2	3	4
Modes of operation-	Structured and stable, adherence to stereotypes and reject conflicting information from them, focusing attention on the efficiency of the processes taking place within the organization	Each adapted to the situation, the continuous reconstruction of the inner and external world of organization, rejecting stereotypes	Each time adapted to the situation, the continuous reconstruction of the organization's inner and external world, rejecting stereotypes, look at the organization as a whole. Attention is paid to all aspects of the organization to achieve its goals.
Relations of power - the ability of the entity to use its influence	Stable, hierarchical, based on the emotional aspects of executive authority	Heterarchy, the instability of the power	Decentralization of power, ad hoc leadership, the main goal is not power, but the project and the tasks that are to perform
The dependency of the worker –	High dependence on the leader	A large autonomy supported by the knowledge and professionalism	Independent external knowledge worker as appropriate to the specific project. External knowledge worker, which is characterized by a unique expertise and knowledge necessary to complete the project and having sufficient competence and experience.
Relationships with people	Stable relationships, minimum mobility, a sense of belonging	High mobility thanks to the rotation applied, harmony in the interaction	High mobility, external knowledge workers matched to the individual projects. Interaction, mutual support and deepening knowledge. The use of a synergistic effect at each stage of realization of the project. Knowledge sharing. High self-esteem of each external knowledge worker.

<b>Criterion</b>	<b>Traditional organization</b>	<b>New models of organization</b>	<b>Proposed model of small training services enterprise</b>
1	2	3	4
The approach to uncertainty	Treating atypical events as danger	Treating atypical events as a source of inspiration	Each project is an event during which you can be inspired, acquire better skills to be able to react in advance. Managing risk and opportunity.
Organizational structure	Traditional, focused on enterprise functions	Network cooperatively related, self-managing units focused on processes	Network, partnership, collaboration, project teams, external knowledge workers
The boundaries of organization	Bright and clear	Blurred	Blurred or lack of them
Dominant communication in the organization	Vertical, formalized	Horizontal, informal	Vertical, horizontal, informal
Participation in the group	Exclusive and persistent	High mobility, temporary participation	Frequent change of external knowledge workers depending on the project, changing roles (eg. Once a leader, other time co-worker), continuous or temporary participation depending on the project
Dominant type of personal identity of organization	Collective identity	Personal identity	Collective or personal identity, depending on the project
Organizational forms	Permanent and structured	High dynamism of variability	High dynamism of variability, execution of projects in teams

Source: Own study based on Mikula, Pietruszka-Ortyl, Potocki (2002), p. 34.

## 6. Conclusion

Changes in the modern world permeate all fields of science and life. They also relate to management sciences, which are characterized by internal diversity and provide a wide range of problems. They can be considered from different perspectives and levels due to (Zakrzewska-Bielawska, 2012, p. 20): type of organization, management functions, processes, resources, management levels, sectors, management concepts and methods. In today's enterprises we see changes in the following areas (Gierszewska, 2011, p. 14): structural

(virtualization), operating systems (creating flexible systems), competence (creation of new knowledge), technologies and organizational procedures (introduction of e-business), and values (emphasis on social responsibility). Financial assets cease to be regarded as the most important and basic for the assessment of the company become intangible assets. Of particular significance are external knowledge workers and their unique competencies, which, if used properly, may be an opportunity for the development of small training services enterprises. They allow companies to gain a sustainable competitive advantage based on unique strategic resources that are difficult to imitate. In addition, the effective and efficient utilization of sustainable development gives them an opportunity to meet and respond to the needs of the market.

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# THE IMPACT OF TOURISM ON THE SOCIO-CULTURAL ENVIRONMENT IN THE GORCE NATIONAL PARK AND ITS VICINITY

**Małgorzata Luberda<sup>1</sup>**

## **Abstract**

*The paper presents the problems of tourism in terms of its relationship with the social as well as cultural environment. The purpose of the article was to examine how tourism affects the socio-cultural environment in the Gorce National Park and its vicinity. I examined whether tourist traffic in the Park brings about more benefits or problems, and whether changes taking place in communities visited by tourists are positive or negative? The impact of tourism on the socio-cultural environment has been analyzed on the basis of a questionnaire I conducted. At the end I present a balance of benefits and costs of tourism in the Gorce National Park and its surroundings in the social and cultural contexts.*

**Keywords:** *Gorce National Park, tourism, benefits of tourism, costs of tourism.*

## **1. Introduction**

Tourism occupies an increasingly important place in the modern world, being one of the fastest growing areas of life. The tourist traffic increases, and thus socio-cultural tourism develops, carrying numerous risks for the residents of the visited sites and the environment. It has been calculated that in the whole world about 650 million people travel every year. By 2020, the number of travels in world tourism will increase three times, and the revenue from it will have nearly quadrupled (Różycki, 2006, p. 120). Worldwide turnover coming from the services related to various forms of travel make tourism one of the leading economic sectors in the world. Let us consider, however, whether everybody is happy with this widespread phenomenon. Does its scope bring about fears and resistance? Information about damage wrought by modern tourism to communities in tourist regions constitutes only a small percentage of the knowledge that we would have if more implications of research and observation were brought out. Hence the idea to write this paper.

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Its main purpose was to examine how tourism affects the socio-cultural environment in the Gorce National Park and its vicinity. It was important to examine how residents of the visited locations perceive tourists and reversely, how tourists perceive local residents. I was looking for answers to questions whether tourism brings more benefits or damage and whether tourists respect the cultural heritage of the Gorce mountains and by association with the Gorce National Park.

The question of changes taking place requires initial discussion. Basically, the question arises whether the changes taking place in communities under the influence of tourism are good or bad, positive or negative? Is incoming tourism a functional factor or a dysfunctional one?

Source materials that I used in the implementation of the work were mainly book publications. The materials related to tourism in the Park were obtained from the Park Directorate. The impact of tourism on the socio-cultural environment was studied by means of a survey and the conclusions therefrom.

The study performed used a questionnaire as a tool of choice. The survey is an indirect method of obtaining information by means of questions posed to selected people through a printed list called the questionnaire. "A survey poll, therefore, is a technique for collecting information to complete a test most commonly by specific questionnaires of a generally a high degree of standardization in the presence or often in the absence of an interviewer" (Plich, 1995, p. 86-87).

We refer to this method when we want to obtain information about what others know, think and how they see and evaluate phenomena and events of interest to us.

Due to the category of questions we distinguish two types of questionnaires (Zaczyński, 1997, p. 150):

- open questionnaire,
- closed (categorized) questions survey.

Questionnaires used in this work are specific, clear and focus on a single issue. Frequently, the questions are closed, i.e. the respondent cannot go beyond, but only selects among the possible answers, which are provided in a question form. Some questions contain a set of possible answers to choose from that include one point designated by the word "other", allowing the respondent to present their answers, if it is not in any proposed wording.

The respondents completed the questionnaire, which contained 16 questions, including 9 closed questions, 3 open-ended questions, 4 semi-open ones. The printed copy contained three questions that have generated the most important information on the characteristics of the respondents. Their random

selection, which I used, was in the selection of a specific population of people in such a way so as to make chance decide.

I was interested in conducting a survey among residents of five municipalities located in the Gorce National Park or in its near vicinity. Accordingly, each municipality has been tested, which gave a total of 54 respondents (Table 1). The survey was participated by 29 women, representing 54% of the respondents, and 25 men - 46%. The research was a pilot study. In the future, studies are planned involving a larger number of tourists visiting the Park. The age span of respondents was 16 to 59 years. The study was conducted in April 2014.

**Table 1.** Number of respondents in individual town and village communes

Commune	Kamienica	Mszana Dolna	Niedźwiedź	Ochoznica Dolna	Nowy Targ	Total
Female	4	7	8	5	5	29
Male	6	5	2	5	7	25

## 2. The role and character of tourism for the Gorce National Park

Gorce is a well separated mountain range located in the center of the Polish Carpathians, almost exactly between the Tatra Mountains and Krakow. They form a tall mountain massif with the highest summit Turbacz (1310 m amsl) (Róžański, 2006, p. 13). Central and north-eastern part of the massif is occupied by the Gorce National Park. The Park is located in the Malopolska province, in the districts of Limanowa (77.8% of the area) and Nowy Targ (22.2%). It is located in the macro-region of the central Beskids, the north-eastern part of mesoregion Gorce (approx. 13% of Gorce) (Loch, 1998, p. 27).

Tourism in Gorce National Park has an impact not only on the tourists, but it also affects the visited location. On the one hand, tourism contributes to the socio-economic development of these regions, and the consequence is usually the improvement of the living standards of the local population. The positive sides of influx of tourists are undoubtedly the development of the communication network, the production of consumer goods, and the enrichment of the society. One of the most important things is to create real jobs in the tourism services sector. 250 million people are employed in tourism worldwide.

According to the respondents, tourism in Gorce National Park and the surrounding area has many useful functions and benefits. It is reflected in the different areas of life: social, psychological, cultural, spatial and economic.

Usually, the respondents included the following positive effects of the influx of tourists to the Park: revenue growth (47%), infrastructure development (18%), employment (16%), promotion of the region (12%) and the opportunity to make new friends (7%). Useful features, according to them, are: education, provision of training, it was often stated that tourism provides the opportunity to meet new people and other cultures. The positive changes in attitudes and behavior of the local population affected by the opportunities that tourism brings were mentioned in terms of personal development and the acquisition of new experiences. Tourism incoming to the Park creates an opportunity for the local communities to make new contacts. Tourists are an important source of information and expanding knowledge about the world. People who have frequent contacts with tourists, compared to others, have wider horizons, are more hospitable and open.

On the other hand, cultural values, both spiritual and material, are disappearing, which cannot be repaired by financial means. The threat of the commonly growing tourism is the commercialization of culture and presenting it to the needs of tourism, and the destruction of religious and local culture.

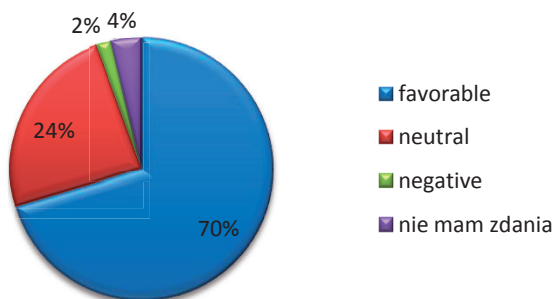
The impact of tourism on the socio-cultural environment relates primarily to the local communities living in areas of interest, their traditions, customs and habits, beliefs and values, family and friendships, social relations, etc.. These are the qualities determining the distinctiveness and specificity of a given community and the region, and their disappearance as a result of the development of civilization, which is also tourism, is usually irreversible. They defend themselves by rebuilding their vitality and identity after each tourist season, with increasing effort.

### **3. Residents' attitudes towards tourists visiting the Park**

In the area of research the differences between the communities of visitors and hosts are highlighted. This applies to the distance separating their economic but also cultural differences. This can produce a sense of dominance, superiority and can lead to many unpleasant situations. The financial status, behavior, attitudes of tourists who are highly visible, have formed a so-called demonstration effect, which is one of the essential elements of the impact of tourism on the host community.

70% of the respondents expressed a favorable attitude towards tourists, 24% considered their attitude towards tourists as neutral, 4% had no opinion, and only 2% of the population considered their relationship as disrespectful (Figure 1).





**Figure 1.** Local attitudes towards tourists

The trend towards concentration of tourism means that the inhabitants of a village or tourist region remain in close, spatial, psychological and social, as well as and personal, contact with the community of tourists. The trend towards concentration of tourism means that the inhabitants of a village or tourist region remain in close, spatial, psychological and social, as well as and personal contact with the collectivity of tourists. This situation must result in several changes.

**Table 2.** Phenomena related to tourist traffic cause most problems for the residents

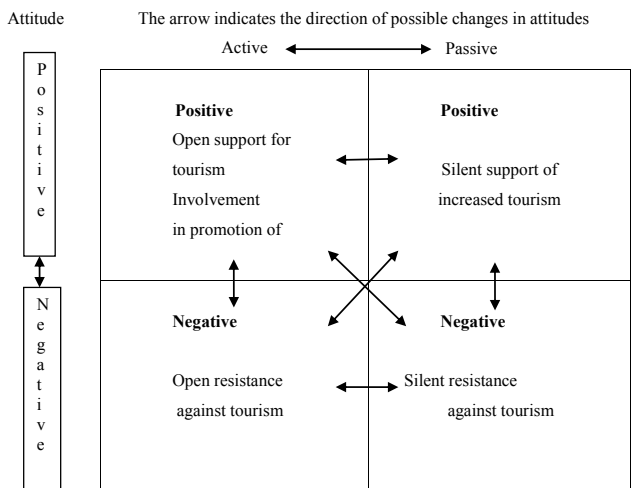
Phenomenon	Number of indications (in %)
Hooliganism, vandalism	2%
Alcohol abuse	5%
Violence	0%
Assaults and robberies	0%
Theft	2%
Disturbing the peace at night	39%
Intrusion into private matters (nosiness)	7%
Tourists' opposition to traditional ways of conduct and behavior	3%
Inappropriate behavior of tourists	9%
Overcrowding of the home town or village	26%
Other	3%

Most problems for the residents are caused by disturbing of silence at night - 39%, congestion - 26%, inappropriate behavior and conduct of tourists - 9%, meddling in private affairs - 7%, excessive alcohol intake - 5%, interference with traditional customs and behavior norms - 3%, none of the respondents noted problems with violence and assaults and robberies. The questions allowed adding other phenomena, and 3% of respondents (2 persons) reported littering (Table 2).

The presence of tourists disrupts the social order. Reservations cover: fear, anxiety, lack of citizen satisfaction, and later also reluctance along with noticing only negative aspects of tourism. Local people from the Gorce evaluate tourism negatively when its development is under the control of foreign entities, and the share in the economic benefits of local hosts is insufficient and often negligible. Nuisance related to tourism in the Park is felt strongly by these residents who do not have income from tourism.

One of the social consequences of the development of incoming tourism that change the attitude of residents towards tourists is shown in Figure 2.

That ratio depends on the individual or public perception of the positive and negative effects of its development. It is the basis to explain and describe the relations between the tourists and the hosts.



**Figure 2.** Attitudes of representatives of the local community towards the growth of tourism

Source: Mika (2008), p. 434.

According to this model, the attitudes adopted by the locals towards tourists may be positive or negative, and active or passive. Among the inhabitants of the Gorce area, two variants are characteristic of “passive” attitudes.

The biggest problem, however, lies in the fact that not all residents living around the Park achieve tangible benefits from the development of tourism. 11% of respondents fear for foreign ownership and employment of outsiders in the tourism sector. Thus, only certain social groups benefit from the tourist arrivals. Moreover, most of the money spent by tourists in the region does not remain there, but goes to “the wallet” of tourism operators from the outside.

**Table 3.** Reservations of the residents of the destination areas

<b>Reservations of the residents of the destination areas</b>	<b>Number of indications (in %)</b>
Changes to customs and behavior patterns	8%
Disappearance of the local culture	11%
Worsening living conditions in the home town or village	43%
External property and employment of external individuals in the tourist sector	11%
Conflicts with tourists	8%
Increase in crime and alcoholism	6%
Damage to historical sites	13%
Other	0%

Respondents mostly feared of worsening living conditions in their place of residence on the part of tourism - as many as 43% of them placed the devastation of historic sites as the second (Table 3).

#### **4. Balance of socio-cultural benefits and losses connected with increased tourism**

Tourism has an impact not only on the tourists but it also affects the visited destination. On the one hand, tourism contributes to the socio-economic development of a region, and the consequence is usually to improve the living standard of the local population.

The respondents also noticed positive effects of incoming tourism (Table 4) mostly including financial benefits (47%), infrastructure development(18%), employment growth (16%), promotion of the region (12%), while 7% of the respondents felt positive about the effect of the influx of tourists as an opportunity to make new friends.

27% of respondents saw the negative effects of incoming tourists (Table 5) including excessive traffic, an important issue for them was also the environmental impact of tourism (23%), and littering, which was indicated by 20% of responses. In fourth place came noise and disturbing the peace, noticed by 16% of respondents, while the last comes the destruction of the cultural environment (14%).

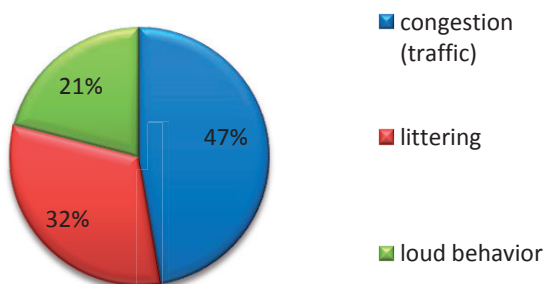
**Table 4.** Positive effects of incoming tourism

Positive effects	Number of indications (in %)
Financial benefits	47%
Infrastructure development	18%
Rise in employment	16%
Promotion of the region	12%
Making new friends	7%

**Table 5.** Negative effects of incoming tourism

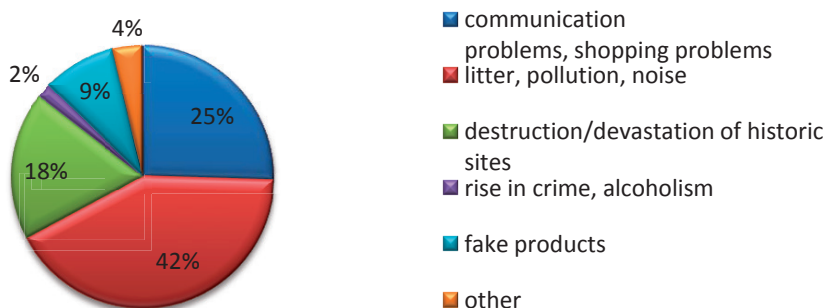
Negative effects	Number of indications (in %)
Too much traffic	27%
Pollution	23%
Littering	20%
Noisiness, noise offences	16%
Destruction of the cultural environment	14%

Respondents believe that tourism directly affects them by congestion (traffic jams) - 47% of respondents, another group reported littering - 32% of respondents, while 21% answered that tourists behaved too loud (Figure 3).



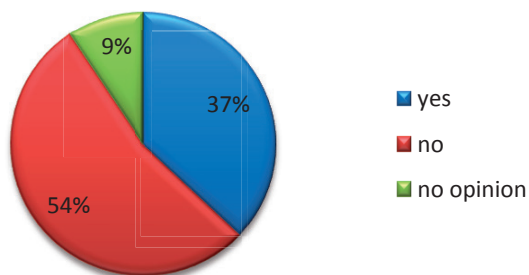
**Figure 3.** Difficulties in the performance of daily tasks of the residents due to increased tourist traffic

42% of those surveyed for damage caused by tourism in the Gorce National Park mentioned litter, pollution and noise. A major problem for the residents were traffic problems (25%), destruction/devastation of historic sites in the Park occupied the third place, because this answer was marked by 20% of respondents, imitation was noted by 9%, 4% of respondents cited other damages, namely, littering, and 2% of respondents noticed the damage in the form of crime and alcoholism (Figure 4).



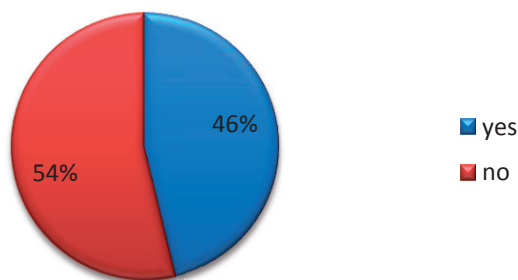
**Figure 4.** Damage to the Gorce National Park caused by tourism

54% of respondents answered that tourists did not respect the cultural heritage of the Park and its environs, while 37% said that tourists respected the cultural heritage. 9% of the respondents had no opinion on the subject (Figure 5).



**Figure 5.** Tourists' respect to the cultural heritage of the Gorce National Park

Among those surveyed, 54% reported seeing damage in the Gorce National Park and the Gorce caused by tourist traffic or tourists themselves, the remainder of respondents, i.e. 46% have not noticed any such damage (Figure 6).



**Figure 6.** Damage of cultural sites in the area of the Park resulting from tourism or caused by tourists

The presentation of the work carried out on the impact of tourism on the socio-cultural environment stresses the need for balance in the final assessment of the situation.

Tourism has become, in the past century, something inseparable from contemporary culture of living societies. Domestic tourism, growing faster in countries with adequate tourist attractiveness, covers large numbers of the public sphere, dynamically transforming the face of the visited towns, regions and the entire country (Gaworecki, 1997, p. 346).

At the same time, with the development of tourism, there have been a growing number of critical voices against it. Considering the functions and dysfunctions of tourism, many questions can be raised.

It is a fact that doubts arise as to the consequences of analyzing tourism development for the various spheres of modern life. One thing is certain and confirmed: the development of modern tourism cannot be stopped. If so, this is where one can present the balance of benefits and costs of tourism in the Gorce National Park and its social and cultural surroundings. These are only examples because all of the advantages and disadvantages cannot be listed.

#### **Socio-cultural benefits**

- 1) Increased diversity of economic activity, especially using local resources and products,
- 2) Investment,
- 3) Utilization of existing infrastructure,

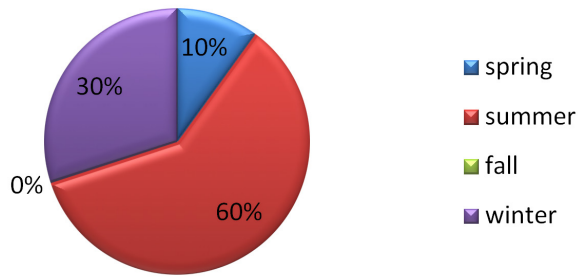
- 4) Utilization of existing tourist infrastructure by the local residents,
- 5) Increased job offer (increased employment),
- 6) Protection of cultural resources,
- 7) Breaking barriers, e.g. languages, social ones,
- 8) Encountering different sociological and cultural patterns by the local people, mixing of civilizations,
- 9) Valuing one's own as well as other socio-cultural norms.

**Socio-cultural costs**

- 1) Seasonality,
- 2) Failure to make alternative use of local resources and their destruction,
- 3) Overloading of the ecological system by tourism,
- 4) Commercialism in culture, arts and crafts as a result to try to match the tastes of tourists, and thus loss of identity,
- 5) Pathology and distortion of the material and spiritual culture,
- 6) Conflicts, the lack of mutual understanding, artificial behavior,
- 7) Consumerism,
- 8) Pathologies: alcoholism, crime,
- 9) Destroying the natural and cultural environment,
- 10) Communication problems, shopping problems, pollution, noise,
- 11) Urbanization of rural areas.

**5. Possibilities to limit the negative effect of tourism on the Park's socio-cultural heritage**

Mass tourism causes excessive concentration of people in areas shared by tourists and hosts. Tourist traffic overload occurs when the number of tourists exceeds the number of permanent residents. This is due to the seasonality of tourism and its strong concentration in the summer months. 60% of the tourists come to the Gorce National Park in the summer (Figure 7). It would be worthwhile to start marketing activities in order to balance the demand throughout the calendar year, so that the Park is not overloaded with tourists in the summer season only.



**Figure 7.** The season when the tourists arrive to the Park

The key task of protecting the socio-cultural heritage of the Gorce National Park and its closest surroundings is to encourage all tourists to use these goods in a manner as little detrimental to the population and heritage, while the local population must be convinced of the advantages and benefits of development of tourism and understand its meaning and essence.

Tourism is a part of modern culture and a carrier of many cultural values. At the same time, its development can be a source of adverse consequences for culture. 54% of the respondents answered that tourists do not respect their cultural heritage. 46% of them noted damage to cultural objects in the Park and its surroundings caused by tourist traffic or tourists themselves. The respondents admitted (31%) that the awareness of the meaning of cultural sites should be promoted among tourists. 26% of the respondents would consider placing valuable information about objects important for culture, and even some of them (16%) wanted to punish tourists financially for the damages caused (Table 6).

**Table 6.** Ways to increase tourists' respect towards cultural heritage

Ways to increase tourists' respect towards cultural heritage	Number of indications (in %)
Spread information about valuable cultural sites	26%
Spread awareness and disseminate their importance among tourists	31%
Form desirable behaviors in tourists	9%
Promote eco-tourism	7%
Introduce more prohibitions and obligations	0%
Increase the number of Park service employees	11%
Fine tourists for damages caused	16%
Limit the accessibility of the most precious sites to tourists	0%
Other	0%



However, in my view, positive attitudes depend largely on the personal involvement of individuals, their attitude and preparation for contact with tourists.

## **6. Conclusion**

Tourism can be seen in social terms - because it is the human being who is involved in it, cultural - because it is a manifestation of culture, economic - because it is accompanied by the circulation of capital. Its essence is the movement of people, however, in order to meet the needs of leisure and personal development. This phenomenon has its cause, but it produces certain effects for both tourists and the areas to which they come as well as permanent residents (Przeclawski, 1997, p. 61).

Tourism, and especially mass tourism, is considered to be an important factor in social and cultural changes in the areas of its development. The trend towards concentration of tourism means that the inhabitants of a village or tourist region remain in close, spatial, psychological and social, as well as personal, contact with the community of tourists. This situation must result in several changes.

The conflict situation also arises from the different attitudes and needs - tourist-oriented entertainment and leisure and the residents immersed in daily tasks, work, and satisfying the needs of guests.

The presence of tourists disrupts the social order. Reservations arise: fear, anxiety, lack of citizen satisfaction, and later also reluctance along with noticing only negative aspects of tourism. Local people from the Gorce evaluate tourism negatively when its development is under the control of foreign entities, and the share in the economic benefits of local hosts is insufficient and often negligible. Nuisance related to tourism in the Park is felt strongly by these residents who do not have income from tourism.

It should be noted that the effects of increased tourism may also deserve a negative rating when accompanied by some pathological phenomena, for example devastation of the environment (23%), and cultural traditions (14%). There is no denying that the respondents feel they are affected by the disturbing of their peace at night (16%), complaining about the sound of quad bikes, motorbikes and other vehicles, and the congestion of their place of residence by excessive tourist traffic (27%). They also say they have trouble getting fast to a certain place or shopping without standing in queues. A serious problem for them is litter (20%) which tourists leave behind.

The survey shows that tourism reduces the quality of life of residents. Increased noise limits the right to peace and quiet.

As another example of the adverse consequences of tourism, one can indicate the disappearance of traditional values, changes in customs, moral and religious views, along with deterioration of family ties. Residents of neighboring communes surrounding the Park are most afraid of worsening living conditions (43%). It can be said that the influence of mass tourism is followed by solid and rapid changes in the lives of the local population, accompanied by emphasis on imitation of the patterns of behavior of tourists.

The Park's cultural environment is an important attraction for the tourism industry, also representing the cultural goods in the form of museums, monuments, log cabins, wooden chapels, crosses and pastoral huts, which are also vulnerable to destruction caused by visitors and high tourist traffic.

Tourism cultivated by most people is usually associated with a very superficial interest in learning about cultural regions. The tourists' lifestyle is comfortable and passive. Close and sincere relations with the local population are rare. Newcomers behave differently than residents of the tourist destinations and do not try to adapt to local traditions. The encounter of two different cultures can lead to irreversible changes in habits and patterns of behavior (Zaręba, 2006, p. 27).

Unfortunately, having collected all the positive and negative effects of socio-cultural development of tourism in the Gorce National Park, I can say that it carries more negative changes for permanent residents.

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# THE ANALYSIS OF THE DEVELOPMENT STRATEGIES OF SELECTED LOCAL GOVERNMENT UNITS, INCLUDING TYPES OF COMMUNES

**Emilia Norkowska<sup>1</sup>**

## **Abstract**

*This operation is aimed at economic growth, meeting the needs of local communities, creating new practical values of the commune, and improving the already existing ones. Local government units are a major reference point for the local development. The aim of this paper is to check whether the type of selected municipalities, urban-rural and rural units influences the direction of local development, as it is in the case of practical values of the unit, available natural resources, and funds. To meet this end, an analysis of the development strategies of three different communal units was made: Krakow municipality, Kęty rural-urban commune, and Klucze rural commune. Based on a comparison of strategic and operational objectives included within the strategies, the hypothesis which claims that the type of units adopted to be analyzed influence the direction of their local development was confirmed. In their objectives of development strategies, all of the studied units emphasize the need to take action for economic development, education, and housing. However, the remaining strategic and operational objectives are divergent. The most significant difference was noticed between the municipality and the rural unit. Their targets range from fulfilling the need for international promotion of the city, to the necessity of ensuring the residents access to water and sewer systems. The conclusions derived from this analysis will allow further research. Its effect is to facilitate the selection of appropriate tools for local development in relation to a certain administrative unit.*

**Keywords:** *local development, local development objectives, commune, local government unit, local development strategy.*

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## **1. Introduction**

The problem of localism originated in the late '70s when the crisis of regional politics manifested itself in Western Europe. As a result, economic stagnation painfully affected local communities and their environment, including large enterprises (Pająk, 2001, p. 44). These enterprises were recognized as carriers of progress, making small and medium enterprises completely unnecessary. In addition, it was believed that the smaller units do not generate any innovation, which is indispensable in the development process (Jewtuchowicz, 2005, p. 61). It was not until the modification of this trend and resignation from subordination of peripheral areas to the central ones, when the potential of local development was recognized. In Poland, this approach was primarily a reaction to the excessive political and economic centralism and its weakness regarding new social needs. Currently, this development is often put first due to the argument that small units are a driving force for the development of the whole country. However, the development processes of individual units and areas often differ substantially. This is mainly due to the specificity of individual units, which in turn is the cause of defining local development objectives in various ways. One of the ways to distinguish between individual units of local government is to divide them into: municipalities, urban-rural, and rural communes. The aim of this paper is to present the idea of local development, and to check whether the objectives of the said development are subject to the type of commune units chosen to serve this analysis. To answer the abovementioned question, the literature on the subject, which defines local development, will be analyzed. The second part of the paper will contain the comparison of the development strategies of selected communes in the province of Małopolska: Krakow municipality, as well as Kęty, and Klucze communes.

## **2. The essence of local development**

Local development is the subject often undertaken in both discussions and scientific studies concerning, *inter alia*, local government. It is also reflected in the multitude of terms defining this issue. However, there is a common belief stating that local development should be associated with desirable and positive qualitative, quantitative, and structural transformations of a given system. This idea relates to two principal terms, that is territory and change (Naworól, 2006, p. 81). In order to facilitate the formulation of the definition, it is worth to analyze both elements of the term "local development".

Development is associated with a change of the current state. However, this is, by all means a process that brings benefits and leads to even more perfect

states. Development is defined by W. Krajewski (1997, p. 33) as ‘a kind of chain of directed and irreversible changes occurring in the structure of complex objects’ (Nermend, 2009, p.7). In the following analysis, local government units can be considered as such a complex object. This development consists of particular phases and stages, which take place over a longer period of time. These phases are full of both quantitative and qualitative changes. In addition, it is emphasized that development is a fundamental category, occurring in many areas of life and science (Piontek, 2006, p. 36). One of these areas is economy, where we distinguish, among others, socio-economic, sustainable, or local development, which is the subject of this paper.

Local development is associated with a certain territorially limited area. There is no clear framework suggesting the size of this area. In Poland, taking into account its current administrative division, it is considered that the local scale may cover the following areas (Małkowska, 2011, p. 19):

- the area of districts and communes
- the area of communes

This divergence stems from the objectives and resources used on a given territory. Some of the tasks require cooperation at a higher level than the local authorities. The literature on the subject is very helpful in determining this distinction. According to M. Trojanek’s interpretation (1994, p. 9-10), locality can be understood in three various ways:

- locality as an element characterizing a property of the analyzed system or entity, with respect to the interconnected surrounding and primary systems (in this regard, commune is a local system in relation to province which, in turn, is local in relation to the country),
- locality as a measure of a given part of the territory in relation to the whole, standing as its relatively small part (it is assumed that locality refers to what is bigger than a single settlement unit but smaller than the region),
- locality as distinctness, which means a possibility to undertake autonomous actions in relation to similar systems.

This interpretation indicates that in local development locality does not apply exclusively to the territory. Locality should be understood as a relation of subordination between units and the ability to take certain independent actions. What is more, this restriction characterizes not only geographical constraint, but it also relates to the society, which plays a very essential role in local development. Within the theory of local development, this population is referred to as “local community” (Brol, 1995, p. 91 ). The characteristics of this community are convergent with the foregoing interpretation of locality proposed by M. Trojanek. This is a group of people who are connected with each other by a certain system of relationships. This group has some common values and it considerably distinguishes itself from other communities,

according to the principle of distinction. To some extent, local community is self-sufficient and capable of meeting the basic needs of its members. According to A. Sztando (1998), the influence which a local community has on local development can appear in two forms:

- Community living in a given territory transforms it through individual actions of its members.
- Transformations within the territory are held on the basis of the activities executed jointly by the community. Individuals join with each other to form business entities, institutions, and organizations. The most important of them is the group that joins all the units of a given community. The group that decides about the direction and pace of development is a self-government community. Its members at large, and all of its characteristics, are called local government.

Combining the abovementioned considerations relating to the development, locality, and community of residents, we can move to define local development. Firstly, we can cite R. Rezsóhazy, who defined local development as ‘harmonized and systematic action carried out in a local community, involving people interested, the results of which serve to meet the social needs of the locals and contribute to the overall progress’ (Sztando, 1998, p. 12). The importance of local community in the creation of local development is also emphasized by J. Parysek (1995, p. 37), who defines it as ‘operating for economic and social development of a given territorial unit (city, commune), using its resources, taking into account the needs of the residents, taking into consideration their contribution to the activities undertaken’. The last of the definitions was formulated by R. Brol (1998, quoted after: Małkowska, 2011, p. 16). Apart from local community, he pays attention to a highly essential aspect, which is how development influences regional ecology. He defines development as ‘harmonized and systematic action carried out by local community, local authority and other subjects functioning in the commune and intended to create new and improve the already existing practical values of the commune, provide favorable conditions for the local economy and ensure spatial and ecological order’.

While looking at these definitions, one can notice that they emphasize not only the importance of local communities, but also the practical values of a given unit. Each and every territory has a certain potential determined by internal social, economic and environmental resources. This potential is also determined by a closer and a more distant environment of a unit. These resources are defined as the development factors that determine the character and direction of the development. J. Nowak (2006, p.23) divides these factors into internal and external ones. Among the external factors he enumerates government politics, including international programs (e.g. the actions of



the European Union) and the actions of the investors. The internal factors, according to the author, involve local resources such as: society, economy, current infrastructure and environment, as well as local administration, that is, the actions undertaken by local authorities, adaptability of the unit, and newly constructed social and technical infrastructure. Properly recognized and interpreted factors are a source and a driving force for local development. Their absence may, however, constitute a major obstacle to the development and even change into the development barriers. These barriers constitute significant limitations in the development process. They can be removed using economic or legal and organizational means (Bagdziński, 1994, p. 27).

### **3. Local development objectives**

Definitions of local development emphasize its various levels. The most frequently indicated levels of development are social, economic, environmental, political, cultural, and spatial. It should be noted that the above-mentioned areas interfere with each other and complement each other. These levels can also be noticed in the aspects of commune development enumerated below and proposed by M. Adamowicz (2003, p. 18). According to the author, local development of a commune manifests itself by:

- economic growth,
- increase of prosperity and quality of life of the population,
- increase of investment attractiveness,
- technical development and implementation of innovations,
- restructuring and diversification of business activity,
- development of public welfare services and resources,
- growth of job and social mobility of the population,
- development of the institutional infrastructure,
- re-cultivation and improvement of the quality of the natural environment,
- strengthening local, regional, and environmental identity.

The aforementioned levels of development can also be noticed by analyzing the development objectives, which relate mainly to the areas enumerated above. The local development objectives are universal, but under certain local conditions they are specified and hierarchized, and adjusted to the existing conditions of development (Wojtasiewicz, 1997, p. 9). It means that, depending on a direction of development, the authorities of the unit establish adequate main and detailed objectives.

In its activities, the authorities of the communal local government are obliged to follow the well-being of the citizens and meet their basic needs (Act of 8 March 1990, art.7) It is their needs that should be given priority while designing local development. For this reason, in the literature on the

subject, it is assumed that the strategic objective of local authorities within local development is to ‘provide the residents of a given self-government unit with jobs and income at a level which allows decent standard of living’ (Chądzyński, Nowakowska, Przygodzki, 2007, p. 81). Complete implementation of the above-assumed objective allows further development of a society and a region.

All the other objectives of regional development can be divided into several main groups, which are: economic, social, psychosocial, technological, political, and cultural. The following table presents detailed objectives within each of these categories.

**Table 1.** Main groups of local development objectives

Economic Objectives	Pursuits taken to ensure the residents high economic development through their self-realization and a certain external aid.
Social Objectives	Social integration of people inhabiting a certain region.
Psychosocial Objectives	Increase in the identification of single individuals of the society with a whole group and with action programs implemented in the region.
Technological Objectives	Increase of technical conditions of life in the region.
Political Objectives	Pursuits undertaken to increase participation of local communities in a decision-making system. Creation of democratic structures of power in the region.
Cultural Objectives	Creation of a regional system of norms and values accepted by the residents; identification of the residents with the region inhabited.

Source: Own work on the basis of Chądzyński et al. (2007), p. 81.

The problem of local development is also raised by the Organization for Economic Co-operation and Development. It stems from the main objective of the organization, which is to help the citizens achieve the highest standard of living. The objectives of local development politics, formulated by OECD, refer primarily to the generally formulated economic objectives (see Table 1). According to the OECD, the local development objectives should be understood as:

- increase of competitiveness of the region through skillful and appropriate use of available resources, including adequate promotion of regional products and services,
- improvement in the employment levels and the pursuit to provide long-term career opportunities for the residents of the region,
- pursuits undertaken to increase participation of the disabled and the national minorities in local economy,
- taking care of land management which contributes to the quality of residents’ life and determines the possibilities to undertake business activities.

#### **4. Diversification of local development objectives depending on the administrative type of a communal unit**

The catalogue of local development objectives mentioned in the previous chapter (see Table 1) is a universal one. Particular territorial units can, or even should, establish the abovementioned objectives individually, being dependent only on a situation and the needs appearing on a given area. This catalogue can be extended by new objectives, while the already included points can be ordered and hierarchized. The properly chosen objectives will serve to obtain a long-term local development.

The commune is the basic unit of local government (the Constitution of the Republic of Poland, art.164). In Poland we can distinguish between three types of a commune. These are:

- municipalities – this name is used to denote the communes which are located within the administrative borders of a given city,
- urban-rural communes – these are the communes which enclose the city and the surrounding villages; local authorities are usually located within a given city,
- rural communes – these are the communes without any city on their territory.

Different statuses of a given unit should considerably determine the direction of local development. Such diversification should be signaled by the discrepancies within the local development objectives adopted by particular units. In order to test the abovementioned hypothesis, the development strategies of 3 Lesser Poland communes with different statuses were compared: Krakow municipality, Kęty rural-urban commune, and Klucze rural commune.



**Figure 1.** Location of Krakow municipality, Kęty and Klucze communes on the administrative map of Małopolska

Krakow is a city with district rights and a residence of the Małopolska province authorities. In addition, Krakow is the second largest city in Poland, also in terms of population. Currently, it is a residence of culture and science. In the Development Strategy of the City of Krakow, the city authorities have to take into account, not only its status and the needs of its residents, but also the economic, tourist, and scientific potential. To meet this end, 3 equally important objectives were created:

- Strategic objective I – Krakow as a family-friendly city and a place attractive to live or visit.
- Strategic objective II – Krakow as a city of competitive and modern economy.
- Strategic objective III – Krakow as a European metropolis with important functions in science, culture and sport.

To specify the strategic objectives, the city adopted a catalogue of operational objectives followed by programs, which are to help with their realization. The following table presents the list of these objectives.

**Table 2.** Operational objectives according to the Development Strategy of the City of Krakow

Strategic objective I	Strategic objective II	Strategic objective III
-improving natural environment, -providing broader scope and better access to education for all age groups, ensuring higher educational standards, -guaranteeing a greater sense of public security, -developing the housing industry and revitalizing the degraded areas, -providing the residents with a proper level of health service, -guaranteeing protection of a family status and welfare, -enabling the individuals and whole groups at risk of exclusion participation in social development, -developing local self-administration and improving management methods, enhancing social awareness and interest in the life of the city.	-shaping spatial conditions for economic development, retaining balanced development of the city and a topographic order, -improving access to public transport, -developing technical infrastructure, -developing small and medium enterprises (SME), -raising competitiveness in the labor market, -improving touristic attractiveness of the city.	-improving working conditions of the Krakow scientific center, -supporting institutions maintaining co-operation between science and economy, -preserving the cultural heritage, including revitalization of historical complexes of the city, -creating material and institutional conditions for cultural development, -making conditions for localization of head offices and the representatives of national and international organizations, -creating conditions for sport, physical education and recreation.

Source: The Development Strategy of the City of Krakow.

Kęty is a rural-urban commune located in western part of the Lesser Poland in the Oświęcim district. The residence of the commune is situated in Kęty. Apart from the town, the commune consists of Bielany, Bulowice, Łęki, Nowa Wieś, Malec and Witkowice villages. Currently, the commune lost its typically industrial character. Most of the inhabitants are employed in micro and small enterprises located in Kęty and the surrounding area. In addition, the unit has a high potential in terms of residential facilities, tourism and recreation for nearby urban centers. In its Strategy, as it was in the case of Krakow, the local authorities established 3 main strategic objectives:

- Strategic objective I – higher economic competitiveness and investment attractiveness of the commune.
- Strategic objective II – expansion and modernization of transport routes, which should increase the access to transport.
- Strategic objective III – broader access to high quality public services.

Short-term (3-5 years) operational objectives were developed to complete the strategic objectives enumerated above. Their structure was presented in the following table.

**Table 3.** Operational objectives according to the Development Strategy of Kęty Commune for the years 2012-2020

Strategic objective I	Strategic objective II	Strategic objective III
<ul style="list-style-type: none"> <li>-creating local areas of economic activity,</li> <li>-increasing competitiveness among micro and small enterprises through establishing cooperative connections,</li> <li>-developing and implementing a coherent system of economic and investment promotion,</li> <li>-creating the touristic image of the city of Kęty,</li> <li>-creating entrepreneurial skills among local community,</li> <li>-alleviating the effects of unemployment and enhancing vocational activation, reflecting changes in the local labor market.</li> </ul>	<ul style="list-style-type: none"> <li>-improving external accessibility to Kęty in terms of transport,</li> <li>-developing local road system,</li> <li>-improving the quality of collective transport between rural areas and the urban centers.</li> </ul>	<ul style="list-style-type: none"> <li>-maintaining high standard of technical infrastructure and protecting the environment,</li> <li>-developing crisis management systems and the infrastructure protecting from the effects of floods and other natural disasters,</li> <li>-developing the institutional base and increasing effectiveness in terms of social assistance in the district,</li> <li>-developing information society,</li> <li>-ensuring optimal premises, sports facilities and high-quality educational services in the commune,</li> <li>-focusing on a policy of long-term cooperation with non-governmental organizations (NGOs)</li> <li>-initiating and supporting the actions which serve the development of housing,</li> <li>-efficiently managing the commune.</li> </ul>

Source: The Development Strategy of Kęty Commune 2012-2020.

The last commune to be analyzed is the rural commune of Klucze. It is located in the northern part of Małopolska in the Olkusz district. The residence of the commune is situated in Klucze. This unit consists of 15 villages. What determines the attractiveness of this commune is its location, which is the Kraków-Częstochowa Upland – a very interesting and picturesque southern part of Poland. In this area there are such manufacturing plants as Kimberly Clark Ltd and a glass factory in Jaroszowiec. Agriculture is also highly developed. The structure of the division of development objectives in the Klucze commune is similar to these presented in the case of the preceding

communes. In order to make their actions more precise, the local authorities decided to formulate 4 strategic objectives.

- Strategic objective I – supporting the development of modern entrepreneurship and enhancing competitiveness of local economy.
- Strategic objective II – developing the local infrastructure, which serves to improve the quality of natural environment and local natural resources.
- Strategic objective III – creating the conditions for harmonious development of tourism and culture and securing the durability of cultural heritage.
- Strategic objective IV – striving for improvement in the quality of life of the residents and ensuring favorable conditions for social development of the Commune.

In the Development Strategy of the Klucze Commune, the local authorities thoroughly defined the operational objectives. These objectives were presented in the following table.

All of the analyzed development strategies have a similar pattern and hierarchy of the objectives. Local authorities define main strategic objectives, which point out directions of the development. Afterwards, the operational objectives and tasks are formulated, the completion of which allows to obtain the assumed development direction of the unit.

The common characteristic of all these strategies is the emphasis placed on the importance of the economic development within the development programs. This development is, however, adjusted to the type of the unit. The municipality, here represented by Krakow, aims at developing modern economy. The rural-urban and rural communes, in their actions, strive to improve competitiveness of the economic actions implemented within their areas. In addition, in the case of the municipality, the need to support small and medium enterprises was emphasized within the operational objectives. The remaining administrative units focus on micro and small enterprises. The aim of this support is to activate local community. The Klucze rural commune, within its strategy, even included the development of small food outlets. Their task is not only to have a positive influence on the touristic side of the commune, but also to provide new places of work. The analyzed units pay attention also to the problem of education.

**Table 4.** Operational objectives according to the Development Strategy of Klucze Commune

Strategic objective I	Strategic objective II	Strategic objective III	Strategic objective IV
<p>-creating favorable conditions of entrepreneurship development,</p> <p>-providing institutional support to farmers in terms of rationalization of agricultural land management, and providing help in occupational requalification of people leaving agriculture,</p> <p>-developing information society and increasing the number of people using information networks. Improving quality of and accessibility to public services.</p>	<p>-ensuring water resources and modernizing the drinking water supply system for the residents of the commune,</p> <p>-maximizing the amount of discharged and treated waste water,</p> <p>-increasing the segregation and disposal of municipal waste,</p> <p>-reducing road traffic that is a nuisance for the residents and increasing road safety, improving the accessibility to transport in selected parts of the commune,</p> <p>-protecting and revitalizing natural and landscape values,</p> <p>-minimizing the emission of gas and dust pollutants produced locally,</p> <p>-increasing flood safety and enhancing water retention basins.</p>	<p>-constructing and improving the quality of leisure facilities and increasing the number of small catering businesses,</p> <p>-intensively promoting the landscape and recreational values of the Commune and supporting cultural initiatives in the Commune,</p> <p>-creating conditions favorable for the development of tourism,</p> <p>-using and protecting the historical monuments of the Commune, in order to develop public space and create the center of the village.</p>	<p>-extending the educational offer and organizing a flexible system of education in the commune,</p> <p>-providing equal opportunities for education and development of the young generation,</p> <p>-developing educational infrastructure and providing the schools within the area with specialized equipment and sports facilities,</p> <p>-providing equal life chances for the disabled,</p> <p>-increasing employment and economic activity of the residents; preventing social exclusion,</p> <p>-renovating unsafe residential areas and improving safety in the commune,</p> <p>-preparing appropriate amount of land for house and residential building (for summer) and increasing the number of council flats,</p> <p>-improving quality of health care services,</p> <p>-enhancing civil society.</p>

Source: The Development Strategy of Klucze Commune.

The municipality, due to its nature, emphasizes the importance of higher education, whereas the rural-urban and rural units recognize the problem within such a basic need as equal access to education. The last common, and sharply



outlined area is the development of housing. In the case of Krakow, this development relates primarily to multifamily housing. Additionally, this objective was increased by revitalization of degraded areas. The Kęty rural-urban commune and the Klucze rural commune included information concerning single-family housing. This development should be supported through initiating certain activities and preparing appropriate areas by the local authorities. The objectives defined in this way are consistent with the universal objectives of local development (see Table 1) and the strategic objective of local development, which is to provide the residents of a given local government unit with places of work and incomes on a level that ensures them a decent standard of living.

Due to its nature, the municipality differs substantially from other communes in a number of objectives (Table 2). Above all, attention was given to the international character of the city. This refers not only to the already mentioned modern economy and the branches of foreign companies established in the city, but also to the support given to the scientific center and touristic promotion of Krakow carried abroad. Due to the historical character of the city, new objectives aimed at preserving the monuments and revitalizing certain areas were included in the strategy. The Development Strategy of the City of Krakow is the only one that raises the problem of spatial order, usually noticed only in reference to bigger urban centers. In this case, the problem of public security was also noticed. It was not included in the strategies of the other units. What is interesting, is that the strategic and operational objectives do not raise, at least directly, the issue of unemployment. The actions undertaken to resolve this problem were included only in the detailed provisions of the Strategy.

The urban-rural Kęty commune, as the only one, in its objectives (Table 3) emphasizes the expansion and modernization of transport routes. Through implementation of certain tasks, local authorities want to ensure that all residents of the commune have equal access to the main urban center, which is Kęty. These actions refer not only to the construction of infrastructure, but their aim is also to promote public transport. As it was mentioned above, in case of this unit, they significantly emphasize the need to create entrepreneurial skills among the local community. Fulfillment of this task, alongside with the formation of local areas of economic activity, should help to enhance economic competitiveness in the commune.

The operational objectives were most thoroughly defined in the strategy of the last unit, that is the Klucze rural commune (Table 4). Due to its nature, this commune is the only one that raises the issue of agriculture. Local authorities recognize the need to support the farmers in terms of rationalization of agricultural land management, as well as the necessity to help those people

who decide to leave agriculture. This part of the community needs also to be supported in the occupational requalification. Klucze is the only commune that focuses on increasing the number of people using information networks. This issue was raised only in the case of the rural commune, as the access to information networks does not pose any problems in the municipalities. The last of the operational objectives which distinguishes the rural commune on the background of other units is how to ensure water resources, modernize current drinking water supply systems and construct new sewer systems, which should encompass as much of the communal area as possible. As it was in the case of information networks, most of the land in urban centers is covered by a full water supply and sewer system. In rural areas, on the other hand, providing full access to the media is becoming a priority for the authorities.

## **5. Conclusion**

For several years, local development has been gaining much importance. This is because the authorities noticed that the potential of smaller units could, to a large extent, contribute to the development of larger areas. The development of certain communal units is subject to the available resources, funds, and the local community. The aim of this paper was to check whether this development was determined by the type of the communal units chosen. In order to test this hypothesis, the development strategies of 3 communes were compared: the Krakow municipality, the Kęty rural-urban commune, and the Klucze rural commune. The analysis showed that, in their strategies, all units recognize the need to support specific areas, such as economic development, education, and housing. However, other objectives of the units differ from each other. The most significant divergence can be noticed between the municipality and the rural commune. The objectives enumerated in their strategies relate to totally different problems – from international promotion of the image of the city, to ensuring the residents full access to water and sewer systems. Comparison of the development strategies enabled to conclude that the type of selected units also influences the specificity of local development. This differentiation will allow further research, which, in turn, will provide the possibility to analyze a larger number of communal units. As a result, it will be possible to demonstrate the way to plan development in a particular communal unit, and, above all, to show which development tools should be considered as essential.

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# MANAGING THE COMPETITIVENESS OF REGIONS

**Karolina Olejniczak<sup>1</sup>**

## **Abstract:**

*Competitiveness of regions depends on the establishment of public administration and the forms of governance. Of great importance is the tendency to cooperation and social responsibility of both the public authorities and entrepreneurs. To implement tasks facing public administration in modern economies, it becomes necessary to combine the administration within the meaning of traditional active management, which is a professional directing oriented at adapting to changes in the environment, but also distribution and efficient use of resources. Only such management is strategic and enables optimal management of resources affecting local and regional economic development. Member countries of the European Union, including Poland, should implement new methods of management in their administrations. Although many Polish government at various levels are already implementing both traditional and modern forms of governance, the current activities in this field are still unsatisfactory and do not lead to a substantial improvement in the public sector in Poland.*

**Keywords:** *management, region, competitiveness, public, authorities.*

## **1.Introduction**

When studying economics, a conclusion may be derived that management applies mostly to private entities and profit-driven organizations. Management is defined as the influence of the managing entity on the resources under its control in order to realize the objectives of the organization while maintaining the principle of economic rationality. The reference to private entities bases on the assumption that independent and rational economic decisions are possible only in the case of private property. However, in recent years, the management of public sector has been more and more in the focus of the science of economics. According to P. F. Drucker (2009) the not profit-oriented public sector will be the major growth area in the twenty-first century. Also in other modern organizations management will play an increasingly important role, at

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least because, for example, non-profit organizations and government agencies are generally less flexible than enterprises.

The increase of the importance of public sector reflects its incrementing spending but also the qualitative and structural changes it is undergoing. Today it functions similarly to the private sector, striving to achieve its own objectives in a rational way. The efficient implementation of these goals requires efficient management (Kozuch, 2004). On the other hand, changes in the modern world such as the development of civil society, an increase in the level of education and democratization evoke social pressure to increase the efficiency of public spending. Along with that the role of public administration at both central and local level has also been changing. Many countries stand up to the challenges of decentralization of public affairs and the use of the market mechanism in the process of satisfying social needs. The government is gradually moving from administration to management. This process is most advanced in the Anglo-Saxon countries (Kosiedowski, 2008).

The principle of the social market economy is laid down in Constitution of the Polish Republic, which presupposes the existence of regulators of economic processes, whose task is the realization of social needs. These regulators are created by the state. It can affect the elements of the market mechanism and complement them. These tasks can be executed at the central, as well as regional and local level through local and regional governments. The Law on Regional Government highlights realizing development policy of provinces and shaping their development strategies in a way that takes into account, among others, objectives such as boosting economic activity and increasing innovation and competitiveness of provinces (Osiński, 2008). Also the principle of decentralization of administrative system, which is provided in the Constitution, grants a special role in public management to municipal, county and provincial authorities. In order to be able to perform the steering functions the model of local government must respond to the current conditions, social needs and expectations directed at public authorities. Therefore it becomes necessary to modify the model of public management in a way that will optimize the activities of local government, through, among others, the adaptation of methods and forms of work as well as an adaptation of organizational structures (Lutrzykowski, 2010).

From the perspective of modern economies, ensuring the proper conditions for constant improvement of the competitiveness of regions is becoming more and more crucial. The author concentrates on the modern management in the public sector and on region's development planning in the context of ensuring the right conditions for the improving its competitiveness. She also attempts to show the influence of public sector management on the competitiveness of the local economy.

## 2. Modern management in public institutions

Specialist literature does not give a clear definition of public management. The subject of public management is often portrayed as management in the public sector or public administration. The public sector includes government, municipal associations, regional boards, public companies and the organizations created by these entities. Public affairs are classified as finance and public safety, health, education, culture and infrastructure business. As opposed to business management, the following aspects are important characteristics in public management:

- realization of management by public bodies, local authorities,
- in the public sector management we are dealing with a number of institutions rather than a single organization. The objectives of these institutions do not have to be compatible with each other and contribute to the success of the whole system,
- the right to manage does not result from the property, but from the power of state and local authorities,
- the management of the public sector is always about the good of society,
- public institutions cannot be assessed on their earnings or market value,
- objectives of political organizations and social policies are of great importance in public management,
- the realization of tasks is entrusted by administrative acts,
- the activities are regulated by administrative law (Lissowski, 2009).

An interesting example of a subject of public sector management which involves the participation of international, national and regional administrations, public and private entities as well as non-governmental organizations, is the European Union.

As a network of institutions, rules and decisions that are to pursue their goals, it is a multi-level and multi-purpose structure. It is hard to find in the contemporary world any other such system or structure which would correspond to the model of the European Union (Mendza-Drozd, 2010). From the point of view of management it is a very complex system, which should adapt to the changing international environment and economic competition. It should adapt its policies to the long-term challenges, but also effectively respond to changes and emerging crises. Many observers consider the EU system as the system with many performance problems, and are concerned with effectiveness of decision making and its democratic legitimacy (Eberlein and Kerwer, 2004). In response to these challenges, new methods are introduced, also called modes of governance. Particularly important are the New Modes of Governance of European Union. These include a variety of processes and

institutions such as the open method of coordination, voluntary agreements, regulatory agencies, networks, management by informing, competition and informal agreements. It is assumed that New Modes of Governance have one of the following characteristics:

- they introduce social participation (such as social dialogue and social pacts) into public tasks,
- they lead to greater transparency and openness of the administration and a better flow of information between citizens and the administration, for example by publishing regular reports of the local authorities,
- they move away from prescriptive instruments to incentive activities and encourage voluntary cooperation,
- instead of vertical relationships they introduce horizontal cooperation such as horizontal networks and the creation of task forces.

New Modes of Governance are opposed to the traditional top-down and command-and-inspection methods of conducting public policy. They are implemented in the economy especially when there is a public-private partnership and in the managing bodies of administration in areas such as employment policy, sustainable development and social inclusion (Kolarska-Bobińska, 2009). European Governance - A White Paper elaborated and published by the European Commission (2001) refers to New Modes of Governance in general, in a more detailed way - numerous policy papers.

Also in the traditional public institutions in many countries around the world modern management concepts are introduced. Among the current trends of modern management concepts the following can be also distinguished: New Public Management (NPM), which plays a special role in countries such as New Zealand, Australia, Great Britain, Sweden, Canada, Finland, Germany and Reinventing Government dominant mainly in the United States. NPM represents four essential aspects of public sector management: managing as administration, management of the public sector as a business management, as following a policy and as managing people (Krynicka, 2006). The main goal of NPM is an improved thriftiness, efficiency and effectiveness of the public sector and an increase in the quality of its services. These aims are pursued, among others, through the following actions: result orientation, the use of strategic planning, building market relationships and competition in the provision of services, customer orientation, the separation of public policy from operational management and the introduction of measurers and service standards (Rajca, 2009). Central and local administrations in many countries are reforming their public service according to these concepts. The essence of those concepts can be described as an attempt to ensure that the



public administration has acted in a situation cross political competition and in competition with private entities.

New Zealand is the flagship model of changes in the public sector with the use of the NPM theory. The public sector management system is based on the following principles: clear-cut goals and tasks for managers, their freedom in resource allocation and power to take decisions, the accountability of managers, proper estimation of the work effects and an effective information flow in public sector which allows for an evaluation of the people as well as their work. It is a task-based model leading to an increase in efficiency. The managers play a crucial role in it. What is very important for the functioning of the system is a differentiation between the production of goods and services supplied by the public sector departments and their results, understood as the consequences for the society. Departments over there are differentiated from the government. What is also essential is the distinction of the roles of the state as the buyer of goods and services on one hand and their owner on the other. High fiscal policy transparency standards are crucial for the functioning of the whole system (Piwowarski, 2011).

The effects of the reforms initiated by the NPM are very visible also in the United Kingdom. The changes commenced at the beginning of the 80s of the 20th century evolved throughout the years. Their main areas include compulsory competitive tendering, the transfer of local authority functions to quasi-non-governmental organizations, Best-Value principle (the best quality at given costs) and Comprehensive Performance Assessments through a set of Performance Indicators. The beginning of the 21<sup>st</sup> century is related to the shift of the idea of management to local governance and multi-level governance (Rajca, 2009). In the recent years the importance of information technology-centered changes in public sector management has been growing and „digital era-governance” has been gaining popularity (Dunleavy, Margetts, Bastow and Tinkler, 2005).

In Poland, it seems appropriate to combine these concepts. Still, the country specifics needs to be considered as well. In particular, it seems important to reduce costs of this sector, shift the weight of benefits for certain services to the private sector, flatten structures, increase the role of teamwork and training for managers, as well as focus on the quality of services and the implementation of modern management concepts (Opolski and Modzelewski, 2009). Currently, traditional methods such as strategic management and quality management are used. Also modern methods such as benchmarking, outsourcing, the concept of learning organization and time based management are being introduced (Niedziółka, 2010).

In the context of raising the competitiveness of regions, the concept of multi-level governance or integrated management has been recently gaining

more and more importance. It denotes such management of the public sector which consists in integrating the various market actors operating in many areas and at different levels, to realize common tasks in contact with the public administration. It occurs when conventional forms of control seem to be insufficient in relation to the new requirements such as: modernizing public administration, social control and development funds (Województwo Dolnośląskie, 2010). An integrated approach means combining activities in various sectors and at various levels of government to coordinate better the tasks at various levels of management. In place of the administrative units functional units are created, in which the partners are the government and all levels of public administration as well as non-governmental organizations, education institutions and business representatives. Thanks to that the realized subject-based development policy allows for better use of public funds (Ministry of Regional Development, 2011).

Another important aspect of public management is the introduction of quality management systems such as Total Quality Management (Lissowski, 2009). In the context of Polish presence in the structures of the European Union and the standards applicable in this organization it is necessary to launch the processes of high quality public services. From the point of view of local governments the need to care about their image and increasing the investment attractiveness should be an incentive to implement quality management systems. With better management it is easier to gain the support of structural funds of the European Union. Moreover, a better cooperation with institutional client can greatly improve the cooperation related to the projects realized in public-private partnership.

The topic of quality of public services is very complex. Professional literature distinguishes three of its levels: the level of macro, mezo and micro, which determine the quality of governance in the public sector. Macro level (decision-making bodies), the level at which changes in the functioning of public administration are implemented. This is also the quality of legislation. Mezo level is the management of the institution which can take decisions leading to the improved quality of services. Micro level is the level of employees in direct contact with customers (Opolski and Modzelewski, 2009). In summary, it can be stated that the quality of services in local government bodies include: standards of service, effectiveness, maximum results with minimal effort, the timely provision of services, meeting the needs of citizens and to gain public confidence (Wodecka-Hyjek, 2013).

All the mentioned management aspects play an important role in creating the local authorities' capability to compete and in building the competitiveness of regions.

### 3. Competitiveness of regions

Taking into account the mutual interaction between the region and production systems operating in it, the competitiveness of regions can be defined in two main ways: from the point of view of the public authorities and the business entities. From the point of view of the public authorities competitiveness of the region is its ability to produce sustainable growth of regional prosperity and growing standard of living for its inhabitants which is based on:

- Optimal use of the internal and external resources and the management of the regional economy,
- Building the attractiveness of the region for local entrepreneurs, external investors and residents,
- Adapting to current development trends. Competitiveness of the region is its ability to effectively compete with other regions.

From the business perspective competitiveness of the region means the ability of the companies located there to produce goods and services meeting the needs of the markets, to maintain high employment and profitability, thereby creating a permanent basis for a higher standard of living for its population.

Taking into account the regional policy it seems appropriate to combine both points of view and understand the competitiveness of the region, both as an advantage for the companies due to the presence in the region, as well as the ability for local authorities to compete effectively (Przygodzki, 2012).

The concept of competitiveness of the region includes its investment attractiveness representing the advantages of location in this region. From the point of view of economic and social factors particularly important are: the links between entities, business environment, social environment, the quality of the labor market and the activity of local authorities in this regard.

Primary determinant of competitiveness is innovation, and the primary medium of innovation are business enterprises. From the point of view of locational advantages and competitiveness of regions, local innovation systems and merging companies into clusters and economic networks are gaining more and more importance (Skawińska and Zalewski, 2009).

According to Porter a competitive region is a region that has matured 'diamonds', industry clusters capable of international competition, an appropriately high level of productivity, and thus an attractive location offer from the viewpoint of entrepreneurs and investors.

The experience of developed countries shows clear evidence of a network-specific character of modern growing businesses, whose main strength is the regionalization of innovation capabilities. Modern trends in the development of innovative systems indicate the need to build strong, competitive regions, and

the essence for supporting innovative economy are networks forming regional innovation systems. These are the regional socio-economic systems with wide connections being able to use local resources of production processes, products and services in accordance with the specificity of the region or sub-region. These links are related to public authorities and systems of education, finance, universities, research, development and industry sectors. They are based on a strong network connections and the existence of innovative environment. The actions of individual subsystems composing them are connected through the policy of innovation of regional and local authorities. The regional innovation systems include:

- manufacturing and service subsystem - these are the companies implementing new solutions,
- scientific research subsystem - it consists of institutions of research and development responsible for technology transfer,
- institutional subsystem - these are the business environment institutions supporting innovation processes,
- financial subsystem - these are financial entities assisting in the transfer of new technologies to the business,
- socio-cultural subsystem - these are the cultural and structural characteristics of a given region or sub region.

Regional innovation systems thus form a unique public-private forum for cooperation between all the actors of the region or sub region making better use of local resources and factors of economic growth. Functioning within the system reduces the risk and lowers the costs of innovation, increases the ability of knowledge commercialization, facilitates the flow of knowledge and experience contributing to the competitiveness of the region (Gaczek, 2009).

#### **4. The impact of public management on the competitiveness of the regional economy.**

The regional economy is a huge collection of diverse entities, grouped according to certain rules, however, it is also the totality of relationships formed between them. These relationships are managed by the various decision-making centers, which are not always located in the given region. Local government is, therefore, a very important entity of management in the region but not the only one. Thus, one cannot talk about the management of the region in the traditional sense, in analogy to corporate management. Local government acts as a management entity only in the relation to the local government sector.

However, regional government is a host in a given territory and, as a host, it should be active in the relation to other elements of the regional economy. One cannot manage them, but these elements should be supported by creating a friendly environment for entrepreneurship. Local government should be the

coordinator and the impeller of regional development, as well as the most important entity which manages the process of change in the region. It should plan and organize the implementation of these changes, convince others to them and monitor the implementation of the established objectives and tasks. In the context of these functions the term “management of regional development” in relation to the regional government is justified (Kosiedowski, 2008).

Development and competitiveness of the local economy is dependent on the activities of public administration. The factor that indicates effectiveness of local government in the economic sphere is entrepreneurship, which requires support: creating optimal conditions for doing business, developing civic attitudes and providing incentives for economic activity. The tasks that local governments should pursue in this area can be divided into:

- undertaking initiatives for local development,
- stimulating development through a system of facilities and amenities,
- identifying local needs and resources,
- promotional and organizational activities,
- public aid activities,
- creation and development of economic infrastructure,
- creation of favorable financial conditions,
- attracting investors,
- creating local education system.

In addition, the role of local governments is to incorporate growing companies in the local development in such a way that it is possible to support the process of their development and to use this process as an impulse for economic activation of the local government. A policy which supports this goal is based on development strategies and operations leading to creation of economic clusters and networks.

Supporting the development of clusters, whose functioning is based on regional and local conditions, is now considered as a priority task of the public authorities, which is used to enhance innovation and competitiveness of the regional and local economy. The presence of clusters is associated with many positive phenomena that affect not only the companies involved in cluster structures, but also the local economy. These are phenomena such as specialization of the region, accelerating the transfer of knowledge, building a local culture of innovation, greater availability of financial resources, the creation of an attractive labor market, concentration and development of resources, improvement of the region image, development of the services sector and the science base as well as increased investment attractiveness of the region (Kogut-Jaworska, 2011).

More and more important from the point of view of efficient competition of small and medium-sized businesses is the quality of the business environment.

Cooperation between enterprises becomes an instrument which enables us to remain on the market and effectively compete. Cooperation of companies and inclusion in the network structure enhances the learning processes, building public-private partnerships, expansion in the operation area that is enlarged by networks, sharing risks associated with innovation and strengthens the clout on the market in situations that may overwhelm the abilities of one company.

The inclusion in the cooperation within the network, cooperation with the business environment and functioning in organized surroundings can be comparable in terms of benefits to the functioning of large companies and outputs which are produced by them. These effects are associated with a particular territory and provide additional benefits of competitive advantage by accelerating the development of the region (Przygodzki, 2012).

## **5. Planning the development in the region**

Regional development planning is the process of preparing local and regional development, assignment of tasks, their execution, coordination, evaluation of progress, current intervention and corrections. Planning is thus a complex, autonomous process which covers all phases of development, from idea to evaluation of results, where the timeframes play an important role. This process can be divided into the following steps:

- strategic analysis of the current state,
- forecasting changes,
- development of a strategic vision,
- preparation of a development strategy,
- detailing of the tasks,
- preparation of the investment plan and financial strategy.

The strategy should be assessed by the degree of addressing social needs, efficient use of resources, its functional character, the openness for development and the possible negative consequences of its implementation. The difficulties of strategic planning are related to the complexity of local and regional problems, the lack of relevant information and financial constraints (Szewczuk, 2011).

To plan development in the region it is necessary to analyze and diagnose the socio-economic situation and identify factors affecting the development of the region. The development of the region and its competitiveness lies in several factors of endogenous origin. In recent times, the role of the so-called resource agents such as natural resources has been decreasing, giving place to the qualitative factors. These include: qualifications of employees, administrative efficiency, diversification of the economic structure, quality and efficiency of transport and communication infrastructure as well as living

conditions, and image of the area. It should be expected that the importance of factors such as: institutional conditions, the quality of the functioning of public authorities, the way the region is managed, the scientific and research base, accessibility and environmental conditions will continue to increase (Ministry of Regional Development, 2009). In addition to that the development of the region is affected by a number of the so-called exogenous factors, coming from outside of the region, such as economic conditions, political situation, the competitiveness of the neighboring regions, taxes, state spending on research and development and sectorial policies.

In the context of factors influencing the development of a region it can be compared to the functioning of a production system. Seemingly it is situated in a specific environment. This environment affects the functioning of the system and at the same time the system influences the environment. It is assumed that the environment of a production system has a two-level structure. The first-level environment is the enterprise itself and the second-level environment is the economy of the country or region in which the enterprise is located. The organization of a production system is affected by such first-level environmental factors as for example: lower-level and executive staff, research and development activities run in the area of the production system, the level of technical advancement, the way sales is organized, post-sales service, marketing, materials management, financial resources, methods and forms of administration, for example quality management etc. Second-level environmental factors affecting a production system include first of all: the technical level, advancement, modernity and quality level of the machinery and the production processes. The technical level is also determined by the capabilities to create modern production facilities. This is affected by a series of diversified factors for example the banking system, domestic and international competition, the economic conditions of the country, governmental regulations, socio-political environment, natural environment, methods and forms of management and controlling of production by the country and regional authorities (Durlík, 2007).

## **6. Conclusion**

Competitiveness of regions depends on the entrepreneurship of public administration and applied methods of management. Of great importance is the attitude towards cooperation and social responsibility of both the public authorities and entrepreneurs. To make it possible to implement tasks



assigned to public administration in modern economies, it becomes necessary to combine the administration within the traditional meaning with active management, which is a professional operating oriented on adapting to changes in the environment, but also with distribution and efficient use of resources. Management is strategic and enables optimal resource allocation only when it affects local and regional economic development.

Member countries of the European Union, including Poland, should implement the New Management Methods in their public administrations. Although many Polish authorities at different levels already implement the modern management methods along with the traditional ones, the activities undertaken so far in this regards are not sufficient and have not resulted in a significant improvement in the functioning of the public sector in Poland.

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zarządzania obszarem metropolitarnym na region.*

# THE PROBLEM OF SECURING INTERESTS OF PERSONS WITH DISABILITIES IN ACCORDANCE WITH PROVISIONS OF THE CONVENTION ON THE RIGHTS OF PERSONS WITH DISABILITIES

**Monika Trętko<sup>1</sup>**

## **Abstract**

*The Polish society is unprepared to integrate people with disabilities into the labor market. This is due to inadequate state promotion of existing legislation in this area, which accounts for the lack of preparation of entrepreneurs in the context of the problems of people with disabilities and their knowledge of the hiring. Often unpreparedness leads to violations of basic human and worker rights. Previous attempts to include people with disabilities have been considered as insufficient. In order to prevent the marginalization of people with disabilities in the labor market it is necessary to make further attempts to integrate them into the labor market, despite the many difficulties involved. Special obstacle are the costs incurred by businesses related to the employment of people with disabilities, resulting from the need to adapt workplaces to their needs and to remove architectural barriers.*

**Keywords:** *employment of people with disabilities, the Convention on the Rights of Persons with Disabilities, the rights of an employee with a disability.*

## **1. Introduction**

The aim of the study is to determine the degree of preparation of Polish entrepreneurs (in the context of the problem and knowledge) to implement the provisions of Convention on the Rights of Persons with Disabilities. It is worth noting that the most important role in shaping the knowledge of the provisions of the Convention is that of the state.

One of the most serious challenges related to issues of diversity in the workplace is the issue of inclusion of people with disabilities to the group of employees and providing them with decent working conditions. The paper deals with the problems of ensuring the right conditions for businesses

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employing people with disabilities in line with the Convention. It is important for enterprises to promote the implementation of the Convention and emphasize the importance of its provisions.

Companies often unknowingly abuse human rights while employees do not know the provisions of the Convention, which is why it is important that the state should take responsibility for their promotion. The author was interested in the issues presented in the article while working in a company employing people with disabilities, which did not take into account the provisions of the Convention. This problem resulted from the management's ignorance of its provisions.

The article is theoretical in nature and refers to the provisions of Convention on the Rights of Persons with Disabilities, which should be used by employers.

## **2. The principles of the Convention on the Rights of People with Disabilities**

The rights of persons with disabilities are subject to regulations approved by international organizations and relate to around 650 million people around the world. People with disabilities are therefore a significant part of the population, which translates into a problem of their treatment in the workplace. So it becomes necessary to comply with laws relating to fundamental human rights. The legal basis for defining them is the UN Convention on the Rights of Persons with Disabilities.

The Convention was adopted by the UN General Assembly December 13, 2006, signed by the Polish government on 20 March 2007, and the ratification of the Convention by Poland, which took place after September 6, 2012 (*Convention on the Rights of Persons with Disabilities*, 2006, p.1). It is the first international legal instrument which refers to the complex issues of how disabled people should function in the society and to contribute to the improvement of their situation, by allowing them to reach full and equal enjoyment of all human rights and fundamental freedoms on an equal basis with other citizens.

The shape of respect for people with disabilities in the workplace in our country is affected by the following regulations:

- 1) International (arising from Polish organizations with international scope) - regulations applicable to all countries belonging to the organization. Our country belongs to the UN (United Nations) and ILO (International Labor Organization). The purpose of the UN is, among others, the promotion of human rights in the countries belonging to it. It is this organization which has developed, among

others, Convention on the Rights of Persons with Disabilities. In contrast, the ILO deals with problems of workers and the protection of the rights of workers, improving living and working conditions, job creation and training. To those produced by it we must include the Code of Practice - Managing Disability in the Workplace,

- 2) European - regulations covering EU Member States. Among them we can find the new strategy of the European Community with regard to people with disabilities,
- 3) Polish - legal regulations in force only in our country, which include: Polish Constitution, Labor Law Code and the Law on Vocational and Social Rehabilitation and Employment of Disabled Persons, the Law on Higher Education.

International law offers our country the membership in the United Nations General Assembly. In terms of respect for the dignity of persons with disabilities, citizens of our country are obliged to observe the rules of, inter alia, the Convention on the Rights of Persons with Disabilities. The Convention is the culmination of all previous organizations established by the legislation in the field of disability.

In the preamble to the Convention its creators confirm the fact that in society there is a need to guarantee the full enjoyment of fundamental human rights by persons with disabilities. These persons are entitled to full enjoyment without any acts of discrimination on grounds of disability, because they shall be considered a violation of human dignity and value. The provisions of the Convention recognize that people with disabilities, especially women and girls are often exposed to various forms of discrimination (*Convention on the Rights of Persons with Disabilities*, Preamble paragraph q, 2006, p.1). It also recognizes that disability is the result of interaction between people affected by problems in the sphere of health, and barriers resulting from the attitudes and environment that make it difficult in terms of total social participation of persons with disabilities, on an equal footing with others. What is also important is the diversity of persons with disabilities and their significant contribution to the varied form of society. It should be emphasized that the role is to meet the Convention for stimulating the activity of people with disabilities in key areas of everyday life: civil, political, economic, social and cultural. Convention here refers to the important legal regulations of the Constitution, which say that no one shall be discriminated against in political, social and economic life for any reason (*The Polish Constitution*, article 32, paragraph 2, 1997, p.7). The Convention emphasizes the importance of self-reliance and independence of people with disabilities and the need to create opportunities to engage them in all kinds of decision-making. It is important to offer health care, education and bring jobs to disabled persons.

The aim of the Convention is to promote, protect and ensure the full and equal enjoyment of human rights and fundamental freedoms by all persons with disabilities (*Convention on the Rights of Persons with Disabilities*, article 1, 2006, p.1). The Constitution also emphasizes the equality of all citizens before the law (*The Polish Constitution*, article 32, paragraph 1, 1997, p.7).

A person with a disability is a person with a physically or mentally disturbed character. In combination with various barriers this may hinder the achievements of the disabled people in the society on an equal basis with others. Therefore, employing a variety of in terms of efficiency, i.e. people without disabilities and people with disabilities, be sure to enter the elements of the management concept of mutual acceptance and integration.

Specific actions toward people with disabilities improve their existence, both in society and at the level of a company, as article 3 of the Convention states:

- respect for the dignity and autonomy of persons with disabilities,
- the freedom to make choices,
- non-discrimination,
- active participation in social life,
- respect for diversity and mutual acceptance, because they are all part of humanity and have equal rights and opportunities for the existence and development.

### **3. The provisions contained in the Convention supported by Polish regulations**

The provisions of Convention on the Rights of Persons with Disabilities refer to a wide audience, ranging from the regulation of the government, and ending with the regulations relating to ordinary citizens of the state. In addition to the universal dimension, which means that the law applies to all spheres of life of people with disabilities at the same time, they have records of commitment to people with disabilities from the website:

- 1) state,
- 2) local services,
- 3) employers.

It should be emphasized that the formation of state policy towards disabled people has significantly been affected by conditions in the Polish companies. Therefore, the provisions of the Convention apply in enterprises and it is necessary for the government policy to be directed at promoting its provisions.

### 3.1. Obligations of the State

The Convention, in its regulations has also regulated the duties of states. Member States are obliged to refrain from engaging in activities incompatible with the Convention. The provisions of the Convention do not impose a requirement to take measures to eliminate discrimination on the basis of disability by individuals, organizations and private companies, as well as undertake or promote research and development and to promote the availability and use of new technologies. In addition, states have an obligation to organize, consult and mutually co-operate with persons with disabilities or organizations representing them in the process of creating and implementing legislation and policies to implement the provisions of the Convention (*Convention on the Rights of Persons with Disabilities*, article 1, 2006, p.1). Member States are obliged to take steps to the maximum of available resources in the field of economic, social and cultural rights, the recurrent use of international cooperation in order to achieve their implementation, without prejudice to those obligations which, in accordance with international law, shall have immediate effect.

Poland is obliged to implement the Convention's standards of conduct in order to ensure that persons with disabilities to exercise their rights in the society around them. Its priorities are:

- 1) promotion of the rights of persons with disabilities to dignity and respect,
- 2) the ability to customize the environment of persons with disabilities, to become free of barriers, and the right to obtain information and use of communications services,
- 3) support non-governmental organizations, associations of persons with disabilities through the Voluntary Trust Fund for Persons with Disabilities, in the implementation of the provisions of the Convention. The Fund supports organizations to raise awareness of disability, the exchange of experiences and dissemination of technologies to facilitate the functioning of persons with disabilities,
- 4) inclusion of disability issues relating to the socio-economic development of the state.

Convention on the Rights is an international agreement, which means that after its ratification in all countries that have signed it, it is to call the records specified in its legal effects (Kędziorska, 2007, p. 21).

People with disabilities are equal before the law, together with non-disabled people. They have legal capacity. The state, under regulations contained in the Convention, adopts solutions to support the exercise of legal capacity and protection against fraud (*Convention on the Rights of Persons with Disabilities*, article 12, 2006, p.1).

Convention on the Rights of Persons with Disabilities also guarantees equal political rights with others. It presupposes that participation in political and public life. People with disabilities can use both active and passive voting rights. They also serve all public functions at all levels of management, including through facilitating the use of assistive and new technologies (*Convention on the Rights of Persons with Disabilities*, article 29, 2006, p.1).

At the same time, keep in mind that in relation to people with disabilities, as to the general public basic human rights are related, such as the protection of personal data, the prohibition of unlawful infringement of the honor and reputation of or interference with the private life of a disabled person (*Convention on the Rights of Persons with Disabilities*, article 22, 2006, p.1). persons with disabilities as other citizens have the right to be loved and happy. They have the right to marry, start a family, making decisions about the number and spacing of their children and to acquire information concerning assistance in the upbringing of children. The provisions of the Convention prohibit any acts of discrimination in this sphere.

For the gradual implementation of the provisions of the Convention it is important to cooperate with other countries and international organizations in support of national efforts.

Laws of the Constitution oblige public authorities to provide health care, among others, to persons with disabilities (*The Polish Constitution*, article 68, paragraph 3, 1997, p 15). The good health of a person can be achieved through the process of rehabilitation. Rehabilitation consists in taking certain actions, which mainly aim to enable, to obtain and maintain full physical, intellectual, social and professional care (*Convention on the Rights of Persons with Disabilities*, article 26, 2006, p.1). The Law on Vocational and Social Rehabilitation and Employment of Persons with Disabilities defines the purpose of social and vocational rehabilitation. The aim of social rehabilitation is to enable people with disabilities to participate in social life (*The Act on Vocational and Social Rehabilitation and Employment of Persons with Disabilities*, article 9, paragraph 1, p 3). In contrast, vocational rehabilitation is to facilitate the person with a disability to obtain and maintain suitable employment and career advancement by allowing the use of vocational guidance, vocational training and job placement (*The Act on Vocational and Social Rehabilitation and Employment of Persons with Disabilities*, article 8, paragraph 1, p. 3).

Disabled persons with must have a number of specific needs satisfied. The Convention provides for the financing of these expenditures. Co-financing such expenditure in our country is dealt with by State Fund for Rehabilitation of Persons with Disabilities.



### 3.2. Commitment on the part of local services

The Convention includes a number of provisions in relation to the rights of persons with disabilities who form a significant part of our society. Just as the Constitution, the Convention advocates for equality and the protection of the rights of all people (*The Polish Constitution*, article 32, paragraph 1, 1997, p.7). The provisions of the Convention require the creation of conditions for use of the rights of persons with disabilities on an equal basis with other non-disabled persons and the introduction of solutions specifically targeted to people with disabilities. It prohibits any form of discrimination on grounds of disability (*The Polish Constitution*, article 32, paragraph 2, 1997, p.7). Prohibition of discrimination was also underlined by the Laws: Labor Code, the Act on employment promotion and labor market institutions and the European Council Directive No. 2000/78/EC of 27 November 2000 establishing a general framework for equal treatment in employment and occupation.

Social policy towards people with disabilities creates a set of actions of public bodies and non-governmental organizations, aimed at balancing unjustified differences in social functioning and to create opportunities for people with disabilities in all areas of economic and social life, to enable their full integration into society (Kurzynowski, 1996, p. 44).

Family plays an important role in the life of a young person with a disability. It is the family that determines the life chances of disabled people, their educational, professional and sociable activity. However, the family often cannot cope with the problems of disability and institutional support is insufficient. As a result, some of the young disabled people have low self-esteem and sense of isolation. In adulthood this often results in a reluctance to change their fate, lack of social or professional activity (Raszeja-Ossowska, 2012, p.6). In accordance with the provisions of the Convention, persons with disabilities should have access to support services in the community, and to be widely available to prevent social isolation.

The Convention indicates the need to combat stereotypes, prejudices and harmful actions in relation to persons with disabilities. It is a common civic duty to combat the symptoms of different ways to dislike. You can contribute to this in different ways depending on the capabilities of the data groups. The reluctance can be overcome by advertising campaigns in the media and training in enterprises. The provisions of the Convention refer to the need to ensure access to the physical environment, to transportation, to information and communications.

People with disabilities have the right to keep living independently in the community, with choices equal with others. They can participate fully in the

life of society around them with the right to full integration. The new strategy of active social inclusion of people with disabilities has become necessary to change the conditions of socio-economic development and as a result of fundamental changes in institutional governance, which are associated with widespread adoption of the doctrine of equal treatment as the basis of disability policy and recognizing the rights of people with disabilities as an integral part of human rights. The first set of factors causes that people with disabilities must begin to be treated as human resource, as economic agents whose inclusion in market relations becomes necessary due to the ability of a society to cope with the contemporary development challenges. This second factor is the need to reform the regulatory and institutional system, so that they can cope with the implementation of policies and social integration of people with disabilities (Gačlarz, 2014, p. 8).

People with disabilities in everyday life seek to maximize independence. They try to do most of the tasks themselves, even if they are sometimes difficult for them. Often, however, they need different types of facilities in different areas, specific to their disability. The provisions of the Convention state that a possible way to take measures to enable them to personal mobility with the greatest possible independence is by facilitating their access to high quality assistance to support movement, devices, assistive technologies and forms of live assistance and intermediaries from other people and even animals.

The provisions of the Convention shall guarantee to persons with disabilities access to all activities in the field of culture, development and use of their creative, artistic and intellectual skills. Nowadays, there are many events organized to promote the culture of persons with disabilities: Krakow Integration Days organized since 2007 by the Office for Persons with Disabilities Cracow universities, or the Festival of Poetry Migan popularizing the culture of deaf people.

### **3.3. Commitment on the part of employers**

The UN Convention on the Rights of Persons with Disabilities is an excellent source of information for employers who want to adapt the workplace to the needs of the disabled persons. The company employees - people with disabilities, and supervisors are not always able to adequately manage the staff. This is due to ignorance of the regulations regarding persons with disabilities and their needs and directing the stereotypes prevalent in society. It is therefore important that supervisors have an appropriate knowledge in this field.

Provisions of the Constitution require public authorities to pursue a policy aimed at full, productive employment by implementing programs to combat

unemployment, including organizing and supporting guidance and training (*The Polish Constitution*, article 65, paragraph 5, p 14). People with disabilities have the right to choose work and to receive adequate remuneration from it in an open, inclusive and accessible work environment, along with the adaptation of the workplace to their individual needs.

In accordance with European regulations contained in the *Code of good practice in the employment of people with disabilities* in the European institutions responsible for ensuring the necessary improvements in the workplace. It covers all areas of employment: recruitment, selection and appointment, career development, training, career development, interpersonal relations (*Employing disabled*, 2014, p.23). Information on the employment of people with disabilities and the responsibilities and powers of the establishments in this field is also provided by the Law on Vocational and Social Rehabilitation and Employment of Persons with Disabilities.

Many of the obstacles people with disabilities face when looking for work and in the workplace results in a great degree from social barriers rather than their actual inability to work (Kantyka, 2010, p. 41). The main barriers associated with the opening of the employers on a variety of workers are ignorance and fear of the unknown (*Absent in the labor market*, 2013, p.1). Employment of people with disabilities from the perspective of employers brings a number of problems and hence the cost. Problems related to employment may arise from relationships between employees with disabilities and the rest of the workforce. Employers do not recognize that people with disabilities are equally valuable employees, doors open to new perspectives and horizons expanders as other employees. Another problem is the phenomenon of discrimination. Discrimination on grounds of disability, according to research is one of the most common in our country, the situation of unequal treatment (37% of respondents in the survey “Discrimination in the European Union in 2012” Eurobarometer). The criterion of disability is according to 29% of Polish respondents the main reason for the rejection of a candidate or candidates to work (*Discrimination in the European Union - the results of 2012*, p.1).

Convention advocates the adaptation of buildings and workplaces for people with disabilities, which will significantly facilitate the existence of people with disabilities in the workplace. Therefore, it becomes important to verify the current forms of amenities and facilities for helping people with disabilities on the market. Thus, if the company employs people with disabilities, it is necessary to supply the place of work with facilities for them and with modern technologies. (Hasse, 2011, pp. 194-202). They will serve them to improve their work, and thus their work will become effective and remain profitable company.

In light of the existing provisions in Polish enterprises, where people with disabilities are working their non-discrimination on grounds of disability. Law Labor Code prohibits discrimination, inter alia, on the grounds of disability, and also because of the employment, fixed-term or indefinite full-time or part-time work (*Law Labor Code*, article 11, 1974, p.4).

The employer according to regulations contained in the Convention should refrain from ill-treatment and punishment of employees. The Convention also prohibits employers issuing any opinion on the parenting of people with disabilities, even if they were contrary to their views on the subject.

People with disabilities are often subjected to acts of psychological violence. The employer should provide assistance in the form of the creation of working conditions while ensuring a good atmosphere in the workplace. On the field, the company can apply the broad integration of employees with disabilities with other employees, to prevent their isolation within the company. The activity of disability superiors can be stimulated through various techniques of motivation. The best technique is the ability to present and implement the ideas of employees, motivating them to do, to be reported and rewarding them for it. In this way, employees will gain self-esteem, which usually positively stimulates their efficiency. Implementation of new ideas can become crucial for the successive actions of the company on the market and gaining new customers, and thus achieving a competitive advantage over rival firms in the same industry. Companies should also have knowledge of the various forms of social communication (*The Polish Constitution*, article 69, 1997, p 15), as it is significantly easier for people with disabilities to communicate freely, and thus to increase the effectiveness of their work in the company. This fact should be well-known to both managers in a company employing workers with disabilities, as well as to managers of companies whose services can benefit people with disabilities. By providing enterprise services they should take into account the fact they not only provide consumers efficiently, but these customers are disabled. The company has a chance to not only gain new customers, but to be a company providing services to all. This, in turn, publicized by the media, could build respect in the eyes of existing customers and increase their loyalty to the brand. The company may also encourage other private entities providing services to the general public, to adjust to the needs of people with disabilities.

The Convention provides people with disabilities with the right to education to improve their communication with one another and with the public. Communication with people with disabilities on the basis of the company is very important due to the fact that it significantly facilitates the work efficiency in the enterprise. Therefore, to simplify it, it becomes essential to send or organize training courses. The need for education can

also be applied to learning something new arising from the need to perform the job. Educational institutions of persons with disabilities should implement a mechanism for training of staff at all levels of education and a training system to create a trigger that allows the integration of workers with disabilities at all levels of education.

If the disabled person has an established right to a pension, there is the possibility of employment on the basis of flexible forms of employment in the selection of an employment contract or a civil contract (Kantyka, 2010, p. 81-83). However, if the person does not have a right to a pension they should be employed under a contract of employment, because only then they have the right to health insurance. Insurance, as we know, helps people with disabilities to strive for a satisfactory state of health through access to free health care. People with disabilities have the established right to a pension, which ultimately reduces the cost of their employment. Work and pension create a source of financial and social security in the event of inability to work due to chronic illness (*The Polish Constitution*, article 67, paragraph. 1, p.15).

#### **4. Enforcement of regulations**

All countries of the UN are to undergo continuous control of implemented provisions of the Convention at the national level. In Poland, keeping control of all disability provisions is dealt with Government Spokesperson for Persons with Disabilities. This is done through an independent mechanism for monitoring the implementation of the Convention. Its mission is to promote, protect and monitor implementation of the Convention. The process of promoting the provisions of the Convention in our country is insufficient, because a few of people with disabilities know the rules, let alone other citizens in the entrepreneur. These people are the most educated people, and as we know in our country in 2013, only 7.7% of disabled people had higher education (*Education of Persons with Disabilities*, 2013, p.1). The source from which they most often learn about the Convention is the special media, which is only at the stage of development.

At international level, countries that have introduced the principles of the Convention are obliged to submit the first report on the implementation of the Convention within two years, and then prepare it every four years. These reports are reviewed by the Committee on the Rights of Persons with Disabilities, composed of independent experts.

All matters relevant to the implementation of the Convention and proposals to amend the Convention are dealt with at the conference of the

Member States, organized at least every two years (*Convention on the Rights of Persons with Disabilities*, article 22, 2006, p.1).

## 5. Conclusion

Convention on the Rights of Persons with Disabilities is a valuable source of information for the states to the local environment, as well as businesses that employ people with disabilities around the world. It obliges all people to respect the rights of others, treatment of employees with disabilities on an equal footing with non-disabled, to adapt the workplace to the needs of employees with disabilities against discrimination in the workplace and the integration of employees. It should be stressed that the diversity of employees translates into their diverse experience, which may benefit and affect the actions of the company. In this way, businesses have the opportunity to create an integrated team of efficient employees with the prospect of success.

The aim of this study was to prepare the Polish entrepreneurs (in terms of awareness and knowledge) to implement the provisions of Convention on the Rights of Persons with Disabilities. An important role for the development of knowledge of the provisions of the Convention shall be played by the state since the regulatory framework affect the validity of the provisions in enterprises.

Taking into account all aspects of the situation of young people with inefficiencies, it should be noted that comprehensive support is required in this group - starting with the treatment and rehabilitation, by facilitating and adaptation in education, psychological support, to the support of the development of educational and professional paths.

Poland needs significant reforms in the area of the existing legislation on disability. The government began by reducing working time of persons with disabilities to seven hours a day. It should be noted, however, that this provision was not consulted with the disabled, so you cannot assume that it will be a good solution. The entry rule is delayed and put on after a long time of waiting for passing it. Slowness of the government in matters of amendments to the provisions relating to persons with disabilities harms their interests both in society and the place of employment.

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**IV.**  
**FINANCIAL ASPECTS OF**  
**ORGANIZATIONAL**  
**MANAGEMENT**



# THE APPLICATION OF THE EVENT STUDY TO THE ANALYSIS OF THE PUBLIC INFORMATION IMPACT ON THE CORPORATE BOND PRICES

**Anna Rybka<sup>1</sup>**

## **Abstract**

*This paper reflects on the characteristics of the event study analysis as a method for investigating the impact of the public information on the corporate bonds prices. There are certain aspects of the event study methodology presented and the application of the method to research on the corporate debt market is shown. The empirical part of the paper analyses the reaction of the financial instruments traded on the Catalyst market on the several events that concern the financial condition of the issuer.*

**Keywords:** *corporate bonds, informational efficiency, event study, Catalyst market.*

## **1. Introduction**

Every day a lot of information is supplied to the financial markets worldwide. The information concerns financial condition of the issuers, their macroeconomic environments and geopolitical events. The information is provided to market participants by different channels and can have smaller or bigger impact on the prices of the financial instruments that are traded on both regulated and OTC market. Hence, in the recent years, researchers have paid notable attention to the strength and direction of the impact of the public information on the financial instruments prices, important from issuers and investors' perspective.

Scientific research on the Polish capital market that aimed to quantify the impact of various information and events on the market prices was focused mainly on the equity market. Among the literature concerning this subject there can be found: Jajuga (2000), Czekaj (2001), Frąckowiak (2001), Gruszczyński (2002), Gurgul and Majdosz (2005) and Gurgul (2006). Much poorer is domestic literature focused on the corporate bond market and its reaction to the public information. That fact is not surprising taking into account that no sooner than in the 2009 Warsaw Stock Exchange established

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the Catalyst market – the trading platform dedicated for debt financial instruments. Before the Catalyst was set up, the regulated market had been dominated by the government bonds, while corporate bonds had accounted for a small percentage of the total amount of the bonds traded on the Warsaw Stock Exchange.

One of the most popular scientific methods used for identifying the impact of the information on the market prices is the event study analysis. The aim of this article is to present the application of the event study for investigating the reaction of corporate bonds prices on the public information appearing on the market and to verify the impact of the certain events on the prices of financial instruments traded on the Catalyst market.

The first part of this article starts with the efficient market theory and presents the methodology of the event study analysis. The second part, based on the review of the foreign literature, indicates the areas of event study applications to the research on corporate debt market. The last part focuses on the empirical verification of the impact of certain events on the prices of corporate bonds traded on the Polish debt market.

## **2. Informational efficiency of the financial markets**

While discussing the significance of the information on the capital markets and its influence on the prices of financial instruments it is worth to start with the rational expectation hypothesis. That concept was presented for the first time in 1961 in the article „Rational expectations and the theory of price movements” (Muth, 1961). J. F. Muth, having investigated the possibilities of market prices forecasting, concluded that market participants formulate their expectations based on all available information. Then, they make investment decisions that are reflected in the changes in prices of financial instrument. That dependency results in the fact that all significant (from the forecasting’s perspective) information appearing on the market is immediately incorporated into the prices.

The assumption that expectations are formulated in the rational way found its application in one of the hypotheses that tries to explain the process of market prices’ behaviour – the efficient market hypothesis (Ziarko-Siwiek, 2005). In the literature the notion of the financial market efficiency is not unambiguous. There can be found at least three different meanings. These are (Czekaj, 2001):

- funding efficiency
- transactional efficiency
- informational efficiency.

Funding efficiency occurs when the market ensures inflow of the capital to those companies that are able to invest it in the most profitable way. It means that only the best investment projects are run in the market's economy scale. The market is transactionally efficient when its mechanism allows to buy and sell instruments immediately and without any constraints. Moreover, the competition of the financial intermediaries leads to the low transactional costs. However, from this article subject's perspective, the key concept of the market efficiency is the third one – the informational efficiency.

It is considered that the research on the information efficiency began with the publication of the article of E. F. Fama in 1970 „Efficient Capital Market: A Review of Theory and Empirical Work” (Fama, 1970). E. F. Fama defined a market as efficient if and only if prices of financial instruments always fully reflect all available information. Apart from that, according to E. F. Fama, prices of financial instruments are affected not only by the historical information but also by the events that are expected to happen in the future based on the current market status.

Since „Efficient Capital Market...” was published, a lot of articles concerning informational efficiency of the financial markets have been published worldwide. There can be also found in the literature many definitions of the informationally efficient market. Most of these refer to the definition proposed by E. F. Fama. What is worth mentioning and concluding of all other definitions that can be found in the foreign and domestic literature is the one given by J. Czekaj: „ (...) *the market is informationally efficient if it ensures quick transfer of the information to all of market participants so the information is fully and immediately reflected in the prices of financial instruments. Hence, market prices always fully reflect the real value of the instruments*” (Czekaj, 2001).

With respect to the definitions given above, the empirical verification of the efficient market hypothesis should imply the need of answering three following questions:

- 1) How quickly is new information provided to the market participants ?
- 2) Do prices of the financial instruments incorporate all information that appear on the market ?
- 3) How quick is the reaction of the market prices to the new information ?

It must be emphasized that the concept of the information is wide and not unambiguous. Changes in market prices, official company's announcement, press release or news provided by the information agencies – these all can convey a content important from issuers or investor's perspective. Moreover, significant information might concern not only the company itself but also its macroeconomic environment.

E. F. Fama (1970) classified informational efficiency subjected to the type of the information that is reflected in market prices. He pointed out:

- weak efficiency
- semi – strong efficiency
- strong efficiency.

The market is weakly efficient if prices incorporate information that concerns historical trades. Semi – strong effectiveness means that apart from the historical information prices of the instruments reflect all public information available on the market (e.g. information that concerns financial condition of a company). Finally, the strong efficiency assumes that prices reflect not only public information but also the confidential one.

Each of these three hypotheses owns specific tools of its verification. Presentation of all of these methods exceeds the scope of this article, however, taking into account the aim of this paper, tools for semi – strong hypothesis verification are crucial. These allow to investigate whether and how quick the market prices react to the public information coming to the market from the companies directly and from their further surrounding. Moreover, these methods allow the researchers to quantify the strength and the direction of the information impact.

The literature presents several methods of testing the semi – strong effectiveness. Among these, the event study methodology can be found. An event study can be used to check the significance of the reaction of market prices to the certain events. The only requirement is to specify exact dates of the events (dates of the public announcements) and to gather long enough time series of the financial instruments prices.

Each research that uses event study methodology consists of four basic steps (Gurgul, 2006):

- 1) identification of the event and the research sample
- 2) specification of the time frameworks
- 3) setting the relation between the returns from the financial instrument and the market portfolio
- 4) estimation of the event effect based on the research sample.

The first step aims to identify a significant, from market participants' perspective, information that concerns certain actions that have already been undertaken or planned by the company. No less important is identification of a date when the information was announced to the public. What needs to be emphasized, these actions can concern the company directly or other market participants (e.g. competitors or the government). According to the event study methodology, not all information can be the subject of the research. Fulfilment of the specific conditions is crucial. These are given by D. Tabak and F. Dunbar (1999):

- 1) the information must be unambiguous and precise
- 2) it is possible to specify the exact moment when the information was announced to the public audience
- 3) market participants cannot anticipate the information before it has been announced
- 4) at the moment of its announcement the information cannot be disturbed by any other news that can impact significantly the prices of financial instruments.

The crucial step in the event study analysis is specification of its time frameworks. There are two notions that concern this step: an event window and an estimation window. An event window is defined as a time period in which the response of the market prices to the information announcements is tested. In line with the efficient market hypothesis prices of financial instruments should react to the news immediately and without a delay. That would suggest choosing rather short event windows. In the practice, however, taking into account market deficiencies and possible delays in the prices reactions, lengths of event windows are very different. These are set from a few minutes (on the most liquid markets) up to the few months after the information has been announced.

It is often emphasized by the researchers that the choice of the event window's length is significant. Too long time periods involve a risk that results of the analysis are influenced by the disturbing events. On the other hand, too short an event window might not fully cover reactions of the prices. H. Gurgul (2006) gives a guideline on how the event window should be set: „(...) *it should be long enough to allow the effect of the event to be reflected entirely in the market prices*”.

Not less important than an event window is an estimation window. This is a time period based on that the parameters to the respective models are estimated. These models are used further to generate the expected returns of the financial instruments in the event window. An estimation window is usually followed by the event window and its length is between a few weeks and a few months. What is important, the estimation window must not intersect with the period in which an impact of the event on the market prices is expected.

The third step of the event study analysis is setting the relation between the returns from the financial instrument and the market portfolio. By using parameters obtained from the analysis of the estimation window it is possible to specify the expected returns that would be observed in the event window if the event had not occurred. In order to specify the impact of the given event, the difference between real and theoretical returns in the event window is tested. Verification of the statistical significance of this difference is the fourth and the last step of the event study analysis.

### **3. Application of the event study analysis to the research on the corporate bond markets**

The foreign literature that concerns the event study analysis and its application to the research on the corporate bond markets is very rich (specific literature references are provided in the further parts of this paper). There can be found articles that present results of the research done for well developed and liquid markets and for the emerging markets. Moreover, the catalogue of the events and information that lie in the scope of the researchers' interest is very broad. H. Gurgul (2006), having emphasized the wide application of the event study analysis, notices that one of the reasons for the popularity of this method is the fact that it requires only long enough time series of the prices and these are available for the researchers without any constraints. H. Gurgul also mentions that application of the event study does not require access to the periodical financial reports published by the company. That decreases the costs of the research. Moreover, results are independent of the other external factors e.g. accounting systems used by the issuers.

We can identify two types of the events which impact on the market prices was investigated by the foreign researchers:

- events that concern the internal situation of the issuer
- macroeconomic events that concern the entire market.

With respect to the first type of events, there can be found a lot of papers investigating the impact of the earnings announcements on the corporate bonds market prices. Most of the research that were reviewed by the author confirm the statistical significance of the changes in the corporate bond prices as a response to the announcement of the company's profit gained within particular period. T. Roxen and X. Zhou (2009) indicate that corporate bonds prices fully anticipate the information about the issuer's earnings within half an hour after it has been announced. M. L. DeFond and J. Zhang (2011), having investigated the differences between the impact of the information about earnings below and above the forecast, concluded that within one day after the announcement date there can be observed a significant prices reaction to the profits lower that were expected.

Among events in the scope of the researchers' interest there are also new debt issues. However, in this case the results are not unambiguous in terms of direction of the information impact. R. Kolodny and D. R. Suhler (1988) indicate the significant and positive reaction of the corporate bond prices while A. Akhigbe, J. C. Easterwood and R. Pettit (1997) confirm the statistical significance of decreases in the instruments prices – both results obtained for one day perspective after the announcement date.



There is also lack of the clear conclusion on the impact of the new equity offerings. A. Kalay and A. Shimrat (1987) investigated the reaction of bond prices within time period starting two days before and ending one day after the announcement date and they observed the significant decrease in the corporate bonds prices. Similar results were presented by W. B. Elliot, A. K. Prevost and R. P. Rao (2002), who investigated the reaction of the short term bonds. For the long term instruments the reaction was significantly positive however.

A significant number of papers concern the impact of the dividend payout announcements and share repurchases. Research results on both events are not unambiguous. Usually, researchers tend to analyse separately the impact of the increase and decrease of the dividend rate. J. R. Woolridge (1983) and G. Handjinicolaou and A. Kalay (1984) indicate the significant decrease in the corporate bond prices just a few days after the information about the decrease in the dividend ratio has been announced. The opposite reaction was observed by U. Dhillon and H. Johnson (1994) – they both proved the statistical significance of the increase in the bond market prices after announcement of positive change in the dividend rate.

The results of the research on the share repurchases are more consistent. There can be mentioned papers by L. Y. Danna (1981) and W. F. Macwell and C. P. Stephens (2003). They observed the significant decrease in the bonds prices on the same day when the repurchase program was announced.

Mergers and acquisitions are another events that were investigated by researchers in terms of the impact on the bond prices. Similarly to the previous examples, there is a lack of the common conclusion on how corporate bond prices react to these announcements. C. E. Eger (1983) notices that there exist positive abnormal returns from the acquirer's bonds within one month after the announcement. On the other hand, M. T. Billet, T. H. D. King and D. C. Mauer (2004) show statistically significant decreases in the bond returns that can be observed even before the acquisitions has been announced to the public. The lack of the significant impact was proved by P. Asquith and E. Kim (1982) and M. Walker (1994). They analysed the reaction of the acquirer's bond prices one month before and after the announcement respectively.

Apart from the events that refer to the internal situation of the issuer there are many articles that concern the impact of the macroeconomic factors on the bond market prices. Worth mentioning is the paper by C. Ying (2006) who investigated the reaction of the corporate bond prices to the announcements of changes in twenty one different macroeconomic metrics. C. Ying analysed the reactions of the corporate bond prices within 50 minutes after the announcements and he concluded with the significant reaction of the thirteen metrics, e.g. consumer price index, change in nonfarm payrolls and trade balance.

Examples that have been given so far do not obviously cover the whole catalogue of the events that can be investigated in terms of their impact on the market prices. Also, it needs to be emphasized that all results that were mentioned with respect to the research done on US market can also be a subject of the research on the Polish corporate bond market. The key point here is, however, the access to the databases of the information announcements and the ability to precise specification of the announcement date.

According to the Polish law, the issuers of the financial instruments traded on the organized market are obliged to publish all information that concerns financial condition of the company and events that can influence the investment risk. The complete catalogue of the current and periodical reports is included in the Regulation of the Minister of Finance of 19th February 2009 establishing the responsibilities of the issuers in terms of the current and periodical reports and conditions under which reports published in line with the law of non – EU members are acknowledged as equivalent. Additionally, information that is given to the investors must be authentic, reliable and completed. Moreover, current and periodical reports must be prepared in the way that allows to assess the impact of the information on the economic and financial condition of the issuer.

For the companies whose bonds are traded on the organized market the scope, form, place and the frequency of the public announcements are specified by the regulations of this organized market. Issuers of the instruments traded on the Catalyst market are obliged to publish information in form of the current and periodical reports. According to the Catalyst Market Rules *“The issuer is obliged to publish current reports in case of any circumstances or events that can have a significant impact on its financial or economic condition, mainly on the ability to meet obligations that result from the debt financial instruments that were authorized by the Catalyst”*. Additionally, *“the current report must be published immediately, no later than 24 hours after the circumstances occurred or the issuer found out about it”*. With respect to the periodical reports, Catalyst Market Rules state that *“the issuer is obliged to publish periodical reports annually”*.

In practice, the issuers of the corporate bonds traded on Catalyst market fulfil their informational obligations using Stock Exchange Announcement System: ESPI and EBI (for regulated and alternative markets respectively).

#### **4. The examples of event study application to the research on the corporate bonds prices reaction on Catalyst market**

To verify the possible areas of event study application to research on Polish debt market, the impact of certain events that concern financial condition of

companies on the bonds market prices was measured. Events and research sample were identified using announcements published by the issuers in the EBI system. The following events were identified: violation of the public announcement obligations by the issuer, violation of the financial metrics maintenance agreed in the issuance letter, delays in the coupon payments or bond repurchase, bank accounts execution and voluntary submission to the execution process. The events are various but all of them can imply the deterioration of the company's financial conditions or problems with paying off a debt. Moreover, they have negative reputational impact. Similar research (based on the global sample) was done by B. Imbierowicz and M. Wahrenburg (2013). Instead of analyzing particular announcements separately, they classified all information into several groups and verified the total effect of the each group on the bonds prices<sup>2</sup>.

The research sample consisted of the announcements published between 1 January 2001 and 30 April 2014. The sampling process started with the identification of all of the announcements informing about negative events listed in the previous paragraph (violation of the public announcement obligations by the issuer, delays in the coupon payments or bond repurchase etc.). There were 62 announcements identified that were published by 28 companies. Because of the fact that several companies had issued more than one bond series traded on the market, the final sample consisted of 71 events. There were few events that had to be excluded from the sample. Among these there were announcements that were exposed to the influence of other disturbing events (it means that several significant reports were published by the issuer on the same or relatively close days.). Moreover, some announcements related to the illiquid instruments were excluded. The reason was that due to the lack of the liquidity the result of statistical tests would be unreliable. In the end, events concerning convertible bonds were excluded. Because of some additional rights incorporated into these instruments, convertible bonds could potentially disturb the research results.

The final sample consisted of 46 events and was identified based on the 28 announcements published by the 18 companies. (majority of these companies had issued more than one bond series). All events included in the final sample are presented in Table 1.

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<sup>2</sup> Announcements were grouped based on the events' classification that is used for the rating grading provided by the Moody's agency.

**Table 1.** Companies and events included into the final research sample

Companies	Events	Announcement Day
Admiral Boats S.A.	Violation of the public announcement obligations by the issuer	22/06/2012 (18:27) 18/10/2012 (20:11) 22/04/2014 (20:49)
Budostal – 5 S.A.	Delays in the bond repurchase	30/12/2011 (20:02)
Digate S.A.	Violation of the public announcement obligations by the issuer	04/04/2013 (13:25)
c – Kancelaria Grupa Prawno – Finansowa S.A.	Violation of the public announcement obligations by the issuer	02/08/2012 (15:38) 08/08/2012 (20:57)
East Pictures S.A.	Violation of the public announcement obligations by the issuer	25/06/2012 (23:05)
East Pictures S.A.	Delays in the coupon payments	02/07/2013 (17:41) 30/09/2013 (10:39)
Instalexport S.A.	Delays in the coupon payments	22/04/2014 (14:34)
Jedyńka S.A.	Delays in the coupon payments	05/04/2013 (15:50)
Marka S.A.	Violation of the financial metrics maintenance agreed in the issuance letter	12/06/2013 (10:32) 14/08/2013 (8:38) 14/11/2013 (9:03)
Milmex Systemy Komputerowe Sp. z .o.o.	Delays in the coupon payments	31/05/2013 (13:11)
Milmex Systemy Komputerowe Sp. z .o.o.	Delays in the bond repurchase	30/08/2013 (9:49)
Orzeł S.A.	Delays in the coupon payments	20/11/2013 (23:27)
Orzeł S.A.	Bank accounts execution	08/04/2014 (21:43)
Przedsiębiorstwo Produkcyjno – Usługowo – Handlowe VIG Sp. z o.o.	Delays in the coupon payments	31/01/2014 (09:13)
Religa Development S.A.	Violation of the public announcement obligations by the issuer	08/06/2012 (13:30)
Rodan Systems S.A.	Violation of the public announcement obligations by the issuer	01/02/2013 (15:49)
TimberOne S.A.	Delays in the coupon payments	09/01/2013 (15:30)
Trust S.A.	Delays in the coupon payments	05/12/2012 (13:12) 03/06/2013 (16:20)
Uboat Line S.A.	Violation of the public announcement obligations by the issuer	10/07/2013 (10:47)
Voxel S.A.	Voluntary submission to the execution process	24/09/2012 (15:12)
Widok Energia S.A.	Violation of the public announcement obligations by the issuer	18/06/2012 (22:21)

Source: Based on the EBI Stock Exchange Announcement System. Retrieved from: [www.gpwcatalyst.pl](http://www.gpwcatalyst.pl).

In the next stage of the analysis there was a time framework specified. The event window covered 26 days, in the symbolical notation [-5,+20]. That means that the prices were observed starting from the five days before the information had been published up to the twenty days after the announcement. There were two reasons for such a length of the event window. Firstly, because of the specificity of the considered announcements, it could be expected that some investors might have anticipated information before it was published.

Secondly, due to the lack of the detailed research on the informational efficiency of Polish corporate bond market and hence the lack of the references in the research results, there was a risk that short event window would have resulted in the omission of the statistically significant prices reactions.

The estimation window was set for 40 days ([-45, -6]). Such a time horizon was in line with typical lengths used in the literature. As an event day we specified the day when the information was announced to the public. It was also assumed that in case the report was published after 5 p.m., the event actually happened on the next business day.

Daily bond returns, according to the methodology presented in the reference literature (Bessembinder et al., 2008), were calculated as follows:

$$BR_{i,t} = \frac{(P_{i,t} - P_{i,t-1}) + (AI_{i,t} - AI_{i,t-1})}{P_{i,t-1} + AI_{i,t-1}}, \quad (1)$$

where  $P_{i,t}$  means a clear price of the  $i$ -th bond on the day  $t$  and  $AI_{i,t}$  represents the coupon interest accrued on the day  $t$ .

To calculate the abnormal bond returns the formula proposed by G. Handjinicolaou and A. Kalay (1984)<sup>3</sup> was used. The basic assumption here is that there exists a constant premium that can be gained by the investment in the corporate bonds above the return from the government bonds with the same time to maturity. The premium calculated for the  $i$ -th bond on day  $t$  can be calculated by the formula below:

$$PBR_{i,t} = BR_{i,t} - TR_{i,t}, \quad (2)$$

Where  $TR_{i,t}$  means the return from the government bond with the maturity date the same as the  $i$ -th corporate bond.

It must be emphasized that to apply the formula (2), it was required to identify, for each corporate bond included in the research sample, a respective government bond with the same (in practise similar) time to maturity. This step was feasible thanks to the sufficient liquidity of the government debt instruments traded on the Catalyst and a variety of these instruments with respect to the maturity dates. Eventually, there were used daily returns of zero coupon bonds calculated based on the data gathered from the archive available on the Catalyst market website.

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<sup>3</sup> The original name of the model is „*Mean - Adjusted Model*”.

The next step of the analysis was a calculation of the average premium in the estimation window for each bond using formula (3)

$$EBR_i = \left( \sum_{t=t_0}^{t_0+T-1} PBR_t \right) \frac{1}{T}, \quad (3)$$

where  $t_0$  means the oldest observation in the estimation window and  $T$  is the length of the estimation window.

Abnormal bond returns ( $ABR_{i,t}$ ) in the event windows were calculated with the formula (4).

$$ABR_{i,t} = PBR_{i,t} - EBR_i \quad (4)$$

To check the impact of the events in scope on the corporate bond prices, there were two statistical tests used: t-student test and non-parametric sign test.

To verify the announcements effects by the t-student test there was an estimator used proposed by the H. Gurgul (2006). Using formula (5) there were abnormal bond returns calculated for each day  $t$  in the event day.

$$\overline{ABR}_t = \frac{\sum_{i=1}^N ABR_{i,t}}{N}, \quad (5)$$

where  $N$  means the number of events included in the final sample ( $N=46$ ). To calculate the standard deviation of the abnormal bond returns, formula (6) was used.

$$\widehat{\sigma_{\overline{ABR}_t}} = \sqrt{\frac{1}{T-1} \sum_{t=t_0}^{t_0+T-1} (\overline{ABR}_t - \overline{\overline{ABR}})^2}, \quad (6)$$

where  $\overline{\overline{ABR}}_t$  was calculated in line with the formula (7).

$$\overline{\overline{ABR}}_t = \frac{1}{T} \sum_{t=t_0}^{t_0+T-1} \overline{ABR}_t \quad (7)$$

The test statistics, described by the ratio of (5) and (6), is a variable of a Student's t - distribution with the N-1 degrees of freedom. What is verified by the test (in a sense of falsification), is a null hypothesis claiming that the average abnormal bond return on the day t in the event window differs insignificantly from zero ( $H_0: \overline{ABR}_t = 0$ )

To verify the results obtained from the t- test there was a non-parametric sign test applied. The null hypothesis that was tested was  $H_0: p \geq 0,5$ , where p means the probability of the negative abnormal bond returns occurrence. The alternative hypothesis was  $H_0: p < 0,5$  (Campbell, Lo, MacKinlay, 1997). The test statistics for the day t in the event window is expressed by the formula (8):

$$\theta_t = \left[ \frac{N^+}{N} - 0.5 \right] \frac{\sqrt{N}}{0.5}, \quad (8)$$

where  $N^+$  is the number of the observations for which the abnormal bond returns on day t were positive. Estimator (8) is standard normally distributed.

Both tests results are presented in Table 2. It shows statistics for the particular days within the event window and respective p-values for each day (the lowest significance levels for which the null hypothesis stating no meaningful price reaction can be rejected).

It can be spotted that for the days prior the announcement day the p-values are very high. Hence, for any reasonable significance level<sup>4</sup> the null hypothesis cannot be rejected. This conclusion is common for both tests used in the research. Any value of the estimator calculated for the period  $[t_0 - 5, t_0 - 1]$  is statistically insignificant. However, depends on the type of the test, the results are different for the period following the announcement day.

Sign test, for the significance levels higher than 0,071, indicates the meaningful decrease in the corporate bond prices on the announcement day. These results are not confirmed by the t-test. The t- test statistics and respective p-value calculated for  $t_0$  would allow to reject the null hypothesis only for the high significance level  $\alpha = 0.827$ .

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4 The most frequently used in significance levels are  $\alpha = 0.05$  or  $\alpha = 0.1$  (Campbell, Lo, MacKinlay, 1997)

The results of parametric and non-parametric tests are more consistent for the period that follows the announcement day. T-test, for the significance level  $\alpha = 0.134$ , indicates the meaningful reaction of the prices on the sixth day after the information has been published. On the other hand, the sign test, for  $\alpha = 0.119$ , confirms existence of the statistically meaningful decreases in the bond prices on the fourth day. However, statistical powers of the test, defined as  $1-\alpha$ , are not big.

**Table 2.** Statistical tests results in the event window

Date	Estimator t	p-value	Estimator	p-value
$t_0 - 5$	-0.168	0.867	0.295	0.615
$t_0 - 4$	-0.014	0.989	0	0.5
$t_0 - 3$	-0.140	0.889	0.589	0.722
$t_0 - 2$	-0.201	0.841	-1.179	0.119
$t_0 - 1$	-0.172	0.864	-0.294	0.385
$t_0$	-0.220	0.827	<b>-1.474*</b>	<b>0.071</b>
$t_0 + 1$	-0.176	0.861	1.474	0.929
$t_0 + 2$	-0.186	0.853	-0.589	0.278
$t_0 + 3$	-0.143	0.887	0.589	0.722
$t_0 + 4$	-0.348	0.729	<b>-1.179*</b>	<b>0.119</b>
$t_0 + 5$	-0.873	0.387	0.589	0.722
$t_0 + 6$	<b>-1.527*</b>	<b>0.134</b>	0	0.5
$t_0 + 7$	-0.136	0.892	0.589	0.722
$t_0 + 8$	-0.180	0.858	-0.589	0.278
$t_0 + 9$	-0.139	0.890	0.294	0.615
$t_0 + 10$	-0.202	0.841	-0.589	0.278
$t_0 + 11$	-0.224	0.824	0.149	0.557
$t_0 + 12$	-0.147	0.884	0.149	0.557
$t_0 + 13$	-0.191	0.849	-0.745	0.228
$t_0 + 14$	0.544	0.589	0.745	0.772
$t_0 + 15$	-0.171	0.865	0.302	0.618
$t_0 + 16$	-0.260	0.796	-0.904	0.184
$t_0 + 17$	-0.211	0.834	0.302	0.618
$t_0 + 18$	-0.178	0.859	0.603	0.726
$t_0 + 19$	-0.748	0.458	0	0.5
$t_0 + 20$	-0.159	0.874	0.603	0.726

Source: Author's calculations performed in the R statistical application.

Both tests, for the significance levels set relatively high, prove that there are days when the corporate bond market reacts significantly to the information that concerns the deterioration of the company's financial condition or imply such a deterioration is probable to happen in a future. Tests results are not unambiguous however. The differences can result from the methodological



background. H. Gurgul (2006) emphasizes that  $t$  – statistics requires the assumption that average abnormal bond returns are independently normally distributed. In the case of the strong autocorrelation, the value of the  $t$  – statistics can be overestimated. Hence, non-parametric tests that do not require such assumption are often used in practice to verify results obtained from the parametric tests.

## **5. Conclusion**

For many years the impact of information announcements on the financial instruments prices has been very popular area of the economic research. The research has usually been connected with the question about the types of the information that are important enough so investors undertake certain actions that are reflected in the changes of market prices. One of the tools that allows to answer these questions is the event study analysis.

The method, despite its long history, is not only still valid but also constantly developed, mainly thanks to the latest numerical computing techniques and better access to the market data. What also proves the importance of the even study analysis, is the rich literature on that topic and a lot of research that has been done so far.

The event study was applied to check the impact of certain announcements on the corporate bond prices traded on Catalyst market. The research, done in line with the event study methodology, confirmed the existence of significant, although delayed reaction of the debt instruments prices to the information appearing on the market. Unfortunately, the results obtained from the parametric and non-parametric tests are not consistent with respect to the time and the strength of the prices reaction. The reason for these discrepancies can be found in the methodology. As an example of problematic cases we can give the length of the event window and the estimation window, the algorithm used to calculate abnormal bond returns or types of test applied to verify research hypothesis.

The results obtained in the empirical part of the article, although they do not allow us to conclude on the information efficiency of the Polish corporate bond market, point at the potential on this research area and prove its purposefulness. Because of the specificity of the relatively young Catalyst market, further research will involve taking into consideration a number of important factors. One of them is a poor liquidity of the corporate bond market that might have meaningful impact on the size and variety of the research sample. The second important factor is the lack of the rating grades assigned to the instruments traded on the Catalyst. This fact limits the possibility to plan the research based on the foreign research frameworks. It is also worth

to mention the subject of taxation, especially the calculation of the capital income tax with respect to the corporate bond returns.

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# NON-RETURNABLE AND RETURNABLE INSTRUMENTS OF EUROPEAN UNION'S PUBLIC AID FOR ENTREPRENEURS

**Ludmiła Frydrych<sup>1</sup>**

## **Abstract**

*The role of the state within the economy, its range and form of activities have long been in the center of disputes on economic theory among many outstanding economists. Different functions and tasks were assigned to the state depending on the economic school of thought and the applied policy. This article deals with the questions of public aid within the economic theory as well as with the non-returnable and returnable instruments of the public aid, it also presents the tendencies in their applications in the financial perspective of 2007–2013 and 2014–2020.*

**Keywords:** *aid, instruments, EU, funds.*

## **1. Introduction**

Poland's accession to the EU arose interest in the public aid, most commonly associated with the EU's funds (Famielec, 2007, No 732). The state can influence the economy through various groups of instruments. There are regulations and controls, tax instruments, public expenses and transfer payments. Public aid is a public expense and can be delivered by means of returnable and non-returnable instruments.

The aim of this paper is to present the public aid within the economic theory and in the context of the main economic approaches, to describe the basic instruments of public aid for enterprises and to indicate the tendencies which will be present within the so called new financial perspective of the European Union. The added value of this work is the analysis of the assumptions of application of the returnable and non-returnable instruments of public aid in the years 2007–2013 and 2014–2020.

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In order to accomplish the first goal of the work, the following hypothesis will be conducted: the returnable instruments, as compared to the non-returnable, are a better tool to level-off the capital gap in the economy due to its renewable character and the ability to enforce economic effectiveness of the entrepreneurial actions.

The discussion on the returnable and non-returnable instruments is based on literature research, analysis of the program data, reports and interview with a representative of the Managing Institution responsible for implementation of the returnable instruments for 2007-2013.

## **2. Public aid in the economic theory**

The state, as a historic institution, has played its economic functions from the moment of its formation. The oldest function is the gathering, collection of means for the coverage of social needs and building the military potential from part of the economic resources of the country (Breński, 2008, p. 22). The role of the state within the economy, its range and form of activities have always been in the center of disputes on economic theory among many outstanding economists. Different functions and tasks were assigned to the state depending on the economic school of thought and the applied policy.

Already in the ancient times and during the medieval ages there were discussions about state's engagement in the areas of the economic life. For example, the representative of the ancient Roman thought, Xenophon, supported the state's integration within all aspects of the economy, whereas Heraclitus is considered a precursor of the self-regulated market and competition. The medieval scholastics – supporters of private property – called for limitation of the state's roles and state's expenditures as well as for decreasing the public tributes. However, it was the development of the economy based on private property in the modern times that sparked the biggest discussions and arguments among the economists, supporters and opponents of the state's interventionism (Gwiazdowski, 2007, p. 90-91). The modern economy took on the criterion of economic theories the following division of the socio-economic programs: the interventionist (non-liberal) and liberal. The interventionist ones are related to the active financial policy of the state, whereas the liberal ones are based on the neutrality of the public finance.

The beginnings of the interventionist concepts lies in the mercantile economy. Its supporters claimed that the development of one's own production by means of protecting the producers and with indiscriminately centralized power and strong economic policy of the state is the basic way towards increasing state's wealth. A. Fredro and W. Gostkowski are counted amongst the Polish mercantilists. The cameralists, and in particular J. Justi and J. Nax,

considered the use of taxes as one of the instruments of state's interventionist policy to be of great significance. They pointed to the impact of state's fiscal policies on the social welfare (Ziółkowska, 2012, p.34). German economists attempted to develop the state's protectionist policies during 18<sup>th</sup> and 19<sup>th</sup> centuries. L. von Stain claimed that state's actions lead to surpluses which in turn generate additional accumulation of capital when they are returned into the economy. A. Wagner, who is the alleged author of the law of the increasing public spending "the law of A. Wagner", postulated the necessity of state's intervention in the mechanisms of the market. He stated that social growth has to be accompanied by increased public spending. The basic assumption of his concept was that the market mechanism is defective, because it creates conditions for the remuneration of the factors of production – land, work and capital, but it cannot satisfy the society's growing demands (Kozuch, 2013, s.24).

The theoretical base of the concept of interventionism was formed by the renowned English economist J. Keynes in the beginning of the 20<sup>th</sup> century. It is worthwhile to mention that the Polish economist M. Kalecki formed the basic elements of the Keynes' theory three years earlier. Kalecki developed a macroeconomic model of more accuracy than Keynes' that explained the causes of the mass unemployment in the 1930's. However, his work was translated into English later, when Keynes' model was already known in the West (Ziółkowska, 2012, p. 36). According to Keynes' views, the capitalist economy cannot function without interferences that manifest themselves as lack of balance and incomplete use of the production capacities and unemployment. The most important source of these interferences is the insufficient propensity of the private entities to invest which creates the necessity for state's interventionism. Under these conditions the state's income instruments (tax relieves, loans) and expenditure instruments (subventions) became the main tools of the state interventionism. The goals of the instruments were (Owsiak, 2005, p. 55):

- stimulating effective demand in the economy that conditions investment development and, through that, the increase in production and decrease in unemployment,
- mitigation of the fluctuations of the economic cycle by means of automatic stabilizers in the form of taxes, and in particular the tax scale - depending on the cycle – and the unemployment benefits.

Based on the assumptions for the use of public expenditure in order to limit the fluctuations of the cycle and its negative effects, the theory of anti-cyclic financing was formed. According to this theory, the state incurs public expenditure for programmes such as the socio-economic infrastructure, in

order to limit the demand in the economy, which is expected to lead towards new job creation, increase in production, income and economic recovery.

A. Smith was the precursor of the theoretic and ideological basis of the economic liberalism, and opposed the state's interventionism. At the end of the 18<sup>th</sup> century he tried to convince the public that state's interventions in the economy should be limited and that the self-regulatory market mechanism, the so called "market's invisible hand" is efficient. During the 19<sup>th</sup> century, the prevailing theories were that the state should get involved in the economic issues as little as possible and the economic decision making should be done through the mutual interaction between demand and supply in the market (Friedman, 2006, p. 28). A. Smith was a doctor so he treated the economy as if it was a living organism. He claimed that the state should finance only the external defense, justice system, protection of property and organization of public works. He supported the neutral character of the state. This model became quite popular in the 19<sup>th</sup> century until the great crisis in 1929-1935. Later on these ideas were developed by J. Say, among others, who also pointed to the necessity of limiting the state's activities due to the expense generating nature of interventionism which in turn causes tax burdens (Kwaśnicki, 2001, p.45). According to Smith, the budget can be created only up to the level which allows for financing the necessary public tasks of the state. And therefore, it should be balanced in a sustainable manner. He was of the opinion that deficit is a damaging factor for the economy and it is not ethical (Ziółkowska, 2012, p.38).

The evolution of the economic theory shows that the notion of public aid was already known in the ancient times. The state intervened in the economic issues by means of various instruments. The state's aid is a specific instrument of its policies directed towards the socio-economic development of the country. The notion of public aid itself has various definitions. In most cases, however, the public aid is defined as a selectively applied financial advantage for the enterprise with a corresponding financial burden created on the part of the public finance (Choroszczak, 2009, p. 11).

State's interventionism in the economy is against the idea of European integration since it weakens the competition, causes interferences in its mechanisms acting on the local and international markets. The definition of public aid which applies to Poland is the one formulated in the Treaty on the Functioning of the European Union (TFEU) and applicable since Poland's accession to the EU. Aid comes into effect when the most important premises are met cumulatively: the public aid was granted from the public financial resources, it threatens the competition, gives privileges to some enterprises or production of some goods, has negative impact on trade, supports the local enterprises and discriminates the foreign ones (Jankowska, 2005, p. 6).



The public aid can be granted to the country's regions, economic sectors and categories of entrepreneurs. Depending on its destination, aid can be of regional, sector-wise or horizontal character (*Raport...*, 2013). The regional aid targets exclusively those entities active in the poorest regions of the EU. The sector-wise aid is directed to specific sectors which call for support from the public sources in order to solve their problems. The horizontal aid reaches out towards all enterprises, independent from their location or sector of activity, on the condition that they will contribute towards the achievement of specific goals once the aid is granted (Podsiadło, 2011).

### **3. Identification of returnable and non-returnable instruments of the public aid for enterprises**

The state can effect the economic processes by means of various groups of instruments. There are regulations and controls, taxation instruments, public expenditures and transfer payments. The core of the regulation and control is the use of the authoritative powers of the state to impose some changes in the functioning of the market in order to fix it and to obtain the expected social goals. The state should ensure most of all the adequate management for the economic process (Eucken, 2005, p. 296). These regulations encompass both the economic as well as social regulations. The first ones are related to the control of prices, production and market structure, the second ones consist of laws aimed at control of the effects of economic activity on the society's health. Their main goal is to protect the values that are not easy to be priced on the market. The regulatory instruments may cause limited tendency towards increasing public spending, they might be their substitute, when the costs of adjustments to certain standards are covered by the entities to which the regulations apply. These instruments are meant to prevent the monopolistic tendencies, to mitigate and to remove the negative external economic actions (Kozuch, 2013, p.31). The key means through which the state can effect the economy are the instruments of fiscal policy which encompass: taxes, customs, fees, grants, subventions, treasury bills, warranties and governmental guarantees. These instruments allow the state to influence the economy and the income situation of the economic entities in a stabilizing fashion. These actions depend on the previously adopted socio-economic doctrine and are parts of the implemented fiscal policy. The fiscal policy can accelerate economic growth when the market fails, however, public spending is targeted towards the increase of capital efficiency. This phenomenon takes place when the private sector cannot deliver suitable means and the public expenditure improves the effects of the competition or the consequences of the external effects (Siwińska, 2007, p. 119). Another group of instruments

which influence the economic processes are the instruments of the monetary policy. They are applied to the basic phenomena in the monetary area and to regulate the quantity of money in time. These are, among others: interest rates, required reserve ratio for commercial banks and level of guarantees for bank deposits.

The case of interest in this work is the group of instruments which belong to the public expenditure and which, depending on their form, can become the public aid. Expenses are the main instrument for implementation of the allocation function of public finance. The amount and structure of the expenses are historically conditioned and depend on: the range of state's financing of the public tasks, social services, the scale of state's interventionism into the economic processes, fiscal efficiency measured according to income redistribution. It is worth mentioning that not all of the resources allocated by the public authorities are considered as expenses (Ziółkowska, 2012, p. 154). From the perspective of their legal forms, public expenses are categorized as: grants and subventions, benefits to individuals, current expenditure, expenditure on public debt and capital expenditure (Kosikowski, 2008, p. 69). From the economic point of view, the key distinction is between the redistribution expenses (transfers) and purchasing expenses (final, actual, real). The latter ones are made in relation to purchasing by the state the goods and services of material character. They represent the share of the public sector in the national income, in this case the state is the final recipient. The transfer expenses can take the form of external transfers that empower private entities which stay beyond the public sector with money from the public resources and internal transfers made within the sector of public finance that represent expenses of one type of financial administrators of public funding for the benefit of other administrators (Kožuch, 2013, p. 69).

Public expenditure is one of the most crucial instrument used by the state to influence the economic processes and quite often are the public aid. The aid of the state encompasses any means from the public resources, made available in any form, and offering advantages that the beneficiaries would not be able to obtain in the regular course of their activities. Depending on the character of the transfers, public aid can be divided into direct and indirect aid. The direct aid means that the public financial resources are transferred directly from the state's budget or local government or other entities to the aid's beneficiary. The following instruments belong to this group: grants, preferential credits, guaranties, warranties and capital investments from the public resources. One can speak of indirect public aid when the state or other public institution waives their own resources for the beneficiary of the aid. This group includes: tax relieves and exemptions, application of accelerated depreciation, postponement of tax payment date (Kožuch, 2011, s. 69). According to the

guidelines of the European Commission, the types of public aids are as follow: grants and tax relieves, capital-investment subsidies, soft crediting, warranties and credit guaranties. Table 1 presents the basic categories of the returnable and non-returnable instruments.

**Table 1.** Division of types of returnable and non-returnable instruments

Returnable instruments	Non-returnable instruments
Seed and Venture capital	Grants
Loans	Interest subsidies
Guarantee for repayment of a credit or other financial obligation	Subsidies
Preferential credits	Redeemable credits
Guarantees	Tax relieves

The first type of public aid is based on a grant mechanism – non-returnable aid, characterized by its direct financial resources transfer from the state’s budget, local government unit or other entities to the beneficiary. The other form belongs to the returnable mechanisms, also called the instruments of financial engineering. There are two groups among the returnable instruments: the debt instruments (loans, guarantees, warrantees) and capital instruments – increased risk capital (seed and venture capital).

Grants are the resources from the state’s budget, local government units, state special-purpose funds, that require special rules of grant settlement and which are directed to finance or co-finance the implementation of public tasks (Postula, 2012, p.111). The grants can take the following forms: special purpose grant from the state budget, investment grant, object-oriented (selective, special), subject-oriented (general, global). The special-purpose grants finance a wide range of activities and come from both the central as well as from local government budgets. These grants may be applied to finance or co-finance tasks from the area of governmental administration, other tasks delegated to local government units, tasks delegated to non-governmental organization and to entities acting for the public benefit, programmes implemented by financial means from foreign sources and co-financing of bank credits. Investment grant is formally considered as a special-purpose grant, however, it is regulated by the legislation as a grant for investment purposes. This grant can be applied from the state budget to local government units as well as to entrepreneurs to invest in infrastructure and environment protection. The object-oriented grant is a very specific type, and its characteristic feature is the co-financing of specific products or services, calculated according to the tax rates. The object-oriented grants allow the state, in specific circumstances, to reduce the market price of specific products or services, under the condition that it is justified by

social, educational, cultural and economic policy. The subject-oriented grant goes from the state's budget to co-finance the on-going activities of the entities (subjects) specified by the legislation. The main beneficiaries of such grants are: educational units, cultural institutions, insurance funds (Wernik, 2011, p. 40). The above enumerated types of budget grants are not unified, they vary according to the application procedures and the areas in which they can be applied. The subject and object-oriented grants are transfer expenses and, as an instrument, they are characterized by a single or periodically re-occurring non-returnable money flow, directed by public institutions towards a specific economic entity, local government or a public sector unit.

The public authorities, by applying the non-returnable instruments, add financially to public goods and products that arouse positive external effects. The goal of application of the returnable instruments is to counter-react to the market imperfections, but still, these instruments can also cause them. By direct granting to the entity, the public authorities increase its market competitiveness at the expense of other entities. Due to this fact, there is a possibility of favoring selected groups of entities and branches by the public authorities. The non-returnable aid increases thus the probability of financing non-efficient undertakings and, at the same time, pushing out investments financed with private means. Such aid may lead to an effect of a loss – financing activities that would be carried out anyway. On the other hand, such aid motivates the entities to implement innovations and to take risks. The biggest disadvantage of the non-returnable instruments is the accompanying bureaucracy. The grants are distributed through calls for proposals and sometimes there is a long time before the results are known. For this reason these instruments are less attractive source for the newly established entities. The non-returnable aid is more effective when used for the benefit of entities that produces public goods (*Analiza...*, 2012).

The returnable instruments, also called the instruments of financial engineering, are regulated by the decree that sets out the legal rules for the European Fund for Regional Development, European Social Fund and Cohesion Fund (COMMISSION REGULATION (EC) No 1828/2006). The returnability means that the final beneficiary returns the financial means after certain time so that they could be reinvested in other projects. The returnable instruments encompass among others: loans, guarantees, warranties and instruments of the increased-risk-capital. Despite their common trait of returnability, these instruments can take various forms: loan funds, investment funds or guarantee funds.

The preferential loan instruments finance activities with foreign means, but need to be returned together with the fee for using these resources (interest). Loans as the instrument of financial engineering are directed towards entities

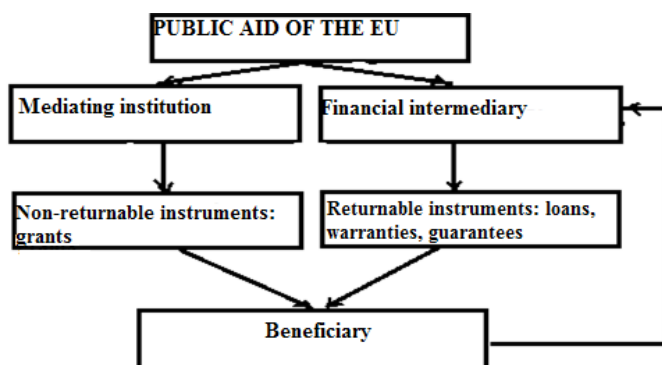
with little ability of credit. These instruments are divided into preferential and market loans, based on the conditions of their application. Financing according to the market rules is meant to support the entities with low ability of credit and not to be a competitive offer in comparison to offers of the financial institutions available on the market. The interest rates are usually lower than in commercial banks due to the fact that the instruments are not profit-making and a zero-cost of obtaining the loan capital.

Guarantees and warranties are specific returnable instruments because they do not finance directly the economic entities but give guarantees and warranties that increase the possibilities of getting financing from external sources. They secure the loans or credits. They oblige the guarantor to pay back the obligations in case these are not returned by the debtor. Their advantage lies in taking over the risk related with the guarantee or warranties (*Analiza...*, 2012).

The capital instruments that belong to the group of instruments of financial engineering are direct investments in innovative activities that entail risk, in return for shares in the company. The instrument is characterized by long time of return on investment. The capital funds encompass the seed capital, which means investing funds at the early stage of entity's development, and venture capital, meaning investments in young entities in their growth phase.

The above described returnable instruments that belong to the group of debt instruments, add obligations on the side of liabilities of the entity (mostly long-term). The capital instruments cause the increase in the ownership capital. These instruments have a common trait of limiting in time the ownership of the financial resources, and thus the necessity of return.

The structure of distribution of financial resources within returnable and non-returnable instruments of support is presented in Figure 1.



**Figure 1.** Returnable and non-returnable system of financial resources distribution

The analysis of Scheme 1 reveals the basic differences between the returnable and non-returnable instruments in the following areas:

- resource returnability – in case of the non-returnable instruments the obtained resources remain with the beneficiary,
- rolling-effect in case of the returnable instruments – multi-usage of the invested resources for the aim of multiplication. The resources applied once become the support for a number of entities,
- type of entity that can apply for the aid – SME and local government units apply for the nonreturnable resources through call for proposals, whereas banks, guarantee funds and loan funds, fund for development of rural areas apply for the returnable instruments. After they obtain the resources these entities distribute further in the form of credits, warranties, loans for SME and local government units.

The returnable instruments allow for the use of financial leverage: application of foreign capital, for example in the form of a loan, allows for increasing the obtained profit and the efficiency of ownership capital. The more the assets are financed by foreign capital, the lesser the ownership capital engaged in implementation of the undertaking. Due to that, the profit rate per unit of invested capital is higher. As a result, the bigger the part of assets which is financed by foreign capital, the more the share of debt servicing in the profit. For this reason the usage of the leverage is justified in case if the foreign capital interest is lower than the investment return rate (Peřka, 2012).

#### **4. The tendencies in application of returnable and non-returnable instruments of public aid in the years 2007-2013 and 2014-2020**

Since the accession into the EU, Poland has been covered by the cohesion policy of the EU and thus granted the access to the structural funds which are the main financial instrument for implementation of the EU cohesion policy and the other remaining types of common policies of the Member Countries. The structural funds are used in order to increase the economic and social cohesion of all the EU and to reduce the differences in development among the Member Countries (Dylewski 2009, p. 22). Poland was the biggest beneficiary of the structural and cohesion Funds in the financial perspective of 2007-2013, with the aid of over 67 billion Euro for implementation of the Cohesion Policy. Most of these funds were distributed by means of non-returnable grants (applying the rules of n+2). The returnable instruments in that financial perspective were only to complement the distribution system of the resources from the EU budget, dominated by the grant mechanisms. Table 2 presents the returnable and non-returnable instruments available on both local and international level in the years 2007-2013. These instruments were available through the implemented programmes. Some programmes offered

both returnable and non-returnable instruments, for example on the country level: Regional Operational Programmes, Innovative Economy Operational Programme and Development of East Poland Operational Programme. On the other hand, the Infrastructure and Environment Operational Programme held mostly the non-returnable instruments in the form of grants. On the international level the non-returnable and returnable instruments were available through the following programmes: The Framework Programme for Competition and Innovation, International Cooperation Programme of the 7<sup>th</sup> Framework Programme.

Within the time-frame of 2007-2013 the system of returnable and non-returnable instruments was fragmented, there was a lack of appointed institution for coordination of the implementation of the instruments. The returnable instruments in this time-perspective, were financed mainly within the 16 regional operational programmes and thus the support was directed towards the strategic objectives of specific region and not the objectives on the country level. In the perspective of 2014-2020 the Ministry of Regional Development will be responsible for the coordination of the goals and tasks implemented within the specific operational programmes by means of the returnable instruments on the level of both region and country.

The main rules for financing the EU's cohesion policy for the period of 2014-2020 were set out in the document "Multiannual financial frame 2014-2020". It contains the financial plan related to the strategy "Europe 2020" which assumes that the non-grant instruments will be the core financing means for the cohesion policy: credits, loans, warranties, capital shares, redemption or partial redemption of credit or loan, redemption or partial redemption of part of the interest on credit or loan (Peřka, 2012). The financial perspective of 2014-2020 assumes the increase in application of financial instruments. Additionally new returnable instruments, not used before, are planned to be introduced within the Common Agricultural and Fishing Policy. **Table 2.** Map of selected returnable and non-returnable instruments within the specific programmes in the years 2007-2013

	Program	Returnable instruments	Non-returnable instruments
Country level	Innovative Economy Operational Program	<p><b>Technological credit</b> – support for investment in implementation of new technologies by means of technological credit with possibility of partial payback from the resources of the Technological Credit Fund in form of technological premium</p> <p><b>Capital instrument</b> – the aim is to increase accessibility to external sources of funding of the SME sector in the early stages of growth for particularly innovative entities or active in R&amp;D. Market support VC.</p>	<p><b>Grants</b> – support for activities that directly or indirectly encourage the establishment and development of innovative enterprises.</p>
	Development of East Poland Operational Program	<p><b>Warranties/Guaranties</b> – in the form of Re-warranty for guarantee funds, for support of the SME sector in 5 provinces of Eastern Poland. The aim is to increase the accessibility to external sources of funding.</p>	<p><b>Grants</b> - the aim is to create conditions for economic growth and employment.</p>
European Level	Regional Operational Program	<p><b>Loans, credit, warranties</b> within the initiative JEREMIE – the aim is to improve the application and efficiency of the resources aimed to support the SME sector in the framework of the EU funding in Poland; funds selected from the Regional Operational Program resources.</p> <p><b>Loans, guarantees</b> within the initiative JESSICA – instrument targeting the local government units, facilitates the complex approach towards the issues of revitalization of urban areas.</p>	<p><b>Grants</b> – the aim is to improve Poland and its region's attractiveness as investment destination by means of technical infrastructure development and accompanying protection and improvement of the environment, health, cultural identity and territorial cohesion.</p> <p><b>Grants</b> for initiatives related with the educational and training programs and structural and cohesion funds for the benefit of regional convergence and competitiveness.</p>
	Infrastructure and Environment Operational Program	<p><b>GIF</b> – (High Growth and Innovative SME Facility) Instrument It encompasses the investments of the European Investment Fund in specialized funds of increased risk.</p> <p><b>SMEG</b> – (SME Guarantee Facility) warranty system for SME, issuing of re-guaranties for the operating guarantee programs, issuing direct guaranties for the financial institutions.</p> <p><b>CBS</b> – (Capacity Building Scheme) system for development of the capabilities of financial brokerage institutions increasing the supply of credit for SME by means of improvement in the financial reliability procedures in the framework of crediting for SME.</p> <p><b>JOSEFIN</b> – Program of the Baltic Sea Region</p> <p><b>JASSMINE</b> – support for the market of micro-loans by means of technical assistance and financial support</p>	<p><b>Grants</b> for initiatives related with research, that play the key role in realization of the objectives of growth in competitiveness and employment, education and training programs and structural and cohesion fund for the benefit of regional convergence and competitiveness.</p>
	7th Framework Program	<p>Innovative credit for innovative projects RSFF directed towards R&amp;D projects.</p>	



According to the forecasts, in the financial perspective of 2014-2020 the returnable instruments allocation may reach even 10 billion Euro, which may constitute 15% of the allocation (*Instrumenty...*, 2013), whereas the share of the returnable instruments in the previous perspective was about 1 billion Euro and made not more than 2% of the allocation (Peřka, 2012). The returnable instruments in the new perspective will be applied to finance activities of entities that experience difficulties in accessing external financing due to the lack of ability of credit, lack of adequate securities or lack of interest from the capital funds. The EU documents suggest preferring those instruments that ensure the highest share of private resources in project financing in order to achieve the maximum level of financial leverage. The suggested returnable instruments for 2014-2020 are presented in Table 3.

**Table 3.** The returnable instruments planned for 2014-2020

<b>Returnable instruments catalogue</b>	<b>Assumptions</b>
Capital Instruments	The system beneficiary Country Capital Fund, range similar to Innovative Economy Operational Program
Loan/warranty Mechanisms	Financing of high-budget key undertakings, for example in the sector of renewable energy or energy efficiency for consideration of NFOŠiGW as the system beneficiary, BOŠ as the financial intermediary.
Loans/warranties	Financing of undertakings of lower value in the renewable energy sector and in energy efficiency, for the consideration – usage of the system offered by WFOS.
Loans/credit lines	Granted directly by the Managing Institution or Implementing Institution, similar to the activity of the Regional Financing Institution, in the form of refund of payments made for the final recipients.
Warranties	Individual warranties, portfolio, granted by guarantee Funds.
Capital instruments: seed capital	Offer the resources in exchange for shares
Mixed instruments	Combining financial instruments with grants

The financial perspective for 2014-2020 will include also instruments available on the international level, as recommended by the European Commission (*Instrumenty...*,2013):

- 1) Horizon Programme 2020, Equity and Risk Sharing Instruments combines the three programmes and initiatives available so far: 7<sup>th</sup> Framework Programme of the European Community, the Framework Programme for the Competitiveness and Innovation and the support for the European Institute for Innovation and Technology. Within this program there are three priorities: excellent scientific base, leading

- position in industry and social challenges. The program will include both returnable and non-returnable instruments.
- 2) Programme for the competitiveness of enterprises and of SME (2014-2020) – it will include activities supporting the improved access of SME to financing. It covers capital instrument as well as loan guarantees.
  - 3) Capital instrument for the benefit of growth (EFG) – funds offering the capital of high risk.
  - 4) Loan Guarantee Instrument (LGF) – includes counter-guarantees and other solutions which aim at dividing risks for the guarantee systems and direct guarantees as well as other solutions for risk division for other financial intermediaries that are comply with the qualification criteria. LGF consists of the following instruments: loans, leasing and securitization of debt portfolios of SMEs.
  - 5) “Creative Europe Programme aims at preservation of the cultural heritage and increasing the range of distribution of creative works as well as supporting the stimulation of trans-border cooperation. The program will ensure access to debt and capital financing for the cultural sector.

Previous experiences in application of the returnable instruments within the financial perspective of 2007-2013 point at many problems. Among them are: lack of legislation for the returnable funds on the country level as well as lack of clarity and high level of generalization of the EU regulations in this respect. Moreover, the European Commission tends to give disadvantageous interpretations of these unclear and over-generalized rules to the particular Management Institutions and claims back resources that were presumable inadequately spent. Another problem was the lack of possibility of warranty and loan giving before 2012 for financing of the acting capital (since 2012 there is such a possibility but it is not clear in what circumstances such support can be granted). The lack of possibility to warrant loans obtained from the funds financed from EU resources is also an inconvenience. Additionally, the launching by Bank Gospodarstwa Krajowego of a competitive instrument “Gwarancje de minimis” negatively effected the results of the guarantee funds, that act within the Regional Operational Programs. In the financial perspective of 2014-2020 there is also the need to point to the actual owner of the financial resources that are returned from particular instruments of financial engineering. To make such a distinction, there will be a requirement for a change in legislation on a country level. It should also be mentioned that in the current financial perspective there is a lack of legislation on the policies of exit from the particular returnable funds. In order to make the returnable instruments more accessible and attractive for the interested entities and to

make their implementation more smooth, the abovementioned difficulties should be improved.

Additionally, in the perspective of 2014-2020 there should be a reduction in time-consuming procedures for application for the EU resources, that negatively effect their attractiveness. There should be also an increase in the awareness of the beneficiaries about the EU funds and about their nature and availability of the returnable instruments. These instruments allow for reduction of the capital gap in the economy and thus make the capital more accessible for SMEs.

## **5. Conclusion**

The state in the market economy has various economic and social tasks, takes on activities that stimulate the economic growth, stabilize the economic cycles, limit unemployment and make structural changes. The public aid plays the key role in the socio-economic development of the country. These tasks can be carried out by means of (among others) engagement of public resources in some entrepreneurial activities that form support for specific or selected group of enterprises. The focus of this article was a group of instruments that are part of the public expenditure and which, depending on the form, constitute the public aid offered by the state. The article presents the tendencies for application of the returnable and non-returnable instruments in the new financial perspective of 2014-2020. In this perspective, it is forecasted that the allocation for returnable instruments may reach 15% of the total allocation, whereas the share of these instruments in the previous perspective of 2007-2013 barely reached 2%. The returnable instruments, in comparison to the non-returnable ones, are not very popular among the entrepreneurs. Public aid is associated mainly with grants, as this was the most common form used during the years 2004-2006 and 2007-2013.

It is worthwhile to mention that despite many advantages of grants, there is one main disadvantage – it is of one-time use. That means that it is granted for one project and after its completion it cannot finance more. The circulation of financial resources may be ensured by the use of returnable instruments. Due to their renewable character, such financial means can be re-distributed by financial intermediaries: banks, guarantee, loans or investments funds. The returnable instruments are not much popular among entrepreneurs due to the availability of the non-returnable instruments. This results in practices such as adjusting the investment needs to the subject of the call for proposals and that creates ineffective use of the resources and makes the competitiveness imbalanced. One can conclude that as long as there are grants available in the market, that target a wide range of entrepreneurs, the returnable instruments

will not be popular. The advantages of the returnable instruments require that they outnumber the non-returnable ones, since they require to base the investments in an accurate economic account and allow for financing larger number of projects and in a longer time period.

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# THE EFFECTIVENESS OF THE LENIENCY PROGRAM IN COMBATING CARTEL AGREEMENTS IN POLAND

**Jerzy Choroszczak<sup>1</sup>**

## **Abstract**

*The Leniency program that has been analyzed raises the question concerning its effectiveness in fighting with the cartel agreements and whether it encourages the participants of the cartel enough to betray other participants of the cartel agreement. Examining such effectiveness is hard enough because of the secret character of functioning of cartels themselves and, in fact, it is not known how many cartel agreements exist in the Polish economy. The aim of the article is to analyze the effectiveness of methods of combating anti-competitive agreements such as cartels through mechanisms of the Leniency program. The intention of the Author is to make an attempt at researching the construction of the Leniency program itself and then, basing on the analysis of documents and reports of the Office for Competition and Consumer Protection, researching the rate of cartel agreements from 2005 to 2012.*

**Keywords:** *cartel, competition law, Leniency program.*

## **1. Introduction**

Cartel agreements, which are aimed against the competition, constitute one of the toughest areas for the competition law and institutions that uphold the law to deal with. The negative and multidimensional influence of such agreements on the situation of other participants of the market game brings about the situation in which the fight with cartels is particularly important from the viewpoint of the development of the economy of the particular country. On the other hand, the high “attractiveness” of this form of cooperation offering benefits for cartel members as well as the characteristic “conspiratorial” nature of the cooperation make the combat with cartels very hard.

The aim of the article is to analyze the effectiveness of methods of combating anti-competitive agreements such as cartels through mechanisms of the Leniency program. The intention of the Author is to make an attempt at researching the construction of the Leniency program itself and then, basing

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on the analysis of documents and reports of the Office for Competition and Consumer Protection, researching the rate of cartel agreements from 2005 to 2012.

## **2. The specificity of cartel agreements**

Companies, in their activities on different levels of development and trying to strengthen their competitive position, often enter into various contracts between themselves. Some of those contracts are compliant with the law and made in honest circumstances such as strategic alliances. Others are unfortunately forbidden by the law because of the fact that they are aimed against the competition and free market mechanisms.

Cartel agreements, which are made between competitors - entities that function on the same level of production or turnover - constitute one type of such anti-competitive agreements. One should consider agreements between competitors that function in the market on the side of supply as well as demand. In this case, companies that are usually competing with each other can be particularly interested in achieving the cooperative market result and sharing the achieved benefits between themselves. Such an agreement can contain arrangements regarding prices, the scale of production and sale, the division of the geographical and product market and, in result, give each participant of the agreement the comfortable dominant or even monopolistic position at the allowed segments of the market. The stability and durability of those agreements are favored by such factors as: market transparency, the lack of internal competition, low asymmetry of participants and less elastic demand. Companies that create anti-competitive agreements by settling the price policy, the scale of production or dividing sales markets between themselves behave as an ordinary monopolist or a company that holds the dominant position. It means that they can maximize profits by limiting the scale of production and raising prices. Every company that is separately operating on the market would never achieve such profits and such a market position.

The anti-competitive agreement should be distinguished from so-called parallel behaviors (Piejko, 2007, p. 145). Successive, related, and very similar actions of competitors constitute parallel behaviors. However, they do not result from earlier arrangements but from natural observations of the market, analyzing moves of competitors and adjusting to them. Quick reaction to promotional actions, changing prices of the company as an answer to the earlier changes in prices of other market players, and imitation within the framework of the distribution constitute the sign and result of the competition and not the lack of competition. Thus, parallel market behaviors of the company are distinguished from agreements that are forbidden by the law and limit the



competition by the lack of the characteristic element of agreement taken in any form.

Cartels constitute one of agreements limiting the competition. The cartel is the agreement between competitive companies that observe, with respect to each other, the legal, economic and organizational independence. It aims at limiting or eliminating the competition on the market – companies that did not join the cartel (Sloman, 2001, p. 163). Such agreements can be made between salesmen and customers. The reason why salesmen create the cartel is to make the agreement concerning prices of selling products, division of the market, assigning recipients to particular suppliers and markets, quantitative amounts of the sale or arrangement regarding the tenders lodged. On the other hand, the motives that push purchasers forward to create the cartel are common shaping of purchase prices, agreements in the range of allocation of suppliers among participants of the agreement, division of the supply market and arranging the principles of procedure in putting purchase of goods and services out to tender (Fornalczyk, 2007, p. 86). In general, those motives of companies creating the cartel have an effect in achieving profits which are usually gained only by the monopoly.

The essence of the cartel agreement is the coordination of the business of its participants, which is the settling of such parameters as: contribution to the supply and sales market, the scale of the sale and the price. Thus, in this case, it is the serial coordination because of the fact that the subject of arrangements comprises only some symptoms of the economic activity, and not the full coordination, whereby the agreement in the range of more than one parameter is possible (Włodyka, 2006, p. 127).

Therefore, cartel-type agreements can contain a larger or a smaller number of parameters of the market activity, which are used by businessmen in the market. Such a parameter, for example the price, which becomes the subject of the agreement between participants of the cartel, stops being the instrument of the competition for the individual businessman – a participant of the cartel, and becomes the variable known, which is artificially shaped, and not the variable unknown, which is proposed by the market but not influenced by it.

From the point of view of the price and production policy, the cartel is comparable with the monopoly consisting of many companies. It comes into being when companies of one branch bind together in order to coordinate the scale of the production or activities concerning the sale. According to Hovenkamp (Hovenkamp, 1989, p.55), cartels are more dangerous than the monopoly because they originate more quickly and do not need so many expenses that are necessary for setting a monopolistic company through the internal development or making capital takeovers or the amalgamation. On the other hand, in accordance with features of agreements that have been already

presented, they are more impermanent than the group of companies or the linked\_enterprise.

Therefore, cartels are very dangerous for the market. Forming a cartel helps to minimize the amount of production, increase prices, decrease the quality of production and, thanks to this, significantly increase the profit while minimizing costs of production. They deal with the pressure of the market in the direction of taking actions in order to increase the productivity, improve the technology, increase the quality and rationalize methods of production and sale. Such cartels help less effective companies to survive. They deprive companies of stimuli to improve honest ways of market fight. Those cartels are also very dangerous for customers, who receive the product that is more expensive, has lower quality and is technologically less advanced, in relation to such a situation in which there would be high intensity of the competitive fight on the market.

### **3. Cartel agreements in the eyes of the competition law**

From the legal point of view, anti-competitive agreements such as cartels are broadly understood as all contracts between businessmen, arrangements made in any form by two or more businessmen as well as resolutions and other acts of businessmen associations made both in writing and verbally, which constitute agreements (Bernatt M. Jurkowska A, Skoczny T. 2007, p. 43). The inclusion of arranged behaviors of companies in legally forbidden anti-competitive practices stems from the need to counterattack circumventing of the ban on making agreements in the form of legal activity – the contract, through the cooperation of businessmen in other forms that, de facto, will be limiting the free-market competition. Such arrangements can be understood as behaviors that escape formal rigors, which are characteristic for agreements and acts of associations. These are all situations in which partners act in harmony, but without obvious traits of the open connection between them when it is decided that their behaviors have characteristics of cooperation made in any form and directed to the competitors who are not covered by this cooperation. Therefore, the prevailing meaning (negative impact on the market) belongs to the economic criteria, not formal and legal ones. It is even assumed in the doctrine that the agreement which expired, for example, as a result of the passage of time can be questioned as the competition law-breaking if the results of such agreement are still noticeable. Similarly, it is assumed that all participants of the forbidden agreement, regardless of their actual involvement in the current activity of the cartel, are responsible (Krasnodębska-Tomkiel, 2006, p. 38).

In order to affirm that the certain agreement was forbidden by the Protection of Competition law, it is important to present anti-competitive results, the loss that the competition suffered on the relevant market. However, there is a presumption regarding a certain group of agreements saying that agreements aimed at harming the competition and because of that they are “automatically” considered as violating competition law. This group includes agreements concerning, for example, setting prices, the division of the market, the purposeful limiting of the production, limiting of the sales as well as exchanging information about prices, setting the minimal prices of resale and imposing the export limits. Therefore, in such case, the fact that the aim of such agreements was anti-competitive would be enough to prove it legally and it is not necessary to present its anti-competitive results (Etro, 2006, p. 78).

For assessing if the agreement violates the competition rules, it makes no difference if it was realized in the practical way. Thus, such an agreement that aims at distorting the conditions of the competition on the market, but, for some reason, was not carried into effect, would be the violation of the competition law. Moreover, the agreement that only aimed at the intended limitation or distorting the competition is illegal. In order to assume that the competition regulations were violated, the awareness of violating law regulations by the parties of the agreement is not necessary (Jurczyk, 2004, p. 38). It is enough that they are aware of the fact that this agreement menaces the competition. Everything speaks for the high rate of the restrictive character of the competition law.

In the light of the above consideration, it is worth emphasizing that it is not important if the cartel conspiracy was made in writing, verbally, as so-called “*gentlemen’s agreement*” or any other form. Any cartel agreements that result in or even aim at the limitation of the competition are forbidden. The Protection of Competition law allows financially penalizing also those companies that participated in the unrealized conspiracy or even those that belonged to the cartel but did not apply to all decisions of the cartel.

When starting the analysis of legal regulations concerning cartel agreements, it can be affirmed that, on the basis of the Protection of the Competition law, they are absolutely forbidden. The general clause contained in the article no. 101 of the Treaty on the Functioning of the European Union (old article no. 81 of the TEC) outlaws any agreements between companies, decisions made by associations of companies and agreed practices that can have the influence on the trade between member states and whose aim or result is prevention, limitation or violation of the competition within the Common Market and especially those that concerns:

- setting prices of purchase or sale or other conditions of the transaction in the direct or indirect way,

- limiting or controlling production, markets, technological development or investments,
- the division of markets or the source of supply,
- applying inconsistent conditions for equivalent services for trading partners and as a result generating disadvantageous competitive conditions for them,
- concluding the contract which is dependent on the acceptance of additional obligations by partners who, because of their character or trading habits, do not have any connection with the subject of those contracts.

It is worth to mention Polish regulations of the anti-monopolistic law, because, according to the Protection of Competition and Consumers Act of February 16, 2007, it is forbidden to take actions that limit competition, aiming at creating forbidden agreements that limit the competition (art. 6, paragraph 1), especially those connected with:

- setting prices personally or indirectly,
- limiting or controlling production and sales,
- division of the sales market or purchase,
- applying strenuous or homogenous work conditions, which can create various competition terms for those people in similar agreements with third parties,
- making the agreement dependent on the acceptance or fulfillment of the other service which does not have factual and common connection with the subject of the agreement by the second party,
- limiting the access to the market or excluding businessmen that are not covered by the agreement from the market,
- setting conditions of the offers and, especially, the range of jobs and the price by the businessmen, who join the bidding or by those businessmen and the organizer of the bidding.

Both catalogues are not complete, as they include only examples of inconsistency with the law in agreements made between businessmen.

Legally forbidden cartel agreements constitute one of the most serious breaches of law and that is why their participants have to take into consideration very serious consequences. The administrative procedure concerning the practice of cartels is launched by the President of the Office for Competition and Consumer Protection (UOKiK). The procedure is instituted *ex officio* and everyone can put the written notification about the suspicion of using cartel practices. As a result of anti-monopolistic proceedings, the President of UOKiK can give the decision on accepting the particular practice as limiting the competition and order omission of its use. Apart from the administrative sanction, the President of UOKiK has the possibility of fining with the financial penalty that constitutes 10% of the income for the settlement period preceding the financial fine.

#### 4. The Leniency Institution

Applying anti-cartel regulations in the European Union is accompanied by the Leniency program, which for the first time was introduced in 1978 in the USA by the Justice Department (Król-Bogomilska, 2013, p. 18). In the European Union this program has been used since 1996 on the basis of the special Notice of the European Commission. From the beginning of applying this program in the European Union, it has had the form of the soft regulation prepared by the European Commission, which means that the Commission is not in any formal way connected with any procedure or any results of submitting the application for leniency of the penalty by the businessman (Kovacic and Shapiro 2000, p. 98). In Poland, the Leniency institution was introduced as legal regulation in 2004. At present, only few participating countries do not have the prepared Leniency system in their legal systems.

The aim of the Leniency program is to break the conspiracy of silence among the participants of the cartel and reveal such agreements more easily. It has to be remembered that agreements that limit the competition belong to the most serious breaches of the competition law. Because of their top-secret character, it is very hard to reveal them as well as overcome them. That is why businessmen, who decide to cooperate with the anti-monopolistic body and provide the proof of the existence of the cartel conspiracy, will be treated leniently.

Only the businessman who is the first to apply for the Leniency and was not the originator of creating the cartel (art. 109 of the Protection of Competition and Consumers Act) can count on the full leniency of the penalty. The rest of participants who applied can receive the reduction of penalty (Leniency, 2004):

- The second applicant in the line – reduction of the penalty up to no more than 50%
- The third applicant in the line - reduction of the penalty up to no more than 30%
- The rest of applicants - reduction of the penalty up to no more than 20%

Thus, this construction pays a bonus to first businessmen who will inform UOKiK about the cartel. It is worth mentioning that changes which were proposed in the project of the new Protection of Competition and Consumers Act are going further when it comes to the above solutions. Suggested changes constitute so-called “*Leniency plus*” that can help the businessman who applied as the second or the next to receive the additional reduction of the penalty up to 30% if they inform the Office about another conspiracy in which

they were also participating. In the second case they will have the status of the first applicant and avoid the financial penalty.

Thus, the Leniency construction itself somehow resembles the institution of the key witness, who, despite the fact of being one of the offenders of the prohibited act, can count on the leniency of the penalty, but certainly, only when they decide on revealing details of the activities of the criminal association. Therefore, both institutions – the Leniency and the key witness are based on a similar assumption: instead of giving information on the forbidden act and withdrawing from the legally forbidden activity, the person or the subject can count on the specific reward in the form of withdrawal from the penalty. The additional impulse in the case of the Leniency institution, in order to “reveal the participants of the forbidden agreement”, is the gradation of the award, which means that only the first subject can count on the full remitting of the penalty. The point is to break the conspiracy of silence among participants of the cartel, spread the suspiciousness, raise a kind of competition of being the first to inform about the cartel and, in this way, try to break the cartel agreement.

Discussing the legal construction of the Leniency institution, it has to be mentioned that it is the legal act or another document (announcement, directives) that generates legal expectations on the side of businessmen participating in the cartel that are declared at the address of the anti-monopolistic body, on the basis of which such a participant can apply for withdrawing from the penalty or reducing the penalty for the participation in the cartel, in the case that they freely provide the anti-monopolistic body with the information on the existence of the cartel.

The cooperation within the framework of the Leniency is always based on the assumption that the participant of the cartel decides on full cooperation with the anti-monopolistic body and reveals everything that is known. Revealing part of the truth or the untruth is out of the question because, in the case of insufficient cooperation, the benefit of withdrawing from the penalty can be retreated in any moment. In such a situation the businessman stays somehow empty-handed: as they devoted good relations with the cartel partners, who may take revenge in some ways, and, on the other hand, they did not benefit from betraying their partners in the form of the simple leniency of the penalty.

The businessman who applies for being covered by the program can personally put forward the formal application (as well as the abridged and simplified version) to the headquarters of the Office for Competition and Consumer Protection in Warsaw, to the worker of UOKiK for the report, by post, fax as well as email. In the last two cases, it is necessary to provide the Office with the original application within 3 days (Directives of the President

of the Office for Competition and Consumer Protection concerning the Leniency program).

The application of withdrawing from the financial penalty or reducing its range should include the description of the agreement presenting:

- businessmen that made the agreement,
- products or services that are mentioned in the agreement,
- the area covered by the agreement,
- the purpose of the agreement (for example, setting the minimum prices of the resale, the division of the market),
- circumstances of making the agreement,
- roles of the particular participants of the agreement (mainly, presenting the originator of the agreement),
- the duration of the agreement,
- if the application was also put forward to protection of competition bodies of other participating countries and European Union,
- how the agreement functioned, especially including dates, places, content and the frequency of meetings of participants of the agreement,
- names and positions of people that play key roles in the agreement.

The declaration of desisting the participation in the forbidden agreement as well as the statement that the applicant was not the originator of the agreement and did not encourage other businessmen to participate in the agreement should be attached to the application. Moreover, the proof of supporting the statements should be attached to the application.

## **5. The analysis of the effectiveness of the Leniency program**

The Leniency program that has been analyzed raises the question concerning its effectiveness in fighting with the cartel agreements and whether it encourages the participants of the cartel enough to betray other participants of the cartel agreement. Examining such effectiveness is hard enough because of the secret character of functioning of cartels themselves and, in fact, it is not known how many cartel agreements exist in the Polish economy. This effectiveness can be examined for the number of applications that were put forward by repentant businessmen as well as for amounts of money that had to be paid by participants of the cartel. Examining the effectiveness of the Leniency program, decisions of the President of the Office for Competition and Consumer Protection as well as reports of UOKiK from 2004 to 2012 were analyzed.

The table mentioned below presents the summary report of the number of applications that were put forward to UOKiK within the Leniency programme framework.

**Table 1.** The number of applications that were put forward to UOKiK regarding the Leniency programme

Year	2004	2005	2006	2007	2008	2009	2010	2011	2012
The number of applications put forward to UOKiK	0	2	3	6	3	6	8	2	16

Source: Own elaboration based on the reports of UOKiK.

Analyzing data contained in the Table 1 it can be affirmed that in the initial term of the program its effectiveness was not very high, which could arise from the novelty of this mechanism and its little command by businessmen as well as a number of formal requirements that need to be fulfilled while putting forward the application to UOKiK. However, beginning from 2007 to 2012, the number of applications concerning the information on the existing cartel, which were put forward to UOKiK, increased. In this respect, 2012 turned out to be the record-breaking year in which 12 businessmen who were earlier participating in cartel agreements freely informed UOKiK about that fact.

**Table 2.** Main cartels that were found from 2005 to 2010 by means of the Leniency institution and the penalty amount that was fined by the president of UOKiK

No.	Year	Cartel	The total penalty amount fined by the president of UOKiK
1.	2012	Cartel at the market of wood-like boards	PLN 14 million
2.	2011	Household chemicals cartel	PLN 2 million
3.	2010	Paper cartel	PLN 89 343
4.	2009	Cement cartel	PLN 411 586 477
5.	2008	Cartel of paints and varnishes	PLN 45 758
6.	2007	Cartel of paints and varnishes	PLN 2658 257
7.	2006	Cartel of paints and varnishes	PLN 110 million

Source: Own elaboration based on the reports of UOKiK for the period of 2006-2012.

Analyzing the Table 2 presenting main cartels that were revealed thanks to the Leniency institution, it can be claimed that the penalty amount imposed on participants of the cartel by UOKiK increases all the time, which is mainly the result of the fact that, thanks to the Leniency program, bigger cartels are found (as it was said before, the penalty is connected with incomes of the participant of the cartel).



## 6. Conclusion

In conclusion, as the last period from 2008 to 2012 is taken into consideration, it can be claimed that the effectiveness of the Leniency institution in revealing cartels is moderate, or even low. For example, in 2008 and 2011 the number of applications was very small and amounted to three. 2012 turned out to be the exceptional year and, if this tendency lasted for a longer period of time, then one can argue for the growing effectiveness of the Leniency institution in revealing cartel agreements. The circumstance that can have positive influence on the shape of the growing trend is basically the fact that businessmen are more aware of violating the law by creating cartels and penalties that threaten for that practices. On the other hand, it is the increasing knowledge of businessmen about the Leniency institution itself. It is not accidental that the greatest number of applications on benefitting from the Leniency program was in 2012, when the intensive informative action of UOKiK, concerning the essence of the Leniency program as well as penalties for participating in such an agreement, was taken. Greater knowledge of professional participants of the market about the Leniency institution arises from actions taken by UOKiK. It can be certified by the newest research, which was conducted by EU-Consult as requested by UOKiK. From March to May 2012, 1200 businessmen answered questions in the poll. As the surveys present, 41.5% of subjects know about the Leniency program. It is much more than, for example, in 2009 when only 19% of respondents demonstrated such knowledge.

Big companies turned out to constitute the biggest group that knows the Leniency program. Among subjects of at least 250 employees, 57.4% of them knew about the program, and in the case of employers of maximum 9 employees, only 15.4% of interviewees heard about the Leniency program. Among those who know the Leniency institution, more than 45% of them believe that the Leniency program can persuade businessmen to reveal price fixing (10.4% - YES answers, 35.7% - RATHER YES answers), and 70% of them would be willing to use it (YES answers – 19.4%, RATHER YES answers – 48.6%).

All in all, one can be sure that the Leniency institution will not fully eliminate the phenomenon of cartels as the temptation to take huge advantages and function comfortably for participants of cartels is too big – there will always be a certain group of dishonest companies that will be taking “shortcuts” when it comes to the improvement of the competitive position. However, the Leniency institution can be an efficient tool in fighting with cartels and its strength will be dependent on several factors:

- the awareness of businessmen about the illegality of actions taken by participants of the cartel and the amount of penalties for participating in the cartel,
- the awareness of the fact that the extraordinary program of mitigating penalties among businessmen exist,
- successes in the amount of cartels that were revealed during the inquisitorial procedure by UOKiK,
- simplifying the procedure of applying for the Leniency program.

The Leniency program itself and its influence can be additionally strengthened by increasing penalties for the participation in the cartel. The penalty of 10% of incomes for a very big company which enjoys great profits for participating in the cartel, might not be the sufficient impulse to discourage them from participating in this type of agreement and encourage this participant to cooperate with UOKiK. Also, the modification of the Leniency institution, so-called Leniency plus, which was proposed in the project of the Protection of Competition and Consumers Act, can contribute to the increase in the effectiveness of revealing new cartels. The future will show if the Leniency program will be more useful for revealing anti-competitive agreements between companies.

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# PRE-SALE OF FLATS AS A METHOD TO LIMIT MARKET RISK

**Marcin Sitek<sup>1</sup>**

## **Abstract**

*The focus of this study is on the analysis of the developer's and purchaser's risks that result from pre-sale of flats in the real estate market. This study attempts to analyze developer's and purchaser's risks that result from pre-sale of flats in the real estate market. The study discusses the results concerning the economic indices that stimulate behaviors of participants and analysis of the Developer's Act in the aspect of benefits and risk for market participants. The provisions of the new Developer's Act that introduce regulations beneficial for both customers and developers (thus improving their safety) were also discussed. The Developers Act emphasizes the importance of pre-sale as a limitation of market risk that results from finding customers at the stage of pre-sale, guarantee to sell investments at the pre-defined prices and finding funds for financing developer's projects. The analysis of benefits for both purchasers and developers that result from pre-sale of flats secured with escrow accounts points directly to reduced market and financial risks incurred by developers and lower purchaser's risk of losing their resources. It was also stressed that, however, the costs of all the legal and financial solutions increase the financial load for the customers.*

**Keywords:** *developer, pre-sale of flats, developer's risk, escrow account.*

## **1. Introduction**

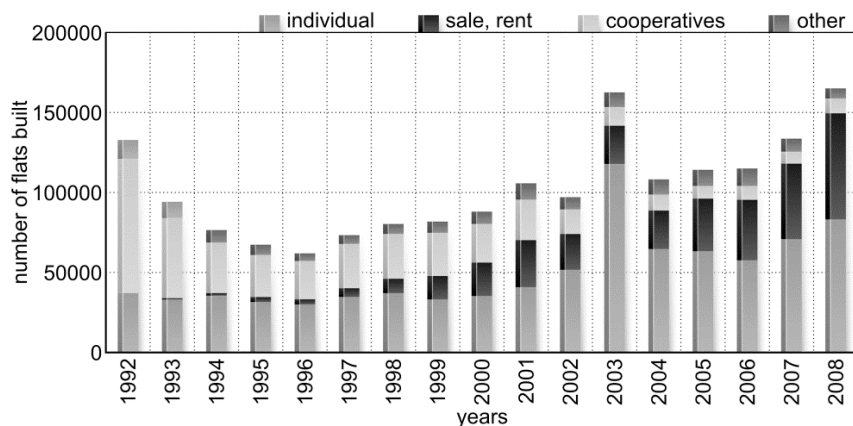
A dynamic decline in the size of flat construction sector in the beginning of the process of transformation has revealed a number of barriers of structural character in the real estate market. Diagram 1 presents the dynamics of changes in flat construction sector with a number of flats built in Poland in 1992-2008.

As we can see from the analysis of the data presented in Diagram 1, the process of transformation was started in Poland with a relatively low level of construction. The number of flats built was declining in consecutive years,

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reaching a minimum level (slightly over 62,000) in 1996. Since that moment, a gradual increase was observed until reaching the threshold of 115,000 in 2006 (Kirejczyk, 2009).



**Figure 1.** Structure of flats built in Poland in 1992-2008 with respect to investor's category

Source: Kirejczyk (2009, p.4)

Low income of people, connected with even lower level of economic growth, represented the basic barrier in market development, pointing to the necessity of subsidizing the real estate sector.

An average monthly salary in Poland is sufficient for only 0.8 square meters of a flat. An even worse situation is observed in the biggest cities, where the average salary allows for buying only 0.5 to 0.6 square meters.<sup>2</sup> In the Western European countries, the average salary of a citizen is sufficient to buy ca. 2 to 3 square meters of a flat. In Poland, the purchase of an average-size flat necessitates spending 6 to 8 yearly salaries, whereas in better developed countries, these needs can be covered using only 2.5 to 3.5 years' salaries (Łaszek et al., 2013; Łaszek, 2004).

Low incomes of society and high costs of building/prices of new flats cause that only part of society is able to satisfy their housing needs directly in the market. The factor that substantially increases financial ability of households with medium incomes in the housing sector is long-term financing, which usually adopts a form of mortgage loans. Availability of loans, especially mortgage loans, has increased substantially in the past two decades through

<sup>2</sup> „Główne problemy, cele i kierunki programu wspierania rozwoju budownictwa mieszkaniowego do 2020 roku” – author: Council of Ministers, print No. 3725, status: March 4, 2011, adopted through voting and directed to the Commission of the Infrastructure

competition and gradual economic stabilization. However, it remains lower than in highly developed countries.

For a long time, banks avoided financing of housing construction sector, whereas developers shifted the high risk of building flats on consumers and compensated it with high gratuities, which resulted in increasing the prices. Consequently, the purchaser's situation was unfavorable since, while competing for flats, they accepted unfavorable terms of contracts proposed by the developers. Due to the fundamental problem of risk in the real estate market, the integral part of investments in this segment, suggestion of actions aimed at achievement of greater transparency of activities of financial institutions in order to stabilize the system and its effective operation inspired the analysis of the research problem presented in this study.

The focus of the study is on analysis of developer's and purchaser's risks that result from pre-sale of flats in the real estate market.

The analyses used the data from the Real Estate Market Database (BaRN), National Reports on Mortgage Loans and Transactional Prices of Real Estate AMRON-SARFIN Polish Banks Association and analysis and reports of the Financial Supervision Commission (KNF), published collective credit data from Credit Information Bureau (BIK) and the Central Statistical Office of Poland (GUS) and documents containing sector-related data.

## **2. Risk of developer's activity**

Any activity based on the banking sector as the greatest segment in the financing system is exposed to risk. Also in Poland, especially in the real estate sector, the investment activity is exposed to a substantial risk, particularly in the period after the crisis in 2008-2010. Since flat aspirations of the Polish society remain unsatisfied (being still estimated in Poland at 1,500,000 flats; Raport Polska, 2011) while the main participant in the real estate market are developers, it is necessary due to very risky investments in this sector to implement measures to minimize the risk either through risk segmentation, compensation (self-insurance and insurance), division and repressive methods. With regard to the risk specific to the real estate market as connected with the properties of real estate, there are methods of its observation, evaluation and opportunities for risk manipulation and consequently, substantial minimization. Furthermore, the systematic risk that results from economic risk depending on economic policy, inflation and evaluation of the economy by the foreign capital is not reduced by the real estate market but the whole economy.

A particularly important kind of risk for developers is market risk (Bechciński, 2008). Any entrepreneur operates under variable market environment, but long period of implementation of developer's investments

causes that their activity is particularly exposed to the variability of situations in the market. Pre-sale helps to reduce market risk connected with the decline in the demand for flats as well as connected with the decline in prices which might occur during realization of investments until the moment of a flat transfer.

The risk of changing the economic situation affects, in a direct manner, formation of the level of selling prices and relationship between the supply and demand for flats. Rapid changes in prices of building materials, difficulties with finding qualified workforce (2007) that resulted in prices of costs of labor, noticeable increase in supply that manifested with a high number of flats built presently and planned to be released in the next year and competition are other determinants of developer's risk.

Despite improved economic tendencies, a particularly sensitive area of risk is the risk related to financing investments by banks and other financial institutions (Bryx, 2001). The pre-sale helped developers collect the resources which were presented in the bank as their own contribution, which allowed them to present good credit standing or reduced costs of credits. If a developer demonstrated to a bank that part of flats were sold through a pre-sale, the financial risk of this project was regarded as lower since banks evaluated this situation as a sufficient demand for particular flats in the area.

It should be emphasized that developer's activity is characterized by high exposure to risk factors, both due to its capital-intensity and long term of the investment process, necessity of involvement and coordination of work with many market participants and insignificant flexibility of the final product which declined with the progress of works. However, the pre-sale is limited by both market and financial risks of housing investments.

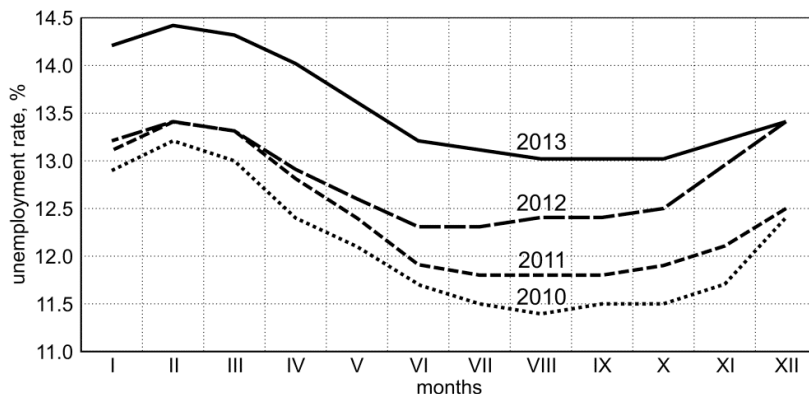
### **3. Selected economic indices that stimulate behavior of real estate market participants**

Proper assessment of the phenomena that occur in the market remains a key task for making market decisions by investors. Reliable information about changes that occur in the market will allow for limitation of the risk of a specific investment to the minimum level. The basic criterion for evaluation of the status of individual markets are indices used for improving market transparency. It can be improved as a result of collecting and sharing market information, whose usefulness consists, among other things, in limitation of the risk of improper evaluation of the real estate, which translates directly on investment effectiveness.

Economic indices, such as unemployment rate, GDP increase rate, inflation and levels of interest rates translate directly into behavior of the real



estate market participants, with particular focus on the purchasing power of potential customers. Diagrams 2, 3, 4 and 5 present basic economic indices that affect behavior of the real estate market participants.

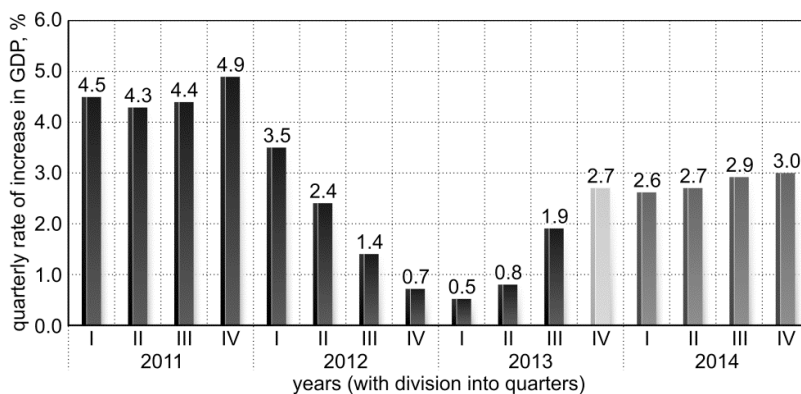


**Figure 2.** Unemployment rate in Poland

Source: GUS, IBnGR (2014, p. 2)

The data presented in Diagram 2 demonstrate that the unemployment rate at the end of the year 2013 was 13.4 %. However, the analysis of the data reveals its changes compared to the end of 2012 and increase by 0.4% compared to the end of the third quarter.

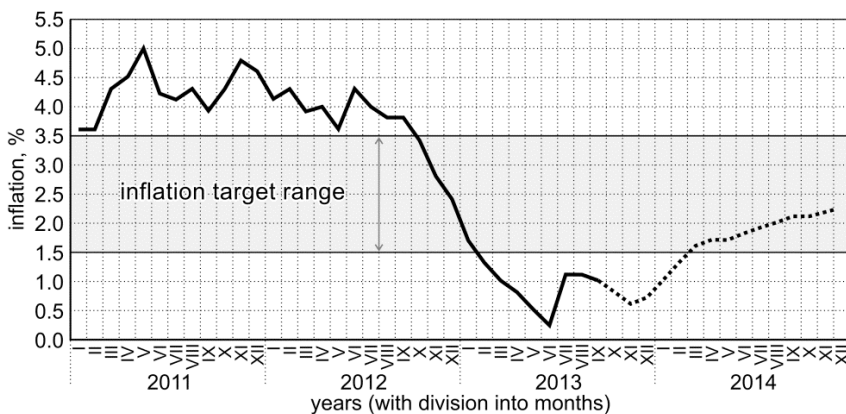
Furthermore, the increase in unemployment rate in previous years at the end of the fourth quarters compared to the situation from the third quarters was greater. This reflects the gradually improving situation in the labor market.



**Figure 3.** Quarterly rate of increase in GDP

Source: GUS, IBnGR (2014, p. 3)

Diagram 3 shows that mean rate of increase in gross national product in 2014 will reach 2.8% in 2014, which means that it will be substantially higher than in 2013, with the rate of GDB increase being 1.48%. It is remarkable that the economic growth will accelerate in consecutive quarters of 2014, but the differences between quarters will be insignificant: in the first quarter, the GDP will increase by 2.6%, while in the fourth quarter, this value will increase by 3.0%. According to the forecast of IBnGR, further acceleration in the economic growth at the level of 3.5% is expected in 2015.



**Figure 4.** Inflation in Poland

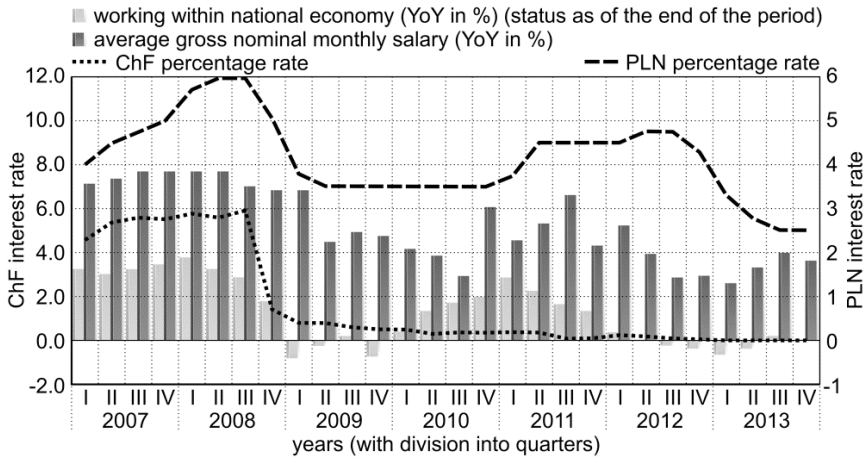
Source: GUS, IBnGR (2014, p. 4)

Diagram 4 and forecast of IBnGR show that inflation will reach 1.9% on average in 2014 and 2.2% at the end of December. In 2015, inflation will remain actually at the 2014 level, with mean level forecast at 2.0% and the level for the end of December at 2.1%. Relatively low inflation will be one of the factors to positively contribute to the dynamics of individual consumption. (Inflation below the inflation target of the National Bank of Poland means that changes in interest rates in the central bank should not be expected).

In the whole 2013, sales reached the level of 36,000 flats i.e. they increased by 17.5% YOY and were similar to the record number from 2007 (according to the National Bank of Poland, ca. 74% of total sales of flat resources built are performed by developers).

Furthermore, low interest rates (diagram 5) were conducive to the tendencies of withdrawing resources from deposits and converting them into investments in relatively cheap real estate. From the viewpoint of credit customers, the beginning of 2013 was characterized by an accumulated demand for flats in the fourth quarter of 2012 connected with completion of the Program Rodzina na Swoim (Family with their Own Flat). On the other hand,

also in the fourth quarter of 2013, the amendment of the Recommendation S and introduction, from 2014, of the requirement of the 5% own contribution stimulated demand and increased the interest in loans with 100% LTV.



**Figure 5.** Dynamics of employment and average salary in national economy on YOY basis and interest rates

Source: NBP Macroeconomic Analysis (2014, p. 10)

The dynamics presented and the analysis of selected economic indices that stimulate behavior of participants of the real estate market show that improvement in economic tendencies in general in 2013 and, first and foremost, the lack of changes in the unemployment rate compared to the end of 2012 (Diagram 2), forecast rate of GDP increase in 2014 (Diagram 3), low inflation below the inflation goal of the GDP (Diagram 4) and low percentage rates (Diagram 5) at relatively low prices of flats, generated in 2013 a strong demand impulse. The demand growing from quarter to quarter, reaching 10,900 flats (according to REAS) in the last (fourth) quarter of 2013, is comparable with the sales observed in the boom peak i.e. in the beginning of 2007.

#### **4. Developers Act: benefits and risk for real estate market participants.** **Pre-sale**

Specific conditions of operation of Polish housing market (previous lack of legal regulations for developer's activity, limited financing of developers by banks, imbalance between supply and demand in the primary market) have led to the situation where financing the growth of the primary real estate market in Poland is based mainly on the loans granted by individual customers. Loans

for developers' projects represent an insignificant part of the market of real estate financing and cause that the risk of failure of developer's projects is incurred mainly by the future purchasers of the flats who finance the building with their payments at the account of the developer (Jajuga, 2007). This model of operation of the housing market does not ensure steady development and sufficient securing of the rights of flat purchasers.

On September 1, 2011, Polish Parliament passed the Act on protecting the rights of purchasers of flats and houses which is supposed to protect customers of developer companies from losing the money in the case of bankruptcy of the developer which are not the developer's current assets. Since April 29, 2012, the act of September 16, 2011 started to be enforced concerning the protection of rights of purchasers of flats or detached houses (Journal of Laws No. 232, 2011). The new act is expected to prevent from malpractices connected with concluding and realization of developer's contracts and protect the rights of purchasers in case of developer's bankruptcy.

With respect to the investments implemented with so-called developer's system, i.e. from the resources paid by the customers, the money paid will not become the current assets of the developer but they will be redirected to one of the three types of escrow accounts. The resources from the escrow account will be paid to the developer after completion of the investment (in the case of closed escrow account) or after completion of a stage of the investment (in the case of open escrow account or open escrow account with insurance or banking guarantee). It can be expected that the most frequently used solution will be open escrow account<sup>3</sup>. In this case, the payment of the part of resources occurs after completion of a specific stage in advancement of construction works (adequately to its level) after controlling it by the bank. With closed account, the payment of the resources deposited occurs once, but only after transfer of rights to flats or houses on purchasers i.e. at the stage that ended the whole investment. Additional guaranty is supposed to protect the purchasers in case of a company's bankruptcy. This solutions is most likely to be commonly used. Furthermore, in the event of developer's bankruptcy, only the people that concluded the preliminary agreement in the form of the notarial deed will be best protected since presence of the solicitor improves the safety of transactions, but preparation of the preliminary agreement in the form of the notarial deed means additional costs for purchasers.

Changes implemented by the Developers Act with respect to the previous status are presented in Table 1.

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<sup>3</sup> Minimum payment for starting an open escrow account in Bank PKO BP (according to the information provided in the bank's website [www.pkobp.pl](http://www.pkobp.pl)) was PLN 4,500 as of January 1, 2012 whereas the cost of closed escrow account was PLN 3,600.

Despite implementation of particular legal regulations, new developer's act raises much controversy and reservations e.g. with respect to escrow account i.e. opportunities for using alternative forms of protecting the purchasers of flats or through banking escrow account, providing almost unlimited control of the developer's sector by the banking sector.

**Table 1.** Comparison of the previous status and changes implemented with new act on protecting the rights of purchasers of developer's flats

No. Previous status	Changes after April 29
1. Preliminary agreement is not obligatory to be signed in the form of the notarial deed	Preliminary agreement must be signed in the form of the notarial deed and claims of purchasers should be considered within the <u>mortgage register</u>
2. Lack of protection of the purchasers in the case of bankruptcy of developer, making them "stand in a long queue" to get the money back after liquidation of the bankruptcy	Payments of customers for the real estate built are excluded from the bankruptcy estate and can be also guaranteed by the insurer and banks
3. Escrow account is not obligatory	<u>Escrow account is obligatory</u>
4. Conditions of resolving the contract between developers and purchasers are determined individually	Conditions of concluding the contract between developer and purchaser are contained in the act
5. Developer provides information about the company and investment with limited scope	Developer is obliged to prepare a comprehensive information brochure about the investment, previous achievements and financial standing

Source: Turek (2012)

It is banks that decide who should be assigned the escrow account and whether it should be open or closed. Furthermore, in the case of an open escrow account, banks are obliged to transfer resources to the developer's account. However, this is possible after previous inspection of the documentation and completion of a particular stage in realization of the initiative. For prudential reasons, banks are allowed to request making several independent inspections of the state of realization of a particular initiative (obviously, at the expense of the developer).

Home Broker and Polish Developer Association conducted a survey among the companies that built anonymous flats concerning the hierarchy of problems and barriers the developers have to face in their activity (Siwek, Turek/Home Broker, 2012). The survey concerned the macroeconomic situation, administrative barriers and market conditions. The evaluation was

conducted on a scale of 1 to 5 (1 – the question does not represent a problem, 5 – the question represents a big problem).

The results of the survey show that 3 groups of problems are dominant:

- present macroeconomic conditions:

- unstable economic conditions: 3.93 indications (78% of the respondents),
- danger of decline in prices of real estate: 3.76 indication (75% of the respondents),

- administration barriers and risk of decline in prices of flats:

- administrative procedures of obtaining the building permission (including development conditions if there are no Local Plan of Spatial Development): 3.85 indications (77% of the respondents),
- frequent changes in administrative procedures connected with construction process: 3.56 indications (71% of the respondents),
- frequent changes of fiscal regulations: 3.27 indications (65% of the respondents),
- risk of a decline in the prices of flats: 3.75 indications (74% of the respondents),

- market conditions:

- achievement of the required level of pre-sale of the project before payment of the first tranche: 3.27 indications (65% of the respondents). However, according to developers pre-sale represents a barrier for financing of developer's activity since reaching the required level of pre-sale of project before payment of the first tranche of banking financing received the average score at the level of 3.27 points. According to the new act, developers, before obtaining the funds from financial institutions, are obliged to conclude preliminary agreements to sell from 10% to 30% of flats. This high assessment of this aspect of business activity demonstrates that the requirements imposed by banks are often difficult to meet by developers. Therefore, as many as 53% of the enterprises that built flats did not use banking financing. The funds are obtained in these cases from the own capital or e.g. payments of customers,
- finding an attractive land: 3.20 indications (64% of the respondents),
- obtaining financing for a project: 3.17 indications (63% of the respondents).

As results from the analysis of the results of the survey:

- macroeconomic situation represents the main threat to the developer's sector. It is manifested in particular by a reduction in the demand due to the reduced number of the mortgage loans granted, which represents a serious problem for the whole construction sector,
- on the second position, developers mentioned administrative barriers which still represent a serious threat that inhibits investments,

- insignificantly fewer problems are caused by market conditions, especially obtaining financing of developer's projects. The problem becomes very important at the moment of implementation of the developer's act that limits the access to these loans.

In light of regulation of the mechanisms, National Real Estate Market (2011) aimed at improving credibility of the primary housing market and its organization and amended Recommendation S that concerns good practices in terms of granting mortgage loans, minimum own contribution in the case of applying for a mortgage loan amounts to 5% of the purchased flat or a house from beginning of the year 2014. According to the recommendations of the Financial Supervision Commission, the minimal own contribution in 2015 will be 10%, followed by 15% in 2016 (or 10% after purchasing an additional policy) to reach the target value of 20% (or 10% for insured loans) in 2017.

With this respect and particularly according to a new Developers Act, it becomes very important to protect the purchasers of the flat or house from losing the money paid in the case of the developer's bankruptcy in order for them not to become the developer's current assets. The pre-sale of flats before starting construction investments or in the middle of this investments causes, according to the new developer's agreement, that:

- the purchaser has better choice of flats and houses sold within a single investment,
- the purchaser of the real estate has an opportunity to withdraw from the contract in the case of developer's being unable to ensure updating or changing information in the information brochure of the developer's company,
- benefits to the purchaser of the real estate being built include stability of the price, which, in light of the results of the survey, represents a serious problem for developers since, on the one hand, developers are protected from the fall of prices and, on the other hand, they incur the risk of the increase of costs during realization of the investment. However, depending on the content of the developer's agreement, the final price can be sometimes higher than the primary price,
- while concluding a higher number of developer's agreements, developer increases the number of flats sold within the pre-sale if a particular project in the real estate market is sold within the escrow account,
- through pre-sale, the developer:
  - earns greater financial revenues,
  - is able to repay the loan more efficiently,
  - is exposed to much lower risk that the investment will not be sold at the assumed prices, producing the expected income.

In order to counteract the effect of another threat i.e. the market risk of competition, developers offer interesting gratuities to prevent a decline in the rate of sales and correction of prices of flats. Instead of reducing prices for flats, developers guarantee free finishing of the interior, goods vouchers, radical reduction in prices of parking places or they offer attractive schedule of payments.

Therefore, pre-sale of real estate performed through developers' agreement as a legal instrument is beneficial for both developer and purchaser of the real estate. However, it has also a small drawback compared to the pre-sale of other goods: long period between concluding the agreement and obtaining the goods ordered.

In general, pre-sale generates high risk if it does not result from the new Developers Act (Thornhill, 1993). This is connected with not obtaining the goods the purchaser paid for i.e. the real estate. The determinant of this risk is time since the longer the time between a pre-sale and transition of the real estate, the higher the risk of unexpected events (financial problems of the developer leading to delays or bankruptcy, problems with subcontractors, with administration and other participants in the real estate market).

The risk for purchaser is eliminated in light of the new Developers Act by the escrow account which ensures that pre-sale is safe.

Therefore, it should be emphasized that, considering the benefits for purchaser and developer that result from the pre-sale of flats within the escrow account, pre-sale limits the market and financial risk of the developer while it reduces the risk of losing the resources of the purchaser paid within the pre-sale.

## **5. Conclusion**

The analysis of risk of developer's activity in the context of selected economic indices that stimulate behavior of participants in the real estate market and legal regulations implemented with the new Developers Act demonstrated the requirement of pre-sale of housing resources built before the payment of the first tranche of banking financing at the level of 10% to 30% of flats.

Pre-sale of flats offers benefits to both purchasers and developers. For developers, the pre-sale limits the market risk and financial risk of a particular investment. In light of the new act, pre-sale also increases the safety of the purchaser, especially in case of the developer's bankruptcy.



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# THE DEVELOPMENT AND IMPORTANCE OF SMALL AND MEDIUM ENTERPRISES IN THE POLISH ECONOMY DURING THE ECONOMIC SLOWDOWN

**Anna Nijakowska-Augustyn<sup>1</sup>**

## **Abstract**

*The purpose of this article is to discuss the condition of the sector of small and medium-sized enterprises (SMEs) and its importance in the Polish economy during the economic slowdown. The SMEs around the world play a significant role in the economic growth of many countries, as well as in the job creation or in the development of selected sectors or whole countries. The paper presents a classification of SMEs and the current state of the SME sector in Poland. In addition, the study attempts to prove that this sector, currently represents a significant segment of the Polish economy in the context of the micro- and macro-economic factors, especially during the economic downturn.*

**Keywords:** *SME sector, economic slowdown, importance of SMEs*

## **1. Introduction**

In the second half of 2008 the crisis hit the financial markets and contributed to the economic crisis in many countries and to the slowdown of the Polish economy. In 2012 the economic downturn was felt again both in Europe and in the rest of the world. The financial crisis is identified with a dynamic increase in the scale of the insolvency of banks and companies in a way that significantly exceeds the level of the phenomenon observed in previous periods. It is also closely connected with the economic crisis, which is associated with a decrease in production, with an increase in corporate bankruptcies as well as with a fall in employment in the economy (Puszer 2012, pp. 11-12).

The SME sector constitutes the basis of the modern economy. It plays an important role in the economic growth of the country, in the job creation or in the development of many sectors of the economy. Thus, the improvement of the condition of the national and regional economies depends on the development of this sector. In Poland, as in the economies of Western Europe

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or both Americas, the SME sector is referred to as „the engine of growth”, while it is often associated with the negligible interest or study of its needs and expectations (Bober i Kalupa, 2007, p. 25). World experience shows that countries characterized by dynamic economic development are based on the free-market economy, in which the predominant business form is private property based on the freedom of establishment and in which the functioning of the SME sector is essential for the proper economy development. Year by year the importance of the SME sector in Poland has been showing an upward trend and it results in a high participation of SMEs in the GDP (they generate almost 50% of GDP) or in the growing number of people employed by the sector concerned. Small enterprises develop their businesses mainly on a local scale (Szreder, 2000, p. 177), but some of them also play an important role in the regional development and even successfully compete in the international arena contributing to the export increase and the development of globalization (Bąk and Kulawczuk, 1999, pp. 5 – 8). Due to their high flexibility, SMEs have a chance to compete even with the largest enterprises, among others thanks to their great abilities to control costs and their mitigation, as well as to the high motivation of owners and employees of those companies (Stankiewicz, 2002, p. 36).

The primary aim of this article is to analyze the selected aspects considered in the SME sector against the background of the changes that occurred in Poland in the years 2008 – 2012 as well as to discuss the condition of this sector in the context of its importance during the economic slowdown. Therefore, a hypothesis was formulated which says that the SME sector during the economic downturn plays a key role in the micro- and macroeconomic growth of the national economy.

This paper is mainly based on reference books and papers, partly theoretical, as well as statistical data from various sources (such as Central Statistical Office, Polish Agency of Entrepreneurship Development). The first section of the paper presents the criteria according to which the assignment of the companies to the SME sector was made. What is more, it presents the size of the sector in the period of analyzed economic downturn. It then attempts to identify the importance of SME sector to the economy of the entire country considered in the context of micro- and macroeconomic factors, particularly in the period of the economic slowdown.

## **2. The character of the SME sector on the Polish market**

The enterprise is currently the most common form of an economic organization that participates in the market exchange in an orderly and systematic manner. The Freedom of Economic Activity Act of 19 November 1999 has replaced

the business entity term that was used in the previous Act of 1988 as an entrepreneur (Journal of Law No. 101, item 1178, year 2000 No. 86, item 958 and No. 114, item 1193 as amended). The company is “an entity that conducts a business activity and tends to meet the needs of other social actors (individuals or institutions) by the production of products or services, considering the fact that such activity is motivated by the desire to obtain material benefits and is managed independently at the owner’s or owners’ risk” (Sudoł, 2006, p. 37).

Enterprises are classified according to various criteria but one of the most important is their size. In this regard, the most frequently mentioned division is that of small, medium and large businesses. Additionally, amongst small entities microenterprises are being singled out.

The definition of small and medium entrepreneurs is contained in Articles 54 and 55 of the Freedom of Economic Activity Act (Journal of Law 1999 No. 101, item 1178 as amended). According to the Act, a small entrepreneur is an entrepreneur that in the previous fiscal year employed on average less than 50 employees and achieved net revenue from sales of goods, products, services and financial transactions not exceeding the PLN equivalent of EUR 7 million or total assets of its balance sheet at the end of the final year does not exceed the PLN equivalent of EUR 5 million. However, the concept does not include a company in which entrepreneurs other than small ones hold more than 25% of deposits, shares and rights to more than 25% share in the profits or more than 25% of votes in the general meeting of shareholders.

The act also specified the definition of medium-sized enterprise, which is the entity that in the previous year employed on average less than 250 employees and achieved net revenue from sales of goods, products and services and financial transactions exceeding the PLN equivalent of EUR 40 million or total assets in its balance sheet at the end of financial year does not exceed the PLN equivalent of EUR 27 million. The entrepreneur in which entrepreneurs other than small and medium hold more than 25% of the of deposits, shares and rights to more than 25% share in the profits or more than 25% of votes in the general meeting of shareholders, was not considered as a medium-sized one.

In the case of an entrepreneur operating on the market for less than a year, it was classified as small or medium-sized according to the size of average monthly employment for the last complete month of its functioning.

The regulations defining the SME sector were changed in paragraphs 103 – 110 of The Freedom of Economic Activity Act of 2 July 2004 (Journal of Law 2013 item 672 as amended). The size of the employment as well as the amount of annual net sales or the sum of assets remained a criterion of distinguishing the size of the companies. The act still includes three categories of enterprises, namely micro-, small- and medium-sized. A microenterprise

is the one that employed on average less than 10 employees in the last two years and reached the annual turnover not exceeding the equivalent of EUR 2 million, or the sum of assets not exceeding EUR 2 million. Small enterprises are entities employing respectively less than 50 employees and reaching the annual turnover or the sum of assets not larger than the EUR 10 million. When it comes to medium-sized entities, they employ respectively less than 250 people and generate annual turnover not exceeding EUR 50 million, or total assets less than EUR 43 million.

In the case of an entrepreneur operating on the market for less than a year, its expected net turnover from sales of goods, products and services and financial transactions, as well as the average annual employment are estimated on a basis of the data for the last period, documented by the entrepreneur.

The introduction of the definition of microenterprise and the change of the definition of small and medium entrepreneurs in relation to the content of The Freedom of Economic Activity Act of 19 November 1999 (Journal of Law 1999 No. 101, item 1178 as amended) was a result of the recommendations of the Commission of 6 May 2003 (J. L. of the European Community No. L 124z 20/05/2003). The inclusion of microenterprises to the SME sector results from the fact that in Poland the number of entities employing up to nine workers exceeds 3.5 million. The SME definitions adopted in the Polish legal system constitute the basis for granting the state aid that is necessary for the development and survival of businesses discussed.

Broader recognition says that the category of SMEs should comprise the enterprises which employ a relatively small number of employees, have relatively little capital and whose owner is usually the manager. Such approach eliminates complex administrative – bureaucratic structures. Such companies also have a small share in the market, or are financially and legally independent from other entities (Krajewski, 2004, p. 7). However, in practice it was accepted that the main criterion for the companies defining, there are quantitative criteria which have been mentioned above.

Micro, small and medium-sized enterprises are the driving force of the European economy as they are a basic source of employment and play a major role in the process of market competitiveness increase. The great share of SMEs in the economy affects the distinct improvement in the functioning of the mechanisms of market competition. Furthermore, an economy based mainly on a large number of small enterprises which are acting effectively is possibly a condition of effective functioning of the market (Kamrowski, 1998, p. 293). SMEs contribute also to the development of the local governments and therefore to the improved quality of life of inhabitants because of the better and cheaper goods and services offered. Therefore, local and regional

governments are taking the sequence of the operations related to the support of SMEs.

Analyzing the importance of SMEs for the development of the national economy it should be emphasized that micro, small and medium-sized enterprises currently constitute a majority of all business entities in Poland. The establishment of the company in the SME sector, especially of microenterprise, is relatively simple and does not require high financial outlays, at least at the beginning of the activity. In 2012 the companies from SME sector constituted 99.8% of all subjects which actively operated on the market, namely microenterprises constituted 95.8% of all enterprises operating on the market in Poland, small entities accounted for slightly more than 3%, while medium-sized enterprises for about 0.9%. Analyzing the structure of enterprises, a dominance of micro subjects is clearly seen. Detailed numeric characteristics of entities from the SME sector are presented in Table 1.

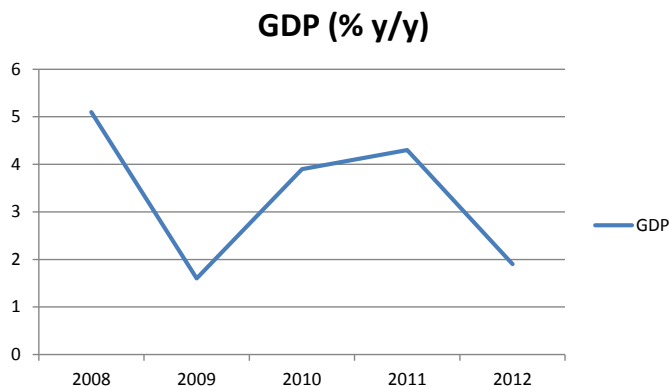
**Table 1.** Total number of enterprises operating in Poland in the years 2008 – 2012 including the small and medium-sized business sector (figures in thousands)

Enterprises	2008	2009	2010	2011	2012
Total	1 788.3	1 673.5	1 726.7	1 784.6	1 794.9
SME sector, including:	1 785.2	1 670.4	1 723.5	1 781.4	1 791.8
Micro-sized	1 714.8	1 604.4	1 655.1	1 710.6	1 719.62
Small-sized	54.3	50.2	52.6	55.0	57.1
Medium-sized	16.1	15.8	15.8	15.8	15.5

Source: Self-study on the basis of PARP (2013), p. 20.

The data presented in Table 1 allow us to conclude that in the period considered, despite minor fluctuations, all categories of enterprises affected the growth trend. Although the difference between the general quantity of companies operating at that time on the market basically did not change, it should be noted that the increases are most distinct amongst enterprises employing up to 49 persons. In the number of all companies, microenterprises have the biggest participation level, despite its visible fall in 2009, as in the case of other types of businesses. This fall should be connected with the economic slowdown that took place at that time. The reason for the slowdown was, without doubt, the economic downturn since the second quarter of 2007 in the U.S. and in the euro zone due to the increasing financial crisis, which affected adversely the economies of many countries. The following years show a gradual improvement and increase in the number of entities operating on the market, as well as the strengthening of the position of microenterprises,

especially between 2010 and 2011 which brought economic recovery and improvement in the business environment, which in turn resulted in improved companies performance and the increase in the number of active entities. Unfortunately, in 2012 there was a sharp slowdown in the economic activity of national economy resulting in deterioration of macroeconomic determinants of running a business. In 2012 the real growth rate of gross domestic product decreased to 1.9% comparing with growth rate on the level 4.3% in 2011, as illustrated on Figure 1.



**Figure 1.** GDP growth in Poland in the years 2008 – 2012.

Source: Self-study on the basis of Eurostat data.

Unfavorable fluctuations in GDP growth does not influence negatively the number of companies, because in the analyzed period, the number of business entities operating in Poland was characterized by the growing trend – in 2009 there was a visible decrease in the number of entities in comparison to the previous year, but in 2012 positive dynamics was observed compared to 2011.

The share of micro enterprises in the total number of companies in Poland is very high, because in the entire study period they accounted for about 96% of the population. Microenterprises indicate the high growth rate of increase, among others, because they have low capital intensity, what is more, they rely on the low-skilled labor (PARP. Raport o stanie sektora..., 2013, p. 21). The increase in the number of microenterprises in recent years is also combined with the effect of economic slowdown which could speed up the decisions of many persons connected with the foundation of the company when they lost their jobs.

Another important group of companies in the Polish economy, in terms of the size, were small entities because their number amounted to an average of 3% of the total number of enterprises. Moreover, the number of such entities



clearly increases substantially in the entire period of research, and as in the case of microenterprises, it should be attributed to the fact that they can be simply established. Medium-sized enterprises made the smallest part of the whole number of enterprises because their share in the population totaled approximately 0,9% in each period.

### **3. The role of the SME sector in the Polish economy – analysis of the selected aspects**

The conviction of the important role of the SME sector for the whole economy is common. Enterprises classified into the SME sector are mostly common companies in Poland. The significance of the SME sector for the economy of the entire country is great which is influenced by many factors considered in the micro and macro scale. Enterprises from the SME sector set largely the frames of socio-economic development. They have an impact on the various segments of the economy and on entities, and ultimately, also on achieving maximum values of macroeconomic indicators, as well as on the changes in local and regional markets (Bera, 2010, p. 388). The SME sector affects economic, social and political processes of contemporary market economies around the world (Steinerowska-Streb, 2012, pp. 18-21). On the other hand, H. H. Bass (2006, pp. 10 - 11) draws attention to its substantial role in the job creation, to generating the innovation, or in to the integration of the national economy with the world economy.

Examining the chosen economic sizes in relation to enterprises operating in the SME sector it should be emphasized that during the period covered in this paper, i.e. during the years 2008 – 2012, the global economy was struggling twice with the problem of economic slowdown, firstly in 2009, and then again in 2012. In this connection, the author made an analysis of the selected and, in her opinion, most interesting figures in relation to the enterprises operating in the SME sector taking the macroeconomic situation of the country into account.

#### **3.1. The share of SMEs in GDP creation**

The importance of the SME sector in the economy should be examined among others through the prism of the measures of economic growth. Small and medium-sized enterprises remain the driving force of the Polish economy. The share of such enterprises in GDP creation is the basis of the above-mentioned measures. According to data obtained from Central Statistical Office (GUS) presented in Table 2, companies in Poland generated 71.8% of GDP in the year 2011. This result was about 0.5% lower than in 2009 when a strong economic

downturn took place. The share of SMEs in the creation of the gross domestic product amounted to 47.3%. Micro-enterprises created every third zloty (29.4%), small-enterprises every thirteenth (7.8%) and medium-sized only every tenth (10.1%) (PARP. Raport o stanie sektora..., 2013, p. 14). In recent years we could observe that the share of SMEs in GDP creation remained on a rather stable level, despite the fact that the consolidation process is visible on the market and it leads to the strengthening of the position of large enterprises. Maintaining a high share of SMEs in GDP creation in the considered period confirms that even during the economic slowdown, such entities are very important links in Polish economy.

**Table 2.** The share of enterprises in GDP creation

Year	SME Enterprises					
	Enterprises total	Total	Micro	Small	Medium	Large
<b>2007</b>	70.80%	47.30%	30.40%	7.20%	9.80%	23.50%
<b>2008</b>	71.10%	47.20%	29.90%	7.40%	9.90%	23.90%
<b>2009</b>	72.30%	48.40%	30.40%	7.90%	10.10%	23.90%
<b>2010</b>	71.60%	47.60%	29.60%	7.70%	10.40%	24.00%
<b>2011</b>	71.80%	47.30%	29.40%	7.80%	10.10%	24.50%

Source: Self-study on the basis of PARP (2013), p. 16.

The share of SME sector in GDP creation is a commonly accepted ratio of the economic growth and a measure of the importance of this sector in the national economy, however, it is not possible to overlook that with reference to the small and medium-sized business sector, it has a number of defects, i.e.:

- Difficulty with the calculation of the real result of the SME sector business activity, particularly in family enterprises in which determining the cost and working hours of family members is often impossible,
- The final level of GDP growth is distorted by the significant share of black economy in the SME sector,
- Lack of authoritative statistical quantities dedicated especially to microenterprises.

As a result, the degree of the influence of the SME sector on GDP creation is in some way limited, although definitely indisputable (Bednarz and Gostomski, 2006, p. 25).

### **3.2. SME sector as a major employer**

The employment growth is one of the consequences of the increase in the number of enterprises, but also of comparatively favorable macroeconomic situation of Poland and the satisfying financial standing of Polish enterprises in the analyzed period. Although the number of employees in Poland is highly dependent on the economic situation in other EU member states due to the high mobility of workers, it should be emphasized that comparing to EU countries, the economic situation of Poland is unusually good in terms of the past few years. The economic slowdown in the EU which began in 2008 caused that the employment growth pace in the EU decreased significantly by 7%. In the following years a temporary improvement of the situation was noticed, that is why in 2010 the rate of employment growth in the economy across Europe reaching the level of 2.9% practically coincided with the level of the year 2007 (2.5%). In 2011 another fall in GDP growth took place, which implied a deterioration of the situation on the labor market and in comparison with the previous year, a decrease by 1.5% of the number of employees in the EU.

As of 31 December 2012, the number of employees working in Polish enterprises amounted to 9 million people; 6.2 million (69.9%) of them worked in SMEs. In the same year microenterprises employed about 3.4 million people, i.e. 38.7% of persons, who were employed by SMEs. Small-enterprises employed around 1.2 million people that represented 13.5% of total employment in the SME sector, while medium-enterprises employed over 1.6 million people and 17.9% of all employees of SME sector (PARP. Raport o stanie sektora..., 2013, pp. 27 - 31). Compared to 2011 there has been a slight decline in the employment level in the analyzed sector and in enterprises in general, although there has been a growth in small companies and simultaneous decrease in employment in medium-sized enterprises. The discussed trend was presented in table 3.

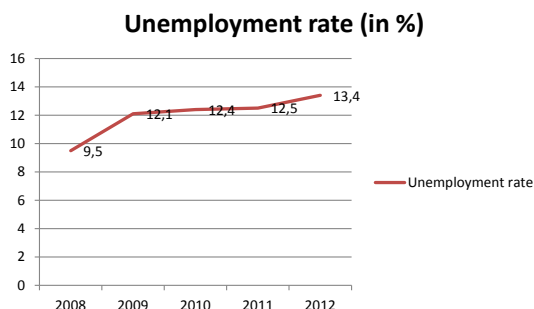
**Table 3.** The number of people working in Polish enterprises in general by size classes in the years 2008 - 2010 (figures in thousands of persons)

Enterprises											
Year	TOTAL	SME total	% of total	micro	% of total	small	% of total	medium	% of total	large	% of total
2008	9 494	6 620	69.73%	3 727	39.26%	1 195	12.59%	1 698	17.88%	2 874	30.27%
2009	8 830	6 230	70.55%	3 464	39.23%	1 123	12.72%	1 643	18.61%	2 599	29.43%
2010	8 859	6 192	69.90%	3 399	38.37%	1 143	12.90%	1 649	18.61%	2 667	30.10%
2011	9 029	6 337	70.18%	3 509	38.86%	1 182	13.09%	1 646	18.23%	2 692	29.82%
2012	8 937	6 266	70.11%	3 459	38.70%	1 204	13.47%	1 602	17.93%	2 671	29.89%

Source: Self-study on the basis of PARP (2013), p. 16.

Generally, taking the 5-year period into account, it should be noted that the number of people employed decreased by 5% from 6.62 million in 2008 to 6.27 million in 2012. The decline in the demand for the workforce in the analyzed period was probably caused by the adverse declines in GDP growth and in the limited consumer demand. However, even in spite of worsening on the labor market, Polish micro-enterprises play a huge part in the country as the major employer.

Decline in the number of workers, especially in 2012, corresponded to an increase in the unemployment rate. In the period analyzed the situation on the labor market deteriorated, therefore, according to Figure 2, unemployment rate gradually increased.



**Figure 2.** Unemployment registered in Poland in the years 2008 – 2012 (in %)

Source: Self-study on the basis of PARP (2013), p. 10.

The increase in unemployment during the study period was undoubtedly caused by the economic downturn, which resulted in downtimes in businesses, in many bankruptcies in collective redundancies and in new employment limiting.

Despite the fact that during the analyzed period the number of people working both in SMEs and in enterprises in general fell by approximately 6%, according to the European Commission (EC) forecasts, by the end of 2014 the number of employees in European companies will grow by more than 6 million people (4.6%) of which more than a million will work in the SME sector. Positive employment growth dynamic will also be visible in Poland. According to estimates by the European Commission, Polish companies will create over 600 000 jobs by 2014 and two-thirds of them (approximately 430 thousand people) will be working in micro, small and medium-sized enterprises (PARP. Raport o stanie sektora..., 2013, p. 28).

### **3.3. The investment activity of SME sector**

Relatively positive economic situation of Poland in the period 2008-2012, has had an impact on the investment activities of enterprises. In 2012, capital expenditures of enterprises totaled PLN 154.9 billion, which means a decrease of 4% compared with 2011. SMEs investment expenditures accounted for 48.1% of all investments of companies. Compared to the year 2011, the investments of SMEs in 2012 decreased by around 8%, and in relation to the year 2010 it increased by 4.5%. However, throughout the period of study, there has been a continuation of SMEs investment expenditures at a similar level. Taking the economic downturn into account, this fact should be assessed positively. It is worth emphasizing that the main burden of investments of SMEs, more than 40%, is borne by the medium-sized entities, which represent only 0.9% of all the companies functioning in the Polish economy. It is also interesting to note that the greatest growth in investment dynamics was noted in micro-enterprises, in which during the investigation period, investments recorded a significant increase, while small and medium-sized enterprises recorded a decline. It should also be noted that the year 2009 brought a reversal of the dynamics in 2008 and listed in previous years. It is also interesting that the SME sector is dedicating a comparable amount of funds for investment activities in relation to large enterprises. The value of investment expenditures of SMEs in 2012 amounted to PLN 74.5 billion, whereas in the case of large entities it amounted to PLN 80.4 billion. In the case of SMEs expenditures were lower by 8% comparing with the year before, while in the case of large entities the amount was basically unchanged (Table 5).

**Table 5.** Expenditures on business investments (in million PLN)

Enterprises											
Year	Ogółem	SME Total	% of total	micro	% of total	small	% of total	medium	% of total	large	% of total
2008	160 540	74 309	46.29%	20 356	12.68%	19 011	11.84%	34 942	21.77%	86 231	53.71%
2009	143 751	69 075	48.05%	21 853	15.20%	16 416	11.42%	30 806	21.43%	74 676	51.95%
2010	141 939	71 323	50.25%	24 848	17.51%	16 877	11.89%	29 598	20.85%	70 616	49.75%
2011	161 240	80 824	50.13%	28 282	17.54%	18 757	11.63%	33 785	20.95%	80 416	49.87%
2012	154 853	74 489	48.10%	24 370	15.74%	17 332	11.19%	32 787	21.17%	80 365	51.90%

Source: Self-study on the basis of GUS (2012).

The analysis of the data in the table shows that most of the new funds for investments, despite noticeable slowdown, was allocated by microenterprises, in which during the investigation period, expenditures have recorded almost 20% increase from the PLN 20 million in 2008 to more than PLN 24 million in 2012. Other types of companies noticed a decline in investment spending. Small enterprises have reduced purchases by 9% during the whole period, so at the end of 2012 they amounted to more than PLN 17 million, and the medium – sized entities spent in the year 2012 more than 6% less than in 2008. It should also be noted that the year 2012 brought a reversal of the positive dynamics, which was recorded from the year 2009. The analysis of the structure of capital expenditures in the SME sector allows to conclude that majority of the funds for investments were dedicated by medium-sized companies, because the amount of their expenditures is nearly a half of investment expenditures incurred by the SME sector in general.

### 3.4. The size of the foreign trade of SMEs

The contribution of SMEs to the integration of the national economy with the international economy is related to the degree of internationalization of these entities. The most commonly used measure of internationalization is the participation of the entire SME sector in the export and import of the country (Bednarz and Gostomski, 2009, p. 53).

The process of internationalization of SMEs still continues, and with the growth of the Polish economy, Polish participation in international trade grows as well. Clear connection of Polish economy and enterprises with the EU markets results in fluctuations in the value of exports, import and consequently depending on the economic situation in the EU and Poland. It was noticeable in 2009, when the economic crisis caused a collapse in foreign trade, as well

as in the years 2011 to 2012, when the economic downturn in Poland and the EU contributed to the reduction of import and export growth.

Due to the fact that the dynamics of Polish exports is strongly correlated with the GDP dynamics, both in the country and in the EU, as a result of the downturn in the EU in the year 2012 (fall in GDP of 0.4% in comparison with the 2011). The growth of Polish exports slowed down and there was a decrease in its growth pace from 7.3% in 2011 to 3.1% in 2012. It should be emphasized that export growth was not homogeneous in each group of enterprises, because in 2012 the nominal growth of exports was clearly higher in SMEs (13.5%) than in large enterprises (3.6 %). After stagnation in 2008 and 2009, SME sector rapidly increased turnover from export. In 2010 the nominal growth amounted to 13.3% and in 2011 to 15.5 %. Micro-enterprises increased export nominally by more than one-quarter (26.5%), the small entities by more than one-sixth (16.2%), and medium-sized ones by 9%.

Due to the import's explicit dependence on the export as well as the Polish import concentration - mainly on EU countries, in the analyzed period a strong correlation between the export and import dynamic growth and GDP in Poland and other EU countries was observed. A significant decline in the growth of the Polish economy (from 4.3% in 2011 to 1.9% in 2012) and in demand, especially investment, resulted in a decline in import growth (from 104.8% in 2011 to 97.0% in 2012).

As a result, the dynamics of Polish import reached in 2012 the lowest level since 2003, apart from the collapse in 2009, when imports fell by one-sixth (16.4%) in comparison with the previous year. In addition, vice versa, as in the case of export, the nominal import growth rate was significantly lower in SMEs (98.3%) than in large enterprises (103.9%). This deterioration came after a rapid increase in imports in 2010 and 2011, both in terms of SMEs (an increase of 13.1% and 20.1%) and large enterprises (20.2% and 17.4% respectively) (PARP. Raport o stanie sektora..., 2013, pp. 74-87).

So far, the characteristic feature of the Polish economy was a clearly stronger commitment to import than export. Under conditions of moderate level of competitive supply deals from Polish enterprises and at practically full openness of the economy to foreign competition, import activities of SME sector were more profitable than export. However, in recent years, a slow trend has been noticed, in which the value of import is close to the value of export. So far in 2008 the relationship of exports to imports was around 82%, but in 2012 it was at the level of 93%. It indicates a favorable trend in internationalization of Polish enterprises. It should be emphasized that small and medium enterprises have had a major impact on the size of the deficit of the entire Polish foreign trade in previous years, but in 2012 this impact has significantly strengthened.

### 3.5. The importance of SMEs in the microeconomic analysis

In the microeconomic analysis of the SMEs' importance, especially in terms of the contemporary economy, it is worth paying attention to their organizational and managerial characteristics. A beneficial effect on the activities of the companies in this field is exerted by (Nogalski, Karpacz and Wójcik - Karpacz, 2004, pp. 83 – 127):

- transparency of organizational structures,
- small number of levels of management,
- high-speed flow of information,
- the lack of anonymity of employees and of their functions.

Transparency of organizational structures is the result of their simplicity. New organizations, most of which are small companies, are based mostly on a linear structure regardless of the available resources and environment circumstances. From researches conducted by H. Mintzberg (1983, pp. 157-160), it appears that most of the small organizations maintain such a structure not only at the beginning of the development, but also in subsequent periods. This is, in turn, due to the simplified communication that is used in SMEs and is for this type of entities comfortable and effective at the same time.

Simple structure improves the level of management and increases managers' responsibility for their own decisions. The owner of a small or medium-sized enterprise takes final decisions about current operations, but also of its future existence. A positive feature of this type of entities is also the fact that there are no complications resulting from the separation of ownership from management. In conflict situations, there is no question of the responsibility division for many levels of management. Smaller companies mean less coordination problems, moreover a direct contact of the boss with subordinates is eliminating problems of anonymities of employees, of their functions or their responsibilities. Therefore, the management in the SME sector is easier than in large enterprises.

Specific managerial - organizational features of SMEs account for the fact that they are much more flexible than large organizations. Large companies are focused on the needs of the mass, while small companies in a relatively short period of time are able to respond to the environment changes and adapt to individual customer requirements. Thanks to all these features SMEs quickly fill in the market gaps, increase competition and improve the quality of the market mechanism.



## 4. Conclusion

The areas listed in the article are just a small set of examples of the influence of the SME sector on the national economy and on the nearest environment. The economic downturn and the high dynamics of changes in economic conditions in the years 2008 - 2012 were clearly felt both in Poland and abroad, in Poland, particularly in 2009 and 2012. Nevertheless, it should be noted that small and medium-sized enterprises continue to cope well on the market and continue to influence its development, resulting in, among others, the creation of new jobs or the creation of new investments. SME sector is currently the most numerous and the most rapidly growing segment of the national and global economy. It is also a very important source of economic growth in Poland.

The analysis we conducted allows us to positively verify the hypothesis raised. In the period of economic downturn which is clearly felt, the SME sector is of crucial importance, both at the micro-and macroeconomic level. This sector generates generally a half of Polish GDP, it is the largest employer, affects the development in the significant way and increases the innovations of the Polish economy through incurred investments, and finally it is the main source of competition and an animator of the market mechanism. What is more, it is able to quickly accommodate to changing economic conditions. In the period of the last five years, Polish SMEs have proven that they are able to positively affect the development of the economy and to mitigate the effects of the global economic slowdown.

It is worth remembering that the success of the entire Polish economy, the increase of its competitiveness on foreign markets, the reduction of unemployment in the country and improved public mood, are inseparably linked with the development of the sector of small and medium enterprises. Therefore, a positive back-up policy is needed which will be supporting the development of the small and medium enterprises, focusing on reducing barriers in their functioning, facilitating the access to sources of financing and supporting the development of new technologies and of entrepreneurial attitudes.

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# STRATEGIC AND FINANCIAL DRIVERS OF BUSINESS VALUE CREATION

**Iwona Zaręba<sup>1</sup>**

## **Abstract:**

*The main objective of any business activity is to create value for the owners. Taking into consideration the complexity of today's organizations and circumstances of growing customers' demands in which they compete, it is essential that the company's value-oriented goals are effectively managed at every level of the organization. A well-considered strategy can only be successful if the company's objectives are transparent, understandable for the employees and controllable. The article describes strategic and financial drivers of business value creation and presents methods of their communication across an organization, such as the Balanced Scorecard or KPIs.*

**Keywords:** *business value, value creation, free cash flows, capital structure, cost of capital, Balanced Scorecard, KPIs*

## **1. Introduction**

In the theory of company finance it is generally accepted that the main objective of any business activity is to create value for the stakeholders, of whom the most important ones are the owners of the capital – the investors. In the traditional microeconomic theory as well as in journalistic papers, the aim of running a business is often reduced to profit maximizing. This simplification is unjustified due to the fact that such an approach concentrates on present results while disregarding the structure of revenues and profits in time. Also, it omits the aspect of risk connected with managerial decisions, which has an impact on the value of a business. In particular, in the circumstances of increased competition and growing customers' demands it is essential for the managers to maximize efforts to seek opportunities for achieving a competitive advantage and maintaining value growth duration. As K.J. Hatten and M. L. Hatten stated (K.J. Hatten, M.L. Hatten, 1988): “the job of the managers is ultimately to create value” (p. 3).

Since value creation is the main purpose of any business, a question arises as to what factors carry value and how to manage business processes so that

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they are oriented on value creation. The value of a business can be created by different drivers, which recognition and controlling lead to enhanced efficiency of the company business activities. This process is strongly connected with the concept of value based management, hence formulation of a value-oriented strategy has to be preceded by identification of the key factors that influence the value of a business. Such drivers have to be effectively communicated in the organization so that every person in charge understands the company strategy and contributes to the process of business value creation.

The article discusses the key strategic and financial drivers of the business value and methods of their communication across an organization with the Balanced Scorecard and the usage of KPIs.

## 2. Strategic and financial value drivers

The necessary condition for value existence is an ability of a separated, organized set of items to generate income (Borowiecki, 1992, p. 27). But the sufficient condition for business value creation is the ability of a company to consistently maximize its risk-adjusted income generation.

In this sense, four types of value drivers can be distinguished, three of which are directly related to managerial decisions on operational, investment or financing issues and the fourth, general one, referring to a so-called period of competitive advantage duration (Rappaport, 1999, p.37, p.p. 78-79). The value drivers, according to the concept of A. Rappaport are presented in Table 1.

**Table 1.** Strategic business value drivers according to A. Rappaport

General	Operational	Investment	Financing
value growth duration (period of competitive advantage)	sales growth operating profit margin income tax rate	fixed capital investment working capital investment	cost and structure of capital

Source: developed on the basis of (Rappaport, 1999, pp. 78-79).

The Rappaport's strategic drivers of business value are factors which stay within the scope of a company's managerial board responsibilities. The Rappaport's set of drivers was broadened by the additional factors proposed by D. Walters (Walters, 1997, p. 711):

- customers loyalty,
- suppliers and customers engagement in the value creation process,
- operational leverage,
- strategic competence management.

Loyalty of customers and their engagement with suppliers in the value creation process enable reduction of costs connected with seeking new customers and eliminate the cost of changing suppliers.

The operational leverage depicts the structure of fixed and variable costs in the total costs of a company. In the case that business activities are profitable, the higher the fixed costs are, the higher margin the company achieves, as the variable cost per unit is lower. However, in the case of low sales volumes, the higher level of fixed costs is more difficult to cover.

As far as strategic competence is concerned, companies should take notice of the possessed human abilities that are essential for different types of activities – for instance, trading companies should focus on selling competence while production companies would be rather interested in creativity and innovation.

It stems from the above presented sets of drivers that the value of a business is conditioned by the factors which are either operational, investing, financial or intangible. All of them are connected with each other and together can build the value of a business.

The strategic value drivers are closely related to key financial factors which are used to evaluate the effectiveness of business undertakings. Based on them, guidelines for value creation can be developed. These are: free cash flows and the cost and structure of capital.

Contemporary approaches to value driven management are inclined towards the utilization of discounted free cash flows in forecasting future financial results and also – business valuation. In the income-approach methods of valuation, the present value of a company is calculated by adding the residual value to the sum of discounted free cash flows of a several-year period of detailed financial forecast. The concept of free cash flows is complex and contains the above mentioned: general, operational and investment carriers of value, while the cost and structure of capital determine the discount rate. In this way, discounted free cash flows reflect the Rappaport's business value drivers.

Free cash flows represent a surplus of cash generated from operating activities. It is 'free' cash which is left for investors after covering all operating costs and investment expenditure. The question then arises as to why free cash flows are usually adopted as value carriers instead of results calculated in accordance to accounting accrual basis. The subject literature explains this fact claiming that on the financial market, investors are more inclined to make their decisions on the basis of risk-weighted cash flows rather than accounting results (Cornell, 1999, pp. 90-92; Michalski, 2001, p. 49). Moreover, authors (such as: Copeland, Koller, Murrin, 1997; Rappaport, 1999) argue that managers who intend to create business value should focus on cash flows due

to the fact that they allow for consideration of future capital expenditure and are less distorted than the accounting financial result.

In order to present the above problem, A. Black, P. Wright and J.E. Bachman (1998) have conducted a research which consisted in comparing accounting results calculated by managers from different countries on the basis of the same financial data. The outcomes of the study are presented in Tab. 2.

**Table 2.** Accounting results calculated with different accounting rules application

Specification	The mostly expected result	Maximum result	Minimum result
Belgium	135	193	90
Germany	133	140	27
Spain	131	192	121
France	149	160	121
Italy	174	193	167
Netherlands	140	156	76
Great Britain	192	194	171
arithmetic mean	150.5714	175.4286	110.4286
standard deviation	23.50	22.76	51.08
coefficient of variance	16%	13%	46%

Source: developed on the basis of (Black, Wright, Bachman,1998, p. 43).

The research shows that there are high deviations between the accounting results calculated by different managers. The mostly expected results vary by 16% from the average and the coefficient of variance for minimum results amounts 46%. As P. Fernández (2006), remarks: “a company’s (...) net income is quite an arbitrary figure, obtained after assuming certain accounting hypotheses regarding expenses and revenues. On the other hand, its cash flow is an objective measure, a single figure that is not subject to any personal criterion”.

There are two types of free cash flows that can be distinguished:

- free cash flows for equity (FCFE), which constitute the difference between cash inflows and outflows in a given period that are left for the capital owners, and:
- free cash flows for the firm (FCFF), which are hypothetical cash flows for equity that a company would have if there are no debts.

Free cash flows for equity are calculated according to the below formula:

Net income  
+ Depreciation  
+/- Change in working capital requirements (decrease +, increase -)  
+/- Change in financial debt (increase +, decrease -)  
- Capital expenditures  
***FCFE***

Whereas free cash flows for the firm can be calculated as follows:

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Net income  
+ Depreciation  
+/- Change in working capital requirements (decrease +, increase -)  
+ Interest (1 – tax rate)  
- Capital expenditures  
***FCFF***

Thus, the difference between FCFE and FCFF is:

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***FCFF = FCFE -/+*** Change in financial debt + Interest (1 – tax rate) ,  
which means that in the case that there are no debts, the two types of cash flows are equal.

In practice, when focusing on the value of a business, the anticipated future free cash flows are taken into consideration in managerial decisions. Referring to the future results from different points of time requires discounting the values for the same time moment. Depending on the type of free cash flows, a different discounting rate should be used. In the case of FCFE the suitable discount rate is equity cost, whereas for FCFF it is the cost of total capital.

Business activity can be financed by the capital which is either own or borrowed. Own capital is provided by the business owners in a form of shares or retained profits, while borrowed capital has usually a form of loans, bonds, lease obligations or other payables. The diversity of financing methods depends on the company's needs and preferences, but also (Maćkowiak, 2009, p. 47) on: capital availability, flexibility, preferred financial leverage and last but not least – its cost.

The cost of capital is a fundamental issue in the company finance theory, a key factor in the income-approach methods of business valuation as well as methods of assessing investing projects (such as NPV, IRR).

Different definitions of the cost of capital are cited in the subject literature, such as for instance (Szczepankowski, 2007, p. 85):

- the anticipated, average rate of return on an alternative investment of a similar risk level,

- minimum, risk weighted rate of return which a company should generate from its assets in order to be accepted by the business owners (Weston, Copeland, 1992, p. 438),
- minimum profitability for which investors are willing to plough their capital into a project to achieve anticipated profits (Kufel, 1992, p.p. 37-38),
- minimum rate of return on the invested capital needed to retain a business value for the owners (Czekąła, Grzeszkowiak, 1999, p. 83).

It stems from the above definitions that the cost of capital is not an actual cost of capital invested in a business, but the anticipated by the investor minimum rate of return at a given risk level.

The concept of the cost of capital is vital due to the fact that in order to maximize the value of a business, expenditure has to be optimized and the cost of necessary capital – minimized. All decisions on planned investments require assessing the cost of capital needed.

There are several types of the cost of capital that can be distinguished on the ground of company finance theory (Szczepankowski, 2007, pp. 86-87). In general, the cost of capital invested in a business is the sum of the risk free rate and the business premium (Zarzecki, 1999, p. 177). The business premium reflects the investment risk of a particular undertaking and it is a factor which differs rates of return on public bonds, considered as risk-free instruments from risky investments in the shares of companies.

Another category is the cost of borrowed capital. It constitutes a demanded by a lender rate of return after the tax shield effect, which consists in reducing fiscal liabilities of a company as an effect of incurring costs of interests which are tax deductible. The cost of borrowed capital refers to alternative sources of financing available on the market, not the actual interest rate on the company's debts. It reflects the cost of changing the existing debts with a newly borrowed capital.

An important type of the cost of capital is the equity cost. It reflects the rate of return on the invested capital anticipated by the shareholders. Taking into consideration the order of satisfying claims – the priority of creditors before owners, equity cost is the riskiest and, as a consequence, the most expensive form of capital.

Equity capital can be calculated by the following formula (Zarzecki, 1999, p. 177):

**equity cost** = risk free rate + business risk premium + financial risk premium



The additional financial risk is related to uncertainty and instability of profits for the business owners and can be calculated as:

$$\mathbf{financial\ risk\ premium} = (1 - \text{tax rate}) \left( \frac{\text{cost of capital invested in business}}{\text{demanded rate of return on borrowed capital}} - 1 \right) \frac{\text{debt}}{\text{equity}}$$

The above approach to the equity cost is just one of numerous methods presented in the subject literature and used in practice. Another popular way of equity cost estimation is the method based on Capital Assets Pricing Model (CAPM).

In CAPM the risk of investing in shares of a company is divided into systematic (market) risk and unsystematic (specific) risk which refers to an individual stock. According to CAPM, the return on an individual stock should equal its cost of capital, which is calculated in the following way (Dudycz, 2005, p. 81):

$$\mathbf{equity\ cost} = \text{risk free rate} + \beta (\text{anticipated market rate of return} - \text{risk free rate})$$

In the model, the equity cost is the sum of the risk free rate and the equity market premium multiplied by a  $\beta$ -coefficient.

Owing to the fact that equity cost is an anticipated value, all parameters for the cost calculation have to be estimated. The problem refers to, in particular, the market risk premium and the  $\beta$ -coefficient.

The market risk premium, which is the difference between the anticipated market rate of return and the risk free rate, plays the key role in CAPM. The premium has to be estimated on the basis of historical data from a given period of time. According to A. Damodaran (1994, after Szczepankowski, 2007, p. 92) it should be at least a period of ten years. The exemplary risk premiums for different countries, by A. Damodaran are systematically updated on <http://pages.stern.nyu.edu/>.

CAPM introduces  $\beta$  as the relevant measure of specific risk. It describes relative volatility of a security, which means reaction of a stock price to changes of the market index (<http://www.investopedia.com/articles/06/capm.asp>).

Beta can be calculated on the basis of historical data by the formula:

$$\beta = \frac{\text{cov}(r, r_m)}{\sigma_m^2}$$

where:  $cov(r, r_m)$  means covariance between rates of return on a security and the market portfolio, and  $\sigma_m^2$  means variance of rates of return on the market portfolio. Interpretations of possible  $\beta$  values are presented in Tab. 3.

**Table 3.** Beta values interpretations

$\beta$ value	Interpretation
$\beta > 1$	Security price changes in the same direction that the market but it is more volatile
$\beta = 1$	Return on the security is the same as on the market portfolio
$0 < \beta < 1$	Changes of the market index cause changes of the security price in the same direction but less than the benchmark
$\beta < 0$	Security price changes in the opposite direction than the market

Source: author's elaboration developed on the basis of (Szczepankowski, 2007, p. 89)

The last but not least category of the cost of capital is weighted average cost of capital (WACC) which is the total cost of equity and borrowed capital, weighed by the share of each type in the sum of capitals. The level of WACC is a measure of the minimum accepted rate of return for all financing parties and it influences the present and future condition of a company. WACC is often applied for the purpose of business valuation and in value based management. It also plays a key role in economic value added (EVA) calculations (see also: Maćkowiak, 2009).

The structure of capital is, beside its cost, a factor influencing the value of a business. Capital structure means combination of equity capital and long-term debts, which constitute fixed capitals of a company. It informs about the level of long-term indebtedness. Capital structure is connected with a broader issue of financing structure which covers all liabilities of a company (Szczepankowski, 2007, p.p. 83-84). The relations are the following:

$$\mathit{financing\ structure} = \frac{\mathit{total\ liabilities}}{\mathit{equity\ capital}}$$

$$\mathit{capital\ structure} = \mathit{financin\ structure} - \frac{\mathit{short-term\ liabilities}}{\mathit{equity\ capital}} = \frac{\mathit{long-term\ liabilities}}{\mathit{equity\ capital}}$$

### 3. Communicating value drivers across organization

The Rappaport's strategic drivers of the business value are factors which stay within the scope of the managerial board responsibilities. However, in order to manage the company strategically, it is necessary to take into consideration

three different levels of strategic management. These are (Pierścioneck, 1996, p. 78-80):

- corporate level,
- business unit level,
- functional (departmental) level.

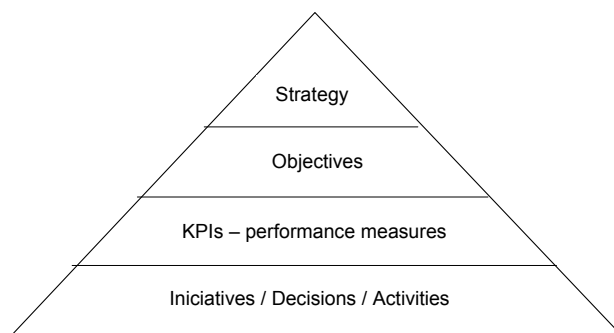
The corporate level deals with problems of development policy and allocation of resources. It manages businesses portfolio ensuring they are compatible with the corporate strategy. This level is, by nature, value-oriented and conceptual, whereas the other two are more concrete.

Managing on the business unit level consists in choosing the type of strategy which fits to the product or the business cycle. The strategic issues on this level are more practical. The managers of the business unit level develop tactics to beat the competition. They aim to achieve and sustain a competitive advantage for the products or services that are produced.

The third level of strategic management contains operational methods for implementing tactics (2<sup>nd</sup> level) and developing the general corporate strategy (1<sup>st</sup> level). The strategic issues at this level are related to functional business processes and value chain.

The central strategy of a company is formulated at the top of the organization and has to be effectively communicated from the top to the bottom. It is an important point of business value creation process because strategy itself does not drive financial performance – execution does (Lowy, 2013).

The Balanced Scorecard (“BSC”) is a method of describing the corporate strategy so that it is transparent and understandable by all people in the organization. It was first developed by R. Kaplan and D. Norton (see: Kaplan, Norton, 1992). BSC translates the value oriented strategy developed at the top of the company into more particular objectives, measures of performance (such as KPIs) and bottom-up initiatives, decisions and other operational activities (see Fig.1).



**Figure 1.** Utilization of Balanced Scorecard to describe the company’s strategy

The objectives which should lead to value creation as well as their measures are grouped into four perspectives (Świdarska, 2006, p.147-150):

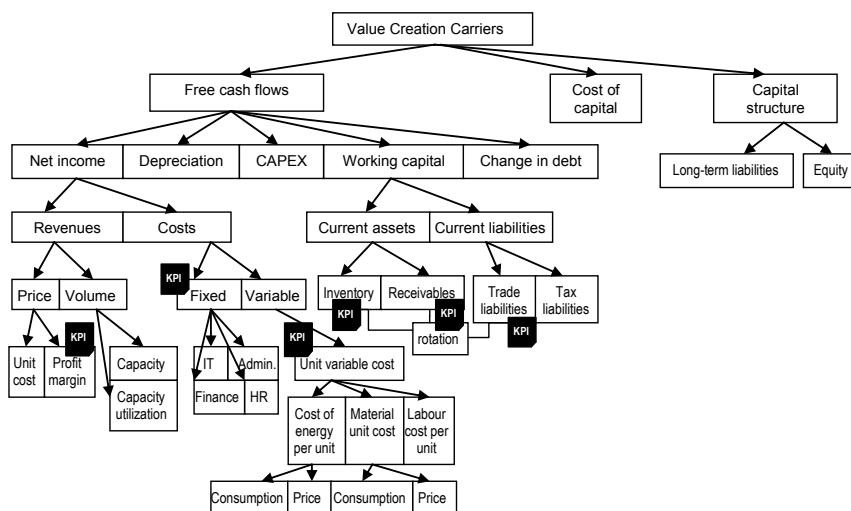
- financial – which contains financial goals, including the general objective of value creation. It answers the question of how we look to shareholders. The examples are: cash flows, sales growth, operating income, ROE, ROA, EVA;
- customer – describes the picture of how we are seen by the customers. It contains the most important – market goals and measures which depict the effects of the company activities in the field of customer relations. From this point of view, the key measures are: market share, percent of sales from new products, customer loyalty level, level of customer satisfaction;
- internal business processes – enables to control efficiency of the strategically essential processes which empower financial and customer objectives. The question that is asked in this perspective is “What must we excel at?”. The measures of internal business processes are such as: product quality, length of production process, unit cost, level of technological advancement;
- learning and growth – indicates the existing deficiencies in ability of people, IT systems and procedures which have to be amended. In this perspective the question is “How can we continue to improve, create value and innovate?” and the exemplary measure are: level of employees’ education, employee satisfaction, measures of IT systems flexibility, time to develop new generation of products.

The BSC focuses on the factors which are essential for achieving the business value growth and puts them together in a single report. Therefore, it is helpful to communicate the strategic goal of the company across the organization. The BSC can ensure that the managers of functional level steer in the same direction as the management board of the company. The value-oriented strategy formulated at the top of the organization can be described in a complex way by the usage of the Balanced Scorecard. The BSC enables us not only to communicate the main goal of value creation but also to control its accomplishment.

Communicating the value-oriented strategy has to accomplish two tasks (Gorzeń, Piernicki, Pniewski, 2008, p. 137). Firstly, it should help to inform effectively all employees of the value growth strategy and ensure it is understandable. Secondly, it is aimed at building motivation in people for strategy realization.

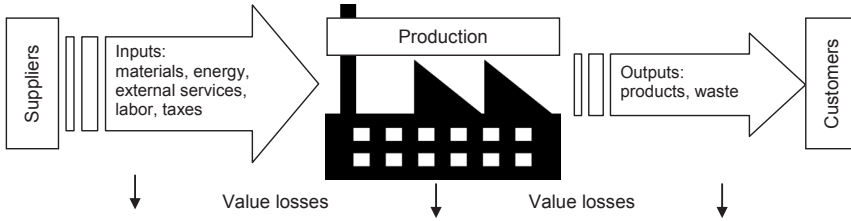
The so-called key performance indicators (KPIs) are a way of translating the company’s strategic targets so that they can be understood and manageable by all people in the organization. The company has to be broken down into

basic financial value carriers and for the chosen controllable ones, indicators of performance can be determined, as presented in Fig. 2. A set of well-considered KPIs is an instrument of setting objectives on the departmental level.



**Figure 2.** Value creation model with exemplary selected value drivers for KPIs  
 Source: Author's work based on the concept of (Gorzeń, Piernicki, Pniowski, 2008, p. 120).

There are three processes which connect KPIs to value creation (Sever, 2007): selection, formatting and communication. Selection of KPIs should be preceded by deliberation and discussion on the inputs, production, outputs and losses. This raises awareness of the business operational process and helps to identify value losses which occur at every stage of it (Fig. 3).



**Figure 3.** Value losses occurrence at each stage of the business process

In the process of KPIs selection it is essential to ensure that people who will later be responsible for chosen metrics are involved as much as possible. It is equally important that the people in charge are able to actually impact measures which are appointed to them.

KPIs formatting consists in choosing dimensions for the variables. It is useful to put four dimensions: prior period, actual, budget and target to see in a perspective about the past, the present, the plans and the possible best.

After selecting and formatting, KPIs have to be communicated to all their users. Good understanding of the KPIs as well as employees' awareness of their share in the process of value creation is essential to achieve the added value from introduction of the system of indicators. Presenting KPIs in a form of groups of charts is a useful and approachable way to communicate value-oriented strategy across the organization. Moreover, grouping of charts for departments which should cooperate together can facilitate removing barriers and enable for the process orientation. Good KPIs communication can change an organization culture by introducing a collaborative problem-solving language, it also helps employees to see themselves in a 'big picture'.

#### 4. Conclusion

The article depicts the strategic and financial drivers of business value creation and methods of their communication across the organization. Reassuring the above deliberations, an effective value-oriented strategy should focus on value drivers such as free cash flows as well as cost and structure of capital. However, developing a successful strategy that would ensure value creation, has to be effectively communicated from the top to the bottom. It can be achieved by

splitting the value-creation objective into factors which are understandable by the company employees, so that they can see their place and role in the whole process, because it is eventually people who create value. The usage of the Balance Scorecard and KPIs can ensure that the company's strategic goal is transparent and controllable at every level of strategic management.

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