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The contingency theory of management accounting and control: 1980–2014

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ABSTRACT

This article reviews the literature on the contingency theory of management accounting since the 1980 review by the author. It traces the expansion of this literature and critically outlines some of the major themes explored over this period. It argues that a mechanistic approach that will develop into a predictive mechanism for the design of optimal control systems is misguided. Rather the existence of management control 'packages' that are continually changing and developing requires studies that follow these changes over time and seek to explain the mechanisms that are observed to be deployed. The 'package' concept has not yet been taken seriously in the design of most empirical studies although this is fundamental to the design of future studies. That is, different elements of control system packages are developed quasi independently by different actors at different times and are only loosely co-ordinated. Full coordination is precluded for several reasons, most notably the rapid pace of change and the addition of new or amended systems at a faster rate than the coordination process can develop. It is suggested that the narrow view of contingency that relies on responses to generally applicable questionnaires needs to be replaced by a more tailored approach that takes into account the context of specific organizations.

1. Introduction

This paper provides an overview of the research on management accounting and control which has used a contingent perspective. It starts from my 1980 review of the topic (Otley, 1980) and seeks to bring this up to the present day.[1] However, there are a number of features that require clarification to define the scope of this review. First, the topic has broadened in its scope over the last three decades and it seems sensible to include aspects of management control systems (MCSs) which are used in conjunction with management accounting information rather than focussing solely on management accounting techniques. Second, management accounting has itself changed with a variety of 'new' techniques being developed and popularized, particularly in the 1980s and 1990s. Third, organizations have changed with traditional hierarchical forms being modified into flatter forms, and strategies which emphasize concentrating on a core business rather than attempting to encompass the whole supply chain within a single legal entity. Thus control systems are increasingly required to operate across organizational boundaries. Finally, the idea of contingency requires further clarification, as it can be argued that all research on these topics has to take a 'contingency' approach as it becomes recognized that universal solutions to problems in organizational control generally do not exist.

In the 1970s management accounting formed the centrepiece of many organizational decision-making and control approaches. Budgetary control was the dominant technique used and most of the early contingency-based research studies concentrated on the deployment and use of budgets. Indeed many of the early studies exposed the flaws that budgetary information possessed when used in a manner that did not acknowledge its limitations. More recently non-financial performance measures have increased in popularity and are seen as part of an overall control system, together with a variety of other control approaches which have little to do with traditional management accounting. For this paper it seems most appropriate to concentrate on the over-arching area of management control systems where much of the research takes an organizational approach. Decision-making, by contrast, tends to take an individual approach informed predominantly by psychology and this is covered in a separate review by Hall (2016) in this issue. However, the boundary is not always clear as some studies use both individual and organizational level variables, and focus on topics which include both decision-making and control, so there is some overlap.

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[1] From this point on I will refer to my own papers in the third person and put any personal comments in a footnote.

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The developments in management accounting began with the introduction of activity-based costing (ABC) in the early 1980s, although this concentrated on generating information for improved decision-making rather than control. However, it was rapidly followed by other techniques often lumped together under the general heading of strategic management accounting. Although this can be interpreted as an attempt by management accountants to maintain their presence at the centre of both organizational decision-making and control, it is also a convenient label to encapsulate the approaches that were developed during this decade. However, the dominance of accounting control was challenged in the early 1990s by the codification of what has become the most widely adopted technique in modern organizations, the Balanced Scorecard (BSC), which combined both financial and non-financial performance measures into a single integrated framework. The scope of management control increasingly began to include issues of both strategic and operational control that had been specifically excluded (for reasons of simplicity and convenience) by Anthony (1965) in his seminal definition of the field.

The context in which management accounting and control is practised has also undergone substantial change. Organizations have become less hierarchical and many have restructured themselves to focus on their 'core businesses', leaving more peripheral activities to be outsourced. Thus organizations now tend to be embedded into supply chains and new forms of control need to be developed in this situation (Anderson and Dekker, 2014).[2] These supply chains span several different legal entities with no hierarchical oversight, although there is often one large organization that dominates the other participants. These developments were reviewed in Otley (1994) but have continued to change subsequently. In particular, the general business environment has shown an increasing rate of change and competition, both locally and globally, which has caused a greater degree of uncertainty to become apparent. Finally, technological developments continue to drive change at an increasing rate, not least in the changes to business practice which have been made available by modern computer technology and the internet. At the very least this has led to increased environmental uncertainty and a breakdown in the (often implicit) predictive models on which control was based.

The idea of the role of contingency theory is also beginning to change. Whereas initially it developed from the idea that no universal solution to the problems of control was feasible, it hoped that empirical work would establish the key contingencies from which prescriptions to suit different sets of circumstance could be developed. However, research over the past four decades has come up with an extended list of possibly significant contingencies that are faced by organizations, many of which suggest conflicting recommendations. Even if research could be progressed on a much greater scale than in the past, it is unlikely that an overall contingency model could be developed to suggest optimal control configurations in all possible combinations of circumstances. And even if was to prove possible, the world would have moved on by the time the results were available. Contingency therefore has to be considered in a much more dynamic context than previously, which leads to the need to use more process-based models which examine the mechanisms of change and the implementation of modified forms of management and control.

This paper will therefore not attempt to perform a comprehensive review of all previous 'contingency' studies, of which there have been a number, most notably that by Chenhall (2007) which updates his 2003 review and this paper will not attempt to duplicate the detailed work he performs in that comprehensive chapter. Chenhall noted that *"the term contingency means that something is true only under specified conditions. As such there is no 'contingency theory', rather a variety of theories may be used to explain and predict the conditions under which particular MCSs will be found or whether they will be associated with enhanced performance."* (p. 191). He goes on to suggest that a much wider range of theories may prove useful, encompassing economics (both agency approaches and behavioural economics), psychology, sociology and information science. He also suggests that prior work has concentrated on traditional, functionalist theories and should move on to use more interpretive and critical views in future. This paper will analyze a number of practical and conceptual issues that appear to make it likely that traditional approaches to contingent theorizations have run their course and to argue that it will require different approaches to provide insightful and useful explanations of this complex subject.

2. What is contingency theory?

The idea of a contingency theory of management accounting began to develop in the 1970s in an attempt to explain the varieties of management accounting practice that were apparent at that time. It drew heavily on the contingency theory of organizational structure which had been developed over the previous twenty years to codify which forms of organizational structure were most appropriate to specific circumstances. The independent variables used to explain organizational structure were often transferred wholesale into the emerging theory of management accounting to explain the design and use of management accounting systems, with additional variables being added as the years progressed.[3] As Hopwood (1974b) had pointed out earlier, the design of a (management accounting) system and the design of an organizational structure are really inseparable and interdependent, although this important observation has tended to be neglected over the years that followed.

In his overview of the contingency theory of management accounting, Otley (1980) specifies that *"a contingency theory must identify **specific aspects** of an accounting system which are associated with certain **defined circumstances** and demonstrate an **appropriate matching**."* (p.413). This indicates three areas to which attention needs to be paid. First, what are the aspects of the management accounting system that are to be explained? In particular, are we concerned just with the existence of specific techniques in an organization, or also with the extent and manner of their use? Studies have tended to be rather arbitrary in their selection of the techniques they focus on, with little consistency between one study and another both in selection and measurement of variables connected with the accounting control system. Second, how are the defined circumstances to be selected? Again, although the contingent variables used by organization theorists have been extensively used here, often only a subset are used in any one study making comparability difficult. Finally, the definition of what constitutes an appropriate matching has caused significant difficulty over the years. At its most simple, existence has been taken as indicating such a matching, although this assumes that a long-run equilibrium has been achieved. More sophisticated studies have used some variant of firm performance to indicate whether an appropriate matching has been found, despite the likelihood that MCSs have only a small impact on performance, although the measures used

[2] See also Dekker, 2016.

[3] This led to an ambiguity in the role of organizational structure which was the dependent variable in the organizational theory, but an independent variable in the management accounting theory, if it was included. Evidently a risk of multicollinearity could exist if it was used together with the common list of explanatory variables.