



journal homepage: [www.elsevier.com/locate/emj](http://www.elsevier.com/locate/emj)

# How can management control system fairness reduce managers' unethical behaviours?

Pascal Langevin <sup>a,\*</sup>, Carla Mendoza <sup>b</sup>

<sup>a</sup> EMLYON Business School, 23 Avenue Guy de Collongue, 69134 Ecully cedex, France

<sup>b</sup> ESCP Europe, 79 Avenue de la République, 75543 Paris Cedex 11, France

## KEYWORDS

Management control systems;  
Ethics;  
Fairness;  
Justice;  
Slack;  
Data manipulation;  
Organisational commitment;  
Trust

**Summary** Empirical research has shown that as management control systems (MCS) put heavy pressure on managers to achieve their objectives, they may induce two types of unethical behaviour: creation of budgetary slack and data manipulation. Recently, studies have introduced Organisational Justice theory into the area of management accounting research and shown the positive effects of organisational justice on managers' attitudes and behaviours. However, few studies have systematically analysed how MCS fairness reduces unethical behaviours and which characteristics of MCS could increase managers' perception that they are treated fairly.

The purpose of the paper is to contribute to this research. It formulates testable hypotheses on how some specific dimensions of MCS can enhance perceived fairness, which in turn helps to reduce the creation of slack and data manipulation through increased Organisational Commitment and Trust in supervisor.

© 2012 Elsevier Ltd. All rights reserved.

## Introduction

Management control systems (MCS) are widely used in companies. They include all the mechanisms (strategic planning; budgeting; resource allocation; performance measurement, evaluation and reward; responsibility centre allocation; and transfer pricing) managers use to ensure that the behaviours and decisions of their subordinates are consistent with the organization's objectives and strategies (Anthony & Govindarajan, 2007; Merchant & Van der Stede, 2007). More specifically, "MCS provide information that is intended to be useful to managers in performing their jobs and to assist

organisations in developing and maintaining viable patterns of behaviour" (Otley, 1999, p. 364). Firstly, MCS help managers to make the right decisions by aligning their objectives with the company's global objectives, and by informing them of their performance so that they can take corrective action if necessary. Secondly, MCS are used to motivate managers: at the beginning of the year, they enable managers to negotiate their objectives and the resources necessary for their achievement; at the end of the year, managers' performance is assessed by comparing their results with the objectives. Organizations often link managers' material rewards, such as bonuses, to how well their unit achieves budgeted performance results (Van der Stede, 2000). The ability to meet budgetary objectives is thus a critical factor in managers' performance evaluation. In addition, managers whose units achieve their budgeted goals

\* Corresponding author. Tel.: +33 478 337 987; fax: +33 478 337 928.

E-mail address: [langevin@em-lyon.com](mailto:langevin@em-lyon.com) (P. Langevin).

may more likely see themselves as “winners” which is a source of psychological rewards such as self-esteem (Merchant & Manzoni, 1989).

However, instead of motivating managers and encouraging them to contribute to the achievement of company objectives, MCS may also induce unethical behaviours. In particular, creation of budgetary slack (e.g., Dunk, 1993; Merchant, 1985; Onsi, 1973; Schiff & Lewin, 1970; Young, 1985), and data manipulation (Bitner & Dolan, 1998; DeFond & Park, 1997; Merchant, 1989; Merchant, 1990; Merchant & Rockness, 1994; Umapathy, 1987) are two unethical behaviours largely observed in organisations.

Slack is generally defined as “resources and effort towards activities that cannot be justified easily in terms of their immediate contribution to organisational objectives” (March, 1988, p. 4). A common type of slack occurs when managers “negotiate highly achievable targets, that is, targets that are deliberately lower than their best-guess forecast about the future” (Merchant & Van der Stede, 2007, p. 183). When created during the management control process, slack is commonly called budgetary slack (Lukka, 1988; Onsi, 1973; Schiff & Lewin, 1970). MCS provide managers with opportunities for understating revenues and/or overstating costs. Such misrepresentation of managers’ true performance capabilities will frequently be to their advantage since it provides more readily achievable performance targets and increases their chances to obtain monetary (e.g., bonuses) and non-monetary (e.g., favourable evaluations, praise) rewards (Merchant, 1985; Merchant & Van der Stede, 2007).

The second type of unethical behaviour that researchers have examined is data manipulation. Management control systems include performance measurement mechanisms, which organisations use, during the year, to verify that results are in line with objectives and, at year-end, to evaluate managers’ performance. During these performance measurement steps, managers can try to look good by manipulating the performance indicators (Merchant & Van der Stede, 2007, p. 185). Data manipulation comes in two basic forms: falsification and data management. Falsification involves reporting erroneous data, whereas data management, also labelled earnings management, can be defined as “any action on the part of the management which affects reported income and which provides no true economic advantage to the organisation and may, in fact, in the long-term, be detrimental” (Merchant & Rockness, 1994, p. 79).

Management accounting research provides considerable evidence that these behaviours exist in organisations (Libby & Lindsay, 2010; Merchant, 1985; Merchant, 1990; Onsi, 1973). This is a problem because these behaviours distort the planning and performance measurement processes, motivate decisions that are contrary to the organization’s interest, and generate useless costs in the forms of unwarranted rewards. An important issue, yet not much addressed in the literature, is how to design MCS that avoid or, at least, limit managers’ propensity to adopt such behaviours. However, over the past decade, a few management control researchers have started to use the insights provided by research on organisational justice (Cohen-Charash & Spector, 2001; Colquitt, Conlon, & Wesson, 2001) to show that these unethical behaviours can be reduced when MCS are perceived

to be fair (Little, Magner, & Welker, 2002; Staley & Magner, 2007; Wentzel, 2004).

Therefore, our purpose is to combine the results produced by research in both management accounting and organisational justice in order to build a general framework (Figure 1) that identifies: (1) which MCS’ characteristics increase their perceived fairness, and (2) how MCS perceived justice<sup>1</sup> reduces managers’ propensity to create slack and manipulate data.

The contribution of such an endeavour is to help academics, as well as practitioners, better understand how to design and implement effective MCS.

The paper is organised as follows. In “Literature review”, we examine the literature to clarify what is known to date concerning the relationships between MCS components, MCS perceived justice and managers’ propensity to create budgetary slack or manipulate data. In “Designing fair MCS to reduce unethical behaviours: identifying key variables”, we build a set of propositions concerning: (1) the most important MCS characteristics that are likely to increase managers’ perceived MCS justice and (2) how justice operates, that is to say, the reasons why MCS that are perceived as fair may reduce managers’ propensity to create slack or manipulate data. Finally, in “Conclusions and future directions”, we conclude with an exploration of managerial implications and suggestions for future research.

## Literature review

### The unethical behaviours of budgetary slack creation and data manipulation

Since the seminal work of Argyris (1952), research has shown that MCS, rather than motivating managers to act in the interests of their company, may induce them to adopt unethical behaviours. According to Jones (1991), an ethical decision is defined as “a decision that is both legal and acceptable to the larger community. Conversely, an unethical decision is either illegal or morally unacceptable to the larger community” (Jones, 1991, p. 367). This definition has been used in studies looking at ethical issues in the context of MCS (e.g., Barsky, 2008; Stevens, 2002).

This paper focuses on two types of unethical behaviours: budgetary slack creation and data manipulation.

There is evidence that budgetary slack exists in many organisations (Libby & Lindsay, 2010; Lowe & Shaw, 1968; Onsi, 1973; Schiff & Lewin, 1970).

Similarly, empirical studies have shown that data management is commonplace in organisations (Bitner & Dolan, 1998; Libby & Lindsay, 2010; Umapathy, 1987).

Budgetary slack creation and data manipulation cause two types of problems. Firstly, they have dysfunctional consequences on the organisation. Slack generates a waste of resources. Although slack may give managers protection from unforeseen negative economic changes, if the economic environment eventually turns out favourable, the excess resources will still have been used. As for data manipulation, it causes bias in the information system.

<sup>1</sup> Following social scientists, we use justice and fairness terms interchangeably (Cropanzano & Stein, 2009, p. 194).

Download English Version:

<https://daneshyari.com/en/article/1014997>

Download Persian Version:

<https://daneshyari.com/article/1014997>

[Daneshyari.com](https://daneshyari.com)