



The rise and fall of management accounting systems: A case study investigation of EVA™



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ARTICLE INFO

Article history:

Received 12 March 2014

Received in revised form 14 December 2015

Accepted 4 February 2016

Available online 9 February 2016

Keywords:

Economic value added

New Zealand

Management accounting systems

Institutional theory

Longitudinal study

ABSTRACT

This paper uses institutional theory as a framework for explaining and understanding the processes involved in the creation, use and decline of comprehensive Economic Value Added™ (EVA) based management accounting systems (MASs) in three substantial New Zealand companies. Longitudinal case studies, each extending to more than a decade through the recent financial crisis, were conducted. Qualitative data from interviews was combined with the investigation of the initial EVA philosophy, technical design (and subsequent evolution thereto) of the firms' new MASs. The result is a study which highlights and emphasises the socio-technical nature of management accounting practice. The interface between the technical accounting issues and the circumstances, beliefs and experiences of participants led to the introduction of extensive EVA-based systems, followed by significant adjustment of them and finally to their eventual abandonment. Thus, the analysis shows that, to fully understand the process of institutionalisation of management accounting, the technical characteristics of change should not be neglected but should be integrated in analysis undertaken. The factors involved in the de-institutionalisation of the above changes are also explored and presented.

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1. Introduction

The purpose of this paper is to configure and explain the life (from birth to death) of a management accounting system (MAS). It is focussed on revealing how and why situational factors and technical accounting method characteristics interact to give rise to the creation of a new system, then influence its development and growth and, finally, initiate its decline and effect its demise. This is achieved through longitudinal, comparative case studies of three major New Zealand companies. In the 1990s, each of these firms adopted and used new MASs based on the Economic Value Added (EVA™) concept (Ehrbar, 1998; Stewart, 1991; Stern, Shiely, & Ross, 2001; Young & O'Byrne, 2001)¹ for periods of between twelve to fifteen years. In each case the EVA-based MAS was eventually abandoned.

The approach used in this study of EVA is processual in nature, where the system is viewed as a cumulative process over time (Burns, 2000; Burns & Scapens, 2000; Contrafatto & Burns, 2013). Initially, the process begins with an adoption stage

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¹ EVA is a registered trademark of the Stern Stewart and Co Consulting firm ('Stern Stewart') and it is defined as net operating profit after tax (NOPAT) less a capital charge (capital multiplied by the cost of capital). For ease of reading, the trademark symbol is omitted from the remainder of the article, although the patent is acknowledged.

where the decision to introduce the EVA philosophy is taken and the EVA-based MAS is rolled out within the organisation. For each case firm, the new EVA philosophy and MAS represented a radical departure from the previous system. It also represented a far-reaching change as it was extensively implemented in performance measurement and control systems throughout the organisation (i.e. at the business unit level, not simply for reporting at the overall firm level) and also used for many important managerial decisions involving planning, investment, control and remuneration determination. Following EVA adoption, the implementation process occurred over a relatively long time period and, during this time, the system's technical nature and use evolved as managers learned and responded to its changing form and impact within their firms and to changes in the internal and external environment. Finally, the process ends with the decision to abandon EVA as the basis of the MAS.

The study centres on the factors which stimulated and influenced each stage of the process for the case firms. The investigation of the factors extends beyond their identification to an explanation of how and why they operate and interact to intervene in the system (Bebbington, 2007). Therefore, the process is not studied as one of technical change occurring in isolation, rather it is enshrined in the organisational and environmental contexts of the case firms. This facilitates the development of a narrative surrounding the complex and dynamic nature of the EVA system as it begins, operates and ceases in the real world setting. One important advantage of this approach is the recognition it accords to the fact that management accounting change is not homogeneous in nature. The adoption, development and abandonment of a MAS constitute very different types of change, with different triggers for these changes. Institutional theory is used as a framework to investigate and explain the nature of the philosophy and routines surrounding EVA in the case firms, together with the motivation for changes over the EVA life cycle. This theory is particularly suitable for investigating the workings of the MAS which came to constitute a series of routines within the firm. Whilst routines may be regarded as repeated patterns of behaviour, or taken for granted beliefs of the way something works in an organisation (Burns, 2000; Burns & Scapens, 2000; Contrafatto & Burns, 2013; North, 2008; Nelson & Winter, 1982), they may also change over time in an evolutionary manner (Feldman, 2000, 2003; Feldman & Pentland, 2003, 2008; Nelson & Winter, 1982; Rerup & Feldman, 2011). Routines can be influenced by a variety of factors at the individual, organisational and environmental level (Miner & Estler, 1985). Furthermore, the internal dynamics of a routine is another possible source of change, leading to a flow of ideas, actions and outcomes (Feldman, 2000). As such, routines have the quality of both stability and change (Pentland & Reuter, 1994; Rerup & Feldman, 2011). Although institutional theory does not specifically focus on change in the form of abandonment, it has the potential to provide an explanatory role at that stage.

The paper makes three main contributions. First, the longitudinal nature provides an opportunity to 'tell the story' of how and why EVA was adopted within the case firms. A longitudinal approach is necessary for an understanding of how MAS change over time (Ryan, Scapens, & Theobald, 2002) whilst case studies have the 'nearly unique capacity to study phenomena in their naturally occurring setting' (Brownell, 1995, p77). A second contribution of the study is, through its contextual nature, the provision of empirical evidence on EVA through the economic cycle, including the recent financial crisis. This complements the exposition of EVA that is now prevalent in management accounting and finance textbooks (for example, Brealey, Myers, & Allen, 2014; Drury, 2012; Merchant & Van der Stede, 2012) by providing evidence on the operation of an EVA system and the circumstances in which it can fail. Third, by focussing on the dynamic nature of EVA routines, explanations for their institutionalisation, evolution and change are developed. The results suggest that particular internal pressures resulting from unintended outcomes may lead to an evolution in routines, while external shocks can lead to the abandonment of a management accounting philosophy such as EVA.

The paper is structured as follows. In the next section, relevant literature on EVA and on the study of management accounting change is reviewed and this defines a gap in existing research which this study is designed to address. The research design is outlined and the findings are then presented in the context of the economic and organisational environments of the case companies. Discussions are then presented, with conclusions drawn in the final section.

2. Relevant literature

Two areas of literature which reflect the socio-technical nature of management accounting are relevant to this study. The first comprises analyses and empirical studies of EVA as an operational and technical accounting method. The second covers institutional theory which has been used widely in the study and explanation of management accounting change. Together they provide a means of contextualising the study and interpreting the significance of the findings.

2.1. EVA studies

EVA-based financial management systems rose to prominence in the 1990s. Their roots lie in the residual income concept (Solomons, 1965) but it has been claimed that extra adjustments to the accounting measures of income, assets and liabilities make the construct more economically meaningful (Stern et al., 2001).² Furthermore, EVA has been promoted as more than a technical tool, as it is argued that it can be the basis of the business philosophy for the firm, with its focus on shareholder value and the drivers for improving that value (Stewart, 1991; Stern et al., 2001; Young & O'Byrne, 2001). In implementing the EVA

² Residual income is defined as net income less a capital charge that reflects the return to equity holders (Solomons, 1965).

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