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Management accounting systems, top management team heterogeneity and strategic change

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Abstract

Institutional and market changes force many organizations across economic sectors to reconsider their strategic position and engage in strategic change. Organizations differ in their ability to realize strategic change, however, which appears to depend on several factors in their strategic management process. In this paper we explore two such factors simultaneously, which are the composition of the top management team and the characteristics of the management accounting system. In particular, the paper investigates how top management team heterogeneity affects strategic change both directly, and indirectly, through the design and use of the management accounting system. Hypotheses are developed and tested through a survey study among 103 Spanish public hospitals. We find significant effects of top management team heterogeneity on the extent and direction of strategic change, and find that the use of the management accounting system partially mediates the relationship between top management team heterogeneity and strategic change. The paper contributes to the extant literature on the complex relationships between strategic change and MAS [Gerdin, J., & Greve, J. (2004). Forms of contingency fit in management accounting research – a critical review. *Accounting, Organizations and Society*, *29*, 303–326], by analysing both extent and direction of strategic change, and by recognizing the importance of top management teams' use of the management accounting system for strategic change.

Introduction

The literature provides evidence that organizations across industries experience increased external pressures to reconsider their strategic positions (e.g., Danneels, 2002; Henri, 2006). This phenomenon appears to affect private and public organizations alike, as the sources of pressure originate in both institutional and market developments (e.g., Frow, Marginson, & Ogden, 2005; Modell, 2004; Nyamori, Perera and Lawrence, 2001). The ability or failure to initiate and execute strategic change in response to such external pressures has serious implications for organizational performance (Nyamori et al., 2001).

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However, our knowledge about the organizational factors and mechanisms that enable strategic change is incomplete and fragmented (e.g., Frow et al., 2005; Henri, 2006; Chenhall & Langfield-Smith, 2003), despite clear evidence across the management literature that organizations systematically differ in their inclination and ability to pursue strategic change (e.g., Abernethy & Brownell, 1999; Lant & Montgomery, 1987; Wiersema & Bantel, 1992). The strategic management literature, for example, suggests that the composition of the organization's top management team (TMT), which is the echelon ultimately responsible for strategy development and deployment, affects the strategic choices of the organization, and the ability to execute them (see, e.g., Carpenter, Geletkanycz, & Sanders, 2004). Several studies following the so-called upper echelon perspective show that TMT heterogeneity, which is the extent to which the team consists of managers with varying backgrounds and competences, systematically varies with the organization's inclination and ability to engage in strategic change (e.g., Finkelstein & Hambrick, 1996; Golden & Zajac, 2001; Jarzabkowski & Searle, 2005). Typical upper echelon studies, however, do not address the process through which TMTs pursue and realize strategies, and they are therefore criticized for providing little explanation of how different TMTs use organizational mechanisms differently to realize strategic change (see, e.g., Carpenter et al., 2004, p. 763; Miller, Burke, & Glick, 1998, p. 40; Rajagopalan, Rasheed, & Datta, 1993, p. 375). The accounting literature, in contrast, emphasizes the role of the management accounting system (MAS) as an organizational mechanism that supports strategic change (e.g., Dent, 1990; Nilsson & Rapp, 1999; Simons, 1995), but empirical studies have not addressed the way in which management uses the MAS to engage in strategic change directly, with a number of interpretative case studies as a notable exception (e.g., Abernethy & Chua, 1996; Ezzamel, Lilley, & Willmott, 2004). An important reason for this lack of evidence is that studies on the MAS-strategy relationship have typically modelled strategy as an (exogenous) determinant of MAS, rather than as an (endogenous) consequence of the MAS, as they typically conceive strategy as an intention and position, rather than in terms of emergence and change (see, e.g., Gerdin & Greve, 2004; Henri, 2006). Therefore, although the broader management literature suggests that TMT composition may affect strategic change via the MAS, there is no direct empirical evidence on this effect. In this paper we aim to provide such evidence by exploring how TMT composition affects strategic change through the use of MAS, using and combining insights from the strategic management and accounting literatures. We focus on TMT heterogeneity, and explore whether the effect of TMT heterogeneity on strategic change is mediated by TMTs' use of the MAS. In line with previous studies on the MAS-strategy relationship, we explore two dimensions of TMTs' use of MAS, which are the *scope* (broad-narrow) of the MAS information that TMTs use and the *style* (diagnostic-interactive) in which TMTs use MAS information (cf. Abernethy & Brownell, 1999; Henri, 2006). Strategic change is defined as the change of strategic stance from defender position to prospector position or *vice versa* in conformity with previous studies (Abernethy & Brownell, 1999; Miles & Snow, 1978; Shortell & Zajac, 1990).

This paper attempts to contribute to the literature in at least three respects. First, we propose that the use of MAS is an important mediator of the relationship between TMT heterogeneity and the organization's strategic behavior, which fills a void in the strategic management literature concerning the organizational mechanisms through which TMTs realize organizational outcomes (see, e.g., Carpenter et al., 2004; Miller et al., 1998; Rajagopalan, Rasheed, & Datta, 1993). Second, by exploring the mediating role of MAS, we answer a recent plea in the management accounting literature for more complete explanations of the origins and consequences of MAS design and use in a single study (cf. Gerdin, 2005a; Luft & Shields, 2003; Hartmann & Moers, 1999, 2003). Third, and in particular, the paper adds to the limited knowledge on the strategic relevance of MAS for organizations engaging in strategic change (Nyamori et al., 2001; Chenhall & Langfield-Smith, 2003).

The remainder of this paper is structured as follows. Section "Literature review and hypotheses development" reviews the literature and develops