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# The role of consultants and management prestige in management control system adoption☆

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A B S T R A C T

Consultants are often involved in management control system (MCS) adoption, but the literature ignores their role. In two experimental studies, I identify conditions in which consultant recommendations and, in turn, manager MCS choices intend to benefit management rather than optimize benefits for the firm. The experiments focus on the effects of management's prestige. I find that professional consultants recommend new (as opposed to established) MCS to high prestige managers, despite believing that established MCS will benefit the firm. In turn, high prestige managers disproportionately choose the new (as opposed to established) MCS when recommended and believe doing so is the highest quality choice, even when NPV and risk are constant across MCS. When prestige is moderate, consultants recommend established MCS and managers gravitate towards these MCS. I argue that consultant involvement can lead to an MCS adoption risk: recommending and choosing MCS because they are new or used by others, not because they are better choices for the firm.

## 1. Introduction

Management control systems (MCS) are formal monitoring, measurement, and compensation processes chosen by management to align goals within the firm (Merchant & Van Der Stede, 2007). The literature portrays MCS choice as management optimizing outcomes for the firm: assessing control needs and efficiently making the adoption or non-adoption choice based on these needs (Chenhall, 2003; Davila, Foster, & Li, 2009). However, this view ignores that managers receive help from consultants whose involvement likely influences the MCS choice. Consultants have incentives to help the firm, but stronger incentives to please the managers who hire them, fire them, and largely determine their future success (Bloomfield & Danieli, 1995; Fincham, 2002; Glückler & Armbrüster, 2003; Nikolova, Moellering, & Reihlen, 2015).[1] Firm and manager interests are often misaligned (Jensen & Meckling, 1976), and I argue that consultants exploit this friction by benefitting management without demonstrably harming the firm. All else equal, consultant involvement likely leads to suboptimal MCS choices that optimize personal benefits for management—such as enhancing its public image—not the firm.

In particular, this study examines how management's *prestige* affects consultant recommendations and, in turn, manager MCS choices. Prestige refers to widespread respect for management based on perceptions of its social position or of its achievements (D'Aveni, 1990; Jensen & Roy, 2008). Management's prestige affects how stakeholders expect managers to act, and choices that match these expectations help managers maintain their prestige (Fast & Chen, 2009; Hayward, Rindova, & Pollock, 2004). Prior research suggests that stakeholders expect high prestige managers to stand out from peers by making distinctive choices and moderate prestige managers to act like their peers by making non-distinctive choices (e.g., Hayward et al., 2004; Phillipe & Durand, 2011). In an MCS domain, high prestige managers can appear distinctive by choosing new MCS—i.e., MCS not yet adopted by managers' peers—whereas moderate prestige managers can conform by choosing established MCS. My general theory is that consultants recommend and help management justify making these self-serving MCS choices. That is, I identify conditions in which MCS recommendations and choices are not based on the firm's control needs, but rather on

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[1] The consultant is an outside professional who earns revenue from selling MCS and from advising the firm on MCS adoption. *Advice* often refers to explicit recommendations to adopt or not adopt an MCS, but advice can also take the form of additional information about MCS, or information about how to make the decision to adopt an MCS.

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whether the MCS is new or used by others.

Specifically, I argue that consultants are motivated to satisfy and build a good reputation with management. As a result, consultants recommend new (as opposed to established) MCS when management prestige is high, but recommend established MCS when prestige is moderate. Moreover, I expect that these recommendations significantly influence managers' MCS choices, because following advice makes self-serving choices easier for managers to justify. Higher justifiability shields managers from downside risk in these high-stakes choices (Kennedy, Kleinmuntz, & Peecher, 1997). Finally, I argue consultants' advice influences managers' choices even when consultants recommend the non-preferred MCS, which is not the general case but likely occurs with some frequency (e.g., Bloomfield & Danieli, 1995). While managers prefer to both act in their self-interest *and* receive advice that justifies doing so, they will switch preferences to ensure their high-stakes choices are justifiable to others, preserving the appearance of a quality MCS choice.

I first use semi-structured interviews with professional consultants to confirm the importance of management prestige in this setting. In particular, I find that consultants believe that prestige is a key consideration for management's MCS choice. The interviews also help guide my research design and theory development (Merchant & van der Stede, 2006). I then test my predictions in two experimental studies, the first focusing on consultants' recommendations and the second focusing on managers' MCS choices. Both studies involve the case of a firm with receivables and performance measurement issues. In study 1, professional consultants assess the likelihood that they would recommend an MCS that may help. I manipulate whether management team prestige is high versus moderate and whether the MCS is new versus established in the firm's industry. In study 2, managers decide between two positive NPV but risky MCS, and receive a consultant's report to help them do so. One MCS is new and one MCS is established, holding risk and NPV constant. I manipulate management team prestige, as in experiment 1, and whether the consultant recommends the new MCS, the established MCS, or a control condition in which the consultant provides information but does not recommend either MCS.

In study 1, as predicted, I find that consultants are less likely to recommend an established, as opposed to new MCS when prestige is high. By contrast, consultants are more likely to recommend an established MCS when prestige is moderate. Supplemental analyses show that recommendations are driven by reputational motivations to please management and not by cost-benefit considerations for the firm. Indeed, when prestige is high, consultants believe the established (as opposed to new) MCS will be *less costly* and equally beneficial for the firm, but nonetheless hesitate to recommend it. That is, consultants do not believe they are recommending the better choice for the firm, but rather the better choice for management.

In study 2, as predicted, I find that moderate (as opposed to high) prestige managers have stronger preferences for the established MCS. I also find that consultant recommendations significantly influence MCS choices, as managers in all conditions value the incremental justification provided by consultant recommendations. Moreover, supplemental tests reveal differences in how moderate versus high prestige managers act on their preferences and use consultant input. Moderate prestige managers choose their preferred, established MCS even without an explicit consultant recommendation to adopt it. However, these managers follow consultant recommendations and believe that doing so results in higher quality choices, even when choosing the new MCS. In sum, moderate prestige managers prefer the established MCS, but believe it is a good choice to switch preferences based on explicit consultant guidance.

By contrast, my findings suggest high prestige managers use consultant advice to act on their preferences, while maintaining the *appearance* of high quality decision making. High prestige managers follow consultant advice, but disproportionately follow advice to adopt the preferred, new MCS. Further, these managers believe the advice they receive and their own subsequent choices are highest quality when the consultant recommends the new MCS, *even though NPV and risk are constant across MCS*. High prestige managers do follow advice to adopt the non-preferred, established MCS. However, unlike moderate prestige managers, they do not necessarily believe it is good advice that will lead to a good MCS choice.

This study contributes to the literature on MCS adoption with theory and evidence on the role of consultants. It identifies an adoption risk: consultants recommending and managers adopting an MCS because it is new or others use it, not because it is a better choice. This extends the literature beyond a focus on management independently choosing MCS based on firm needs or “fit” (Chenhall, 2004; Hong & Kim, 2002). Management receives help from consultants who have incentives to please management by helping justify self-serving choices. In some conditions, consultants recommend the better choice for management's image and may recommend against MCS that could benefit the firm. As noted above, consultants seem aware that they are optimizing manager and not firm outcomes, which suggests that consultants may represent an additional layer of agency risk for firms. These conditions increase the risk of suboptimal MCS choices, because improving management's image often does not benefit the firm, and may even harm it (Malmendier & Tate, 2009; Staw & Epstein, 2000).

This study also contributes to the MCS literature by highlighting the role of management prestige in MCS choice. Interestingly, my findings suggest the risks of questionable MCS recommendations and choices increase with high, as opposed to moderate, prestige management. Specifically, there are conditions in which consultants advise high prestige managers to (1) commit firm resources to image-enhancing adoptions of new MCS and (2) forego adopting potentially beneficial established MCS that could jeopardize this image. In turn, high prestige managers value the chance to make self-serving choices justified by consultant support. These managers disproportionately follow recommendations to adopt new MCS and believe that recommendations to adopt the non-preferred, established MCS are no better than receiving no recommendation at all. While high prestige managers indicate they are willing to adopt established MCS when recommended, they appear to lack commitment to this choice. This exposes firms to risk, as manager commitment is essential for firms to realize the full benefits of an MCS (Elbashir, Collier, & Sutton, 2011; Fayard, Lee, Leitch, & Kettinger, 2012). On a practical and theoretical level, this indicates potential disadvantages of having high prestige management.

Finally, this paper makes a broader practical and theoretical contribution to understanding the role of consultants in management choice. Prior literature presents two opposing views of consultants as either neutral information providers or ruthless opportunists (cf., Schein, 2002; Berglund & Werr, 2000). My findings offer one possible reconciliation of these views. Consultants seek to maintain trustworthy reputations, but are willing to do so by exploiting the natural misalignment between manager and firm interests. In my setting, consultants do not seek to harm the firm, but may recommend suboptimal courses of action in order to benefit managers who, in turn, offer short- and long-term benefits to consultants.

## 2. Background literature on management control systems

MCS adoptions are important, often beneficial choices by a firm's management (Campbell, Datar, & Sandino, 2009; Davila & Foster, 2007; Sandino, 2007; Naranjo-Gil & Hartmann, 2006; Simons, 1995). However, MCS adoptions are also a type of risky investment choice, presenting distinct challenges (Argyris & Kaplan, 1994; Elbashir et al., 2011). Firms often fail to measure MCS adoption costs and benefits adequately, and adoptions often fail or take years to yield benefits (Anderson, 1995; Ittner & Larcker, 2003; Ittner, Lanen, & Larcker, 2002, Ittner, Larcker & Meyer, 2003; Malmi, 1997).

These struggles highlight two reasons for consultant involvement in MCS adoptions. First, MCS adoptions often involve widespread