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Application of the controllability principle and managerial performance: The role of role perceptions

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ABSTRACT

The controllability principle stipulates that the evaluation of a manager should be based only on elements that are under the manager's control. Arguments for and against its application are theoretically well understood, but empirical evidence based on the evaluation of the perceptions of managers and their implications for managerial performance is scarce. By empirically analyzing the effects on managerial performance, this paper explores managers' responses to the application of the controllability principle. We draw on role theory and analyze how role ambiguity and role conflict mediate this basic relationship. Moreover, we test whether application of the controllability principle equally affects role perceptions of top-level managers and those of lower and middle-level managers. Empirical analysis of survey responses from 440 managers reveals that role perceptions completely mediate the effect of application of the controllability principle on managerial performance. This effect is insignificant in the group of top-level managers, who appear to cope with uncontrollable factors more effectively.

1. Introduction

The controllability principle is one of the strongest tenets in management accounting, and is considered to be directly relevant to evaluations of managers' performance (Bhimani et al., 2008; Merchant and Otley, 2006; Merchant and Van der Stede, 2007). Mostly known as a normative principle, the controllability principle stipulates that managers should be held accountable only for results that are within their control (Atkinson et al., 2007; Dalton, 1971; McNally, 1980). Extant literature suggests that non-application of the principle leads to decreased motivation and increased role stress, which result in dysfunctional behavior by individual managers (Dent, 1987; Merchant, 1987; McNally, 1980). Despite this rationale for the application of the principle, there are compelling arguments as to why organizations should not always fully conform to it. Companies can direct managers' attention to critical performance areas and gain additional information about their hidden actions by partially disregarding the principle (Ittner and Larcker, 2002; Manzoni, 2002; Simons, 2007). Given the convincing arguments both for and against applying the controllability principle, prior studies not surprisingly found that companies differ in the extent to which they follow the principle in formal performance evaluations (Drury and El-Shishini, 2005; Huffman and Cain, 2000; Merchant, 1989; Vancil, 1979).

Even though researchers have been interested in the controllability principle for some time, quantitative empirical work investigating the actual consequences of its application is sparse (Drury and El-Shishini, 2005; Simons, 2007) with respect to both the expected benefits of application and the potential drawbacks of strict application. Considering the theoretical importance of the principle

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and its practical relevance for companies, this paucity of research is startling. As Giraud et al. (2008) commented, "The position of *the managers evaluated* has not been much examined" (p. 34).

This paper aims to foster a better understanding of responses of individual managers to the application of the controllability principle, and especially the potential negative effect of non-application on managerial performance. Building on role theory (Kahn et al., 1964, 1966; Katz and Kahn, 1966, 1978), we relate application of the controllability principle to managers' role perceptions. We argue that application of the controllability principle affects role ambiguity and role conflict. We assume that role ambiguity and role conflict, in turn, affect managerial performance. Because role theory emphasizes the importance of the hierarchical position of individuals for their role perceptions, we also account for possible moderating effects of this variable on the relationships between application of the controllability principle and role ambiguity and role conflict.

Investigation of these effects illuminates the dynamics between application of the controllability principle and managerial performance, which is desirable from a theoretical, as well as practical, point of view. Exploration allows the derivation of recommendations on how to effectively mitigate dysfunctional consequences of non-application when full application is not desirable or feasible.

We test our theoretical model with data from 440 managers and find support for most of the proposed hypotheses. We find strong and significant effects of application of the controllability principle on role ambiguity and role conflict—the more superiors apply the controllability principle, the less managers experience role ambiguity and role conflict. These effects are significant even after controlling for managers' trust in their superior. Moreover, we find that it is in particular a decrease in role ambiguity that has a positive impact on managerial performance.

Our analyses reveal that the initial direct effect from application of the controllability principle on managerial performance completely disappears once the indirect effect through role ambiguity and role conflict is taken into account. Cognitive perceptions, therefore, fully mediate the dysfunctional effect of non-application of the principle on managerial performance. Moreover, we find that the relationship between its non-application and role ambiguity is insignificant for the subsample of top-level managers. Compared to lower and middle-level managers, top-level managers seem to be better able to deal with uncontrollable factors. They are also better at withstanding dysfunctional cognitive perceptions that result from being confronted with factors beyond their control. Consequently, companies can disregard the controllability principle for their top-level managers more easily than one might have previously assumed.

Our findings also suggest that companies can mitigate the dysfunctional effects of its non-application among lower and middle-level managers. Companies should consider using more effective personnel controls, which constitute an important element of management control systems (Merchant and Van der Stede, 2007). Personnel controls comprise (a) the adequate selection of people to achieve a high person–job fit and (b) training to prepare managers for new and stressful jobs. Researchers from the field of organizational behavior find that companies often ignore such controls (Cooper et al., 2001). An *ex ante* implementation of appropriate systems would help to avoid control problems, and psychological research has in fact provided evidence of the general effectiveness of such measures (Saunders et al., 1996).

Our paper is organized as follows. Section 2 reviews the previous literature on the controllability principle. Section 3 introduces role theory and relates the role episode model to application of the controllability principle. Considering the application of the principle from a role theory perspective, this section develops our hypotheses. Section 4 describes the research method, data collection, and survey instruments, and Section 5 presents the empirical findings. Finally, Section 6 discusses these findings, highlights the limitations of the study, and proposes avenues for future research.

2. Review of prior literature on the controllability principle

For some time, management accounting literature has put forward strong theoretical arguments for observance of the controllability principle when evaluating the performance of managers. Application of the principle seems advisable from a motivational perspective, because it ensures adequate levels of managerial effort on the job and circumvents dysfunctional behaviors (Hirst, 1983; Huffman and Cain, 2000; McNally, 1980; Ronen and Livingstone, 1975).

Agency theorists have also highlighted the motivational effects of applying the controllability principle. They identify selection and effort effects and advocate its application because it motivates more skilled managers to (a) join and remain in the company (selection effect) and (b) increase or better allocate their effort (effort effect) (Milgrom and Roberts, 1992; Shields and Waller, 1988; Waller and Chow, 1985).

A related stream of literature highlights the motivational effects of managerial perceptions of fairness that arise from applying the controllability principle (Giraud et al., 2008; Huffman and Cain, 2001). Application of the controllability principle, with its alleged emphasis on fairness, seems to reduce managers' propensity to engage in dysfunctional behavior to protect themselves from such uncontrollable factors such as budgetary slack and earnings management (Collins, 1978; Dent, 1987). Furthermore, applying the principle can move the company away from an "excuse culture," because managers waste less time trying to convince superiors that their performance stems from uncontrollable factors rather than their effort (Merchant, 1989; Modell and Lee, 2001).

Previous literature also suggests role stress as an undesirable consequence for managers when companies do not apply the controllability principle to performance evaluation (Choudhury, 1986; McNally, 1980). Role stress can occur when managers regard their responsibilities as inadequately specified, and several studies have found role stress to decrease managerial performance (Fogarty et al.,