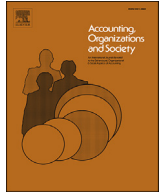




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Misaligned control: The role of management control system imitation in supply chains

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ABSTRACT

This study investigates how interorganizational imitation influences management control decisions in a supply chain setting. Control design in interfirm exchanges is traditionally thought to be based on the principle of matching, where organizations install MCS that align with the transaction context. However, despite these theorized interrelationships, misaligned transactions commonly exist in practice. In this study, we propose a framework on the potential sources of such misalignment. We argue that control misalignment can be attributed to imitating behavior, by which organizations adopt MCS following the example of other organizations. Based on survey data collected from firms involved in a supply chain triad, we demonstrate that buyers control their upstream suppliers partially by imitating how their downstream customer controls them. Notably, buyers appear to imitate despite variations in transaction context, creating a basis for misalignment in line with our predictions.

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1. Introduction

The design of proper management control systems (MCS) is crucial for the management and performance of interfirm relationships.¹ As such, management accounting researchers have devoted considerable effort to explaining firms' MCS choices in such relationships. Predominantly informed by transaction cost economics (TCE), prior research on interfirm collaborations, and supply chain relations in particular, has considered transaction risk as a key determinant of these choices (Dekker, Sakaguchi, & Kawai, 2013). When engaging in interfirm exchanges, firms may experience a variety of risk factors, such as heightened vulnerability and the potential for transaction partners to opportunistically exploit the dependence relationship (Kang, Wu, Hong, & Park, 2012; Langfield-Smith, 2008). Without appropriate control measures in place to manage these risks, firms may not achieve intended or

desired objectives of the relationships they engage in (Anderson, Christ, Dekker, & Sedatole, 2015). The general contention is, then, that transactions with attributes suggesting higher levels of risk, require more extensive use of controls as to foster mutual coordination and collaboration.

According to this perspective, MCS design is essentially based on the principle of *matching*, where firms install MCS that align with the transaction context to mitigate underlying transaction risk. Although this notion of alignment is widely accepted, an organization's control structure and transaction context may often be out of alignment (Anderson & Dekker, 2015). Specifically, choices that entail either insufficient or excessive use of MCS relative to the transaction risk, represent instances of misaligned control. Despite the fact that such misalignments commonly exist in practice (cf. Handley, 2017), our understanding remains limited as to why misalignment occurs. In this study, we argue that the managerial process of *imitating* provides a potential explanation for control misalignment.

Substantial literature documents that individuals and, by extension, organizations rely on imitation in decision-making processes (Nikolaeva, 2014; Ordanini, Rubera, & DeFillippi, 2008). Applied to MCS design, this means that organizations may come to imitate each other's control structures. No studies, however, have hitherto empirically examined the role of imitation in explaining

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¹ Although management control has various definitions, within interfirm relationships, it can be broadly described as the set of mechanisms and practices put in place that motivate and facilitate transaction partners to achieve desired objectives (e.g., Dekker, 2004; Langfield-Smith, 2008; Mahama, 2006).

MCS. We fill this gap in the literature by examining how interorganizational imitation influences MCS decisions in a supply chain setting. Previous work has indicated that interfirm linkages within the supply chain constitute an important channel for imitating management practices (Fu, 2012; McFarland, Bloodgood, & Payan, 2008). Accordingly, we submit that imitation effects in the supply chain often have an important impact on MCS choices, which implies that the MCS of a given transaction may not be based solely on the specific transaction context. Specifically, we advance the argument that MCS are sometimes perceived as valuable or worth imitating, irrespective of the specific transaction context, thus providing a basis for control misalignment.

We test our model using survey data from firms involved in a supply chain triad. Our analyses involve two main steps. First, we examine the relation between MCS extensiveness, transaction context, and performance in a typical supply chain dyad. The results provide new empirical insights supporting the existence of misalignment between the extent of MCS use and transaction context in buyer-supplier relationships. Specifically, we find that the extent of MCS use is related to the transaction context, but significant variations exist across firms, as evidenced by performance differences. Similar to Anderson, Dekker, and Van den Abbeele (2017), this stage also yields a measure of control misalignment, captured by the residuals in the regression between transaction context and MCS extensiveness. Second, turning to the question of why such misalignment occurs, we investigate whether imitative behavior in the supply chain influences MCS use. We expand our view beyond dyadic interactions and consider the customer-buyer relationship in addition to the buyer-supplier one. In our empirical study, we focus on whether the downstream MCS that customers use with specific buyers result in imitative MCS use by the same buyers with upstream suppliers. After controlling for transaction context similarities in the supply chain, our results provide support for imitation effects. Subsequent analyses show that imitation correlates positively with our measure of control misalignment, indicating imitation as a potential source of the observed misalignment.

This study extends prior accounting literature by showing that, in addition to the dyadic focus on supply chain relationships, it is worthwhile to consider a larger network of relationships when studying MCS choices. Although TCE-based studies contribute to our understanding of interfirm management control, most current knowledge is based on the effects of particular mechanisms within the dyad (Kumar, Heide, & Wathne, 2011). Supply chains, however, typically involve multiple interconnected relationships (Meira, Kartalis, Tsamenyi, & Cullen, 2010). Therefore, to gain further insights on MCS choices and, in particular, to explain deviations from TCE-determined patterns, analysis beyond the individual dyad is useful. Specifically, considering imitative behaviors in a supply chain triad, this study provides novel evidence on the behavioral mechanisms underlying MCS design, and points out that MCS decisions can have consequences not only in the focal dyadic relationship, but also in adjacent relationships. We find that the unexplained imitation of other firms' practices in the supply chain can explain why MCS choices may not always fit the transaction context as predicted by traditional transaction cost logic.

From a practical perspective, by providing a deeper understanding of the process of control practice selection, our evidence provides guidance for organizations to achieve a better fit. For many managers, imitation is an important fact of organizational life. Abundant references to best practices in practitioner literature provide indication on the prevalence of willful imitation (Csaszar & Siggelkow, 2010; Sousa & Voss, 2008). However, best practices may not work universally due to contextual mismatches. Therefore, the insights of this study are important, because ignoring the limits of

control practices may lead to imitation and application in unsuitable contexts. To imitate appropriately and, hence, avoid situations of misalignment, firms should consider adapting MCS to meet their specific relationship needs.

The remainder of the paper is organized as follows. Section 2 reviews previous research and introduces our hypotheses. Section 3 presents the research methodology. We then discuss our analysis and results in Section 4. Section 5 concludes.

2. Literature review and hypotheses development

2.1. Theoretical foundation

Extant research on management control in interfirm relationships has generally adopted TCE as a theoretical framework. TCE is based on the premise that organizations make efficient choices in selecting governance forms and management controls to match transaction conditions (Anderson & Dekker, 2015). Indeed, "the calculative choice approach towards management control in interfirm relationships implies the assumption of an outsourcer's efficiency-seeking behavior regarding the structuring of management control" (Vosselman & Van der Meer-Kooistra, 2006, p. 135). Although transaction cost efficiency is pertinent to explaining matching between control structures and transactions, it is not fully deterministic (Speklé, 2001, p. 422). In reality, it is possible that not all organizations adopt efficient MCS design at all times (King & Clarkson, 2015). Of direct relevance, if MCS are designed optimally in relation to the transaction context, this should enhance performance, whereas deviating from proper context-control alignment should adversely influence performance (Yvrande-Billon & Saussier, 2005). Increasing evidence shows that misalignment often occurs with negative performance implications (e.g., Anderson & Dekker, 2005; Mooi & Ghosh, 2010). However, extant research still provides limited insight into the sources of misalignment. Whereas TCE adopts behavioral assumptions of bounded rationality and allows for the possibility of misalignment and resultant performance implications, it has paid little attention to how it affects the decision-making process that accompanies MCS design. Integrating TCE with behavioral theories can provide important insights, and might help explain why some managers behave in ways inconsistent with predictions based on optimal or efficient choice (Chenhall, 2003, p. 159).

Along this line, studies in the organizational literature introduce satisficing search behaviors into an efficiency-based adoption framework (Roberts & Greenwood, 1997). The satisficing principle posits that decision-makers conduct limited searches among available alternatives to obtain satisficing rather than optimizing solutions (Cyert & March, 1963; March & Simon, 1958).² In search of solutions, decision-makers especially seek directions from their own immediate environment and may be motivated to copy the decisions of others (Ketokivi & Schroeder, 2004). For MCS design, this implies that organizational decision-makers may imitate each other's MCS (see Vosselman, 2002). Such imitation allows saving costs and time, because it avoids extensive search and comparison of alternatives by making choices based on other decision-makers' actions (Ordanini et al., 2008; Sun, 2013). However, if this leads firms to imitate MCS uncritically, this might also preclude complete assessment of transaction hazards and, consequently, aligned MCS selection. Hence, in this study, we introduce the role of interorganizational imitation as a potential source of misalignment between

² This does not imply that decision-makers do not care about efficiency; rather, the adoption of organizational practices may be viewed as efficiency-seeking, instead of efficiency-optimizing, under certain cognitive constraints.

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