

BEYOND BUDGETING: DISTINGUISHING MODES OF ADAPTIVE PERFORMANCE MANAGEMENT

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ABSTRACT

Purpose – The purpose of this paper is to analyze the changes organizations can adopt to move beyond budgeting. We show how these changes can be understood as modes of adaptive performance management which explain the ways in which organizations move beyond budgeting to become more adaptive. The proposed modes are then used to derive propositions for future research.

Methodology/approach – We follow a conceptual approach through an analysis of the beyond budgeting principles using the management and systems literatures on radical decentralization. We theorize how organizations can enhance their adaptability to environmental uncertainty through changes to their management structure and control processes.

Findings – We show that organizations can move beyond budgeting by decentralizing within or beyond their management structure and modifying or removing their budget-based control processes. We propose that beyond budgeting can be conceptualized as four modes of adaptive performance management: better budgeting, advanced budgeting, restricted budgeting and non-budgeting.

Research limitations/implications – The four modes of adaptive performance management can be used in future research to consider how changes to management structures and budget-based control processes can enhance the organizational adaptability needed to manage environmental uncertainty.

Practical implications – We show that while the non-budgeting mode may be most suited to organizations facing high levels of environmental uncertainty, organizations facing low to moderate levels of environmental uncertainty can achieve sufficient levels of adaptability with less extensive changes to management structure and budget-based control processes.

Originality/value – The four modes of adaptive performance management reflect different approaches for dealing with environmental uncertainty. Positioning non-budgeting as one mode, and identifying alternate modes of adaptive performance management, provides a basis for comparing and understanding the changes organizations make to move beyond budgeting.

Keywords: Adaptive performance management, beyond budgeting, management structure, radical decentralization, adaptive control processes

INTRODUCTION

Historically, the purpose of organizational structures was to institutionalize stability; in the organization of the future, the goal of design will be to institutionalize change.

(Nadler and Tushman, 1999, p. 49)

One consequence of increasing environmental uncertainty is the need for organizations to adopt more adaptive¹ performance management approaches that provide flexibility that is sufficient to take advantage of emerging opportunities. Beyond Budgeting, viewed as an "adaptive performance management concept" (Daum, 2002, p. 2), offers an approach to dealing with increasingly uncertain environments based on coordinated changes to management structures and control processes. It represents a holistic management approach for enhancing organizational adaptability and responsiveness by changing the "entire management control system" (Horngren, 2004, p. 210).

The changes associated with beyond budgeting are described by Hope, Bunce, and Roosli (2011) in a set of twelve principles. The beyond budgeting principles are listed in Table 1 and explained more fully in the following section. Briefly, the principles outline the basis of an adaptive performance management approach. The six leadership principles (values/vision, governance, transparency, teams, trust, accountability) relate to the management structure necessary to enhance organizational adaptability; while the six process principles (goals, rewards, planning, coordination, resources, controls) describe the types of control processes that enhance it. Thus, adaptive performance management involves changes to two key dimensions, namely management structure and control processes (Dugdale & Lyne, 2010; Hope & Fraser, 2000; Hope et al., 2011).

¹ Adaptability, flexibility and agility are commonly used synonyms referring to an organization's ability to effectively manage environmental change over time (Worley, Zardet, Bonnet, & Savall, 2015, p. 8-9).

Organizations can enhance adaptability by making changes to management structures which involve reducing the layers of management, devolving strategy and key decisions to front line teams, and/or control process changes to replace fixed plans and budgets with more flexible control processes and the use of open and transparent information to hold the organization together (Hope et al., 2011). Following the beyond budgeting principles can “enable an organization to manage its performance and decentralize its decision making process without the need for traditional budgets²” (Hope & Fraser, 2003b, p.212). Decentralization involves converting centralized, hierarchical structures into networks of small, self-managing units resulting in radical changes to organizational structure (Dugdale & Lyne, 2011). The structural changes reduce the environmental³ complexity managed by each unit and increase the adaptability of the organization overall (De Waal, 2005). Implementing adaptive performance management can thus provide managers with a “performative information system, geared for action” (Pickering, 2004, p. 31) and enable them to deal with changing environmental circumstances as they arise.

The literature, though, reveals different interpretations of beyond budgeting. While the Beyond Budgeting Round Table (BBRT) argues that all twelve beyond budgeting principles are necessary components of its adaptive performance management model (Hope & Fraser, 2001), the focus of practitioners (Bogsnes, 2009; Ryan, 2008), consultants (PwC, 2010), accounting bodies (Chartered Institute of Management Accountants, 2007), and academics (De Waal, Hermkens-Janssen, & Van de Ven, 2011; Onaitis & Shastri, 2012) has been on more limited combinations of the principles with a particular focus on the six process

² According to the Chartered Institute of Management Accountants (2005, p.5) a traditional budget is a “quantitative expression of a plan for a defined period of time. It may include planned sales volumes and revenues; resource quantities, costs and expenses; assets, liabilities and cash flows”.

³ Environment encompasses both the external and internal operating environments.

principles. In addition five of eight academic case studies reviewed⁴ reveal organizations typically implement only a subset of these principles (see for example Henttu-Aho & Järvinen, 2013; Østergren & Stensaker, 2011). This selective implementation may be due in part to the lack of clear descriptions for some of the beyond budgeting principles. While the six process principles are relatively well understood the six leadership principles are described in more ambiguous terms giving rise to multiple interpretations.

In contrast to the set of changes proscribed by the BBRT, the literature shows that organizations are developing different configurations or ‘modes’ which often involve fewer changes than specified by the original beyond budgeting concept. Furthermore, organizations are implementing various combinations of principles suggesting they make specific changes to adapt to different levels of environmental uncertainty. Arguably, these alternate modes generate different levels of adaptability that are sufficient for the level of environmental uncertainty organizations face. This research considers the various approaches organizations can use to become more adaptive. The question posed in this research is 'What are the different modes of adaptive performance management and how can they be distinguished'?

The purpose of this conceptual paper is to advance our understanding of beyond budgeting by refocusing attention on the adaptive performance management model that it promotes. There are two main contributions. First, this study clarifies the beyond budgeting leadership principles using the concept of radical decentralization. It proposes that the leadership principles can be operationalized by a holistic consideration of the extent to which management structure is radically decentralized. Second, the paper proposes that beyond budgeting can be understood as modes of adaptive performance management which can be distinguished based on two broad criteria namely the extent of radical decentralization and the extent of changes to budget-based control processes. Combining these two criteria

⁴ The case studies by Lindsay & Libby (2007) and O’Grady & Akroyd (2016) are exceptions as their case organizations implemented all twelve beyond budgeting principles.

generates four modes of adaptive performance management which we label ‘Better Budgeting’, ‘Advanced Budgeting’, ‘Restricted Budgeting’ and ‘Non-Budgeting’. We argue that these modes provide varying levels of organizational adaptability and are suitable for managing different levels of environmental uncertainty. The modes of adaptive performance management are then used to develop propositions for future research.

This paper is organized as follows. The next section introduces the beyond budgeting principles. The following section considers descriptions of radical decentralization from the beyond budgeting, management and systems literatures. The subsequent section presents our modes of adaptive performance management. The proposed modes are then used to derive propositions for future research on adaptive performance management approaches. A discussion of the findings and our conclusions are presented in the final section.

BEYOND BUDGETING

The beyond budgeting concept was introduced by the Consortium of Advanced Management International (Hope & Fraser, 2001). The term ‘beyond’ comes from going “beyond command-and-control toward a management approach that is more empowered and adaptive” (Beyond Budgeting Institute, 2016a). The term ‘budgeting’ is used in a broad sense to refer to the traditional command-and-control management approach with the annual budget planning process at its core. The term budgeting thus describes both a management structure and a performance management system (Beyond Budgeting Institute, 2016a).

The concept of beyond budgeting originated in the belief that budgeting processes were too rigid and unresponsive for companies competing in rapidly changing environments (Hope & Fraser, 1997). Traditional budgets have been criticized for being time consuming and costly to prepare, not creating value, encouraging gaming and perverse and/or unethical behaviours, being disconnected from strategy and reinforcing silos within organization (see

Bourmistrov & Kaarbøe, 2013; Hansen, Otley, & Van der Stede, 2003; Player, 2003; Rickards, 2006). The rationale behind beyond budgeting was to address these issues and thereby enhance an organization’s ability to manage environmental uncertainty (Sandalgaard & Bukh, 2014). Hope and Fraser argue that for companies to compete effectively in uncertain environments they need practices that enable them to respond quickly as conditions change (Hope, 2006, 2007; Hope & Frazer, 1997, 2001, 2003a, 2003a). The essence of the beyond budgeting approach, as set forth by Hope et al. (2011), is summarized in the twelve beyond budgeting principles listed in Table 1.

Table 1: The 12 Beyond Budgeting Principles (2011)

Six Leadership Principles	
1. Values / Vision	Bind people to a common cause; <i>not a central plan</i>
2. Governance	Govern through shared values and sound judgment; <i>not detailed rules and regulations</i>
3. Transparency	Make information open and transparent; <i>don't restrict and control it</i>
4. Teams	Organize around a seamless network of accountable teams; <i>not centralized functions</i>
5. Trust	Trust teams to regulate their performance; <i>don't micro-manage them</i>
6. Accountability	Base accountability on holistic criteria and peer reviews; <i>not on hierarchical relationships</i>
Six Process Principles	
7. Goals	Set ambitious medium-term goals; <i>not short-term fixed targets</i>
8. Rewards	Base rewards on relative performance; <i>not on meeting fixed targets</i>
9. Planning	Make planning a continuous and inclusive process; <i>not a top-down annual event</i>
10. Coordination	Coordinate interactions dynamically; <i>not through annual budgets</i>
11. Resources	Make resources available just-in-time; <i>not just-in-case</i>
12. Controls	Base controls on fast, frequent feedback; <i>not budget variances</i>

(Source: Beyond Budgeting Institute, 2016b)

The six leadership principles focus on management structure while the six process principles focus on technical aspects of performance control (Hope et al., 2011). The six leadership

principles (values, governance, transparency, teams, trust and accountability) establish the management structure that allows responsibility to be devolved to front line managers and teams. This devolution confers responsibility on and demands accountability from empowered managers and teams. According to Hope and Fraser (2003) organizations can expect empowered front line teams to sense and quickly respond to changing business conditions and customer needs.

The six process principles address the key performance management functions typically supported by budgets and suggest how organizations can change budget-based control processes to enhance their adaptability. The adaptive control processes replace budget-based processes with aspirational goals, team rewards based on relative performance, continuous planning, dynamic coordination, just-in-time resource allocation processes and rapid relevant feedback to maintain real time control. While similar management control mechanisms may be found in traditional budget-based control systems, they are implemented differently in beyond budgeting organizations (Becker, Messner, & Schäffer, 2009).

Management structure and control processes are inextricably linked in beyond budgeting organizations (Dugdale & Lyne, 2010) and both can be used to increase adaptability. In five of eight academic case studies of BB practice, the described organizations appear to operate with divisional structures; just three examples are provided of organizations with flat hierarchies (Lindsay & Libby, 2007; O'Grady & Akroyd, 2016; Becker, 2014). There is a wide variation in the adaptive processes used by organizations for planning, evaluating, coordinating, resourcing and controlling their operations. Organizations have, for example, modified traditional budgets (Becker, 2014, Hansen et al., 2003; Sandalgaard, 2012; Sandalgaard & Bukh, 2014), disconnected budgets from performance evaluations (Hansen, et al., 2003; Østergren & Stensaker, 2011), implemented continuous budgeting (Frow, Marginson, & Ogden, 2010), used budget systems in enabling ways (Ahrens & Chapman,

2004), adopted rolling forecasts, speedier approval processes, less detailed budgets and shorter budgeting periods (Bourmistrov & Kaarbøe, 2013; Henttu-Aho & Järvinen, 2013; Kaarbøe, Stensaker, & Malmi, 2013; Sandalgaard, 2012) and developed non-budgeting based control processes (O'Grady & Akroyd, 2016). This paper considers how various modifications to budget-based control processes combine with alternate organizational structures to impact organizational adaptability. A review of this literature reveals the control process changes range from non-budgeting approaches (O'Grady & Akroyd, 2016), in which budgets are completely eliminated, to alternatives such as the introduction of activity-based budgeting or rolling budgets as supplements or replacements for traditional budgets and the streamlining of traditional budget-based control processes (Hansen et al., 2003). Approaches which retain some elements of traditional budgeting are variously described as better budgeting or advanced budgeting (Daum, 2002; Libby & Lindsay, 2007; Lindsay & Libby, 2007; Neely, Bourne, & Adams, 2003; Rickards, 2006; Uyar, 2009).

Organizations have modified traditional budget-based control processes to enhance organizational adaptiveness. The approaches used can be broadly distinguished based on the extent of the changes made. Organizations can improve, selectively modify, restrict or eliminate their budget-based control processes. The improvement approach involves retaining existing budget-based control processes while introducing improvements such as less detailed budgets to reduce the time and cost of budget preparation or the addition of rolling forecasts to make information more accurate and valuable (although this may increase preparation time). The selective modification approach would see organizations replace selected budget-based control processes with more flexible alternatives. For example, relative performance indicators may be used to evaluate performance in place of budget-based measures. Finally, the elimination approach would remove traditional budget-based control processes completely and replace them with a range of alternate adaptive control processes.

In addition to modifying budget-based control processes organizations can increase their adaptability by changing the management structure to become radically decentralized. The following section considers descriptions of radical decentralization found in the management (Hales, 2001; Mintzberg, 1979; Ostroff, 1999) and systems (Beer, 1979, 1985) literatures. Based on this selective review a more refined understanding of radically decentralized management structures is developed and the relationship between radical decentralization and the beyond budgeting leadership principles is clarified

RADICAL DECENTRALIZATION

Radical decentralization was a central part of the excellence literature of the 1980s (see for example: Peters & Austin, 1985; Peters & Waterman, 1982). This literature originated from a McKinsey & Company project lead by Tom Peters in the late 1970's which examined organization structure in 43 of the Fortune 500's top performing companies. It called for a radical change to decentralization involving the flattening of hierarchical structures through re-engineering organizational processes (Gomez, & Korine, 2008). This focus on radically decentralizing structure has been revived in the beyond budgeting literature as a mechanism for increasing organizational adaptability and responsiveness to environmental uncertainty (Dugdale & Lyne, 2010; Hope & Fraser, 2000).

Radical decentralization involves devolving key decisions (including strategy development and implementation) to empowered front-line teams, replacing budgets with more flexible mechanisms and using fast, open and transparent information to hold operational units together (Hope et al., 2011, p. ix). Radical decentralization requires more than devolving authority, flattening hierarchies or introducing team work within traditional management hierarchies; it involves granting autonomy to a greater number of front line teams and empowering them to make their own decisions within clearly communicated

boundaries (Hope & Fraser, 2000). These characteristics are similar to those attributed to horizontal organizations (Hales, 1999).

Despite references to ‘radical decentralization’ (see for example: Hope & Fraser, 2000; Hope & Fraser, 2003b; Dugdale & Lyne, 2011) the beyond budgeting literature does not clearly explain what it is, how it can be recognized or how it contributes to organizational adaptability. For example, authors have stated that radical decentralization involves devolving management authority (which activities?) to a large number (how many?) of small (what size?) front line units. This lack of clarity contributes to the "ambiguity and the general debate about what beyond budgeting actually means... [and the] confusion about the practices and implications associated with this new control system" (Kaarbøe et. al 2013, p.108). If the meaning of radical decentralization, as implied in the beyond budgeting literature, is not clarified, organizations may adopt management structures that do not adequately support the adaptive control processes advocated by beyond budgeting. We draw from the management literature on ‘organizational forms’ and ‘horizontal organizations’ as well as the systems literature on the ‘viable system model’ (VSM) for insights into radical decentralization and its impact on organizational adaptability.

Our search revealed that the management literature identifies two types of radical decentralization. Mintzberg (1979) considers two of his four proposed forms of decentralization, namely strategic business units (SBU) and adhocracies, to be radically decentralized. SBUs, or profit centres, are an adaptation of hierarchically structured organizations. The SBU form is perceived as radical in comparison to a strict hierarchy or a divisional form of organization. SBUs operate as semi-independent mini-businesses in specified markets. Operational control is devolved to SBU managers thereby increasing their autonomy to the extent allowed by the financial plans and performance targets imposed by the centre. Information flows between the centre and the SBUs are mainly vertical and

formal. Adhocracies, on the other hand, have been described as anti-structures (Hales, 2001). While adhocracies are not devoid of structure (Mintzberg, 1979, p. 462) they provide organizations with externally focused flexible structures (Cameron, Quinn, DeGraff, & Thakor, 2014). Thus, the adhocracy structure is more suited than SBUs to highly complex, innovative and technologically sophisticated environments (Mintzberg, 1979, p. 459-460).

Hales (2001) observes that SBU and adhocracy forms of radical decentralization deal with uncertain and unpredictable environments in different ways. They differ in the extent to which they devolve discretionary power and management functions either *within* (to managers) or *beyond* (to non-managers) the management hierarchy (Hales, 2001, p.137). Furthermore, the pattern and type of communications, e.g. vertical, horizontal, periodic or real time, routine or ad hoc vary between the two types of radical decentralization. Table 2 compares the two approaches to radical decentralization on these characteristics.

There are obvious similarities between the characteristics of radical decentralization for adhocracies and the beyond budgeting principles of teams, accountability and transparent information. Adhocracies devolve decision making authority to expert teams which aligns with the beyond budgeting principle of *teams*. Adhocracy teams are held accountable for profitably satisfying customers which reflects the *accountability* principle. Adhocracies give teams ready access to real-time information for managing their own performance as expected by the *transparency* and *open information* principle (Hope et al, 2011). This comparison suggests that the beyond budgeting principles of teams, accountability and transparent information are indicators of radical decentralization beyond management.

Table 2: Comparison of Forms of Radical Decentralization

	Forms of Radical Decentralization (R.D.)	
	SBUs R.D. within management	Adhocracies R.D. beyond management
Criteria 1: Level to which decision making authority is devolved:		
	Individual managers operating within recognisable hierarchy.	Expert teams handling specialized tasks, projects or markets. Organizational structure is relatively flat.
Criteria 2: Management function being devolved:		
Planning	Autonomous unit managers guided by centrally imposed plans and targets.	Broad policies replace centrally imposed plans and targets.
Motivation	Via extrinsic, individual rewards based on unit performance.	Via intrinsic motivation arising from autonomy and achievement ethic supplemented by preferential salaries and group based rewards based on team performance.
Coordination	Mutual adjustment, liaison roles and internal markets.	Shared commitment to broad organizational goals, mutual adjustment and liaison roles.
Accountability and Control	SBU managers accountable for conformance to plans and targets. Control via progress reports against plan monitored by executives.	Teams accountable for customer satisfaction guided by broad policies. Control via peer pressure and self-motivation.
Information flows to support management functions	Mainly formal, vertical communication of routine information.	Sharing of transparent and open information via extensive formal & informal channels both lateral and vertical.

A complementary view of how organizations can devolve authority beyond management is provided by Beer's viable system model (Beer 1972, 1979, 1985). The VSM suggests radical decentralization is appropriate for any organization dealing with high levels of uncertainty. The model has recently been used in the management accounting literature to explain how organizational structures and control processes can be designed to handle environmental uncertainty (O'Grady, Morlidge, & Rouse, 2016). A key mechanism for managing this uncertainty is the non-hierarchical management structure advocated by the model.

The VSM conceptualizes organizations in terms of five management functions, labelled systems 1 to 5, and the communication channels linking them. System 1 undertakes the organizations' value adding activities (the system to be managed). Systems 2 to 5 represent the coordination, control, monitoring, strategic intelligence and policy functions through which the activities of system 1 are regulated (the meta-system for regulating system 1). System 1 operates as autonomous and empowered operational units supported by and linked to the remaining systems by flows of information.

The structure of the VSM is recursive meaning the five systems and communication channels are repeated at different levels of granularity (or recursiveness) similar to a set of nested Russian dolls. Each level of recursion is embedded in an identically structured higher level of recursion and contains an identically structured lower level of recursion. This nested or recursive structure promotes adaptability by devolving authority to and enabling autonomy of the System 1 units at each level of recursion. Each level focuses specifically on managing the environmental conditions impacting its own localized performance.

The VSM holds that the traditional, top down command and control approach, in which strategic plans are developed at the top and implemented by cascading instructions down through the hierarchy, is too slow and inflexible to cope with the increasing rates of environmental change faced by most organizations. The recursive structure of the model specifies a framework for designing flexible, adaptable organizations able to perform in dynamic and changing environments.

The remaining three beyond budgeting leadership principles, namely teams, trust and accountability, influence whether organizations are likely to adopt radical decentralization. The extent to which organizations are willing to devolve decision making authority for particular management functions depends on managements' views about human nature. When managers trust in people – in employees' abilities and willingness to promote organizational

goals – managers are more likely to devolve authority, responsibility and accountability (Hales, 2001; Johanson, 2013). According to Hales (2001, p. 158) “Decentralization relies to a great extent on trusting managers and professionals to monitor their own actions in ways consistent with organizational goals”. Radical decentralization will only be risked when managers trust their subordinates, either because managers have selected their subordinates carefully, socialized them effectively or subjected them to exacting performance controls (Hales, 2001, p.159). In line with this literature, the beyond budgeting leadership principle of *trust* can be viewed as a pre-condition for the devolution of authority, responsibility and accountability.

Ostroff (1999) discusses horizontal organizations and the importance they place on managers’ aspirational goals and corporate culture. He proposes that the aspirational goals of managers are prerequisites for designing horizontal structures and establishing a “single noble purpose” (Ostroff, 1999, p. 22). This type of management culture provides support for managers’ goals by reflecting on their fundamental beliefs, values, views on human nature, status, privilege and rewards, and by providing broad guidance on what is and isn’t done (Ostroff, 1999, p. 175). The management culture of horizontal organizations is typically built on trust, openness, cooperation, collaboration, continuous performance improvement and employee empowerment (Ostroff, 1999, p. 10-11). Ostroff (1999) views the aspirational goals and management culture of horizontal organizations as pre-cursors to, but not components of, structure. Accordingly, we argue the beyond budgeting leadership principles of *values* and *governance*, which encompass managers’ goals and culture, are antecedents of radical decentralization.

In summary, this section reviewed relevant literatures to elaborate on the concept of radical decentralization and clarified its relationship to the beyond budgeting leadership principles. We argue the beyond budgeting leadership principles of teams, accountability and

transparency are characteristics of radical decentralization. The extent to which decision making authority is devolved in the organization, either within or beyond management, is influenced by the leadership principles of trust, values and governance. This approach provides a holistic, rather than a principle by principle, assessment of the beyond budgeting leadership principles.

Both approaches to radical decentralization are more responsive than hierarchal structures to environmental uncertainty and therefore more suitable for managing environmental uncertainty (Ostroff, 1999). The following section considers how management structure combines with control processes to provide different levels of organizational adaptability.

MODES OF ADAPTIVE PERFORMANCE MANAGEMENT

Organizational adaptability can be increased along two dimensions, namely by adopting changes to management structure and/or a more flexible control process. As noted above, organizations can radically decentralize either *within* the hierarchal management structure (the SBU approach) or *beyond* the hierarchal management structure (an adhocracy or VSM approach). Radically decentralized management structures increase an organization's ability to manage variation and change in the environment (Hales, 2001) by increasing their requisite variety (O'Grady et al., 2016).

Organizations can also increase their adaptability by introducing various modifications to the design and use of control processes. They may: retain traditional budget-based control processes and introduce ways to improve them (changes *within* budget-based processes); completely remove budget-based control processes and replace them with more adaptive control processes (changes *beyond* budget-based processes); or selectively replace budget-based control processes, resulting in a mix of budget-based and adaptive control processes (change to *hybridized* budget-based processes). We combine these structural and control

process dimensions of organizational adaptability to distinguish four modes of adaptive performance management (see Table 3 below).

Table 3: Modes of Adaptive Performance Management

Process \ Structure	Radical Decentralization (within management structure)	Radical Decentralization (beyond management structure)
Replace budget-based control processes (<i>beyond budget</i>)		Q3 Non-Budgeting Flexibility enhanced by decentralizing <i>beyond</i> management and <i>beyond</i> budget-based control processes by eliminating budgeting
Modify budget-based control processes by selectively replacing and/or modifying how they are used (<i>hybridized budget</i>)	Q2a Advanced Budgeting Flexibility enhanced by decentralization <i>within</i> management and modifying budgets to create a <i>hybridized</i> control process	Q2b Restricted Budgeting Flexibility enhanced by decentralizing <i>beyond</i> management and by selectively replacing budgets to create a <i>hybridized</i> control process
Modify budget-based control processes by streamlining or supplementing them and/or modifying how they are used (<i>within budget</i>)	Q1 Better Budgeting Flexibility enhanced by decentralization <i>within</i> management and modifying <i>within</i> the budget-based control process	

The ‘Better Budgeting’ quadrant (Q1) in Table 3 refers to organizations that incorporate an SBU management structure while refining or improving how their budget-based control process operates. Organizations can do this by, for example, adopting less detailed budgets, more frequent budget updates, or rolling forecasts. We expect the better budgeting approach would be suitable for organizations facing relatively low levels of environmental uncertainty.

The ‘Non-Budgeting’ quadrant (Q3) in Table 3 reflects the adaptive performance management mode described most closely by the beyond budgeting literature (Hope et al., 2011). Organizations adopting this mode would completely eliminate their traditional budget-based control processes. Budgeting would be replaced with a range of more adaptive control processes which operate within a radically decentralized management structure. In this mode decision making authority is distributed widely beyond management. The combination of

process and structural changes enable these organizations to manage relatively high levels of environmental uncertainty.

The remaining two quadrants typify approaches to adaptive performance management that are suited to relatively moderate levels of environmental uncertainty. The ‘Advanced Budgeting’ quadrant (Q2a) in Table 3 denotes organizations that maintain SBU type structures and make some changes to budget-based control processes. These organizations selectively replace budget-based control processes, likely those that are most problematic for management control in their given circumstances. Arguably, the budget-based control processes that remain could be used differently, such as in an interactive manner (Simons, 1995) to enhance adaptability.

The ‘Restricted Budgeting’ quadrant (Q2b) in Table 3 includes organizations that adopt radically decentralized management structures to widely distribute responsibility and accountability. While these organizations may retain budget-based control processes they will likely modify how they are used to ensure the flexibility generated by the decentralized management structure is not curtailed. Accordingly, these organizations may for example downplay the control dimension of budgets and use them only in a ceremonial way or limit their use to the executive level.

The appropriateness of the different modes of adaptive performance management is determined by the level of adaptability required by organizations to manage their environmental uncertainty. Thus the modes are arguably discrete responses appropriate to varying levels of environmental uncertainty and should not necessarily be viewed as sequential steps towards the non-budgeting mode. Nonetheless, organizations operating in highly uncertain environments may progress through one or more modes incrementally increasing their level of adaptability in response to increasing environmental uncertainty.

PROPOSITIONS

Based on the preceding discussion we suggest a number of propositions for future research into adaptive performance management. The implicit assumption is that organizations need only develop a level of adaptiveness appropriate to the level of environmental uncertainty they face.

By radically decentralizing decision making *beyond* management and replacing all budget-based control processes with more adaptive control processes the non-budgeting mode (Q3) is expected to provide the highest level of adaptability. Accordingly, we would expect that organizations operating in highly uncertain environments who adopt this mode of adaptive performance management to outperform those that maintain SBU structures and/or rely on refining or selectively replacing budget-based control processes. To begin developing more comprehensive insights about how organizations implement this mode of adaptive performance management, budgeting researchers should identify the level to which decision making authority is devolved, the particular management functions that are devolved, and the control mechanisms being used in place of budget-based control processes.

The better budgeting mode (Q1) is expected to provide the lowest level of adaptability as it maintains existing SBU structures and focuses mainly on refinements or additions to existing budget-based control processes or modifications to how they are used to improve their operations. Accordingly, we would expect organizations operating in relatively stable environments that adopt a better budgeting mode can perform as well as organizations adopting more adaptive modes. While modes other than better budgeting may provide greater levels of adaptability this is not required when the level of environmental uncertainty is relatively low and may introduce additional costs that exceed the potential benefits. Existing research identifies examples of better budgeting such as less detailed budgets and speedier approval processes (Libby & Lindsay, 2010; Østergren and Stensaker, 2011) and the use of

rolling forecasts to complement traditional budgets (Ekholm & Wallin, 2000). Future research could identify additional refinements or supplements to budget-based control processes that would extend current understanding of the approaches used by these organizations to enhance their adaptability.

Given moderate levels of environmental uncertainty, the advanced budgeting (Q2a) or restricted budgeting (Q2b) modes of adaptive performance management would provide the intermediated levels of adaptability needed for this level of uncertainty. As environmental uncertainty increases we would expect organizations following these modes to outperform those following a non-budgeting mode as they provide a more cost effective solution. Organizations operating in moderately high levels of environmental uncertainty that adopt either the advanced budgeting mode (Q2a) or the restricted budgeting mode (Q2b) are expected to outperform those adopting a better budgeting mode (Q1) and have more cost effective budget-based control processes than those adopting a non-budgeting mode (Q3).

DISCUSSION AND CONCLUSIONS

The term ‘beyond budgeting’ is used in the management accounting literature to describe a wide variety of practices that organizations adopt to make their operations more adaptive in response to the environmental uncertainty they face. In this paper we follow a conceptual approach through an analysis of the beyond budgeting principles and the management and systems literatures on radical decentralization to theorize how organizations can enhance their adaptability to environmental uncertainty through changes to their management structure and control processes. We show that beyond budgeting can be conceptualized as modes of adaptive performance management.

Beyond budgeting advocates radical decentralization enacted through the management structure described by the six leadership principles. However, the generic descriptions of the

leadership principles are problematic and difficult for researchers and practitioners to apply. This study addressed our understanding of this critical aspect by synthesizing perspectives on radical decentralization, clarifying how this concept relates to the beyond budgeting leadership principles, and proposing that the concept of radical decentralization could be used to assess the adoption of the leadership principles.

Based on this understanding of beyond budgeting we proposed two criteria for distinguishing modes of adaptive performance management. These are the extent of radical decentralization *within* or *beyond* management and the extent to which changes to budget-based control processes are: *improved*, *selectively modified*, *restricted* or *eliminated*. Four modes of adaptive performance management were distinguished based on these criteria, which we labelled better budgeting, advanced budgeting, restricted budgeting and non-budgeting. Each mode is based on a different combination of changes to management structure and budget-based control processes which produces a different level of organizational adaptability. Our conceptualization of beyond budgeting as modes of adaptive performance management confirms observations made in the literature that companies follow different approaches to implementing beyond budgeting (Becker et al., 2009; Hope, et al., 2011).

In this paper we aim to reorient the debate about what constitutes beyond budgeting around modes of adaptive performance management. In our view the non-budgeting mode is just one possible mode of adaptive performance management. It should be noted that not all organizations need to adopt the non-budgeting approach to achieve an adequate level of adaptiveness to its environment. Alternate approaches to adaptive performance management require less comprehensive changes to management structure and budget-based control processes. Nonetheless, organizations operating in highly uncertain environments may

require the relatively high levels of adaptability and may benefit from adopting the non-budgeting mode.

The modes of adaptive performance management proposed in this paper suggest there is no one-size-fits-all approach to managing environmental uncertainty. This is because organizations face different levels of environmental uncertainty and thus require distinct levels of adaptiveness. Our modes of adaptive performance management and associated propositions are intended to stimulate thinking about organizational approaches to adaptive performance management. Future research could use the modes of adaptive performance management to compare changes that organizations are making to their management structures and control processes to better understand the match between an organization and its environment.

This study has implications for beyond budgeting research. Case studies of beyond budgeting organizations need to investigate changes to both management structure and control processes to better understand how organizations are enhancing their adaptability. Beyond budgeting research has tended to focus mainly on changes to control processes without regard to changes in management structures despite acknowledgements that beyond budgeting requires synchronized changes to both management structure and control processes (Becker, et al., 2009; Hope, et al., 2011). This research serves as a reminder to researchers about the importance of addressing both dimensions to understand how organizations are responding to environmental uncertainty.

Future studies could consider the different modes of adaptive performance management from a competing logics perspective. The competing views of organizational control include, for example, the rational, bureaucratic and cultural approaches that reflect different patterns of interaction and socialization (Bititci, Garengo, Dörfler, & Nudurupati, 2012). Organizations are increasingly controlled via social interaction, relationships and peer-

evaluation rather than bureaucratic processes (Bititci, et al., 2012). The rise of the cultural approach may diminish the reliance organization have on control processes.

While this study focused attention on the various ways organizations can manage uncertainty in their environments, Hales (2001, p. 138) argues that organizations seek to achieve the required flexibility or ‘requisite variety’ to handle environmental uncertainty in their operating environments. Future research could consider adaptive performance management approaches from the perspective of requisite variety. Beer’s (1985) viable system model (VSM) indicates how management structures and control processes should be designed to conform to the law of requisite variety. The VSM thus provides a potential framework for considering whether the flexibility introduced by different modes of adaptive performance management achieve requisite variety (see for example O’Grady et al, 2016).

A final issue for future research could be to explore the adoption of beyond budgeting in relation to our four modes of adaptive performance management. Becker et al. (2009) suggest the likely reason for the low adoption rate of beyond budgeting is likely due to the prescriptiveness of the twelve principles and the extensive changes to the underlying management structure associated with moving beyond budgeting. Our conceptual analysis in this paper shows that the changes organizations can make to move beyond budgeting may not be as extensive as previously thought. We believe that our modes of adaptive performance management will help academics and practitioners better understand the ways in which organizations can move beyond budgeting to respond to the environmental uncertainties that they face.

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