Introducing management controls in an entrepreneurial company and its influence on achieving ambidexterity

Sofia Ritzén¹, Susanne Nilsson²

¹KTH, Royal Institute of Technology, ritzen@kth.se
²KTH, Royal Institute of Technology, sumi@kth.se

This paper presents a study of how combinations of management controls are introduced and influencing a small entrepreneurial company over time. Particularly, it studies why these controls are introduced and how they are influencing the company’s ability to achieve ambidexterity i.e. to be flexible and innovative and yet enable the efficiency required. Using a combination of interviews and document analysis in an entrepreneurial clean-tech firm rich data on the emergence of management controls is collected. The preliminary analysis shows that drivers for introducing management controls goes from external to internal factors over time and that personnel controls slowly are replaced by more formal processes until the firm experience a fast growth in size. In this phase, the organisation is seen to intensively introduce both more formal processes and structures in parallel to a strong focus on a consciously strengthen its entrepreneurial cultural to achieve ambidexterity. The study is able to put some light on challenges related to how small entrepreneurial companies are managing an ambition to remain innovative while increasing its level of management control as a response to its growing in size. The result from the study indicates that the types of management controls in use over time builds on each other and that the introduction of management controls to manage innovation is particularly challenging.

1. Introduction

Growing larger, entrepreneurial companies often face a need to structure their organization and implement strategy (Davila, 2005). This is basically due to that growing and scaling-up requires other managerial skills for handling both an increasing number of diverse customer-tailored solutions on the market as well as an increasing number of employees. Also employees are with time more and more unfamiliar with the idea of the start-up and common processes are lacking for e.g. communication and documentation. This need of transition typically occurs in what Moores and Yuen (2001) call the growth phase and Davila (2005) report a size of approximately 30 employees and an age of 8-10 years where management controls of various types are built in the company. However, many small companies fear that an increased formalization and usage of managerial controls will take away the innovation capability based in the entrepreneurial culture and some of the very basic positive characteristics of being a small and flexible growing company (Harryson, 2008). Communication paths are especially easy and self-established in smaller firms (Moores and Yuen, 2001) and in a firm characterized by entrepreneurship new things are constantly found or developed, people act autonomously and uncertainty is embraced (Langlois, 2007). In parallel, a firm with formal structures and management control are likely to be experienced as bureaucratic with long decision paths (Quinn 1985) and strong regulation of resources gives pessimism towards new initiatives (Sykes and Block 1989). Some of the basic positive characteristics of being a smaller entrepreneurial firm seem to vanish with tougher management controls.
(Harryson 2008). Therefore there is a strong need to further understand the consequences of the introduction of management controls in order to increase the knowledge on how to support entrepreneurial companies so that they remain both innovative and entrepreneurial in ways of working and at the same time secure formal requirements as well as the efficiency required.

The need to manage both innovation and efficiency can be described as that these companies need to become ambidextrous organizations (Tushman and O’Reilly, 1995). Large firms are the target for studies in the majority of ambidexterity studies (e.g. Lavie et al., 2010) and consequently to a major extent focus on organisations that need to go from formally structured and with a habit of controls to more flexible and with employees driving innovation. The need to become ambidextrous can hence be described to be similar in small entrepreneurial companies as in large mature firms, though these different types of companies are departing from different positions. In addition the role of the individual in innovation is of specific interest as the entrepreneurial organization so typically is dependent on each person in the organization and their autonomy and the larger organization is deploying controls that in much relate to controlling behaviour and actions of its people (Merchant 1985).

In this study we are investigating how and why different types of management controls are introduced in an entrepreneurial company over time. We investigate the company by illustrating controls deployed during the growth of the company (partly in retrospect) and approach closing a gap that e.g. Davila (2005) identifies, i.e. understanding when adoption of new controls take place, what drives new controls and how they are developed. The paper provides insights on how both innovation and efficiency are handled in an organization determined to grow into an ambidextrous organization and on the consequences from increased structure and new controls.

2. Previous work

Understanding how organizations can achieve ambidexterity has gained an increased focus in the innovation management literature (Lavie et al., 2010). This research focus on how companies identify strategies that enable their organizations to be reasonable successful in both managing activities that focus on refining existing offers and processes and in managing activities that focus on realizing new offers (March, 1991). The former activities are most likely to support operational efficiency and to produce incremental innovations while the latter are required for the production of more radical innovations. For both mature and entrepreneurial organizations this is of outmost importance as refinements means taking small risks to secure a stable cash flow with reasonable resource consumption, while radical innovations, accepting higher risks, may secure a long term survival and keeping the organizations position on the market. Several approaches on how to manage incremental refinements as well as radical innovations have been suggested in literature with separation of exploiting current deliverables and exploring new opportunities as a common denominator, i.e. organizational, timely and domain separations (Raisch et al., 2009; Lavie et al., 2010).

The underlying argument for separations for ambidexterity is due to that the completely different characters of refining existing solutions and realizing completely new offers make them hard to coexist. However, the problem with separations is isolation and as a consequence many innovation initiatives fail to become accepted in the organization and have the accurate resources for being accomplished. A contrasting solution is what is referred to as contextual ambidexterity (Gibson and Birkinshaw, 2004), which put the individual employee in the center. Through contextual ambidexterity individuals make choices between exploiting what they have and exploring new things in their everyday tasks, as for sales or R&D to focus on existing customers’ needs or elaborating on new customers and their needs. This requires systems and structures that are more flexible and allowing employees to use their own judgement as to how they use their time and a greater focus on nurturing a context where employees are autonomous. The role of top management is to shape management controls for the appropriate nurturing and it is also critical how they act themselves on a day-to-day basis. The context will then be further reinforced by the actions taken by the employees throughout the organization. Hence, of particular interest is to understand how the combination of management controls are used to shape the context, defined as according to Goshal and Bartlett (1990) the less visible set of stimuli and pressures that motivates people to act in a certain way.

Gibson and Birkinshaw (2004) shows the importance of combining performance management and social support (a combination of support and trust) creating a high-performance organizational context which in turn gives rise to an ambidextrous organization. They point to the importance in designing a context that is both high performance driving and accomplishing a strong social support. They also showed that the type of leadership enabling an ambidextrous organization can vary, however, communicating and exercising a clear set of few priorities is found to be crucial. In addition the consistencies with which these priorities are applied and the number of employees they affect is more critical than what content these priorities are about. Securing that employees understand these priorities also showed to be important. Translating this to management control literature it means that a few controls of several types, i.e. personnel controls in combination with action and result controls that are performance oriented should be deployed consistently. This is also interesting in relation to what McCarthy and Gordon (2011) found: different management
control systems needed to be put in place in order to secure both exploitation and explorations. Their categorization of
control systems (belief, interactive, boundary, and diagnostics systems) relate well to securing social support and
performance measurement.

In a smaller firm the separation of resources or of different activities might not be feasible or attractive why the building
of an environment that can handle both innovation and efficiency is desirable. There are a number of sources in
innovation management defining what is characteristic for the innovative environment. Kanter (1983) states that sharing
and distributing information and knowledge on strategies, customer needs and markets is characteristic, and Cardinal
(2001) stress the facilitation of using diverse knowledge. Stimulating the tacit dimension of knowledge, i.e. knowledge
that is not easily expressed or documented (Polanyi, 1969) is found to be particularly supportive for innovation. This is
found to be facilitated through face-to-face meetings where dialogues are encouraged and basic assumptions are
challenged (von Krogh et al., 2000), by using strategic plays (Roos and Statler, 2004) or strategic dialogues (Dougherty
and Hardy, 1996). Enabling a creative climate characterized by a high level of trust (Ekvall, 1996), encouraging new
ideas (Damanpour, 1991), and accepting risk taking and conflicts (Ekvall, 1996; King, 1992; West and Anderson, 1992)
have been shown in a large number of studies to support innovation. Other important aspects is e.g. a focus on
employee’s tasks and intrinsic motivation and expertise development (Amabile, 1988), creating conditions for
experimentation and collaboration (Damanpour, 1991; Thomke, 2001; Burgelman and Sayles, 1986) as well as
tolerance of failed ideas (Madjar et al., 2002). Several of these features come hand in hand with an entrepreneurial firm
though they might become more difficult to rely on as appearing themselves with a firm growing in number of
employees. With this growth also comes the need to structure the organization and implement strategy. A wise use of
resources and securing that all employees act according to needs and strategies of the organization becomes critical and
both innovation and efficiency needs to be considered.

Management control is setting directions, regulating and steering people and relate strongly to the implementation of
strategies in organizations (Anthony 1988; Herath 2007). It also relates to the control of behaviour of people. Merchant
(1985) points out that control is the steps that managers take to direct people so that they do what the organization needs
from them. A proper use of different types of management controls have been shown to be supportive in handling
tensions arising from the need to manage conflicting goals and to produce unique capabilities in an organization (Henri,
2006; Widener, 2007) as those arising from being both innovative and efficient. This point to the value in studying how
organisations can achieve ambidexterity by introducing a combination of different types of management controls.
Merchant (1985) developed a categorization of controls based on the target for the control. He defined three categories;
result controls that are defining and setting targets for expected future results; actions controls that define guiding and
monitoring instructions in order to control people’s behaviour; and personnel controls that aim to influence conditions
enabling a certain desired behaviour of people. Results controls, as goals, targets and measures, do not control
behaviour directly but strive to communicate a predefined result. Therefore result controls may be perceived as
facilitating creativity and novelty as employees experience freedom and autonomy (Zollo and Winter, 2002), e.g. action
controls as goal setting. The use of a few and broad challenging goals related to time, cost and performance is a
common approach used by top innovating firms (Quinn 1985). Seemingly impossible goals may in the same time be
experienced as discouraging and research reveal contradictory results concerning the relation between controls and
innovation (Damanpour 1991). Another example is for action controls: formal procedures may restrict an innovative
behaviour, e.g. experimentation (March and Simon, 1958) by restricting autonomy, or rather be used as a tool for
employees own steering of activities rather supporting innovation (Adler and Borys, 1996). Personnel controls is
equally important to reflect upon when it comes to innovation, the characteristics described above for an innovative
environment might not be possible to regulate directly but need to be taken care of through developing the right
circumstances for employees.

How management controls emerge over time is not well-understood although the few studies that have been performed
indicate that such research could provide valuable knowledge (Davila, 2005). Studies performed shows for instance the
path-dependency of management controls and how the introduction of management controls becomes more important
for organisations while moving through their growth stage (Moore and Yuen, 2001). In order to increase understanding
of how entrepreneurial companies in a phase of fast growth are managing the ambition to be both innovative and
efficient, two research questions emerge in need for further investigations:

1) What are the driving forces of management controls and their consequences on managing innovation in a small
environmental company?
2) How is the use of different management controls influencing an entrepreneurial company’s ability to be both
innovative and efficient i.e. ambidextrous?

3. Research design

The company in this study is a Swedish clean-tech company that delivers industrial biotechnology based products and
services for sustainable buildings and waste management. The company has 32 employees and has since its start in
2004 been focused on replacing chemicals with advanced biotech products. Compared to dominant technology in the area the solution sold by this company contributes more effectively to a sustainable society. The company is at present in a strong growth phase and has a strong ambition to start exporting within a few years. The firm started in an entrepreneurial setting by four people still owning and being active in the company.

Interviews with twelve respondents have been conducted, representing a multitude of functions, hierarchical levels and years of working for the company. The interviews were conducted between 60-90 minutes and the interviews were recorded, transcribed, coded and analysed accordingly. NVivo has been used to structure and handle interview data when coding and categorizing. In particular attention has been given to the categorisation of the type of management controls deployed over time. The interview questions related to the value and norms, structure and processes and goals and performance measurement in the company in addition to how the innovation process has emerged over the years. The researchers also gained generous access to relevant documentation to support the identification of what different types of management controls were introduced over time and how these introductions were associated to changes in organisation and product system offers. In an iterative manner researchers have met with company representatives with a dual purpose: to validate findings and to contribute to the development of the company.

4. Findings

4.1 Management controls over time

For the first years, service routines and economic systems were the dominating controls in the organization and the culture was dominated by a problem-solving attitude where everyone did everything. Communication was open and vivid among all people in the organization. Good customer relations were the main focus and over the years a clear principle of “budget rules” settled. The first employee complementing the four founders was an economist managing accounting/financial activities. The company was by then characterized by results controls and also by a state were controlling was not experienced as needed as everyone in the organization were well anchored in its vision and were involved in decisions, i.e. personnel controls where in many ways present though not formulated. As the company was growing, action controls become deployed, e.g. routines for assessment, accounting systems (also legally required) and systematic processes for sales and service were developed. This is clearly seen when the company is about ten years and a COO is hired with a specific aim to reinforce the CEO. Driving forces is a need to coordinate people more efficiently and secure a sound resource usage. “Being in control” becomes attractive. The company has since grown to today’s about 30 people. It was recently re-organized with several changes also on managerial levels. More action and result controls are requested and also established even though this effort is not finished as reported by the managers interviewed. Business goals related to sales are defined on a company level, goals for some groups and individuals are set. For sales and service clear processes are developed and also experienced as highly effective, e.g. new sales personnel is more efficiently introduced to their work and time for customer visits is reduced without actually meeting the customers less. For R&D, formal processes are not yet established.

In parallel, nurturing the culture of the company is an important issue. From start a strong culture of entrepreneurship has permeated the company accompanied by a willingness to have a real impact on sustainable development, sometimes expressed as “we should save the world”. Interviews also reveal a consistency among respondents that each individual is highly valued and a concern to make people involved, stay committed and consequently taking responsibility for progress. The company is experienced as joyful to work in and several principles are developed that relates to personnel controls. When the company is about seven years old the key elements in the company culture is explicitly expressed: from having been present as a more or less invisible set of values and norms or common understanding, a booklet is produced containing the vision, business strategies and basic values of the company. This booklet is renewed every year or even more often and is found to be a highly appreciated and useful tool for communicating the company’s key priorities to its employees. When launching the recent re-organization the booklet was used as a tool to visualize the changes made; functions were illustrated as overlapping circles rather than hierarchical levels in order to communicate the desired culture and uniqueness of the firm. In addition, a formal planning and performance evaluation process for employees on an individual level is also designed and put in place to further strengthen the control of employee behaviours. Also during the fast growth phase, the company is found to employ individuals for specific tasks mostly related to sales and technical services.

4.2 Innovation and Efficiency

The culture of the company was by its start identified as open and all people in the organization were highly involved in every step and with informal meetings and common knowledge development. Still today, much of this is true although decisions have become a management responsibility, as natural when growing in numbers and establishing managerial
levels. The fast pace and flexibility, also a heritage from early years, is still highly appreciated and reveal a company characterized by high-attention to business and with a strong foundation in its basic values. These values concern a strong customer focus and bringing actual value to the market. In much this way of working relates to innovation and employees see the company as highly innovative. In the same time some respondents illustrate that innovation as a concept or goal is not explicitly expressed or discussed though sales is a reoccurring issue and concern. Other respondents report that their view of innovation is that innovation concern a number of things in the organization from incremental process innovations to radical new business.

According to a number of respondents, an innovation process is lacking in the company. An idea management process (an idea box) was introduced a couple of years back which initially was effectively used including promotions for ideas selected by the CEO with instant feedback and clarity on which ideas that would be further developed. However, the idea box has since the last two years lost its function as employees no longer are willing to hand in ideas. The main reason behind the low number of ideas handed in is raised to be due to a lack of feedback from management as well as to a general increase in time pressure. The responsibility of the idea box is also unclear. At a certain point in time also a technology road map, was developed by a consultancy, however it seems for employees to have had a small impact on providing direction or guiding. Specifically top management are by the time of the interview quite determined that it is in particular personnel controls that are needed to get a more effective innovation process in place.

Top management reports a concern and dissatisfaction that innovation is too little considered; a concern that is present despite the company is doing fine financially. An empty idea box is interpreted as an indication of a general lack of ideas. R&D is viewed as having become a service support occupied with incremental product improvements and management would like to see more of individual initiatives focusing on exploring new opportunities. A more visionary and business oriented culture similar to the early days of the company is seen as desirable.

The dynamic business that has emerged with fast decisions and altering directions is for some of the respondents expressed as also putting some negative pressure on employees. Changes are not always experienced as motivated, or at least not at the pace of which changes are made. Other circumstances reported by respondents are unclear responsibilities as effects of changes in functions and priorities within the company. This means that developing formal structures is for many employees seen as something positive and they experience a direct correlation between the introduction of more formal processes and increasing efficiency. Structure and control is needed for a continuous improvement of products, overview of future developments, understanding new needs, strict time plans, documentation and templates, a careful recruitment of new employees and processes for almost every function within the company. Also management expresses a need to increase efficiency, especially in the sense of using the accurate resources and bring value from each action and employee.

5. Discussion

5.1 External and internal driving forces to introduce management controls and its consequences

Merchant (1985) models of different management controls served well to identify the various controls that the entrepreneurial company in this study has introduced during their growth. In their initial start-up phase financial result controls and personnel controls were dominating. The need of steering employees was not necessary as the four founders were all highly committed to an involved in all parts of the business. While growing an increased number of action controls came in place further controlling processes as economy, sales and service. Also, the financial controls were further enhanced by the fact that the company’s first employee was an economist. The company’s initial strong reliance of individuals taking initiatives in combination of the usage of financial result controls is not particularly surprising. Entrepreneurial companies heavily depends on its founders during its start-up phase whose focus is on building the business and securing further financing to support its growth (Harrision, 2008). The founders are naturally committed and knowledgeable and problems are solved one-by one with the focus on building the customer base and adapting the technology to each customer needs. From an ambidexterity perspective, the company in its start-up phase can be described as having a contextual ambidexterity in place (Gibson and Birkingshaw, 2004); every individual decides themselves backed up by the financial controls how much time to spend on existing products and customers and how much time to spend on identifying novel opportunities or addressing new needs. No specialization or separate organization is created to nurture explorative and exploitative activities respectively even though it is believed that the entrepreneurial founders were dominated by exploration activities.

While growing the company is found to meet its need to better manage an increasing number of customers and employees by implementing an increased number of actions controls i.e. guidelines, protocols and work processes. The driving forces in the first years are foremost external ones and the study reveals particularly how troublesome or demanding customers force the organization to introduce an increased number of management controls. In addition,
regulations both financial and quality related, starts to kick in as the business grows and the development of products increases. The specialization of individuals also increases even though everyone is still expected to help the firm with the highest priorities tasks at hand. Referring to the literature, the company studied can be described to follow a corporate life-cycle (Miller and Friesen, 1984) with a typical transition resulting in an increased number of formal management controls (Davila, 2005). It has left a one-side innovation perspective driven by the entrepreneurail founders, entered a phase of increasing structure and strategy and efficiency and bounces back to set up an ambition to secure both innovation and efficiency. A contextual ambidexterity (Gibson and Birkinshaw, 2004) was present in the first stage though has weakened with number of employees. What makes this case company particularly interesting to study is its explicit ambition to not fall into the “trap of formalization” and become an overly bureaucratic, structured and slow-paced company and our results show how the company has taken particular actions to face the challenges related to this issue.

The driving forces to introduce new management controls become over time more internal with the larger workforce requiring more aligned and clear processes. The driving force is a facet of efficiency where the resource frugality is important as the company still requires individuals to not becoming too specialized. The introduction of guidelines and processes etc. is driven by a need to make the introduction of new employees more effective and additional processes are developed with a more clear human resource management focus (personnel policies, incentives, individual goal and follow-up etc.). These efforts are experienced as mainly successful with the consequence to increase efficiency. As an effect from the increasing number of new employees the holistic overview is now lost for the majority of employees. As a compensation for this lack, the management team is found to take a number of actions to strengthen the spirit and values put forward by the original founders as means to support the commitment and initiative of their employees. The result from the study shows that the company has been successful in ensuring that many critical innovation supporting factors are in place including a mix of different management controls. For instance, the management team is generous in sharing and distributing information and knowledge on strategies, customer needs and markets (Kanter, 1983). Tacit dimensions of knowledge, i.e. knowledge that is not easily expressed or documented (Polanyi, 1969) is facilitated through regular face-to-face meetings where dialogues are encouraged and basic assumptions are challenged (von Krogh et al., 2000). The respondents are all emphasizing the human side of the company’s values where individuals feel respected and trusted and new ideas are encouraged; crucial elements of an innovative climate (Amabile; Ekvall, 1991). Also, creating conditions for experimentation and collaboration (Damanpour, 1991; Thomke, 2001; Burgelman and Sayles, 1986) as well as tolerance of failed ideas (Madjar et al., 2002) is found to be prominent features of the company’s values. The company can hence be described to have prepared for remaining flexible and innovative and avoid falling into the trap of the “large company”.

5.2 The challenges associated to introduce controls while securing ambidexterity

There are a number of elements crucial to enable innovation that is present in the company and efforts taken with new management controls have increased efficiency. Still it is not possible to say that ambidexterity is secured. The concern of the management regarding fewer expressed ideas and lacking innovation initiatives must be taken seriously. Employees on the other side bring forward the need to further support the exploitation, i.e. they experience gaps related to structure and support for operational tasks as many of these tasks require repeatedly “the wheel to be reinvented”. This dual view of what the true challenge related to become ambidextrous is for a small growing company shows the importance in not only interviewing managers in order to better understand how companies can become ambidextrous. It is further emphasized as the results show that when action management controls with the purpose to enhance efficiency is introduced in the company these seem to remain and become accepted and used. On the opposite when action controls are implemented to support innovation management, the study shows that these controls have a tendency to not become used over time illustrated by the idea box and the technology road map developed.

It should also be pointed out that it is contextual ambidexterity that the ambition of the company concern, structural ambidexterity is at least not yet considered, which probably should be done as a complement, based on the research by Gibson and Birkinshaw (2004). A benefit of structural ambidexterity is that it accepts that not all employees are suited to exploit and explore activities by will or ability and this has not either been considered in recruitment of new employees in the company studied.

Interestingly, the intention by top management to develop an innovation process is outspoken at the same time as a new controls are deployed driven by internal needs of structure and efficiency. A likely explanation is that the strong business culture and visionary leadership makes the founders and top management reflects upon what could be lost from a firm structure. Though some tensions they have good prerequisites to develop ambidexterity. The explanation to this seems to be the ambition to both be innovative and effective, to not loose innovation from the start-up phase and the entrepreneurial culture and still become more efficient.

Based on both control literature (Merchant, 1985; Henri, 2006; Anthony, 1988; and others), ambidexterity literature (Tushman and O’Reilly 1995; Gibson and Birkinshaw, 2004; Lavie et al, 2010; and others) and from more rare sources
that combines this theoretical fields (e.g. McCarthy and Gordon, 2011) the company investigated in this study has a good foundation for being both innovative and effective. The culture developed from start is still vivid emphasizing both a strong result performance management and generous social support; key elements in a contextual ambidexterity solution (Gibson and Birkinshaw, 2004). Controls are of various types and support both exploitation and exploration (McCarthy and Gordon, 2011). To further support exploration and innovation, innovation goals could be introduced along with a more clear communication on what is expected from employees related to innovation. The booklet developed can be used as a tool to support the communication by making the goals and priorities more clear to employees. Also, a challenge may be for the company to patiently secure innovativeness and efficiency separately and allow separation in time for the actions that are developing their management controls.

6. Concluding remarks

The study is able to put light on the challenges related to how small entrepreneurial companies are managing an ambition to remain innovative while increasing its efficiency through management controls as a response to its growing in size. The result from the study indicates that the types of management controls in use over time builds on each other and that the introduction of controls to manage innovation is found to be particularly challenging. This particular company reveals a diversity in management control types that lay an appropriate foundation for handling tension between conflicting goals. The have also a number of innovation characteristics in place why their point of departure for securing ambidexterity is strong.

The study shows the importance for top management to carefully and consciously consider the mix of management controls introduced. In addition, it reveals the differences in views between management and employees when it comes to whether innovation is in need for management controls or not. Further, the number of controls should be scrutinized so that the ones deployed are consistently used in order to secure ambidexterity, controls should also be analyzed in relation to whether they drive performance with goals and measures or social support in order to secure that both these factors are achieved.

Major limitations of this study are the one-case analysis and that interviews are always describing a specific phase in the company and especially in small entrepreneurial organizations contexts can change fast. Cross-case-studies as well as longitudinal studies should be designed to further explore how small fast growing companies are managing ambidexterity through management controls.

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