

Strategic Cost Management: Critical review over the last three decades

Abdelhak ATOUT*

Abstract:

The major purpose of this paper tackled developed a theoretical model that describes the reciprocal relationship between SCM and some important environmental factors. The findings indicate that researchers and practitioners still suffer from one serious conceptual framework of SCM, meanwhile the term itself is not well understood, and the lack of the widespread adoption of SCM practices makes it difficult to evaluate the success or failure of SCM.

Key words; Cost Management, Strategy, Organizational Performance

ملخص: يهدف هذا المقال لوضع اطارا نظريا يصف العلاقة التبادلية بين التسيير الاستراتيجي للتكاليف واهم المتغيرات البيئية. النتائج بينت ان الباحثين والمهنيين لا زالوا يفتقدون الى اطار مفاهيمي للتسيير الاستراتيجي للتكاليف. فيما يبقى مصطلح التسيير الاستراتيجي للتكاليف نفسه غير مفهوم جيدا، بالنسبة للباحثين والمهنيين. اضافة الى ذلك، يبقى عدم الانتشار الواسع في استعمال طرق التسيير الاستراتيجي للتكاليف يجعل الامر صعبا في تقييم نجاح او فشل هذا المنهج الجديد.

الكلمات المفتاحية: تسيير التكاليف، الاستراتيجية، أداء المؤسسة

Résumé :

L'objectif de cet article nous avons développé un modèle théorique décrivant la relation réciproque entre la GSC et certains facteurs importants. Les résultats indiquent que les chercheurs et les praticiens sont en manque d'un cadre conceptuel sérieux de la GSC. Le non application élargie de ce terme le laisse ambigu et de ce fait on ne peut évaluer sa réussite ou son échec.

Mots clé : Gestion des Coûts, Stratégie, la Performance Organisationnelle

* Assistant professor "B" at University of Blida 2 Ali Lounici

Introduction:

During the 1980s, management accounting and accountants have been criticized for the failure to recognise organizations' new strategic priorities,¹ and the vast majority of management accountants have been regarded as technical specialists. As consequence few years ago, there is no potential for management accountants to participate much more in management decision making². Shank (1989), pointed out that "too many management accountants are asleep at the switch! *What is the evidence that the fundamental concepts of management accounting are changing or that they need to change? What is the evidence that too many management accountants are lagging this change rather than leading?*"³

These criticisms have been accompanied by demands for accountants to take advantage of changes to elevate their position within the management hierarchy, where issues of strategy formulation and choices are discussed and decided. On the other hand, they must not accept the current production environment as given and implement policies that are optimal with respect to these existing conditions. However, management accountants must change the nature of information they provide. Furthermore, this movement of blames and warnings has also directed towards researchers and major accounting research journals.⁴

This movement has been understood as the natural reaction to the dramatic changes that organizations have faced in their business environment which triggered: worldwide competitive pressures, deregulation, growth, lean manufacturing, advances in information technologies (Internet & E-Commerce), greater focus on the customer, and new forms of management organization⁵.

Under such conditions of harsh competition, conventional cost management based on assumption of long production, runs of a standard product with unchanging characteristics and specifications will not be relevant (Kaplan, 1983).

Research objectives:

The purpose of this paper is to provide a review of the origins of SCM*, and to assess its “success” or “failure”, by reviewing some academic papers, since Simmonds has first introduced the concept of strategic management accounting SMA in 1981. By summarizing the different classification of SCM techniques and practices, after more than three decades, finally we will provide some important findings related to the reciprocal relationship between SCM and the internal and external business environment variables.

Research questions:

In order to simplify the main purpose of this paper, the following questions are addressed:

- *To what extent do organizations use strategic cost management techniques?*
- *To what extent SCM techniques could be helpful for organizations to enhance organizational performance and gain sustainable competitive advantage?*

1) Strategic cost management literature review:

The internal and external warning signs of dysfunctional obsolete cost accounting systems⁶, has lead Simmonds (1981) to suggest some changes to conventional management accounting, to include provision and analysis of management accounting data about organization and its competitors to support managers in developing and monitoring the business strategy, which is called “Strategic Management Accounting” SMA*⁷. He defined SMA as "*The provision and analysis of management accounting data about a business and its competitors for use in developing and monitoring the business strategy*"⁸.

SMA has been presented as an efficacious approach to strategy formulation and implementation, and various authors have posited

slightly different terms for this phenomenon⁹, including accounting for strategic position by Simmonds (1986).

Shank (1989) approaches SMA from a different perspective by considering the transition from “cost accounting” to “managerial cost analysis” as one primary accomplishment, looking backward, consequently the transition from “managerial cost analysis” to what is called “strategic cost management (SCM)*” will be consider as the primary challenge looking forward¹⁰.

Shank linked explicitly the role played by SCM to one or more of the four stages of strategic management to create competitive advantage¹¹. Further perspective on SMA have been offered by Guilding et al (2000), which entails and focuses on what constitutes a SMA practice (i.e. focus on competitors; long-term; forward looking orientation). This perspective was considered as confluence of the ideas of earlier writings on SMA, e.g. Bromwich (competitor focus); Simmonds (marketing focus) and Wilson (future focus).

However, the term SCM itself is open to a number of interpretations. Despite the normative work that has made contributions to SCM and SMA, SCM still suffer from one serious drawback and there still seems to be paucity of examples in the literature. These academic researchers are often disconnected from what actually happens in organizations¹². Many authors stated that SCM still ill defined (Tomkins & Carr, 1996; K. Langfied-Smith, 2007). Despite that, there is a consensus that strategic priorities should be supported by appropriate management accounting to interface cost structure with long-term business strategy and short-term tactics¹³.

2) Strategic cost management techniques:

There is no general agreement about what constitutes SCM techniques and practices. This is taken to mean that neither researchers, nor practitioners have a conceptual framework of what cover SCM practices. However, the degree of subjectivity is

considered as primary factor, when attempting to develop a listing of SCM techniques¹⁴.

Guilding et al (2000), provide in their study 12 SCM techniques, which are: attribute costing , brand value budgeting and monitoring, competitor cost assessment, competitive position monitoring, competitor appraisal based on published financial statements, life cycle costing, quality costing, strategic costing, strategic pricing, target costing, and value chain costing. Despite the geographic dissimilarity in their study, most of the SCM techniques appraised were not widely used¹⁵.

In another late study, Cadez & Guilding (2008), gave 16 SCM techniques* derived mostly from the previous studies done by (Guilding& McManus, 2002; Guilding et al, 2000; Cravens & Guilding, 2001). These 16 SCM techniques were categorized into five broad sets, which include: 'costing', 'planning, control and performance measurement', 'strategic decision making', 'competitor accounting', and 'customer accounting'. The table below summarizes the 16 SCM techniques based on Cadez&Guilding (2008) classification.

Table1: SCM techniques classification

SCM technique categories	SCM techniques
Costing	1- Attribute costing 2- Life cycle costing 3- Quality costing 4- Target costing 5- Value-chain costing
Planning, control and performance measurement	6- Benchmarking 7-Integrated performance measurement
Strategic decision making	8- Strategic costing 9- Strategic pricing 10-Brand valuation
Competitor accounting	11-Competitor cost assessment 12-Competitive position monitoring 13-Competitor performance appraisal
Customer accounting	14-Customer profitability analysis 15-Life time customer profitability analysis 16-Valuation of customers as assets

Source: **Cadez, S. & Guilding, C.** *An exploratory investigation of an integrated contingency model of strategic management accounting*, Accounting, Organization and Society, (2008), 33,p: 839.

3) Strategic cost management and competitive advantage:

To survive in today's harsh competitive pressure environment, SCM must provide the information that is necessary for the formulation, implementation and realization of strategies for achieving competitive advantage. The latter is a means to the end of a strategic position. For this reason, strategic position has been named accounting for competitive advantage¹⁶.

The most important strategic elements for an organization are its long-term growth and survival. The key to achieving this goal is to gain "competitive advantage". Therefore, SCM effectively requires a broad focus to develop and identify superior strategies that will produce a sustainable competitive advantage, by creating better customer value for the same or lower cost than offered by competitors¹⁷. Moreover, Porter (1985) argued that the importance of

competitive advantage could hardly be greater due to the fact that organizations face slower growth as well as domestic and global competitors. Hence, simply extending cost management beyond the walls of the factory is not sufficient; SCM requires extending the process beyond the firm's boundaries¹⁸. This extension enables a firm to take advantage between it and its suppliers as well as its customers. Competitive advantage starts with the premise that it can arise from many sources, it grows fundamentally out of value a firm is able to create for its customers that exceeds the firm's cost of creating it¹⁹. Thereby, Porter has proposed two basic types of competitive advantages: cost leadership and differentiation. However, these sources of competitive advantage do not lead to above-average performance unless they are sustainable vis-à-vis competitors.

In summary, depending on the above research findings and arguments, we can conclude that SCM techniques usage may consider as a fundamental key that supports organizations to gain sustainable competitive advantage.

4) Strategic cost management and organizational performance:

In addition to the criticisms that management accounting has received in the earlier 1980s, the warnings has also directed to the dysfunctional of traditional performance measurement systems (PMS) due to several reasons, i.e. well-documented inadequacies, their backward-looking, and their inability to reflect contemporary value-creating actions²⁰. Consequently, managers' actions make them look good in the short term, but not good for shareholders and long-term organizational health²¹. Some other critics go much further in their indictment of financial measures, by considering the latter as the logical consequences of operational actions, they argue that the term of competition has changed, thereby traditional measures do not improve customer satisfaction, quality, cycle time, and employee motivation²². The organizations are strongly urged, that their PMS must embrace operational or non-financial performance measures.

In order to face the general dissatisfaction to the traditional PM, Kaplan and Norton attempted to explain and reduce this disparity between both financial measures and operational measures (customer satisfaction, internal business performance, innovation and improvement), by what they named the “balance scorecard”. However, their set of new measures is derived from the organization’s particular view as key success factors, and this view is not necessarily correct. Even an excellent set of balanced score ‘BSC’ card measures does not guarantee a winning strategy!²³

In addition, some critics and limitations were associated with BSC, since the latter is not enough comprehensive to consider the other internal and external factors to organization such as employees, customers, suppliers, regulators, technology and environment²⁴. Moreover, Otley (1999) stated that the four dimensions of BSC are rather simplistic and do not take into account some key stakeholders' interests (e.g. competitors)²⁵.

In summary, today executives have awareness that their performance measurement systems strongly affect the behavior of managers and employees. Despite this fact, few organizations appear to have systematic processes in place to ensure that their performance measurement systems continue to reflect their environment and strategies²⁶.

5) Strategic cost management researches and findings:

5-1) SCM and the conflicting points of view:

The variety among institutional theories about SCM may suggest theoretical richness but some argue that there is a need to link all the contributions into a more compact theoretical body of findings that enable researchers to understand the novel approach²⁷.

However, criticisms are in both directions. One supports the transition to new methods and techniques of management accounting, which is called strategic cost management SCM (Simmonds: 1981;

Shank, 1989; Shank & Govindarajan, 1992; Chenhall & Langfield-Smith, 1998; Tillman & Goddard, 2008; Cadez & Guilding, 2008; Anderson & Dekker, 2009), and suggested in addition to the development of SCM, that accountants are assuming to involve much more in the strategic management process²⁸. In summary, SCM has gained momentum as a new conventional position and advocates that firms should shift the focus of their performance measurement to include multiple indicators such as (Quality, inventory levels, flexibility, set-up times, innovation and the so-called balanced scorecard²⁹). Nevertheless, authors and researchers have also debated that the concept of SCM is easier said than done. Guilding et al, in (2000) conclude that SMA appears to be negligible in organizations and practicing accountants have a limited appreciation of what the term means.³⁰ Attention is also paid to some of the problems associated with the various techniques SCM offered, particularly the difficulties involved in ensuring their wide spread adoption by management accountants³¹. Further and, perhaps even more crucial, the extent usage of SCM will continue to be underestimated until management accountants are ready to look at the basic questions of SCM³². This is taken to mean, if SCM done poorly, it cannot be only ineffective, but harmful and indeed destructive.

In contrast, others argue to develop the traditional management accounting methods and ensure its ability to achieve accounting purposes as well as strategic objectives. Bromwich & Bhimani (1994) rejected the view that management accounting is in crisis, and they simply explained that the short-term and internally-focused approaches are inadequate accounting information.³³ Smith (2007) considered that Simmonds's view was a curious claim when he stated that SCM is "spreading rapidly in practice". As several years later, writers maintained that SCM have not been adopted widely (Guilding et al, 2000; Lord, 1996). And too much management accounting research (MA) is divorced from actual MA practices.

Lord (1996) goes much further, and argued in his case study, that the characteristics that have been ascribed to SCM are likely to be

already operating in many firms, and asked whether SCM was “a Figment of academic imagination”.³⁴

The bottom line of this ambiguity is how an organization could quantify and measure the impact of SCM techniques on its financial and non-financial competitive performance, in order to gain sustainable competitive advantage?

5-2) Contingency theory and strategic cost management:

Contingency theory has emerged in the mid-1960. Therefore, the latter theory is relatively new in the accounting literature³⁵. Before the mid-1970, this fact has changed significantly, and the contingency theory approach quickly became the dominant theory in empirical management accounting research.³⁶ This theory hypothesizes that organizational structure is a function of context, a context that is simultaneously determined by the contextual factors³⁷ (e.g. the external environment, size, culture...etc.).

6 -Business environment (contingency variables) and the extent usage of SCM techniques

6-1) Geographic location and the extent usage of SCM techniques:

It is obvious that each country or geographic area has each own features and each own business environment, previous literatures suggested that differences in both practices and purposes across countries and nations are significant.³⁸ Joshi (2001) found in his study that the adoption rate in India for traditional management accounting techniques was higher than for the recently developed techniques, while the implementation rate of SCM techniques had been rather slow. He also found significant differences in the adoption rate between India and Australia, and concluded that these differences related mainly to cultural values³⁹. Another study done by Cadez & Guilding (2007), found that SCM techniques applied in Slovenia varies considerably. Thereby, competitor accounting was the most

extensively applied dimension of SCM techniques. Second findings related to the international comparative analysis of 16 SCM techniques investigated, eight of them have been found to be used significantly more in the Slovenian than in Australian companies. Therefore, and according to the above assertions we could generally state at least in the above studies (samples) that:

There is significant difference across countries in the extent usage rate of SCM techniques (techniques, practices and purposes).

6-2) Competitive forces and the extent usage of SCM techniques:

Intensity of competitive forces also considered as one of the most important factor that affect any organization and its extent usage of SCM techniques. Moreover, the intensity of market competition is one of the reasons that contribute to create this new set of SCM techniques.⁴⁰ Fowzia (2011) found in her study that, increased competition and uncertainty conditions put significant pressure on corporate management. Therefore, range of SCM techniques has emerged in response. She concluded that the usage level is different regarding industry size, strategic pattern, strategic mission and strategic positioning. She also found that only Activity-based Costing, Target Costing, and Strategic Costing Techniques are significant to achieve strategic effectiveness⁴¹. According to the previous assertions, we could generally state at least in the above studies (samples) that:

Intensity of competitive forces has positive impact on the extent usage of SCM techniques. That ultimately affects performance. The higher intensity of competitive forces conditions, the higher extent usage rate of SCM techniques, and the best fit with firm performance.*

6-3) Advanced manufacturing technology AMT, technology advances and the extent usage of SCM techniques :

A major impetus of new methods and approaches of SCM techniques has come from the recent revolution in manufacturing

philosophy and technology.⁴² Consequently, obsolete cost systems are the result of new technologies and changes in the new economic nature.⁴³ A study conducted by Lofsten & Lindelof (2005), has found that the firm's need of management accounting increase when technology and environment have changed⁴⁴. In summary, technology advancement is one of the main principal factors that trigger management accounting changes. Choe (2004) found in his study, high level of AMT requires more types of information, which includes advanced cost control information⁴⁵. Thus, we could state according to the above assertions, and at least in the samples related to above studies that:

A high advanced manufacturing technology & technology advances in the business environment has a positive impact on the extent usage of SCM techniques. That ultimately affects performance. The higher AMT & technology advances condition, the higher extent usage rate of SCM techniques, the best fit with firm performance.

6-4) General environment (Economic, demographic, educational, social and cultural factors) and the extent usage of SCM techniques:

The general environment factors are those events that have indirect impacts on the day-to-day organizational operations. Indeed, general environment was considered as one important reason behind the differences between SCM practices in different countries. On the same time, uncertainty associated with the chosen SCM practices are more related to the reactions of competitors and customers. In other words, it is related to competitive forces. Bhimani (1994) stated that accounting processes are affected by behavioral factors, political pursuit, institutional forces and socio-cultural values. Therefore, generally, the findings of previous studies indicated that:

The general environment factors have an indirect impact on the extent usage of SCM techniques.

7) Internal environmental variables

7-1) Organizational strategy and the extent usage of SCM techniques:

Porter (1980: 1985) argued that each of the generic strategies has an impact of firm's accounting system. Therefore, strategic priorities should supported by appropriate and effectively management accounting as well as SCM techniques.⁴⁶ Moreover, organizational strategy is the most important factor that may affect SCM usage techniques (Cadez & Guilding, 2008). Thus, generally and at least in the above studies, we could state that:

There is a positive interaction between different strategic alternatives and the extent usage of SCM techniques. That ultimately affects firm performance.

7-2) Perceived environment uncertainty(PEU)and the extent usage of SCM techniques:

Perceived environmental uncertainty is part of organizational life. However, PEU is an early contingent factor, which effects management accounting practices.⁴⁷ The distinction between dimensions within external environment such as uncertainty, hostility and complexity are important to design SCM approach.⁴⁸ Therefore, generally and at least in the above studies, we could state that:

There is a positive interaction between the scope of perceived environment uncertainty and the extent usage of SCM techniques that affects organizational performance.

7-3) Management accountants' participation in strategic decision-making and the extent usage of SCM techniques:

Accountants are also expected to play a greater explicit role in the implementation of SCM approaches as well as strategic decision making, rather than their traditional tasks.⁴⁹ Indeed, management accountants in Japanese Firms may spend around three years in different departments including: purchasing, manufacturing, distribution and sales in order to understand the increasing business environment complexity. Therefore, management accountants in Japanese firms may have 12 years' experience in other jobs before

joining the management accounting department.⁵⁰ Another study by Aver & Cadez found that Slovenian accountants are relatively strongly involved in strategic management processes, although the level of participation varies across industries.⁵¹ Therefore, generally and at least in the above studies, we could state that:

There is a positive interaction between a greater accountants' participation in strategic decision making and the extent usage of SCM techniques. That ultimately affects firm performance,

7-4) Organizational culture and the extent usage of SCM techniques:

Organizational culture is considered as an important factor that expected to explicitly influence SCM efficiency and effectiveness. Furthermore, even if firms have a high extent usage of SCM techniques, the successful or failed implementation of SCM techniques will depend on the organizational culture.⁵² Another study conducted by Al chen et al (1997) argued that Japanese culture and management accounting techniques should not be separable. As a result, U.S.-based Japanese firms are similar to Japanese domestic firms in their use of management accounting methods of target costing, and value engineering.⁵³ In addition, cultural differences are crucial. Bhimani (1994) stated “*the predominance of accounting in managing corporate activities in certain countries and not in others has been viewed as culturally contingent*” and concluded that social forces and cultural elements have a broad impact on cost management techniques, since SCM is no longer purely economic characterization where theoretical resolutions can be translated into practice. Therefore, generally and at least in the above studies, we could state that:

Cultural forces have an explicit influence on the extent usage of SCM techniques. That ultimately affects firm performance.

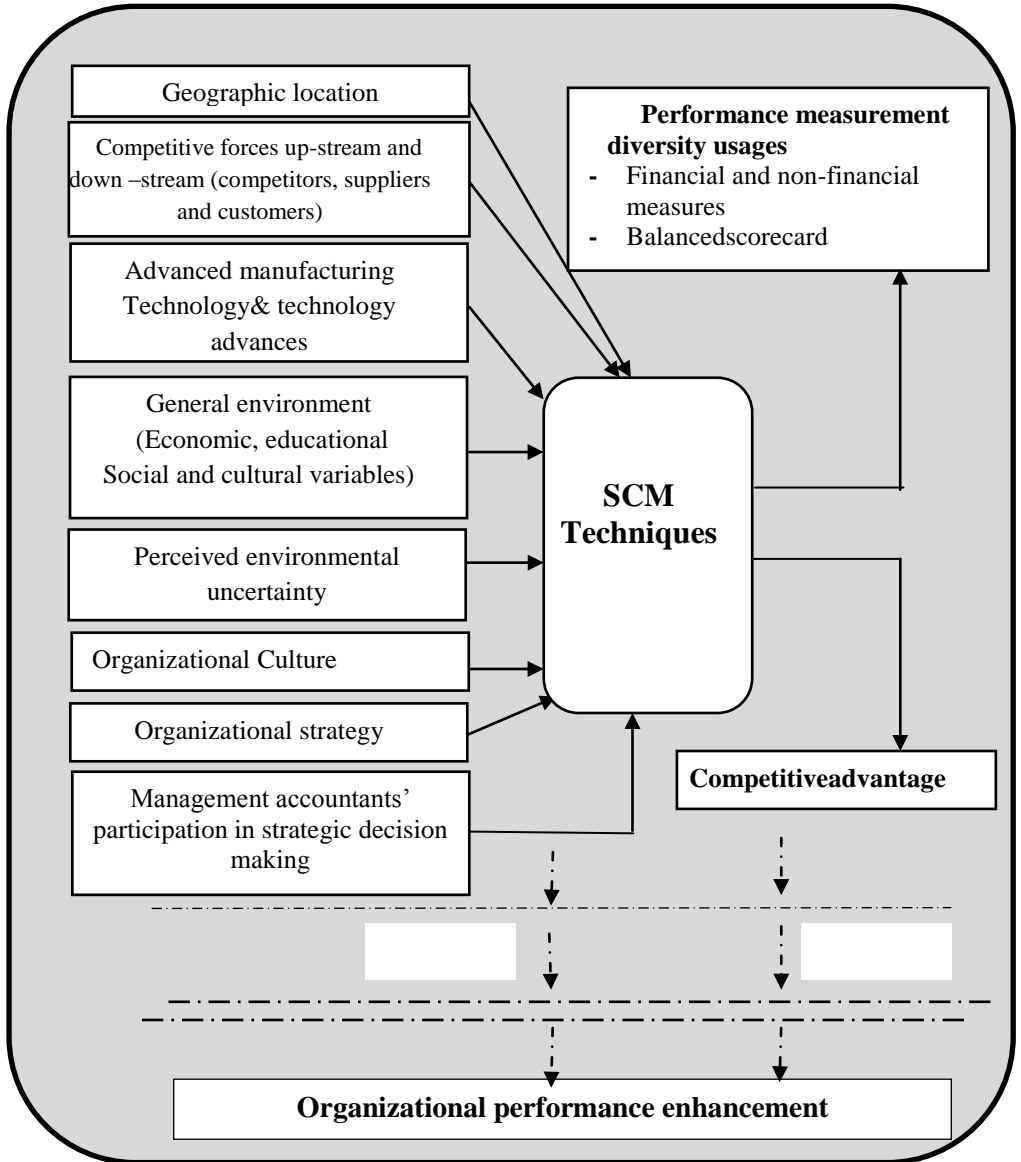
8) The impact of SCM techniques usage on organizational performance:

It has been noted, there is a clear focus on management accounting literature on the relationship between SCM philosophy and organizational performance.⁵⁴ Indeed, the most important change in management accounting is the broad emphasis and the publicity attached to organizational performance measurement. This movement urged firms to diversify their performance measurement to embrace financial and non-financial measures. However, Otley (1999) argued that performance measurement diversity is very important for organization to gain competitive advantage.⁵⁵ As we discussed above, SCM and organizational performance are intertwined in management accounting research. Therefore, generally and at least in the above studies, we could state that:

There is a direct explicit impact between the extent usage of SCM techniques and performance measurement diversity usages which ultimately affects performance.

Finally, the figure below illustrates the overall SCM theoretical research findings model for this paper, which encompasses mainly four axis: Business environment variables, SCM techniques, performance measurement, and organizational performance.

Figure 1: SCM Overall theoretical research findings model



Source: prepared by the researcher

Discussion and conclusion:

Despite the momentum gained by SCM in management accounting literature, researchers and practitioners still suffer from one clear conceptual framework of what constitutes SCM and the term itself is not always so clear cut. Consequently, SCM is often disconnected from what actually happens in organizations. Meanwhile, SCM techniques listed in management accounting literature have already been found in organizations in many cases.⁵⁶ There is also some evidence that SCM success is associated to the degree of resistance to the changes by stakeholders. This resistance in many cases plays a key role in successfully Implementing SCM novel approach.⁵⁷

Despite the disparity of SCM views between the two directions, both research and practice also suffer from an underdeveloped conceptualization of the notion of performance measurability. Therefore, it is crucial to understand under which specific conditions of SCM practices can deliver improved performance. In other words, SCM, which is tailored to support strategy, can enhance competitive advantage and superior performance, although perfect measurement is next to impossible, and trade-offs between measurements qualities are inevitable.

It is clear today that SCM approaches and financial/non-financial performance measurement are intertwined, and cannot be evaluated separately. Thus, the extent usage of SCM & PM is very important for an organization to gain Competitive Advantage. On another hand, the complexities of SCM & performance measures are more far to what textbooks highlighted do to the fact that SCM is not a technique or a method, but rather a philosophy that allows to an organization to integrate its cost management system with its business strategy. In addition, the previous studies indicated that the relationship between performance measurement practices and organizational performance is ambiguous.

In summary, SCM's academic researches cited in this paper indicate that there is generally a positive explicit relationship between SCM techniques usage and internal & external business environment factors, which are geographic location, competitive forces, advanced manufacturing technology & technology advances, general environment, organizational strategy, perceived environment uncertainty, and management accountants participation in strategic decision making and organizational culture. On the other hand, SCM has been found to have a direct explicit impact on the performance measurement diversity usages.

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* SCM= Strategic cost management

⁶ - **Olivier. L**, *Designing Strategic Cost Management Systems, How to unleash the power of cost information*, John Wiley & Sons, Inc, (2004), p: 9.

* the distinction between management accounting and cost management is not so clear-cut and often these terms are interchangeable (Horengren et al ; op, cit, p: 4)

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⁹ - **Yi Ma & Tayles,** *On the emergence of strategic management accounting: An institutional perspective*, Accounting and Business Research, jul (2009), Vol, 39, No. 5, p: 473-495.

* SMA is a term used by accounting academics and sometimes practitioners in the UK, Australia, and New Zealand, in the USA the term strategic cost management (SCM) is more commonly used in the literature. Clearly the definition of SCM has similarities with SMA processes as described by lord 1996 ; Dixon and smith 1993, however some would view SMA as broader than SCM .

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¹¹ IBID.

¹² **Lord, R, B,** *Strategic management accounting: the emperor's new clothes?* Management Accounting Research, 1996,7, pp: 347-366

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¹⁴ **Cadez, S. & Guilding, C.** *Benchmarking the incidence of strategic management accounting in Slovenia*, academic paper, 2007, pp:1-25.

¹⁵ **Guilding, C. & Cravens K & Tayles, M,** op, cit.

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* Fit is defined as the degree to which needs, demands, goals, objectives and/or structure of one component are consistent with the needs, demands, goals, objectives and/or structure of another components (Nadler and Tushman: 1980).

⁴² **Holzer. H. P. &Norreklit. H.**, op, cit, p.

⁴³ **Olivier. L.**, op, cit, p: 1.

⁴⁴ **Lofsten. H,&Lindelof. P.** *Environmental hostility, strategic orientation and the importance of management accounting- an empirical analysis of new technology-based firms*, Technovation, (2005), 25. 725-738.

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⁴⁷ **Lofsten. H,&Lindelof. P.**, op, cit.

⁴⁸ **Chenhall, R.H.** *Theorizing Contingences in management control systems research*. Handbook of management accounting research, Edited by , Christopher s, Chapman Anthony, Hopwood, and Michael shield. 2007,Vol1, pp: 163- 205.

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⁵⁵ **Otley, D**, *Performance management: a framework for management control systems research*, op, cit.

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