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Balancing between Control and Creativity: Budget Use in Five Swedish Startups

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Abstract

This study adds new perspectives, in terms of industry, company size and management characteristics, to the growing literature on MCS use and development in startups. Theoretical as well as empirical literature on budgeting in startups is scarce. Although some studies have provided useful insights on how small entrepreneurial companies use MCS, their focus on certain industries and the size of the companies studied leave other fields unexplored. Using Simons' (1995) levers of control framework, this paper explores how five Swedish startups use budgets to balance between control and creativity. We find that managers in startups actively use and pay attention to the budget. It is shown that the use of the budget is either characterized by diagnostic dominance or interactive dominance, and that the budget system also has implications for belief systems and boundary systems. The budget use cannot be studied in isolation, but informal controls and management philosophy also affect the budget use. In order to balance conflicting needs of control and creativity, we found that the budgets can be leveraged in several ways simultaneously, and that the budget can be transformed into functioning as another lever than what was intended, if the existing levers are unbalanced.

Key Words: Budget, Startups, Balance, Diagnostic, Interactive

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1 Introduction

1.1 Background and problem definition

The importance of entrepreneurs and new firms for economic growth is a common theme in politics and media. Much political effort is put into increasing the number of new firms, encouraging and enabling people to start their own business. There is also an extensive literature on entrepreneurship and what makes people start a new business. However, we still don't know much about what happens in small firms after their birth: during the early years of growth until they reach the size of a medium sized company, or fail.

How Management Control Systems (MCS) are used and developed in young, growing companies is a question that has only recently gained attention from the research community (see Davila et al., 2009b, for an overview). Consequently, theoretical as well as empirical literature is scarce, but growing.

Studies on MCS in small companies have both been quantitative, looking for statistical patterns in MCS adoption (e.g. Davila, 2005; Davila and Foster, 2005 and 2007), and qualitative, studying the use of, and reasons for, adoption of, MCS (e.g. Granlund and Taipaleenmäki, 2005; Sandelin, 2008; Strömsten and Waluszewski, 2011). A common denominator for these studies is the focus on high-tech sectors, implying an engineering-oriented culture and certain management characteristics (Granlund and Taipaleenmäki, 2005; Davila and Foster, 2005 and 2007; Strömsten and Waluszewski, 2011; among others).

Although these studies have provided useful insights on how small entrepreneurial companies use MCS, their focus on certain industries and the fairly large size of the companies studied leave other fields unexplored. In this study, our aim is to contribute to the growing literature on MCS use and development in startups by adding new perspectives in terms of industry, company size and management characteristics. We look at five companies in the service sector, in the size of seven to thirty full time employees, where all CEOs have a business school background.

We have chosen to focus our attention on the budget. The budget has been shown as one of the first MCS adopted by startups (Davila and Foster, 2007), a finding that was verified in our initial interviews.

1.2 Research question

The research question of this thesis is:

“How do startups use the budget to balance the needs for control and creativity?”

To structure our analysis, we will use Simons’ Levers of Control framework (Simons, 1995). This framework is one of the most influential in MCS research and is useful for our purposes as it explicitly deals with the *use* of MCS, and not its design or technical aspects. In our analysis, we will take influence from the growing literature that, based on the levers of control framework, study how organisations use budgets and MCS to handle the conflicting needs of control and creativity (Mundy, 2010; Tuomela, 2005, among others).

1.3 Definitions

1.3.1 Startup

In this study we will use the word “startup” to describe the companies we look at. We define it as a company that is young, small, growing, and aiming for further growth.

There is no clear definition of the word startup and it has been interpreted differently in different studies. In general, the word startup is used to describe companies that are recently founded, small, growing and aiming for further growth. When a company is too old or too big to be called a startup can be discussed. Earlier studies have used the term startup for companies with a size up to 150 employees and an age of up to 10 years (Davila and Foster 2005 and 2007). Startup is in other studies used as a general term for growth firms without a clear definition (Davila et al. 2009b). Some studies have used terms as “New Economy Firms” (Granlund and Taipaleenmäki, 2005) or “Growth Firms” (Sandelin, 2008). These terms are more specific than “startup”, and thus less useful for this study.

As we find the word “startup” being well used in other studies performed on similar companies, and a short and handy word to use, we have decided to use startup as a general term for companies that are recently founded, small, growing and aiming for further growth.

1.3.2 Management control systems

MSC is in this study interpreted in accordance with Simons’ definition, as “formal, information-based routines and procedures managers use to maintain or alter patterns in organizational activities” (Simons, 1995, p. 5).

1.4 Disposition

This study is organised as follows: In chapter 2 we present the previous literature within the field of MCS use and adoption in startups, relevant literature about budget use in large organisations and the theoretical framework for our study. In chapter 3, we discuss the method and our choices regarding research design, data collection etc. In chapter 4 we present the cases. First, the companies are briefly described to give a background for the budget use. Secondly, we present the budget use in the five companies. In chapter 5, we analyse our observations using Simons' (1995) Levers of Control framework. In chapter 6 we summarize our analysis and present our conclusions, as well as the limitations of the study.

2 Literature review

In this chapter we will present relevant previous research and the theoretical starting point for our analysis. The first section presents studies on MCS use in startups. The next section presents studies on factors that are related to MCS adoption in startups. The third section present concepts about budgeting and MCS use in larger firms that are of relevance in understanding budgeting also in a startup context. In the fourth section, we present Simons' Levers of Control framework, which provides us with the theoretical starting point of our analysis.

2.1 MCS use in startups

MCS use in startups is a young and growing area of research. The importance of MCS in growing companies was presented by Greiner already in the seventies (1972, 1998). In his model of company growth, the growth consists of long periods of evolution punctuated by crisis. One such crisis is the “crisis of leadership” where control based on culture breaks down due to the growing size of the company. At a certain company size, personnel control and culture becomes insufficient and formal control systems have to be put in place, the adoption of MCS is thus something that is forced upon the company out of necessity, instead of being part of strategy.

During recent years, the relevance of MCS in entrepreneurship has gained increased attention and some studies have been conducted in order to understand how MCS are used and adopted in a startup context.

The idea of a corporate life-cycle, a linear path companies tend to follow in MCS adoption, has since Greiner been put forward by several authors to explain development of MCS use in organisations (see Moores and Yuen, 2001, for an overview), and the concept of “crisis of leadership” or “entrepreneurial crisis”, where personal controls have to be substituted by formal controls, is still a widely accepted idea (Davila et al., 2010, among others). However, this life-cycle model has also met critique. Sandino

(2007) studies adoption of initial MCS in US early stage retail companies and find that strategy is a better predictor of MCS adoption than life-cycle models.

The life-cycle as a way to understand MCS use and development is also used in a study by Granlund and Taipaleenmäki (2005), who followed nine “new economy firms” in Finland. In an exploratory study, using interviews, questionnaires and internal documentation, they try to understand the management control practices in fast growing firms in information and communications technology and biotech businesses, using a corporate life cycle model presented by Victor and Boynton (1998). They find that although the life cycle model points at some general development trends, there are large discrepancies between the companies. Instead of general life cycle patterns, factors such as demands from venture capitalists and the pace of the growth have a stronger explanatory power. Another important finding of Granlund and Taipaleenmäki (2005) is the time horizon in the studied firms. The time horizon is short, and very forward-looking. As a consequence, planning dominates control and ex-ante controls such as financial planning and forecasting are much more important than performance evaluation and ex-post controls.

The importance of venture capitalists, and other parties in the external network, for the fast growing firm is further explored by Strömsten and Waluzcewski (2011). In a longitudinal case study of venture capital governance in innovation processes they follow a Swedish biotechnology firm and study the importance of the network in which the firm is embedded. They conclude that the idea of a dyadic principal-agent relationship is insufficient in order to understand the relationship between a startup and the venture capital provider as the governance of the venture capital firm spreads in the surrounding network. Specifically, they point out that a venture capital governed startup needs to follow two different logics simultaneously: the “go with the flow” logic of an innovation driven startup, and the logic of strict timelines and uncertainty elimination of the venture capital firm.

In a ten year long longitudinal case study of an Australia-based growing company, Collier concludes that informal control is more frequently used in entrepreneur-governed companies and that formal controls mainly focus on non-financial, not quantified, measures such as customer satisfaction and flexibility. Collier (2005) confirms the conclusions of Granlund and Taipaleenmäki (2005) that fast-growing, technology-driven firms seem to pay very little attention to financial control systems. Collier highlights the usefulness of Simon’s levers of control framework as it points at the importance of belief and boundary systems, and the absence of diagnostic controls, in entrepreneur-governed companies. He also highlights one important limitation of Simons’ levers of control framework (1995): it excludes informal controls, which is a crucial part of understanding the management control practice in an entrepreneur-driven company.

Although these early studies have provided useful insights on how small entrepreneurial companies use MCS, their focus is on companies in sectors where technological innovation and technological change is an important component, e.g. high tech companies in California (Davila et al. 2009), communication technology and biotech (Granlund and Taipaleenmäki, 2005), and biotech (Strömsten and Waluzcewski, 2011). The companies are also generally quite large, most of them in the span between 50 and 150 employees. These factors leave other interesting fields of research unexplored.

2.2 MCS adoption in startups

The quantitative studies on MCS in startups mainly focus on factors that are related to MCS adoption. Davila (2005), Davila and Foster (2005 and 2007) and Davila et al. (2009a) use a database of 78 startup companies in Silicon Valley to empirically study the adoption of a wide range of MCS. They find financial planning (operating budget, cash flow projections, sales projections) to be the first MCS adopted, followed by human resource planning (core values, mission statement, written job description etc.) and strategic planning (customer development plan, investment budget etc.). Their results point out the operating budget as the very first MCS to be adopted.

Factors that are positively correlated with MCS adoption are: growth in terms of employees, presence of venture capital and international operations, but also CEO experience and CEO beliefs about MCS benefits. They also find evidence for a simultaneous effect between MCS adoption and company size, i.e. MCS adoption is not only a result of growth, but also a factor leading to increased growth (Davila and Foster, 2007). Looking specifically at the adoption of operational budgets (Davila and Foster, 2005), they find that fast growth is positively related to fast adoption of operating budget.

Davila and Foster (2007) also find evidence for another important distinction in startups, the difference between entrepreneurs and managers. CEOs that are slow at adopting MCS have shorter tenures, i.e., entrepreneurs can start companies, but as the company grows the demand for managerial skills increases. This is a risk factor, as many startups are built on a technological innovation or another new business idea and the innovator of the new idea, the founder and the CEO often is the same person. If the entrepreneur does not succeed in transforming herself into a manager, she will likely not succeed as CEO (see also Davila et al., 2010).

Implementation of MCS often trails needs, due to limited resources and, perhaps, an entrepreneurial spirit focusing on product development, marketing and other aspects more closely related to the actual business (Davila et al., 2010). However, according to Davila et al. (2010), founders that put MCS in place in order to be prepared for growth, are more likely to survive as CEO and the companies are more likely to experience a fast growth. The reasons for putting MCS in place at an early point in time

could be both internal, e.g. based on CEO experience, or external, such as demands from capital providers (Davila et al., 2010).

2.3 Budgeting and MCS use in large organizations

The traditional view on management control originated in large companies with stable processes where control was seen as a way of reaching the company's pre-defined goals and avoiding deviations. This view of control did not fit with processes such as innovation and entrepreneurship, where the goals are hard to pre-define in a controllable way and deviations constitute a positive and important part of the process. Consequently, MCS were seen as detrimental for dynamic processes such as entrepreneurship and innovation. Instead, research in the area of innovation and entrepreneurial organizations has focused on other aspects, such as culture, team composition, communication dynamics or leadership (Davila et al., 2009b).

The view of budgets has been similar to the general view on MCS: the idea of traditional top-down budgeting has been seen as incompatible with the view of startups as organisations characterised by organic structures, high individual empowerment and flatter hierarchies (see Frow et al., 2010). Likewise, in environments of high uncertainty, the idea of a budget with annually set targets seems inappropriate. The literature on budgeting in startups is therefore, as far as we know, limited.

However, there is an increasing literature on how large organizations living in environments of high uncertainty and constant technological change use budgets and MCS to handle the conflicting needs of control and creativity. These are concepts that are highly relevant also in a startup context. Thus we believe that these studies are fruitful for our analysis, although they are dealing with large organisations.

In his influential book *Levers of Control* (1995), Simons provides a framework for analysing how managers use MCS. The framework consists of four levers: *diagnostic control systems*, *interactive control systems*, *belief systems* and *boundary systems*, which are used simultaneously to balance the needs for control and creativity. The levers of control framework has been used in several studies in order to analyse MCS use in large organisations (Collier, 2005; Tuomela, 2005; Mundy, 2010; among others).

Mundy (2010) explores how managers balance between controlling and enabling uses of MCS and thus create dynamic tensions in the company. Using Simons' levers of control framework, she identified four different, but related, factors that affects managers ability to balance the controlling and enabling aspects of the MCS: *internal consistency*, *logical progression*, *dominance/historical tendency*

and *suppression*. Internal consistency means that employees receive coherent information on the company's priorities in order to understand the common purpose in the organization. Without internal consistency managers will not be able to balance the use of MCS. Logical progression relates to the order in which the levers are used. E.g., belief systems often benefits from being designed *after* interactive systems have been used to debate alternative belief systems. Dominance describes the situation where the use of one, or more, of the levers determines the use of the remaining levers. Historical tendency is when an organization demonstrates a tendency for dominance of one lever during a long period of time, and this dominance prevails regardless of the changing contingencies. Suppression is the other side of the dominance coin: balance is not only affected by the *use* of a certain lever, but also the conscious decision *not* to use it.

Tuomela (2005) conducts a longitudinal study on the implementation of a new performance measurement system in terms of the interplay between different control levers. He demonstrates that a MCS can be used both diagnostically and interactively at the same time. The new system also has implications for the belief and boundary systems. The study also reveals that the use of a MCS may evolve during the use and development of the system, and thus play either diagnostic or interactive roles during different time periods.

One aspect of budgeting that has been given recent attention is its role of giving structure in situations of strategic change and uncertainty. Marginson and Ogden (2005) show how managers experiencing a high degree of role ambiguity tend to commit more strongly to budget targets, not because of accountability or reward connected to the budget, but because of the clarity and structure the budget gives them in their perceived situation of ambiguity and uncertainty. This gives rise to a "design-behaviour" paradox: ambiguous and uncertain situations that demand a flexible budgetary approach may lead to the opposite behaviour from the managers, as they stick hard to the budgets in order to cope with these very uncertainties.

Frow et al. (2010) performs a case study of a large US based multinational company and finds that budgeting contributes to both financial discipline and flexibility at the same time. In terms of levers of control: the budget is used both diagnostically and interactively depending on the situation. In a first step, the budget was used diagnostically, to spot deviations. But depending on the reasons for and complexity of the deviations, the budget was in a second step used either diagnostically or interactively. In the latter case, the budget was used as a basis for discussing the reasons of the deviations, but also the targets and processes. Frow et al. (2010) introduces the idea of "continuous budgeting" to describe the phenomenon, there is no fixed budget, it is rather under constant, continuous development

The budget flexibility was to a large extent on individual level, individual managers had the possibility to use the budget interactively. On a company level there was no such flexibility, pre-defined targets should be met and the use was entirely diagnostic. This was a natural consequence of external capital providers demanding predictability and consistency. In that respect, the case company in Frow et al. connects to the situation described by Strömsten and Waluszewski (2011) of a startup having to live with two different logics at the same time, the flexible logic of a startup working under high uncertainty and the strict logics of a venture capitalist firm.

Frow et al. also connects to the literature stressing the importance of looking at the MCS as a whole. In the case study firm, the budget is neither the only nor the most important control practice and its possibility to function both diagnostically and interactively depends on its integration with other parts of the control system.

2.4 Theoretical framework

As the use of MCS in small growing companies is an area that is largely unexplored, this study will take the form of an exploratory multi-case study. To structure our research we will use Simons (1995) Levers of Control (LOC) framework.

In his influential book *Levers of Control* (1995), Simons states that a fundamental problem facing managers is how to exercise adequate control in organizations that demand flexibility, innovation, and creativity. In order to empower the people's potential to innovate and add value, senior managers have to give up control, allow employees to unleash their potential, and also help them by communicating core values. Simons suggests four levers of control as a tool to reconcile and balance the conflict between creativity and control. The focus of Simons' levers of control framework is the use of the MCS, and not the design or technical aspects. As the purpose of this study is to understand *how* startups use MCS, this feature is a strength of the framework and one of the reasons to why it is a suitable theoretical basis for this study.

According to Simons (1995), the power of control does not lie in the use of one lever at the time, but in the interplay between them, how they complement each other (Simons, 1995). The interplay between the different levers provide arguments for why startups, acting under high uncertainty and having to constantly balance control and empowerment, would see the budget as a useful tool in their functioning, and present insightful guidance for us to study and understand budget from an overall perspective.

2.4.1 Limitations of Simons' framework

However, in adopting Simons' (1995) framework it is important to acknowledge some of its limitations for the analysis in this study. The levers of control framework is constructed from case studies on large firms, which may cause some concerns when applying it to startups. Further, the levers of control explicitly deal with formal controls. In startups, and other small firms, formal controls are of relatively lower importance than informal controls (e.g. Merchant and Simons, 1986; Chenhall, 2003, Collier 2005). Being aware of this limitation in the framework will allow us to adapt and complement our analysis if needed.

2.4.2 Diagnostic control systems

Diagnostic control systems coordinate and monitor the implementation of the intended strategy and ensure efficient and effective achievement of important goals (Simons, 1995). According to prior literature, diagnostic processes represent the traditional controlling use of MCS in which corrective action is taken as a result of feedback received about performance (Fisher, 1995). Managers use MCS in diagnostic ways to identify exceptions and deviations from plans (Abernethy and Lillis, 2001; Perera and Harrison, 1997; Tuomela, 2005). According to Simons' (1995), diagnostic controls are the first controls to be adopted by a growing firm.

With a few exceptions, the vast majority of prior research in management accounting has implicitly or explicitly assumed that budgets are used diagnostically. In this role, budgets serve the traditional purpose of evaluating performance and attributing responsibility for outcomes to particular organizational functions or members. (Abernathy and Brownell, 1999).

Earlier studies have found that managers have a natural tendency to use MCS for controlling purposes, rather than enabling (Ahrens and Chapman, 2004; Wouters and Wilderom, 2008). Studies on MCS in startups have also found that budgets are given high importance in the controlling of the company as it is seen as a starting point for financial controls (Moore and Yuen, 2001). Accordingly, for small companies focusing on sales growth, it might be a reasonable expectation that the budget is used diagnostically as a control tool to identify deviations from sales target and evaluating performance.

On the other hand, there are also reasons to expect managers in entrepreneurial companies to avoid diagnostic controls in order to put more emphasis in the enabling use. Firstly, although control is an important feature of any organisations, a low focus on controls is seen as an important characteristic of startups and a high tolerance of uncertainty and ambiguity, and thus a low need for controls, is an important characteristic of entrepreneurs (Bhidé, 2000). Secondly, too much focus on the coercive use can hamper innovative behaviour (Mundy 2010), something that is an important part of a startup's

work and identity. Thirdly, according to life-cycle theory of MCS adoption and development, companies in the birth and growth phases tend to use rudimentary MCS combined with a low degree of centralization and informal or moderately formal structure of activities (Moore and Yuen, 2001).

2.4.3 Interactive control systems

Interactive control systems enable top managers to involve themselves in strategic uncertainties and to learn about, and respond to, threats and opportunities as competitive conditions change (Simons, 1995). Any MCS that facilitates formal processes of debate can be used interactively. For example, managers can involve employees in budgetary processes and the design of performance measurement systems in order to share information and reduce gaps in knowledge (Abernethy and Brownell, 1999; Haas and Kleingeld, 1999; Shields and Shields, 1998). According to Simons' (1995), interactive controls are the last of the four levers of control to be adopted by a growing firm.

There are four important aspects that make interactive controls different from diagnostic (Simons, 1995): Focus on constantly changing information that top-level managers have identified as potentially strategic; Information is significant enough to demand frequent and regular attention from operating managers at all levels of the organization; The data generated by the interactive system are best interpreted and discussed in face-to-face meetings of superiors, subordinates and peers; The interactive control system acts as a catalyst for an on-going debate about underlying data, assumptions and action plans.

The first aspect is fulfilled more or less by definition by the budget of a small company: as the business is small and the level of complexity low, the information will be potentially strategic and identified as such by top management, e.g. profit and sales. As the targets in the budgets of small companies are very overall, e.g. profit and sales, the information in it also fulfils the second aspect. The aspects where management can make an actual choice are the third one, if they choose to interpret and discuss the data with subordinates and peers, and the fourth one, if they let the budget be the catalyst for a discussion on the data and its implications.

Interactive controls have been pointed out as costly in terms of time and managerial attention (Simons, 1995; Widener, 2007). These are both limited resources in any organisation, and especially in a startup where the resources devoted to, and the interest in, MCS use are assumed to be scarce. This would lead us to expect a low degree of interactive budget use in the case companies. On the other hand, these companies face challenges that interactive systems are supposed to handle: the need to constantly search for innovative business opportunities and handle strategic uncertainties.

2.4.4 Boundary systems

Boundary systems specify the scope and limits of activities by establishing the “rules of the game” to identify what is acceptable and what actions and pitfalls employees must avoid. The boundaries in modern organizations, embedded in standards of ethical behaviour and codes of conduct, are invariably written in terms of activities that are off-limits (Simons, 1995). According to Simons’ (1995), boundary systems is the third of the four levers of control to be adopted by a growing firm.

Any MCS that sets out minimum standards or guidelines for behaviour can be used by managers as a boundary lever of control. Financial data establish boundaries that protect an organisation from financial risk, whereas non-financial data indicate the strategic boundaries within which managers should operate (Tuomela, 2005).

As startups are small and informal controls play an essential role (Simons 1995; Collier 2005), it is hard to expect a formal written code of conduct in terms of activities that are off-limits. This would lead us to expect a low use of formal boundary systems in startups since informal controls are well suited for behavioural control (cf clan control as described by Ouchi (1979)). On the other hand, startups face limited resources, which would imply the use of financial boundaries in line with Tuomela (2005). When resources decrease, the need for a financial boundary would increase. This would lead us to expect a high use of boundary system.

2.4.5 Belief systems

Belief systems promote the search for new opportunities by communicating values, purpose and direction, and inspiring organizational members to commit to the corporate objectives (Simons, 1995). Belief systems provide employees with a stable environment and play an important role in communicating values and assumptions that are not always apparent in other MCS. Belief systems also play an important role in organisations undergoing strategic change as they help managers to introduce new values and priorities (Bruining et al., 2004; Roberts, 1990). According to Simons’ (1995), belief systems is the second lever of control, after diagnostic control systems, to be adopted by a growing firm.

There are two aspects of belief systems that need to be considered when discussing its use in a startup: the need and the alternatives. The purpose of a belief system is as useful in a startup as in any organization. Other controls are often underdeveloped, employees often face a high uncertainty in their tasks, but also in terms of their own benefit, the initial wage is often low and the possibility of failure high (Bhidé, 2000). The need for a formal belief system is further increased when the employees are highly educated, as mere monetary gains are not enough to inspire (Simons 1995). This

would lead us to expect a high use of belief systems in the startups. However, the role belief systems can be expected to be easily filled by informal systems. The clan control described by Ouchi (1979) relies on a strong commitment of the employees and a common agreement on the purpose of the organisation. This kind of control would be expected to be found in startups out of two reasons: the small number of employees makes personal controls easy (Simons, 1995, among others); and startups are usually closely connected to their business idea, i.e. the purpose and idea of the company is given from the start and the employees have themselves decided to commit to this idea when accepting the position (Bhidé, 2000). Thus, the function the belief system is supposed to fulfil will be served by informal systems until the growth, and/or employee turnover, of the company has diluted it. This will lead us to expect a low use of formal belief systems in startups.

The four levers of control are summarized in Table 1.

Table 1
Relating the Four Levers of Control to Strategy

Control System	Purpose	Communicates	Control of Strategy As
Belief System	Empower and expand search activity	Vision	Perspective
Boundary System	Provide limits of freedom	Strategic domain	Competitive position
Diagnostic Systems	Coordinate and monitor the implementation of intended strategy	Plans and goals	Plan
Interactive Systems	Stimulate and guide emergent strategies	Strategic uncertainties	Pattern of action

Source: Simons (1995)

3 Method

This chapter describes the research choices taken during the process of the study.

3.1 Research design

3.1.1 Choice of research strategy

As the use of MCS in small growing companies is an area that is largely unexplored, this study will take the form of an exploratory multi-case study and the research question of this study takes the form of a how-question:

“How do startups use the budget to balance the needs for control and creativity?”

According to Yin (2003), three conditions should guide the choice of research method: (a) the type of research question, (b) the control the researcher have over the events studied, and (c) if the study is focused on historical or contemporary events. In terms of these conditions, our research question is a “how” question, we will have no control over the events, and we focus on contemporary events, which makes a case study the preferred research strategy.

According to Edmondson and McManus (2007), what kind of research method that is suitable for a given research questions within management research depend to a large extent on the maturity of the research field. Edmondson and McManus (2007) describe theory maturity as a continuum, from nascent over intermediate to mature, where a mature field through extensive research has reached “a body of work consisting of points of broad agreement that represent cumulative knowledge gained” (Edmondson and McManus, 2007, p. 1158). Nascent theory, on the other hand, deals with new questions of how and why, proposing merely tentative answers.

Edmondson and McManus present a framework to obtain “methodological fit” in management field research. To obtain methodological fit for a nascent state of previous theory and research, they suggest a research design consisting of: an open-ended research question, qualitative data open for interpretation, collected through interviews, documents or other material; few formal measures or prior constructs will be used and data analyses will aim at identifying patterns through thematic content analysis; the theoretical contribution will mostly consist of a suggestive theory inviting for further research. Following Yin (2003) and Edmondson and McManus (2007), this study will be posing an open-ended research question and use a case study to obtain data.

3.1.2 Theoretical aim

The aim of this thesis in terms of theory development is to combine the two strands of research studying MCS development in growing firms on the one hand, and how budgets are used to balance the need for control and creativity in larger organisations on the other hand, in order to give a better understanding on how budgets are used as control tools in young growing companies.

Two basic ideas on research are the deductive and the inductive approaches. The deductive approach starts in existing knowledge and forms hypotheses that are testable in reality. The inductive approach takes the other way around, starting in empirics and out of that constructs theories, or abstractions, in order to describe reality. The approach taken in this study is a third one, the abductive approach. Studies relying on abduction will start with a framework based in existing literature and prior research. This framework will then be modified during the research process as a result of unexpected empirical findings as well as theoretical insights. Dubois and Gadde (2002) describe this approach as: “[a] fruitful cross-fertilization where new combinations are developed through a mixture of established theoretical models and new concepts derived from the confrontation with reality.” (p. 6).

As our main theoretical starting point we use Simons’ levers of control (1995). Although Simons’ framework was originally developed using large firms as reference, the basic question, how managers balance empowerment and control in MCS use, is as relevant in young growing companies as in larger ones. This starting point has been helpful in order to structure our empirical findings.

3.1.3 Choice of case companies

Designing a case study, one has to decide the number of cases studied, i.e. choose between a single-case study and a multi-case study. The rationales for doing single-case study, according to Yin (2003), are the studies of unusual or rare cases, critical cases, typical cases, revelatory cases, and longitudinal cases. None of these rationales correspond to our research question. The main rationale for doing a multi-case study is the *replication logic*: “choosing two or more cases that are believed to be literal replications” (Yin, 2003, p. 52). In our study, this replication logic has been followed through selecting five cases that are similar in respect of a number of parameters that would make us expect that our research question would have the same answer in all cases. Finding analytical conclusions arising independently in all five cases would strengthen the theoretical implications of our study, and if no common conclusion can be drawn, the exploratory aim of our study would be strengthened by the larger sample.

The case companies in our study have been chosen according to five criteria: (i) they are young, (ii) they have grown steadily in terms of sales and employees since birth, (iii) they are aiming for further growth, (iv) their main operations are in services (B2B or B2C), and finally (v) they have passed the

product development phase and are now pursuing a sales growth strategy.

(i), (ii) and (iii) relate to the definition of startups. (iv) and (v) distinguishes these companies from the high-tech, product development focused companies in earlier studies. (v) also relates to corporate life cycle theory: in the earliest phase of the company life cycle, MCS are likely to be kept at a minimum, whereas in the growth phase, MCS will start to formalize (Moores and Yuen, 2001; Simons, 1995).

The companies were found through SSE Business Lab, an incubator for small startups connected to SSE, and through personal contacts by the authors. A first contact was taken with several companies to check their suitability and the possibility of access whereupon five companies were selected. Although three of the case companies have used SSE Business Lab at an earlier stage, none of them had any connections at the time of the study.

3.2 Data collection

In total, ten interviews were conducted in the five case companies, two interviews at each. The interviews were semi-structured and lasted between 45 and 75 minutes each. The interviews took place in October and November 2011. All respondents and companies are anonymized to allow the respondents to talk freely. In each company the CEO and a manager were interviewed (with one exception, in one of the companies (Epsilon) the CEO was not available for an interview, instead one of the longest serving managers in the company was interviewed). The reason for interviewing the CEOs was that they usually were the main responsible for the budget preparation and for MCS design in general. The CEOs, could also, as CEOs but also as they were all, save one company (Alpha), one of the founders, provide us with overall information of the company as well as background and history. The reason for choosing someone in a managerial position for the second interview group, was that they use the budget, to some extent take part in the preparation, and usually have a better view on how it is used in the operations. We chose not to interview employees in non-managerial or purely operational roles, as the knowledge about, and use of, the budget in this group may be limited.

The respondents were divided into two groups: the CEO group and the manager group, and all respondents in each group were given the same questions. The interviews were recorded and transcribed. In some cases, clarifications or additional questions were sorted out after the interviews through e-mail.

Internal documentations of the companies have been used to crosscheck and verify findings and financial data on the companies have been complemented through databases such as Affärsdata.

3.3 Data analysis

For each company, a within-case analysis was performed. This exercise was helpful as it provided a richer picture of the budget use in the company, and pointed at issues that needed to be clarified through further contact with the respondent. Thereafter, a cross-case analysis was conducted between the five companies. This was done in several steps, looking both at general patterns and at specific issues.

3.4 Validity and reliability

Internal validity concerns to what extent the results of a study interprets the reality (Merriam, 1994). There is no objective, universal way of guaranteeing validity (Ratcliff, 1983), nevertheless, there are certain procedures that can be undertaken to ensure inner validity. In our study, we have used several sources of information (triangulation), such as interviews and documentation. The authors have summarized their impressions of the interviews separately in order to not influence each other in this step. Respondents have been asked to clarify afterwards in case the impressions have shown substantial differences. The interviews have been performed individually and the same questions have been asked to all the respondents in each of the two groups of respondents.

Reliability concerns to what degree the results of the study can be replicated (Merriam, 1994). Reliability is a problematic concept in the social sciences. As human behaviour is dynamic, the reality that is studied changes and so will the results from different studies (Merriam, 1994). As reliability is inseparable from inner validity, we have, according to Guba and Lincoln (1981), concentrated on the inner validity, from which reliability will follow.

External validity concerns to what degree the results of a study are generalizable. Case study results are, due to the nature of the research method, hard to generalize (Merriam, 1994). In this study, the possibility of reaching external validity is increased by the multi-case method, but decreased by the low number of respondents in each company.

4 Empirics

4.1 Background and context

This section presents descriptive information on the five case companies. The companies have been anonymized and are called Alpha, Beta, Gamma, Delta and Epsilon.

All companies' main operations are in the field of services, either B2B or B2C. One company sells a product, but they are operating as a sales and marketing company and all production is outsourced.

In terms of number of fulltime employees, the companies vary between 7 and 27 as of the date for the CEO interview. Two of the companies also rely on a large number of part-time employees. This is due to their business models that require a large number of staff on specific occasions to carry out their operations. For the purposes of this study, the number of fulltime employees is the relevant figure as these are the employees that participate in the daily work and thereby to a large extent use and are affected by the MCS.

The turnover is from 2010, the latest year available. As Company Alpha and Epsilon have not shifted from product development focus to sales focus until 2011, their figures are not comparable to the other three companies. Four of the companies have offices or representatives abroad, but only Gamma and Epsilon perform a significant part of their operations abroad and all of the companies perform a majority of their operations in Sweden. All of the companies intend to expand their foreign operations.

The year of foundation is the year of registration of the company. In all cases, this is also the year when the first operations commenced. However, the first years of operations are not perfectly comparable between the companies. Company Beta and Epsilon spent the first, or the first two, years on product development before they started to make revenues. Company Gamma was started as a hobby project when the founders were still at university and they did not scale up the company to a professional business until 2009. Company Alpha and Delta started to sell from the very beginning, although Alpha kept a low revenue growth in order to develop their product the first year.

All the five CEOs have a business school background. Two of them hold degrees from the same school whereas the other three studied at other schools, all in Sweden. Several of the employees in all five companies have also studied at business schools. In four of the companies, the current CEO was also one of the founders.

There are two main owner categories in the companies: founders and external capital. The founders own a certain amount of the shares in all companies. External capital providers are usually what is sometimes referred to as “business angels” or “seed funding” which is basically a form of venture capital. For convenience, we will use the term VC. Current and former employees hold shares in some of the companies, but these fractions are in no case above five per cent.

All five companies budget for sales, costs and cash flow, but the focus in the budgeting vary. The respondents in Alpha and Epsilon explicitly stated that both the cost and the sales budgets were equally important, whereas Beta, Gamma and Delta stated the sales budget as the top priority. All companies stressed the importance of the cash flow budget, but did not view it as a management tool in the same way as the cost and sales budgets. Book keeping is outsourced in all companies.

The degree of hierarchical level and task division, as well as budget information, is inferred from the interviews and internal documentation of the companies.

Table 2
Company Background

Company	Alpha	Beta	Gamma	Delta	Epsilon
Core Operations	Consumer services	Business services	Consumer services	Business services	Consumer marketing
Year of foundation	2009	2005	2004	2006	2008
Ownership Structure	No VC Founders ≈ 95%	VC ≈ 33% Founders ≈ 67%	No VC Founders 100%	No VC Founders 100%	VC <50% Founders >50%
International operations	No	Yes (USA)	Yes (UK)	Yes (Nordic country)	Yes (USA)
Full time employees	13	8	7	27	8
Part time employees	0	15	50	8	0
Turnover (2010) (Thousands SEK)	≈530	≈7200	≈2900	≈13000	≈260
CEO characteristics					
Business education	Yes	Yes	Yes	Yes	Yes
Experience from startups	Yes	Yes	No	No	No
CEO also founder	No	Yes	Yes	Yes	Yes
Company Organisation					
Centralisation of budget preparation	High	High	Low	High	Low
Task division	High	High	Low	High	Low

4.2 Budget use in terms of levers of control

This section presents the budget use in the five companies, structured according to Simons' four levers of control (1995).

Budgets have traditionally been used as a controlling tool, and are the most commonly used diagnostic control tool in organizations today (Horngren et al., 1997). In three of our case companies, Alpha, Beta and Delta, we find evidence for this view: the budget is mainly used as a diagnostic system and is designed as a tool for target setting, performance evaluation and as a basis for individual incentive systems for all employees (Delta), and for the CEO (Alpha). The budget is on the other hand not used interactively or as an enabling tool, it is not used for discussions about strategic choices or strategy creation.

Even though all the five case companies use budget interactively in some way, there is a clear division among the companies in our study between those which use the budget mainly as a diagnostic tool

(Alpha, Beta and Delta) and those which use it both diagnostically and interactively but with a relatively much larger interactive use (Gamma, Epsilon).

4.3 Diagnostic control systems

4.3.1 Diagnostic dominance

In three of our case companies, we found the diagnostic lever to dominate. That is, the use of the diagnostic lever of control in the budget defined the use of the remaining levers in the budget. But the diagnostic, and controlling, dominance in the budget use should not be interpreted as a controlling focus in the overall management. The three case companies that demonstrate a diagnostic dominance in the budget use, at the same time show an inclination towards flat hierarchies and a strong focus on enabling controls in the company overall management. One of the respondents in Delta describes the hierarchical situation in the company like:

“The CEO is really prestigeless, he doesn’t want to build hierarchies and have cared a lot about that. But of course we have suffered from that sometimes, when it’s unclear who is in charge. But we have also benefited from it, we have had a lot of fun” (Manager, Delta)

The CEO describes his view on MCS as:

“But I mean, given that we are a pretty small company, in entrepreneurial companies... or depending on what people you have running the show, you have a pretty strong focus on bringing in the business, not calculating what it does to the financials” (CFO, Delta)

There is a historical tendency towards suppression of diagnostic controls in the company, in order to focus on the enabling part. This focus is a conscious choice by the management, and the CEO is aware of its benefits and drawbacks. At the same time, the CEO regards formal controls as mainly, or exclusively, controlling: the budget is seen as a controlling tool or planning tool, not a management tool in a broader sense, and the role of formal MCS is to act as a diagnostic system or a boundary system. As some diagnostic systems are seen as necessary, the consequence is that almost all diagnostic tasks are referred to the budget. That is, in the overall management, the interactive lever dominates and the diagnostic lever is to some extent suppressed, and in the budget the opposite is true: the diagnostic use dominates and the interactive is suppressed. Putting all the diagnostic/controlling controls in the budget, and then downplay the use of the budget, is an easy way for the CEO to be seen as informal and still keep the diagnostic controls.

The budget use in Beta is similar to the use in Delta: the budget is seen as a control tool and is mainly

used diagnostically:

“But pretty much now since we have accumulated quite a lot of knowledge on how to run the operations ourselves, we know to the very last cent how the business is run and as well on how to attract new clients, so we are starting to integrate all this knowledge into a package so we can like project the business” (CEO, Beta)

As in Delta, this is paired with an overall view on management that emphasises the enabling use of controls:

“The management overview here is pretty much that we like to have brilliant people. To empower these guys to have a goal, something they can commit to.” (CEO, Beta)

In both Beta and Delta, the budget is seen as an entirely diagnostic tool and the budget preparation is, consequently, highly centralised. In both companies, budget preparation is mainly done by the CEO with some support from the company’s managers. The budget is seen as the CEO’s exclusive sign of power and control.

4.3.2 Target setting

According to prior literature, diagnostic processes represent the traditional use of MCS in which corrective action is taken as a result of feedback received about performance (Fisher, 1995), MCS that are employed diagnostically are used to compare actual performance against pre-set targets (Abernethy and Brownell, 1999; Simons, 1995 and 1999). Consistent with this finding, the diagnostic use of the budget in the five case companies is mainly related to target setting. All companies present the use of budget targets as something evident. There is in none of the companies any discussion on the necessity of it, budget targets are taken for granted. The most common measure to target is sales, which is done in all five companies:

“So in terms of setting a budget, it’s not really a budget, but of course we have a target for overall sales for different sales channels, in Sweden and abroad.” (Manager, Beta)

“We have changed our focus to becoming being much more goal oriented. Now we have monthly goals when it comes to sales.” (CEO, Gamma)

Many of the companies also set budget targets for other measures, such as cost, and in one case non-monetary targets (Epsilon), e.g. behaviours and procedures for purchasing etc.

In several of the companies, there is also an on-going discussion on adding more goals and targets to the existing ones:

“I think we should start tracking one or two goals per person. /.../ quite simple quantitative targets that we should always account for every week. I think that could be very useful, it’s kind of like having homework. If you have to tell everyone what happened last week you will do it and you might actually do a little more.” (Manager, Beta)

Such high confidence in target setting is due to the strong belief in the need for diagnostic controls.

“And now lately we are much more goal oriented than we were previous year, we have changed our focus being much more goal oriented. /.../ Goals are good, especially cause you work hard and get some results from that.” (CEO, Gamma)

The budget is also used by some companies as a diagnostic tool for the board to track and evaluate the company and management/CEO performance.

In Alpha, budget targets are used as a direct means of evaluating the performance of CEO, as explained by CEO:

“If you look at my evaluation, what the board thinks about me, I have quite hard conditions of employment, I have to stick to budget. If we change it more than 10 per cent I won’t get any salary that month. Kind of that easy.” (CEO, Alpha)

4.3.3 Challenges of diagnostic use of target setting

The large focus on diagnostic use of the budget is not without challenges. A MCS needs to have three features to function properly as a diagnostic tool: 1) the ability to measure outputs, 2) predetermined standards to compare against actual results, and 3) the ability to correct deviations from standards (Simons, 1995). The diagnostic use of the budget in the case companies in this study focus on relatively overall measures: sales, costs and cash flow. Also, complexity in the processes are low, making the diagnostic use fulfil the first criterion. Also criterion 3 is typically fulfilled due to the low complexity of the processes. However, several respondents stress the hardship in setting reasonable predetermined standards, budget targets, thus hampering the diagnostic use of the budget. The problems as they are explained by the respondents can be divided into three categories: uncertainty about external factors; uncertainty about internal factors; and external demands/expectations.

First, the high uncertainty about the external factors such as demand and competition, makes it hard to make good estimates on future performance and set predefined budget targets:

“/... / there are so many things that affect your job that is outside your control. It’s tricky to set a budget like that... I think you have to spend a lot of time just setting targets. And we haven’t found a good model for it yet. One easy solution would be to keep it simple and just distribute profit but we haven’t found a good way of doing it.” (Manager, Beta)

Secondly, high uncertainty about the company’s own projects and operations sometimes makes it hard to do good estimates about future performance. Development of new products, marketing projects and setting up operations in new markets is often unpredictable:

“When it comes to kind of sales goals, we do have sales goals, but it’s of course really difficult to work with those because it’s so uncertain at this early stage.” (Manager, Gamma)

Thirdly, quick growth in one time period creates unrealistic demands from actors, leading to budget targets that are not realistic measures for performance evaluation. Asked about if the uncertainty of a startup affects the target setting, one respondent answered:

“Yes, absolutely. And of course, if you are on the board, you own it yourself, when our sales go from 400 to 2000 to 4000 to 9000 to 13000, everybody knew like, ok, 2000, that’s perfect, then 4000, and then next month we go into 2000, what’s wrong, we want 6000. Now everybody has a level like above 10000, it is the minimum, so you are changing very quickly.” (CEO, Alpha).

As a result, several respondents in our study admit that they don’t follow up budget to a large extent:

“(We follow up) to some degree, not too much, to tell the truth. Say in one company, the effect of one person is so hard to evaluate. /.../ In this case there is no overall market figures. We have no idea. /.../ What we try to do is that we evaluate on a more soft basis since the hard figures are not actually present. We hope everyone can do as good as they can.” (CEO, Beta)

“It’s hard to use budget in like performance evaluation in common sense, it’s more about why I would say, If you can’t support why, it’s also performance valuation in some sense, but not the same sense, the regular one...” (Manager, Alpha)

”I do that (follow up), but not in a formal way. I just nag about the costs very much. So everyone here knows that I am on them” (CFO, Epsilon)

4.4 Interactive control systems

4.4.1 Interactive dominance

In two of the case study companies, Gamma and Epsilon, interactive use of MCS dominates. In Epsilon, two parallel budget systems are used. Liquidity budget and sales budget are set for specific time periods and mainly function diagnostically, while the operational budget is constantly updated on a project basis and the main function is interactive control. The liquidity budget and sales budget function as diagnostic controls, in line with how budgets traditionally are used (Horngren et al., 1997), the liquidity budget to plan and control, and the sales budget for performance evaluation on an overall company basis.

In Epsilon, the operational budget is not set for any specific time period. Instead, all employees will, for every project planned, write a project specific budget, specifying planned costs, benefit for the company and best alternative option. The project budget will be discussed with the CFO, CEO, and other employees and if the planned cost is above a certain limit, a board approval is needed. After the project is completed, a follow-up report is written. The idea is to create a system where all major projects are discussed among the managers and are well-motivated, and to create a link between the on-going operations and the board. Through this kind of discussion, employees can find potential problems, discuss possible solutions and ensure that the project can be implemented successfully. The diagnostic systems are used as a support function for the interactive systems and are adapted to this role. The projects budgets are used to spur discussion. The sales budget is used as a provider of information to identify opportunities for sales growth. Follow up/performance evaluation of the project sheet is not highly prioritized or formalized. Instead, the focus is forward looking, planning the next project:

“I do that (follow up the project budgets), but not in a formal way. I just nag about the costs very much. So everyone here knows that I am on them, so it’s a struggle between sales and marketing and me, so I think now that we have a pretty good balance there.” (CFO, Epsilon)

The system in Epsilon is a good example of how interactive control systems function (Simons, 1995): it’s a formal information system used by top managers (in this case the board and CEO) to involve themselves personally and frequently in the decisions of subordinates. The board, consisting of, except representatives for the company, external capital providers are personally involved in the strategic decisions of the business of the company and have frequent contact with the employees. As expressed by the Senior Manager:

“/.../ someone, usually the CEO, sometimes the CTO, sometimes me, but mainly the CEO has contact with the board every day. And we keep them updated, like cc them on e-mails...”
(Senior manager, Epsilon)

The project system leads to a constant involvement of both employees and board in all major decisions. In Epsilon, the dominance of the interactive system leads to a suppression of the diagnostic controls. The diagnostic controls are mostly taken care of by the CFO and are adapted to the interactive system.

“Cause the main purpose of the project sheet is about the cost. And the main person who should know if it’s doable (in terms of cost and liquidity) is me. But the potential of it, that’s not my area, that’s the CEO or the person who did it. But I have to make a recommendation to the person. So before most project sheets are done, they ask me and present it to me and ask, should we do it?” (CFO, Epsilon)

Also Gamma shows a dominance of interactive use of the sales budget. The sales budget and the budget targets are to a large extent used as a discussion forum and a catalyst for an on-going debate about underlying data, assumptions and action plans (Simons, 1995). Sales goals are followed up weekly and the outfall form a basis for discussion about new ideas on how to reach the targets and improve the results and the meetings also function as a forum for discussing ideas on how to expand the business etc. Also in the most technical parts of the budget preparations, the CEO stresses the importance of the on-going discussions on how to reach the budget targets, not only the level of them:

“For the goals and calculations, I did the calculations, even before that, we had a revenue goal we agreed on together. That would be discussed by all of us and we look at what we have last year, how much is possible for us to increase, and also what should we do in order to reach the goal.” (CEO, Gamma)

Also, the weekly formal meeting for following up on sales and costs also show an interactive use of budgeting. They have sales meeting every week to discuss the sales budget and see what they should do in order to reach their goals. And for costs, they have a meeting every quarter to see whether a particular cost, e.g. marketing costs, grows aligned with budget. Such interactive processes enable organizations to bring together individuals with different sets of information about the organization’s activities (Abernethy and Lillis, 1995; Speklé, 2001), and also facilitate organizational learning through dialogues (Abernathy and Brownell, 1999).

In these two companies, the interactive lever dominates and dictates the use of the other levers. The dominance of one single lever, the interactive, in these two companies is, on the contrary to the companies where the diagnostic lever dominates, seen as a problem. Both Epsilon and Gamma have intentionally started to work for a decreased interactive dominance:

”We rather try to work to create ideas, however, sometimes we have too many smart people, in meetings we discuss concepts and theoretical ideas rather than just doing it. So we try to limit that, discussing everything into too much detail.” (CEO, Gamma)

The dominance of interactive thinking has also, as expected, led to a relatively low focus on developing the diagnostic use of the MCS/the budget. Until recently, there were no clear goals and targets in the budgeting. In Epsilon, the interactive dominance led to a less expected drawback, a lack of long term financial planning as the diagnostic function of the budget was downplayed in favour of the interactive use of the short-term project budgets:

“Because the project sheets become a little bit too... it’s good /.../ but it’s also kind of a hassle because it’s very short sighted, you only think like... its easier if you have a budget, like I have approximately this much to use each month and if a use less one month I could do a bigger project next year or something like that... we need a bit more of continuity.”
(Senior Manager, Epsilon)

Gamma has also experimented with a balanced scorecard, a MCS intended to combine financial and non-financial measures (Kaplan and Norton, 1992). The balanced scorecard was used as a basis for discussion and according to the CEO it was an interesting management tool, but too costly in terms of time:

”It was interesting to see, /.../ but in such a small company, the information is not that relevant yet. But generally when it comes to balance scorecard, I think it’s good way to combine finance with more soft values, so I am definitely in favour, but at this stage, we are too small to use it in an efficient way.” (CEO, Gamma)

The costliness in terms of time consumption is an expected problem concerning interactive controls. Gamma also experienced that the interactive dominance caused a lack of focus, until recently, there were no clear goals and targets in the budgeting. Strategic issues were discussed, but the poor functioning of the diagnostic processes lead to a lack of references on the actual results:

“My perception of kind budgetary work was that we lacked goals at first, which is something that we have just recently implemented /.../ we did follow up but we didn’t really have a reference...” (Manager, Gamma)

The balancing between interactive and diagnostic levers of control has in these cases been fairly straightforward. In Gamma, the awareness of the drawback has led to an intentional suppression of

interactive use (cutting time spent on meetings and strategic follow up), and through implementation of more diagnostic systems (explicit budget targets). In Epsilon, a new system combining interactive and diagnostic controls will be implemented, after experimenting with a purely project based system.

4.4.2 Increased interactive use in terms of crisis/uncertainty

Although the general use of the interactive lever is low in three of the companies, the degree of use increases with uncertainty, as expected. When the level of uncertainty as perceived by management increases, a strategically important question arise, the interactive use of the budget increases. I.e., the budget is used as a basis for discussions in the company about strategic issues. This was explicitly mentioned by respondents in two of the companies:

“And obviously if something needs to be changed, for example we had to change the figures at one point [when a major change in market expectations occurred] and then we get together more often so then we met the four of us every week and just made concrete steps, we needed to cut down on costs a little bit until August so we did that and reprioritise between people we would hire, who would stay on etc. But that’s more when needed so to speak.” (CEO, Delta)

The same pattern was presented in Beta, the interactive use of the budget increased in times with higher uncertainty than usual:

“The times when, since it has been moving like up and down, the times when there are critical periods, these times we really focused a lot on the budgeting part” (CEO, Beta)

Although the interactive use is more leveraged in these situations, the reason is not only a need for strategic discussions, but also a need to communicate new prioritizations and goals. This purpose of the increased budget used in times of uncertainty was mentioned by several respondents:

“[In] the crunch times when we need to focus a bit more they (the budget targets) have been communicated every week” (CEO of Beta)

4.5 Boundary systems

Boundary systems establish the rules of the game and identify actions and pitfalls that employees must avoid, which can be called as the power of negative thinking. They are stated in negative terms or as minimum standards (Simons, 1995). Any MCS that sets out minimum standards or guidelines for behaviour can be used by managers as a boundary lever of control (Tuomela, 2005).

Compared with Simons' definition of boundary, the boundary system in small growth companies is more stated in limits based on financial data, such as cash limits or cost limits, rather than direct behavioural limits (cf. Tuomela, 2005).

The focus on financial boundary system is apparent in many of the companies. In Epsilon and Beta, all expenditures above a certain limit need to be discussed and get approval in a wider group of people. In both companies this limit is fairly low, forcing employees and managers to discuss the costs and benefits of different business choices. The importance of strict cost control is stressed by several respondents:

“The main thing why small companies like us fail, it's often not the business idea or something like that but money. You need to have money to survive a couple of years before you are big and have a market and stuff. It's all about that.” (CEO, Alpha)

In small companies where informal controls play a more important role (Simons, 1995, among others), there are also informal boundary systems. These informal boundaries are expressed by most companies as non-defined limits such as: “restrict the costs and work for more revenue” or “frame of liquidity finance”.

One respondent compared it to the feeding of a horse:

“We always have to restrict the costs and work for more revenues all the time. It is like when you have a horse: you have to feed it and then you run, you always need to stretch on it.”
(CEO, Beta)

That is, the informal boundary system even restricts the growth of the company in order to retain control:

“For budgeting, in our case we are trying to be very cautious because we want to retain control of things /.../We have to hire after we have actually grown, which puts a strain on the whole system when we do it but also slims down the processes, which is good, so we become more efficient.” (CEO, Beta)

One respondent also put forward the idea that the resource limit implied by relying on internally generated money only, could have a positive effect on the business:

“I think when you start a new product line, I think it's good to do it with your own money because it, that's, keep the kind of bootlegged startup quality of the product. So it's not like, 27 here, you have a lot of money, spend it or use it.” (Manager, Gamma)

4.6 Belief systems

None of the companies in our study have a formal, and articulated, belief system. In one of the companies, the story behind the founding of the company is represented by artefacts at the company office, in the shape of a movie poster for the movie that inspired the founders. The poster, and a slogan connected to it, represents a credo for the company. Similar semi-formal belief systems are not present in the other case companies. This does not mean that the other companies don't have visions or credos, only that they are not formalized. Instead they are present as tacit understandings and commitment to the business idea. I.e., belief systems are not absent in general, but formal MCSs leveraged as belief systems are absent.

Examples of informal articulations of visions/credos/strategy in the case companies include inspirational ideas and mottos that are frequently repeated in more or less the same form:

“Because you can have all the ideas in the world but you need to make it happen.”

(CEO, Beta)

“For us, work is number one, life is secondary” (CEO, Gamma)

Product oriented in one case:

“We are very hard working. We have great passion for what we are doing and find the concept of the product that we are working with as something good /.../ rather than a consumer good”

(CEO, Gamma)

And business idea oriented:

“We are looking forward to being the Mercedes-Benz in this industry. We are not gonna be the cheapest but we are gonna be the best” (CEO, Beta)

“Number 1 is selling, number 2 is doing this (budgets/MCS/financial planning)” (CEO, Beta)

“So we are now more sales oriented.” (CEO, Gamma)

“The revenue is always most important, my key priority is just how much sales we do, so obviously when something is not priority one it does not come in first hand, so everything else that is priority two, three, four, five” (CEO, Delta)

“What we do is that we scale up the process and we sell like hell, that’s what we try to do, reach a critical mass of customers which makes it much easier” (Manager, Alpha)

5 Analysis

5.1 Budget use in the case companies

All companies in our study pay large attention to how their budget is designed and used and managers are aware of the positive aspects of MCS. Managers express a high confidence in budgeting as a control device and devote time and money to develop their MCS design and use.

This finding is contradictory to earlier studies, which have concluded that managers in startups pay low attention to MCS use and development out of ignorance or resistance to bureaucracy (Granlund and Taipaleenmäki, 2005; Collier, 2005). We also find that several companies experiment with different budget designs in a proactive manner, i.e. to find a better way to handle the business situation and future growth. Budget development is thus not only reacting to obvious needs, but actually precedes need (cf. Davila et al., 2010). We can also not find any evidence for the MCS use being mainly a result of influence from external pressure, such as VC, which has been suggested in earlier studies (Granlund and Taipaleenmäki, 2005; Frow et al., 2010; Strömsten and Waluszewski, 2011), instead, the interest in and ambition to use and develop MCS seem to stem from internal factors. However, VC is not majority owner in any of the companies and its impact is thus expected to be limited.

In contrast to earlier studies on MCS use in startups, the companies in our study are not engineering-oriented. Earlier studies have proposed the engineering-oriented (or technologically oriented) corporate culture of the companies studied as a possible reason for the low interesting MCS use (Granlund and Taipaleenmäki, 2005). CEO experience of startups and CEO beliefs on the benefits of planning have also been shown to have a correlation with MCS adoption (Davila and Foster, 2005) and studies have found that CEO’s beliefs affect human resource policies of companies (Baron et al., 1999). The notion that CEO and management background should have a significant influence on MCS use and adoption then seems reasonable. In this study, all CEO’s and a large portion of the managers in the companies studied hold a degree from a business school. Thus they can be expected to have a better knowledge and awareness, and probably also a certain interest, in MCS use and design. This would be one probable explaining factor behind the somewhat contradictory results of this study. This finding can also be related to the distinction between entrepreneurs and managers by Davila and Foster (2007). Entrepreneurs start companies and are usually focused on the innovation, whereas managers

manage businesses and succeed in making the company grow. Our findings may indicate that CEOs with a business school background have a higher possibility of acting both as entrepreneurs and managers, than engineers.

5.2 Budget use in terms of levers of control

Although all companies recognize the importance of MCS, the actual use differs between them. In terms of levers of control, there was a distinction between two groups: the companies where diagnostic use dominated and the companies where interactive use dominated. In line with Tuomela (2005) we find that the budget is connected to all four levers of control, and can be leveraged in several ways depending on the situation, but also simultaneously.

5.3 Diagnostic control systems

All respondents stress the importance of diagnostic controls in order to track performance, spot deviation and be able to take corrective action, which is in line with the traditional use of MCS (Fischer, 1995). Earlier studies have found that managers have a natural tendency to use MCS for controlling purposes, rather than enabling (Ahrens and Chapman, 2004; Wouters and Wilderom, 2008) which is in accordance with our findings: the budget is mainly used diagnostically, as a control tool. This finding goes against what is supposed to characterise an entrepreneur, namely the focus on enabling controls and a low need for control (Bhidé, 2000). On the other hand, the idea about entrepreneurs as low-control managers may still hold, as the emphasis on diagnostic controls expressed by our respondents concerns the budget use. A diagnostic focus in the budget use does not necessarily imply a controlling management philosophy on the whole. This issue will be further discussed in 5.6.

For the diagnostic use, we find that all companies set budget targets to serve for planning and as references for performance evaluation. Evaluating performance towards targets is one of the most commonly used functions of a diagnostic system (Simons, 1995). Somewhat surprisingly, managers tend to put some effort into setting budget targets, although they readily admit that this task is extremely difficult. Consequently, they also admit that they don't use the budget targets for ex-post performance evaluation to a very large extent.

The fact that budget targets aren't used for ex-post performance evaluation is in line with the findings of Granlund and Taipaleenmäki (2005). In their study, they find that in companies in the early stage of development, ex-ante planning has a strong prerogative over ex-post control. This prerogative can be said to exist also in the companies of our study and the future-orientation, probably a vital characteristic of all startups, is also strong: budget targets are set as targets but are primarily used as an

ex-ante planning device, not a reference for ex-post evaluation, regardless of managers' stated intent when setting them. However, we do not find any connection between this future orientation and VC funding, as Granlund and Taipaleenmäki (2005) do.

It is hard to disentangle the causality between the lack of ex-post evaluation and the future-orientation. Compared to Granlund and Taipaleenmäki's (2005) study, we don't find evidence for future-orientation as a cause of the absence of performance evaluation. Although a certain future-orientation exists, and certainly makes managers more interested in ex-ante planning, some of this future-orientation may be an involuntary consequence of the problems connected to performance evaluation. Several respondents demonstrated a discontent on the absence of performance evaluation, i.e. the lack of performance evaluation was not seen as a voluntary decision, but rather a natural, but undesired, consequence of the poor quality of the budget targets.

The only company where we can find that a strong future-orientation leads to a low interest in ex-post evaluation is in Epsilon, where the follow-up serves the purpose of making the employees more aware of the cost in the planning of future projects, rather than evaluation of the actual projects.

5.4 Interactive control systems

In contrast to diagnostic processes, interactive systems require a significant amount of attention by senior managers (Simons, 1995; Bisbe and Otley, 2004; Marginson, 2002). As resources for MCS development and use are limited in startups, it is reasonable to expect a low use of the interactive lever of control. This expectation is further strengthened by the point that interactive controls easily can be replaced by informal controls in a small company (Simons, 1995) and in entrepreneurial organisations (Collier, 2005). What is surprising is rather that we find such strong and developed use of the interactive controls in two of the case companies.

Diagnostic controls are needed to structure the interactive controls. Poor diagnostic controls may lead to a lack of focus leading to poor utilization of the interactive controls (Mundy, 2010) and we can see that functioning diagnostic systems still are viewed as the basis for a well-functioning budget, regardless of the attitude to MCS in general. I.e., all companies, also these in which interactive use of the budget dominated, strived for well-functioning diagnostic controls.

In its most general sense, interactive controls are used by top managers to involve themselves personally in subordinates' work, i.e. between hierarchical levels (Simons, 1995). Simons' original work was based on large organisations, and this strict interpretation of interactive controls makes less sense in a startup, where the hierarchical levels are low and blurred. But interactive controls can be

seen as functioning not only vertically, between hierarchical levels, but also horizontally, between functions (Abernethy and Brownell, 1999), an interpretation that is of more use in a startup context.

We find that the interactive dominance is related to the degree of hierarchy and task division within the companies. Companies with low hierarchy and low task division (such as Gamma and Epsilon), tend to prepare the budget in a decentralised way and use the budget more interactively to discuss strategic goals, make forward looking plans and for performance evaluation. A high degree of hierarchy and task division on the other hand coincides with low interactive use. That is, the budget is only used interactively, to discuss strategic issues, with people that work with similar tasks and that are close hierarchically, thus relating it more to the across-function interpretation of interactive controls.

In one way, this finding is counterintuitive, as a flatter organisation with lower task division would be expected to be more dominated by informal controls, such as informal meetings (Ouchi, 1979; Simons, 1995). Formal interactive controls would then be superfluous. One possible explanation to the high interactive use in companies with low task division can be found in the concept of role ambiguity (Marginson and Ogden, 2005). Low task division implies more floating roles and responsibility, something that is supported by respondents in the case companies with low task division. Prior studies have found that managers experiencing a high degree of role ambiguity tend to commit more strongly to budget targets, because of the clarity and structure the budget gives them in their perceived situation of ambiguity and uncertainty (Marginson and Ogden, 2005). Both interactive and diagnostic controls have been shown to be used decrease role ambiguity. In our study, we only find support for interactive controls filling this purpose.

Another possible explanation would be a strong belief in MCS use, and a perception among managers of MCS use as not only diagnostic, but also interactive (cf. Davila et al. 2009).

5.5 Boundary systems

Boundary systems are mainly used to restrict cash expenses, in line with Tuomela (2005): financial data establish boundaries that protect an organisation from financial risk. Since cash is an important resource for startups, this boundary is aimed at protecting the company from running low on cash and being forced to rely on expensive credits or giving up power to external capital providers.

Secondly, the boundary is a requirement from the external capital providers, in line with Strömsten and Waluszewski (2011). The reason for this boundary system is then to ensure carefully planning of major costs and investments.

In contrast to how boundary systems are defined by Simons (1995), this kind of boundary mainly act against the managers themselves, and not between managers and subordinates. I.e., the boundary is rather on managerial decisions such as investments, hiring new staff, rather than on every day decisions of employees.

5.6 Interplay between the levers of control

5.6.1 Interplay between interactive and boundary budget use

The informal boundary systems in the companies of this study prevent employees from too costly activities and from wasting limited resources, which set limits on the employees' behaviour and limit their flexibility.

In the companies using formal boundary systems, these also function as support to the interactive processes, as the cost limits force employees to discuss the projects and related issues with co-workers and the board. The reinforced interactive process thus brings back flexibility.

Operating within changing environments, startups need to be able to launch risky and costly projects, but the prerequisite is that there exists an interactive process to handle the strategic challenges these projects are intended to meet. In this way, the boundary system may both restrict flexibility and support interactive processes in order to give back the flexibility needed in the uncertain startup context.

5.6.2 Balancing the levers of control through suppression

In this study we find that managers continuously balance between enabling and controlling uses of the budget, and they do it both intentionally and unintentionally. We find that the concepts of dominance and suppression (Mundy, 2010) are useful to explain how this balancing act is performed.

To be able to understand the balancing act between controlling and enabling in startups, it is necessary to acknowledge that smaller companies to a higher degree can alter behaviour through informal controls (Simons, 1995; Collier, 2005) and it has been noted that in organisations working under high uncertainty, informal controls play a more important role (e.g. Cooper, 1981). The importance of informal controls will also affect the interplay between the levers of control in the formal MCS. In fact, we find that suppression of one lever in the budget often corresponds with a dominance of the very same lever in the overall management system. Or in other words, that suppression of one lever in the informal controls corresponds with the dominance of the very same lever in the formal controls:

In three of the companies there is a historical tendency towards suppression of diagnostic controls in

the company, and the focus of the management is mainly on the enabling part. The enabling focus is a conscious choice by the management, and the CEO is aware of what he perceives as its benefits and drawbacks. At the same time, the CEO regards formal controls as mainly, or exclusively, controlling: the budget is seen as a controlling tool, not a management tool in a broader sense, and the role of formal MCS is to act as a diagnostic system or a boundary system. The formal diagnostic systems that are necessary are all put in the budget. As no other formal MCS are used, and no other levers of control are formalized, the budget ends up being equal to the diagnostic, controlling controls.

I.e., as an enabling use dominates the overall management philosophy of the company, a controlling use dominates the budget. This pattern is visible when the overall management system focuses on enabling, and the budget thus is dominated by controlling use. The result is then that the diagnostic use of the budget is approximately of the same amplitude in both kinds of companies, but that the budget in companies where interactive controls dominate also use the budget interactively, i.e. the budget use is broader (see **Fig. 1**).

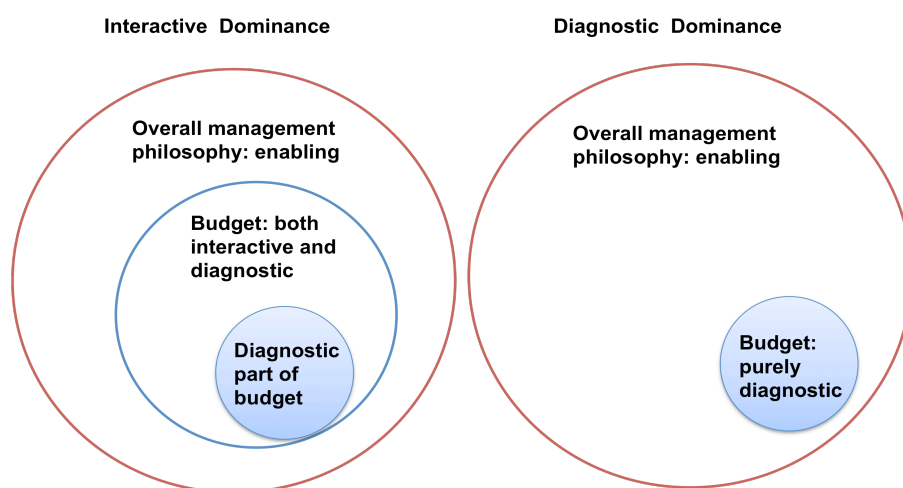


Fig. 1. The role of the diagnostic and interactive levers in the budget use.

The balance between controlling and enabling can thus be attained both through balancing of the levers of control inside the budget, and through balancing the degree of use of the budget. As the budget in itself is seen as a diagnostic tool, the suppression of the budget is a way to manage the balance between the diagnostic lever and the interactive lever that management perceive is executed through informal control systems.

This means that the diagnostic dominance in the budget is a consequence of the diagnostic lever being suppressed in the overall management. Putting all diagnostic controls in the budget makes it possible for management to balance the use of the diagnostic lever by balancing the use of the budget. The balance between control and enabling is thus not so much attained through balancing of the levers of

control inside the budget, but instead through balancing the degree of use of the budget.

Although suppression of the budget use may be an efficient way of suppressing diagnostic use of MCS in the short run, we will highlight three potential drawbacks as the company grows: the risk for hampered budget development; the design-use paradox; and the risk for internal inconsistency:

The first risk is simply that the suppression of the budget from the management's perspective naturally leads to a less functioning budget. This problem is highlighted in Delta where employees complained about the lack of diagnostic controls.

Another potential problem is related to what Marginson and Ogden (2005) labelled the "design-behaviour paradox". In situations where managers perceive a high degree of uncertainty and role ambiguity, Marginson and Ogden (2005) find that managers tend to commit more strongly to budget targets, even if the budget, because of said uncertainties, were supposed to be used in a flexible manner, what they label as the design-behaviour paradox. I.e., the flexible design of the budget turns into an inflexible behaviour. As mentioned earlier, we find that the degree of task division and thus role ambiguity is related to the degree of interactive dominance. In the companies where diagnostic use dominates, role ambiguity is lower. From our study we cannot say that role ambiguity causes interactive use or vice versa. However, if MCS don't adapt (formalize) to the growth, there is a risk that role ambiguity increases with the growth of the company (cf. Moores and Yuen, 2001). When the employees experience increased need for formal controls, they will naturally turn to the controls that actually exist, in this case the budget. I.e. if the need for formal controls increase, and the budget is the only formal control there is, the importance of the budget will increase. As the budget is supposed to be used diagnostically, the diagnostic use of the MCS will increase. This can lead to a situation where the suppression of diagnostic, and thus controlling, use, leads to the opposite. The suppression of the budget and diagnostic controls may then lead to a design-behaviour paradox behaviour among employees.

One example pointing at this risk can be taken from Delta where one respondent, asked about to what extent he used formal MCS in his everyday work, answered bluntly:

"Very, very little, I would say. Not enough to do a really good job. /.../ So it's a lot of guessing-game. It could be much better, much more efficient, less guessing, more formal financial systems." (Manager, Delta)

This is also related to what Mundy (2010) refers to as internal consistency. Management's emphasise on enabling in the overall management philosophy, but controlling (diagnostic) in the budget use may

be internally consistent as long as the budget use is limited. In a situation of increased budget use, e.g. following rapid growth, the risk for internal inconsistency increases as well: the increased budget use will lead to an increased use of diagnostic, and thus controlling, controls. If management keeps emphasis on the enabling overall management philosophy, there will be an obvious internal inconsistency between the enabling overall management and the controlling budget use.

I.e., the balance between enabling and controlling levers has to be obtained both between informal and formal controls, but also inside the formal MCS. This finding implies that the “entrepreneurial crisis” (Moore and Yuen, 2001) may be as much depending on a lack of interactive controls as a lack of diagnostic controls.

5.6.3 The ability to adjust

One common theme in both the diagnostically and interactively dominated systems is that the lack of diagnostic controls is explicitly mentioned as a problem in all the five companies, whereas the absence of interactive controls not is mentioned at all in the companies where diagnostic controls prevail. What we see is thus that in the companies where interactive levers dominate the budget use, managers are aware of this imbalance, and intentionally try to adjust it by implementing new diagnostic uses into the budget. In the companies where diagnostic use dominates the budget, managers don't seem to be aware of the imbalance. Consequently, they don't try to adjust it.

In the companies where interactive control dominates, we have seen a better ability to intentionally balance the MCS use. Both companies have intentionally added and subtracted budget functions to balance the use of diagnostic and interactive levers in order to achieve a balance between enabling and controlling use of the budget.

The dominance of interactive controls, and thus the ability to adjust imbalances, coincides with the ambition to develop the MCS. Both Epsilon and Gamma have experimented with several different MCS during their short lives, using a trial and error process: adding new systems, evaluating them, changing and refining. Delta and Beta, on the other hand, show much less tendency of experimenting and rather follows earlier findings on MCS adoption as trailing needs, as expected from previous studies (Davila et al., 2010).

The causality between interactive dominance and experimenting is not evident. Ambition and ability to develop the MCS use will lead to a higher probability of using a mixture of levers, simply because more controls will be tested. I.e., there is reason to believe that the trial and error approach causes a MCS that is easy to adjust and an atmosphere where new controls are tested and accepted.

On the other hand, there are reasons to believe that the causality goes the other way around too: one of the characteristics of interactive controls is the learning process and the ability to constantly collect and process new information from all levels of the company. This includes learning about shortfalls in the MCS use and discussing possible adjustments.

Obviously, the third possible causality is that both the ambition to experiment with MCS development and the ability to spot and adjust imbalances in MCS use, are caused by underlying characteristics of the managers in the company. Both companies that demonstrate a diagnostic dominance are dominated by highly educated employees, many of whom have business school background, characteristics that may in themselves imply a higher possibility of interest and knowledge about MCS and management in general. Studying high-tech companies, Granlund and Taipaleenmäki (2005) mention the engineering-oriented culture as one possible explanation to the companies' low focus in performance measurement and strategic planning. In contrast, the culture in the two interactive-dominated companies in our study could be seen as business school-oriented. This difference in management culture is one possible reason for the difference in attitudes towards MCS. On the other hand, there are no obvious differences in CEO or management background between the companies that are dominated by interactive controls and the companies that are dominated by diagnostic controls in our study. I.e., a business-oriented culture may lead to a higher degree of MCS development, but is not a sufficient factor in itself.

5.6.4 Leveraging the budget as a belief system

We have found a striking absence of articulated belief systems in the companies of this study. The role of belief systems is closely related to informal controls (cf. Ouchi 1979) and according to Collier (2005), belief systems are important in the management control of entrepreneurial organisations even though they are not formalized or articulated. I.e., the absence of formal belief systems is not surprising. However, we have found that the use of budget targets could be explained by its functioning as a formalized, but unarticulated, belief system (cf. Collier, 2005)

Budgets have traditionally been seen as diagnostic tools, but are to some extent leveraged as a belief system in some of the case companies. The budgets are used by managers to alter or maintain patterns in organisational activities. Managers use the budget to communicate focus, or reduce focus, on growth, and thereby on the alternative uses of time, such as product development, long term customer relations etc. This does not necessarily mean that the intent of managers is to leverage the budget as a belief system. But in the absence of an articulated belief systems, the budget turns into an unarticulated one, filling the same purpose.

This tendency to transformation of one lever into another is seen in the companies where diagnostic controls dominate the budget, and not in the companies where the interactive dominate. This may be a natural consequence of the differences in functioning between diagnostic and interactive systems: interactive controls includes two way and face-to-face communication (Simons, 1995), facilitating transmission of beliefs and visions. Thus they can more easily fulfil the role of a belief system. Diagnostic controls do not permit this to the same extent and the communication needs to be transmitted in some other way. This provides one potential reason to why managers in the diagnostic-dominated companies continue to use diagnostic controls although the quality of the controls is poor: the budget targets are needed as they fulfil another role, and are leveraged as a belief system.

One possible reason to why the budget targets transform into a belief system may be found in the core values a belief system is supposed to communicate. The companies in this study are primarily business-oriented, and not engineering-oriented. The main focus is thus not the product or technology in itself, but rather company growth. In that sense the managers in our companies can, in terms of focus, be compared to the venture capitalists in other studies (Strömsten and Waluzcewski, 2001; Granlund and Taipaleenmäki, 2005), i.e. growth is the overarching goal. Then the leveraging of budget (sales) targets as a belief system makes sense: growth as a core value is best communicated through sales figures. I.e., leveraging the budget as a belief system may serve the purpose of putting sales growth in the spotlight. But at the same time it becomes an extremely limited belief system, as it only can give guidance in what the ultimate aim is, but not direct attention to the ways to go there (Simons, 1995).

The transformation of the budget into a belief system could also be seen as a consequence of the internal inconsistency created by the suppression of the diagnostic systems. As mentioned earlier, managers' suppression of the budget in pursuit of an informal, enabling, overall management philosophy, may cause internal inconsistency when the company grows. In the absence of internally consistent belief systems, employees will attempt to align values and controls in their own way (Mundy, 2010). Here, we can expand this idea to the entire MCS package: in the absence of an internally consistent MCS, employees may attempt to create a belief system out of the formal systems that exists, i.e. the budget, in order to attain internal consistence in their own work.

The transformation of the budget into a belief system is then a part of managers' constant pursuit in balancing controlling and enabling controls (Simons, 1995; Mundy, 2010). The dominance of the diagnostic, and thus controlling, use of the budget must be balanced in relation to the enabling use of interactive and belief systems. The transformation of the budget into a belief system may not necessarily be negative but there are obvious risks connected: belief systems are mainly enabling

while the diagnostic lever is mainly controlling. In one of the companies we saw that the budget targets were leveraged both as a belief system, and simultaneously used as basis for the employee incentive program, which resulted in confusion among employees.

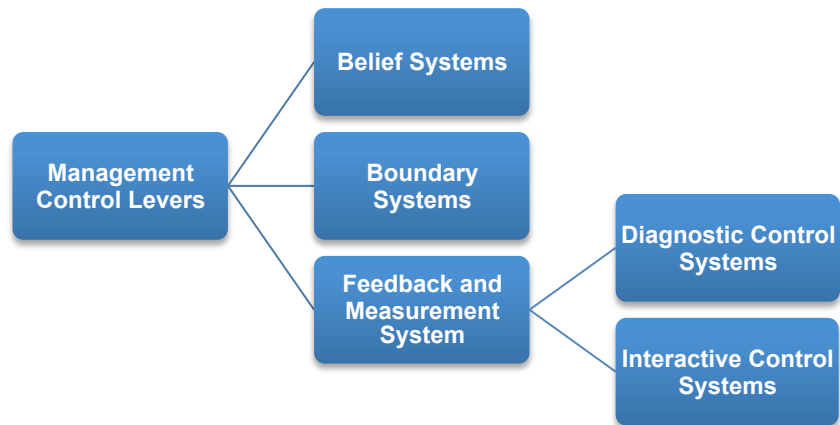


Fig. 2. The four levers of control (Simons, 1995)

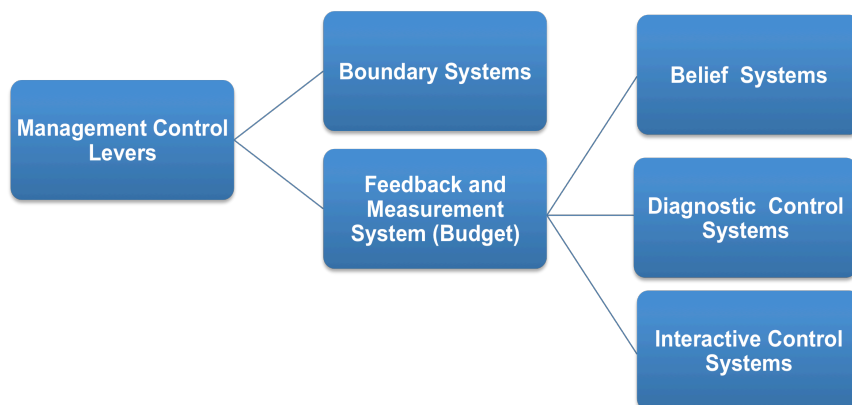


Fig. 3. The four levers of control when the budget is leveraged as a belief system

6 Conclusions and summary of findings

In this study we have examined how managers use budget in order to balance between control and creativity in five Swedish startups. We have used Simons' (1995) levers of control framework in order to analyse how managers use the budget in order to balance between control and creativity.

6.1 Contributions

6.1.1 Budget use in startups

This study contributes to the startup literature by broadening the sample of case companies studied. By looking at startups in the service sector headed by CEOs with business school background, we have broadened the knowledge on how startups use MCS:

Managers in startups pay a lot of attention on MCS development and use, although the way, and to what extent, they use the MCS varies strongly between companies. Managers in startups also experiment proactively with new MCS designs and uses, in order to adapt the MCS to future, and not only present, challenges. These findings are contradictory to earlier studies on MCS use and adaptation. We point at two possible, and related, reasons for this: first, our case companies are sales driven rather than technology driven, and second, the CEOs and top managers of our case companies have business backgrounds rather than engineer backgrounds.

These explanations point at the importance of not limiting research on startups to technology driven and engineer-oriented companies, but also to companies in other industries. It also points at the importance of individual specific reasons to MCS use and adaptation. This is not unexpected, as the size of startups per definition is small, the impact of the CEO is expected to be large. Our findings suggest that the notion of startups in itself might have a low explanatory power in terms of MCS use, but that MCS use rather is explained by other factors, such as industry or CEO background, regardless of size and/or age of the company. In that sense, our findings might suggest that life-cycle theories for MCS use and adaptation are of low use in the early stages of corporate development.

We find that all case companies regard diagnostic controls as the basis for their budget. Nevertheless, the companies differ in their degree of budget use in general and in the use of the interactive lever. In two of the companies, the interactive use dominates the budget use, and defines the use of the diagnostic lever. In the remaining three companies, the diagnostic use of the budget not only dominates, but also is the only intentional use of the budget.

Regarding the companies where interactive controls dominate the budget use, this coincides with a low task division and a high role ambiguity. Our findings strengthen the finding of Marginson and Ogden that MCS can be used to alleviate perceived role ambiguity among managers.

6.1.2 Balancing the levers of control in startups

In terms of the literature on how MCS can be used to manage the conflicting needs of control and creativity, we find that the budgets can be leveraged in several ways simultaneously, and that the

budget can be transformed into functioning as another lever than what was intended, if the existing levers are unbalanced.

In the companies where diagnostic budget use dominates, our findings suggest that this is an effect of the suppression of diagnostic levers in the overall management philosophy. As managers want to conduct an enabling management philosophy, they refer all diagnostic controls to the budget. The budget then turns into a purely diagnostic tool and the diagnostic tools are suppressed through suppression of budget use.

In the companies where interactive use dominates, managers are more aware of how the budget is used and more prone to experimenting with different MCS designs and uses. Controlling and enabling levers of control are in these companies balanced through experimenting and a trial and error process: new MCS features are added and tried in a proactive manner. These companies show a more positive attitude towards their budget use and seem to be better suited to adapt their budgets to meet new challenges. From our findings, we cannot tell whether the interactive use of the budget makes management more susceptible to experimenting as the interactive use improves the understanding of the budget use, or if the experimenting has led to more interactive controls being tried.

Respondents in all the companies where diagnostic budget use dominates, admit that the quality of the diagnostic controls, specifically target setting and performance evaluation, is poor. Still managers continue using it and spend time and attention setting the targets, although they actually don't use them for performance evaluation, there is a collision between intent and use. We find that one possible explanation of this intent and use collision is that the budget targets are leveraged as a belief system, i.e. the stated intent of using the budget targets for ex-post evaluation may not be the actual main purpose of them. This could be done intentionally or unintentionally.

6.1.3 Implications for managers in startups

Our findings can have certain implications how managers in startups use the budget:

Downplaying MCS use in order to obtain an enabling overall management philosophy entails risks: as the company grows, the power of informal controls will weaken, and the intended enabling management philosophy risk being outplayed by the controlling management implied by the diagnostically used budget.

This points at the importance for startups aiming for rapid growth to balance controlling and enabling levers of control in the formal MCS proactively. Specifically it points at the importance of

incorporating interactive uses into the budget at an early stage: interactive controls will help managers to spot flaws and shortcomings in the budget and adjust them before they turn into a real problem. Also, it seems that it is easier to add diagnostic elements to a budget dominated by interactive use, than the other way around.

We have also pointed out that management intent in using the diagnostic lever in the budget may be twofold: to actually plan and evaluate, but also to communicate a vision and create a belief system. Managers use the budget, as it seems, diagnostically, but the high targets are rather used to make employees believe that these targets are attainable. Thus, the budget intentionally or unintentionally can be turned into a belief system, instead of a diagnostic system. This transformation may not necessarily be negative, but if managers are unaware of the phenomenon, they risk misunderstanding the dynamics of the MCS use in their organisation.

6.2 Limitations

Some limitations of this study must be acknowledged before the findings are applied to other settings.

The strength of the multi-case research method in this study is the possibility to compare and crosscheck between different organisations. The weakness is obviously that the depth in each within-case analysis is more limited. Due to the qualitative data used, the study relies on the quality of these interviews, the picture given by the respondents and the authors' interpretations. Although we don't find any reason to believe that the respondents should intentionally provide incorrect information, they can only provide us with their picture. Furthermore, especially the CEOs, as they in four cases also are the founders, may be positively biased towards seeing their company as more successful and well-functioning. As we have only been able to interview two respondents in each company, the risk that the respondents' perspectives affect our results is amplified.

All respondent save one have been male, and all companies save one are headed by a male CEO and have a clear male dominance in the management team. This bias is a result of the limited number of suitable companies from which we were able to pick our sample. The male dominance may decrease the generalizability of our findings, but on the other hand, this male dominance is, sadly, representative for Swedish startups.

As a consequence of the small number of employees in startups, the characteristics of the individual employees, and especially CEOs and founders, have a large impact on MCS use. Although we have found reasons to believe that the business school-oriented culture in the case companies in this study has implications on the MCS use, compared to the engineer-oriented cultures in the companies of most

other studies on MCS use in startups, the high degree of personal impact on MCS use makes it harder to generalize the findings. Other contingencies, such as the fact that all companies in our study are located in central Stockholm, may also affect the results.

6.3 Future Research

This study has provided new knowledge about how startups use the budget to balance the needs for control and creativity. The use of MCS in startups is still a young research field and there are several aspects that need further research.

Since our study is a multi-case study, it would be interesting if future studies could go into depth in one company of the same kind as in our study, or make a longitudinal study on the topic. This would provide a better understanding for the reasoning behind the choices on MCS use and its actual functioning.

We believe a broadening of the research objects in studies on startups would be fruitful. Especially, we believe startups in the service sector, as in this study, to be a fruitful area of research, as this sector is growing in importance and is a sector where many new companies are started. A related issue is that CEO characteristics are likely to differ between industries, as pointed out in this study.

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8 Appendix

8.1 Interview sheet

Background – Respondent

Job title/description

Age

Educational background

Previous working experience

Can you describe what you do in your work?

Can you describe your work situation? flexibility
 freedom
 target setting

Background – Company (Only CEO group)

Ownerships

Overall view on management

Key milestones in the company's history growth pains

Growth challenges

Budgeting

What budget(s) do you use? What kind of budget? (operational, liquidity, capital)
 When? How often? (monthly, yearly, project)
 What level? (company, project, individual)
 Diagnostic vs interactive
 What kind of numbers?
 Used together with other practices?

Why do you use the budget? Planning
 Evaluation
 Communication
 Strategy
 External pressure

How do you use the budget? Planning
 Evaluation

With whom? Alone or together?

Discussed with others?

Formal vs informal

Used together with other practices?

Diagnostic or interactive?

Can you change the budget?

How is the budget prepared?

How often?

By whom?

Does it take long time?