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## **Transfer Pricing's Effects on Accountability**

A conflict of accountability demands

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## **Abstract**

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Title: Transfer pricing's effect on accountability - A conflict of accountability demands

**Background and problem:** Divisionalized firms often use transfer pricing as a means of controlling and evaluating separate units. Since transfer pricing creates an economic relationship between units and accounting information of the unit's performance, transfer pricing is argued to have an effect on accountability. Such research is however limited, to which a possible explanation is the institutionalization of transfer pricing as an organizational everyday practice. As technology and availability develop, the expectations on accountability increase which creates a desire to resume research on transfer pricing's effect on accountability.

**Aim of the study:** The study investigates what impact transfer pricing has on various accountability demands and how it might affect the conflict between them.

**Methodology:** A qualitative case study was performed at the Atlas Copco group, a company with a complex and divisionalized organizational structure with emphasis on their internal transactions. In-depth interviews were the primary source of data. The data analysis was performed using the analytical model developed and presented in the theoretical framework.

**Discussion and Conclusion:** The current principles of the transfer pricing system cause a conflict in terms of viewing the relationship between internal service providers and their customers different were one unit considers the lateral/social accountability as dominant while the other considers the hierarchical accountability as prominent in the relationship. This causes uncertainties for the parties on how to act towards each other and which accounts should be given and demanded. It also opens up possibilities for sub-optimization in terms of a misdirected focus and not taking responsibility, but also in terms of de-motivating managers. The study also concluded that this conflict lead to a change in the object of accountability.

**Keywords:** Transfer pricing, accountability, conflict of accountability demands, management control

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# 1 Introduction

*This paper starts with examining the need for research in the area of transfer pricing's effect on accountability. After an introduction to both transfer pricing and accountability, the research question will be presented.*

In large organizations, centralized control is problematic with multi-locations and large product ranges. To overcome this many companies use a decentralized structure to ensure more effective control (Berry, Broadbent and Otley, 2005). It is argued that by dividing the company into smaller units, either by product or activity, each unit can be measured and evaluated financially (Merchant and Van der Stede, 2012). By doing this the central management is able focus on the strategic issues of the firm and the local managers are encouraged to make the more informed decisions. Local units can organize their own activities but are still accountable for their actions to central management (Berry et al., 2005). One outcome of a divisionalized organizational structure can be the use of transfer pricing (Plesner Rossing and Rohde, 2014), i.e. the internal transactions of purchasing and selling products or services from one unit to another at a transfer price affecting both units' profit. The accounting information created by the transfer pricing system, such as revenue for the selling unit and expense for the buying unit (Merchant and Van der Stede, 2012) is according to Roberts and Scapens (1985) the main information upon which managerial performance and competence is evaluated and the primary path for giving an account for managers (Munro, 1996). Giving an account can be explained by Munro and Hatherly's (1993) definition of accountability: "the willingness and ability to explain and justify one's acts to self and others" (p. 369).

Research regarding transfer prices effects on the individual has been relatively limited. There are some studies such as Choi and Day (1998) which note that decisions regarding transfer pricing may have a significant impact on divisional managers' incentive compensation. Otherwise, research within transfer pricing has taken several directions and in recent literature focus has been devoted to its ability to relocate profit (Merchant and Van der Stede, 2012). The principles of setting an optimal transfer price have also been explored (e.g. Hirschleifer, 1956; Besanko and Sibley, 1991; Dikolli and Vaysman, 2006) together with its consequences on tax (e.g. Clausing, 2003; Hines and Rice, 1994; Bartelsman and Beetsma, 2003; Sikka and Willmott, 2010).

Munro (1996) states that giving account within organizational aspects has undergone somewhat of a revolution with empowerment, democratic workspaces, team-building and corporate values. These notions are work specific attempts to direct and modify the giving of accounts. Transfer pricing in a divisionalized firm may have a large impact on control technologies such as responsibility accounting and performance contracts. Various control technologies have been introduced to make members align in a disciplined way with officially approved corporate values and codes of conduct as a way to redesign accountability. Further, modern technology stresses immediate use, easing of effort and constant availability (Cooper, 1993 in Lilley, 1996). This has brought with it new expectations on accountability (Messner, 2009), which creates a desire to resume research on accountability and more specifically on its relation with transfer pricing as a control technology.

The use of transfer pricing and its effect on accountability, is an area that can be argued to be somewhat overlooked by current research. Plesner Rossing and Rohde (2014) state that there is a limited amount of empirical research done to test the outcomes and theoretical assumptions of transfer pricings' motivational effects. Transfer pricing is suitable when examining accountability

since it creates an economic relationship between organizational members, both between managers and subordinates as well as between individuals of equal power, and may cause unwanted effects and behavior when employed in organizations. A possible explanation to the gap in research might be found in Burns and Scapens' (2000) discussion regarding the institutionalization of management accounting in organizations. In line with their argument, the use of management control techniques, such as transfer pricing, can be seen as an organizational practice that it is embedded and unquestioned in everyday routines of the organization.

Roberts (1991) talks about two types of accountability, the hierarchical and the lateral/social and their different effects on the individual. The hierarchical accountability makes the individual see oneself as only having instrumental relationships with others (Roberts, 2001). In hierarchical accountability control technologies regulate the relationship between superiors and subordinates (Munro and Hatherly, 1993). The social/lateral accountability recognizes the individual's interdependence with others, it is based on the conversations and sense making that occurs face-to-face between people of equal power (Roberts, 2001). Roberts (1991) also notes that obligations from the hierarchical accountability can collide with informal commitments created by the socializing forms of accountability, threatening both the informal loyalties and the formal responsibilities as the individual feel torn between competing demands. Cäker (2007) describes such a conflict of demands since the lateral accountability was not included in the formal accounting system. The study performed by Helden et al. (2001) shows that an opposition between different forms of accountability might arise inside an organization, where the social accountability is displayed through the internal transactions between business units. To contribute to the existing literature on transfer pricing this paper sets out the answer the following question:

*How does transfer pricing affect the interplay between hierarchical and social accountability in a divisionalized organization?*

To answer the above question, this study looks deeper into the case of Atlas Copco, a divisionalized firm that puts emphasis on transfer pricing and internal transactions in order to evaluate each unit in a fair and proper way. Their system of internal transactions will be analyzed using an analytical model built on the various theories of accountability. This study makes a delimitation to the internal transactions regarding services of different kinds since this is the aspect of the transfer pricing system that causes confusion and discussion in the case company.

The next chapter of this report will examine theories regarding accountability resulting in an analytical model, as well as discuss the empirical findings of previous research on transfer pricing relevant when discussing accountability. Thereafter, detailed descriptions of the methodology and method that was used in order to conduct this study will be presented. The case company is presented further and the quality of the study is discussed. In the fourth chapter, empirical results from the interviews are presented, and analyzed in chapter five using the analytical model. Finally, the main findings of the study are presented in chapter six, together with suggestions for future research.



## 2 Literature review

*This chapter introduces the theoretical framework regarding accountability which is summarized in an analytical model. Thereafter, a section is presented about the previous research in which transfer pricing is discussed from an accountability perspective.*

### 2.1 Theoretical framework

#### 2.1.1 Defining accountability

Roberts (1985, 2001) present a broad definition of accountability which “*refers to the giving and demanding of reasons to conduct*” (Roberts, 1985, p. 447). Swift (2001) look at accountability as the provision of information between two parties. The one who is accountable “*explain or justifies actions to the one whom the account is owned*” (Swift, 2001, p. 17). Tricker (1983 in Swift, 2001) uses a narrower definition which includes a contractual agreement to which the accountability is bound. Such definitions stem from the principal-agent framework and the assumptions of an opportunistic agent which gives the need for a contractual regulation (Swift, 2001). It is however Roberts’ (2001) belief that an opportunistic agent is not an assumption but rather a result from the accountability processes within a firm and that trust (and distrust) is a product of ongoing interaction. Merchant and Otley (2007) hold a rather simple view of accountability which focuses on the outcome: “*being held accountable means that the individuals are rewarded when good things happen and punished when bad things happen*” (p. 792). Messner (2009) puts more focus on the expectations before something has happened as he states that: “*To say that someone should be accountable for particular events or actions is to hold certain expectations about what this person or organization should be able and obliged to explain, justify and take responsibility for*” (p. 918). Messner also explains that demanding an account reduces the gap between action and expectation. For the remainder of this paper however, accountability will follow the definition by Munro and Hatherly (1993) since they show that accountability is not only given to others but also to oneself as they define accountability as “*the willingness and ability to explain and justify one’s acts to self and others*” (p. 369). The willingness lies with the person giving an account and what he/she wants to justify and explain, while the ability refers to the means by which the person communicates his/hers account (Cäker, 2007). This definition is well suited for this research paper since it incorporates both the person's willingness and ability to explain and justify which will be taken into account as it is dependent on both organizational structures and the individual. Further it incorporates “*to self and others*” meaning the giving of accounts will not be limited towards only recipients but also the accounts given to oneself.

#### 2.1.2 Accounting information as basis for accountability

Accounting information is a means of negotiating, defining significance, expressing and enforcing expectations as well as enacting power relations in organizations (Roberts, 1991). Roberts and Scapens (1985) state that the importance of accounting increases with the distance between the parties, since accounting is the principal bearer of knowledge when there is no face-to-face interaction. According to Munro (1996) the accounting system becomes an obligatory passage for demanding and giving an account were accounting numbers create a line of visibility and speak for themselves. However, Roberts and Scapens (1985) mention that subordinates cannot fully anticipate and control how the superiors will interpret the accounting information such as cost, revenue or profit. They cannot rely on it being interpreted with an understanding of the specific problems and events that produced them. They can instead only rely on the results being the main information upon which their managerial performance and competence is judged. In addition,

Plesner Rossing and Rohde (2014) state that transfer prices based on actual cost can transfer inefficiencies between units which will then affect the judgment of how the units perform. Further, Cools and Slagmulder (2009) found that transfer prices that were tax compliant had a negative impact on divisional managers' motivation and entrepreneurial spirit.

Problems for the superiors are also present according to Roberts and Scapens (1985), mainly in terms of making sure that they are interpreting the information in a correct way since they are often forced to rely on the information available to them. It is the basic notion that accounting information is often gathered in a context that differs from the context in which it is subsequently interpreted that produces the risk for misinterpretations. Willmott (1996) raises a similar concern regarding the interpretation of accounting information using accountability systems. Accounts are produced and contextualized by the use of accountability, but accountability itself may be complex and problematic causing the interpretations to differ in practice. Carnaghan, Gibbins and Ikäheimo (1996) discuss the management of financial documentation since it is a way for managers to satisfy various accountability pressures. Management of such documentation refers to the activities taken by managers to generate a particular view of the unit or company to its evaluators and it serves as an illustration of an accountability activity. This documentation, and the process of creating it, is not just random but instead directed towards its targets as a comprehensive set of managerial activities.

### **2.1.3 The process of accountability**

According to Kreiner (1996) it can be difficult to establish exactly what is the object of accountability. In theory there is an actor whose judgment, actions and decisions are being judged by the principal. In practice it may however be more difficult to determine both the actor, the conduct and who is doing the evaluation. It may instead be that the action itself is created, actors identified and evaluators mobilized through the process of accountability. Roberts and Scapens (1985) believe that the difficulty in determining who should be held accountable is due to the complexity of interdependent actions in organizations. By considering accountability as a process in which judgments, acts and the giving of accounts are being produced in an interactive way, Kreiner (1996) suggests that individuals are mutually accountable and operate as both authority and actor simultaneously.

Kirk and Mouritsen (1996) see the accounting system as an intermediary that translates information between contexts and it supports the relationship between the institutional principles with the local organizational context. The financial information created and presented by the accounting system, such as targets and reports, facilitates the control of subsidiaries set up by the headquarters and assists in determining if interaction is needed. It also facilitates the comparison of different areas. This process is however not automatic, Kirk and Mouritsen state that the intermediary does not act on its own. Accounting needs actors who respond to it and put it into motion, and this is where accountability comes in. Accountability makes the accounting system important. A common example is measuring profitability which is typically an integral part of an accountability system. The accounting system is also seen as the basis for deeming members (un)reliable and (in)competent since people often have to convince others that actions are reasonable and sensible on a basis that incorporates accounting performance, even in situations where this information is unsatisfactory. Kirk and Mouritsen continue with that it is not only what is visibly created by the accounting system that influence conduct, but also the expectations that come with it. If the management team is expected or known to act on decisions based on accounting information, the subsidiaries might incorporate this as an expectation in their behavior.

#### **2.1.4 Accountability's role in shaping the organizational reality**

Roberts (1996) argues that accounting has established itself as one of the most legitimate and powerful tools for making actions visible in firms due to its capacity to present figures and facts in an objective way. It entails to present a truth that is independent from the groups and individuals whose interests are served and reflected. This is what makes accounting so effective, namely its power to present a seemingly indisputable image of the organization's results.

Accounting systems foster distanced forms of accountability and control. When the information becomes one-dimensional, the underlying processes for creating that information become only a mean for realizing the information and not the processes themselves (Roberts and Scapens, 1985). Lilley (1996) discusses the desire for mastery and control, that is thought to be the underlying aspiration when implementing a system, and the possibility for it may in itself destabilize the possibility to reach this in practice. It may shelter a reversible independence meaning the search for control eliminates the possibility for actual control. When trying to control, the control in itself is all that can be controlled and not the actual actions of the users. The notion of mastery and control can thereby be seen to be something that is wished or hoped for but in fact are illusory or impossible to achieve.

Roberts and Scapens (1985) state that there might be a danger in confusing the reflection created by accounting information with the actual reality of organizational practices. By acting on this view it could lead superiors to believe that this information allows them to objectively determine where responsibilities should lie and where praise and blame are in order. The accounting information is an image of the organization at a certain point in time and from a particular point of view making it selective in focus and subjective to boundaries. What might be missing from this picture is possibly as significant as what is visible since the preparer has a determining impact of what is recorded. Panozzo (1996) argues that accounting only partially reflects an organization's economic reality since it functions not only by being collected but instead created in the way it is classified and arranged. This highlights the way in which a pattern of visibility is shaped, defined by accounting's incomplete view of the organizational functions. Multinational companies which make subsidiaries visible through the accounting system allows accounting to form a "regime of truth" regarding events. This means the system shapes what counts and transports information in the shape of profit back to the headquarters (Kirk and Mouritsen, 1996). Munro (1993) problematizes about accounting numbers as a basis for management control. This stems from the notion of visibility which is a constructivist concept. "It implies that some actions count and others do not; and that this process of counting is socially determined. Unless used with care, however, it carries with it overtones of a realist optics" (Munro, 1993, p. 251). In his paper, Munro assumes that accounting numbers are of limited transparency since they do not automatically provide insight into the underlying operational reality. According to Kirk and Mouritsen (1996), the accounting system then takes the stance to use criteria from the inside rather than the outside to control and respond, thereby inserting the subunit into the same context and strategies as the whole organization rather than according to its own local characteristics. By using accounting performance, it can serve as an intermediary that people mobilize to demand, explore and provide explanations about their own and others' affairs. It can be thought of as a durable intermediary since it is often anticipated in firms and acted upon. The use of it reinforces the usefulness since it is only by mobilizing it that it is shown to be taken seriously. The problematics by doing so can be found if the management control system is not able to fully capture the causes of variation plausibly

found in the reports. The subunits may then question their local business' visibility in the system and the systems' ability to correctly reflect them.

When having a logic of mastery and control as the objective behind establishing the system it gives us two kinds of accountability regarding the promised benefits of the management system (Lilley, 1996). The first accountability is for the establishing of the potential to reach mastery and control and the second is for the actual realization of it. The issues that arise regarding accountability can become problematic if the system is not wanted by the users making it difficult to decide who should be held accountable for the exploitation of benefits it is thought to produce. So before management accounting can be used as a source for accountability it must be rationalized as being a relevant tool by the members of the organization (Ahrens, 1996).

### **2.1.5 Hierarchical and social accountability**

Roberts (1991, 2001) states that accountability processes affects individuals and assists in shaping the self and our relationships to others. Roberts makes a distinction between different accountability processes and practices based on their different effects, i.e. individualizing effects and socializing effects. The individualizing effects stem from the hierarchical accountability which confirms the solitary and isolated self while the socializing effects come from the lateral accountability which confirms the self with an emphasis on the interdependence with others (Roberts, 1991).

#### ***2.1.5.1 Hierarchical accountability***

Roberts (1991) explains that in accountability, recognition and acceptance are important for the individual and are often associated with success. When it comes to hierarchical accountability, the desire for recognition make us adhere to others' expectations, thus one is not accepted for one's uniqueness but rather for one's ability to fit in with the required image. Recognition is a constant ritual of hierarchical accountability and in these rituals accounting information plays an important role. The fear of exclusion raises a concern for one's own survival which is dependent on meeting the demands of routine accountability. In hierarchical accountability each level offers a confirmation of relative value and worth, causing the self to be drawn towards conformity with those standards, in order to be successful.

Individualizing effects are based on formal hierarchical accountability which makes the individual see oneself as only having an instrumental relationship with others (Roberts, 2001). An important part of this formal hierarchical accountability are the technologies which serve to normalize and individualize the self by comparing, differentiating, hierarchize, homogenize and excluding people. Such a technology is the use of accounting information which brings with it disciplinary effects in terms of visibility and facilitates a constant surveillance, making individuals competitive, identifying themselves with the results and creating an instrumental relationship with others. According to Munro and Hatherly (1993) there are often presumptive hierarchical forms of accountability i.e. who should report to whom. There are superiors and subordinates and the relationship between them is regulated through control technologies such as budgeting, responsibility accounting and performance contracts. This has led to control technologies being seen as ensuring that information regarding errors, exceptions and system failures is passed on upwards in the organization.

### **2.1.5.2 Social accountability**

There is more to giving account than financial reporting systems meaning there are other forms of accountability than the mere hierarchical one, namely the social form (Roberts, 1996). Roberts (2001) states that even if accounting plays an important role in shaping an individual's identity, it is not the only thing. The personal experiences of an individual generate many variations in the forming of the self and the relations with others. Recognition can come from the socializing processes of accountability, but it is then based on the conversations and sense making that occurs face-to-face between people of equal power. These talks are located in informal places between those who share a common conception of their world of work. The socializing processes thus allow these talks to confirm and recognize the self at the same time as it confirms the interdependence to others. The socializing processes of accountability provides opportunities to challenge and question which engage the individual who at the same time does not see others as an obstacle to the individual's success but rather as fellow subjects. These socializing processes can be found in the day-to-day work at every level in an organization as well as in the informal conversations in the workplace. Roberts (1991) states that the social forms of accountability are limited to local context where power asymmetry is absent and face-to-face interaction is possible. Jönsson (1996) discusses how lateral accountability can emerge from communication rather than from hierarchical power. When allowing local units to self-manage to a greater extent it can result in an increase of social responsibility that fosters accountability in the way that being a competent participant in various dialogues equals showing one's ability to uphold contracts and contributing to the general problem-solving.

### **2.1.6 Conflicting demands of accountability**

It is possible that obligations from the hierarchical accountability can collide with informal commitments created by the socializing forms of accountability, threatening both the informal loyalties and the formal responsibilities (Roberts, 1991). Such situations confront individuals with a choice in which they may feel torn between competing demands from the formal and the informal. Such a conflict is described by Cäker (2007), when the lateral and hierarchical accountability conflicts since the lateral accountability is not included in the formal accounting system. When conflicts arise between different needs, managers must prioritize between them. Some might argue that this prioritizing is part of being a manager with doing such tradeoffs. Valid or not, if the different stakeholder's demands are not specified or balanced, it will be up to the manager which can create a burden since it might be hard to satisfy all stakeholders simultaneously. Ahrens' (1996) view lies in the notion of management accounting's failure to permeate organizational structures and that management accounting from an ethical and commercial standpoint is seen to play a too dominant role in accountability. His presumption comes from the standpoint of the powerful structures regarding hierarchical accountability and that management accounting plays an important role in those.

Munro and Hatherly (1993) discuss that corporations are implementing strategies which promote flexibility and shift the formal decisions making into lateral flows of information. The use of lateral communication can reduce the need of surveillance, thereby making vertical reporting irrelevant. It may however also reinforce the surveillance in hierarchical accountability as it becomes intensive and formal. If hierarchical accountability is not converted into lateral accountability, it is possible that control technologies which ideally promote lateral accountability are subverted into instead reinforcing hierarchical accountability. In order for new strategies to work, the most crucial action for sustaining the strategy is to overturn the existing hierarchical accountability.

Accountability has limits to it which Messner (2009) has identified to be; the opaque self, the exposed self, and the mediated self. These limitations on the self makes it hard or at times impossible to give account and it is important to be aware of these limits when demanding account from others. The opaque self suggests that there are some areas of the self that are unknown to oneself which limits one's ability to tell a full story about the self. According to Messner, this opacity comes in the shape of implicit knowledge or practical consciousness, which cannot be expressed discursively and therefore, cannot fully be accounted for. The exposed self is created when a demand for accountability arises and the accountable self is expected to answer. You cannot claim to account and then state that there is no need to account at the same time. Once you account, you agree to the need to give an account and to not give an account can be interpreted as a sort of account since when faced with a situation where somebody demands an account, one cannot not account. The mediated self takes the perspective of others and the self is subject to the social categories provided by these others. (Messner, 2009)

## 2.2 Analytical model

The theoretical framework outlined above has generated a model for analysis (figure 1) for this paper. By viewing accountability as a process, accounting information can be seen as input to this process. Further, the accountability process is shaped by the both the hierarchical and the social accountability that exists in an organization. The outcome of this accountability process is the organizational reality is helps to create, which in turn affects what is being put into this process by accounting information.

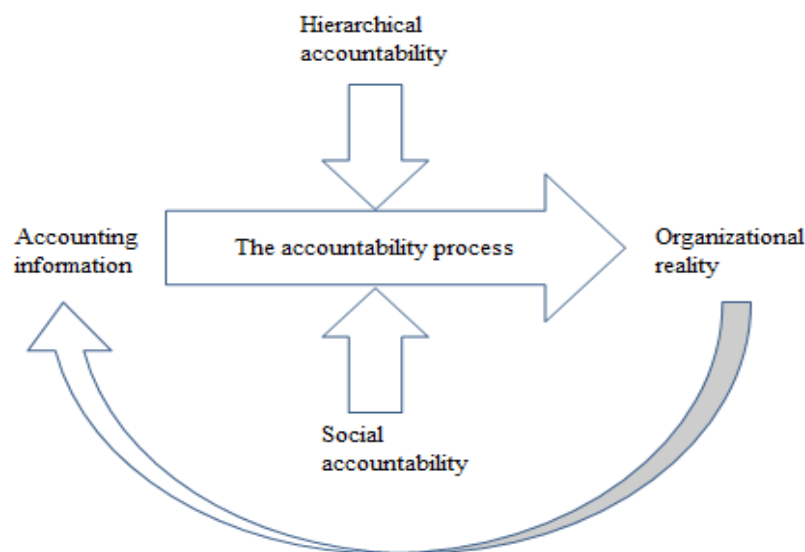


Figure 1. Model for analysis

## 2.3 Previous research on conflicting accountability demands

Carnaghan, Gibbins and Ikäheimo (1996) performed a study which centers around why managers may feel accountability pressures and how they choose among conflicting pressures. Managers may experience behavioral problems due to the complexity in various accountability relationships, there may be no way to satisfy all and to behave in the expected way with all parties involved. The

complexity of these relationships further increases since accountability pressures are not static, they evolve in relation to the actors involved when they are acting and responding to each other.

### **2.3.1 Balance between social and hierarchical accountability**

Cäker (2007) questions the incorporation of customer-related aspects into management accounting since in his study they overrode the hierarchical demands for financial performance. To have a customer focus in an organization could be interpreted as being accountable to the customer by letting them influence internal decisions, but often the correlating measures in the accounting system instead promotes members being accountable for the customers to managers. In his study the focus is to develop an understanding of how customers can influence the use of management accounting in order to understand how it can represent customers since accountability to customers can clash with manageability. Management accounting in connection to customers can be seen as the development of non-financial measures in organizations, but there is no technical difference between these measures and other measures in the system. The problematics with using the customer in this calculative way is that the systemic view of the customer may not say anything about the actual customer. Cäker uses the notions of hierarchical accountability; which is to account in accordance with the organizational structure, and lateral accountability; which is between people or in distance forms to corporate culture etc.

Cäker conducted a case study with interviews, documentary studies and participating observations. He studied a business unit (A) which functioned as a supplier to a manufacturer and belonging to a division with two additional units where one of these (B) had previously formed one unit together with A. After the split A was supposed to deliver goods both to customers outside the organization as well as to the old customer B inside the organization. A had a complex relationship with B due to their history as belonging to the same unit, but management wanted to conduct a split to enable relationships to be conducted in a more business-like manner. This was however perceived as unreasonable to fulfill due to the magnitude of personnel connections between the units. Due to the close geographical proximity between them, B could easily reach A in person and in combination with the previously established personal connections, it was hard for A to treat B in the business-like relationship intended by senior management. In addition, it was considered problematic whether to treat B like a customer or as a part of the organization. For unit A, the lateral (social) accountability thereby dominated over the hierarchical. For B the situation was similar in that members were more prone to accounting for non-financial measures, such as concern for the customers, than financial aspects making performance on delivery override hierarchical accountability. In B it was considered acceptable to disregard demands from senior management since these were thought to be incorrect from the start. Senior management however still regarded financial performance as fundamental regardless of Bs reasons for disregarding it. Senior management wanted to control the accountability to customers but B started using it as an explanation to why it was more important than to be financially aware leading to B taking actions that were not in line with senior management's intentions. Cäker refers to this dilemma as related to an unbalanced use of management accounting since the customer aspects were not leading to financial performance.

Cäker concludes that when the opinion of “what the customer really wants” is picked up, either inside or outside the formal system, it can be hard to redirect it via the management accounting system since it can serve as a strong guidance for organizational behavior. For unit A the personal ties, geographical proximity and joint identification served as factors making the lateral accountability override the hierarchical and it demonstrated the problem with trying to change

established accountability relations with the use of management accounting. For B the customer focused accountability may make manageability unbalanced even though it is in line with hierarchical. Cäker by this demonstrates how measures with the aim at balancing responsibility may pose a risk since the traditional aim of management accounting is to display costs to members. This balance is thus better found in an organization where accounting only plays a part.

### **2.3.2 Conflicting demands and internal transactions**

Helden et al. (2001) performed a study at a steel production company which focused on the coordination of internal transactions. After a reorganization, a multiple of business units were introduced to keep the organization flexible to market changes. The study looked deeper into the coordination of internal transactions between five business units. Four of them were included in the supply process, from production to packaging to sales, while the fifth unit provides services internally to the other units. Each business unit was responsible for their own financial performance and internal transactions which crossed the boundaries of units and had a direct impact on the financial performance of the individual business units. Even if the reorganization allowed for decentralized decision making in the business units, the internal transactions were centrally governed in regards to sourcing and transactions terms such as price. All sourcing needed to be internally supplied and transferred at standard cost prices. These terms placed emphasis on cost efficiency and resource usage which were important for the overall profitability for the company as a whole. It also created interdependencies between business units in the production process as one business unit's performance were partially determined by another business unit's performance and efficiency.

After discussions with controllers from the study's case company, Helden et al. (2001) identified a dilemma regarding the autonomy and the interdependence of the business units. A tension had emerged between autonomous business units with a financial responsibility and a desire not to lose the interdependence. Even if the business unit based decisions regarding the internal transactions on the interest of the company as a whole, there could a time arise conflicting interests between the business unit and the overall company. Such conflicts were normally solved after finding satisfying solutions for the company as a whole, but at a coordinating level concerns were still present. Control tools were therefore introduced to better assess the performance of the business units such as benchmarking and technical efficiency audits. Immediately after the reorganization, business units were pursuing their own interests to a greater extent but had after some time learned to balance the needs of the unit with the needs of the overall company, making the internal transactions a less pressing issue in the organization. What on the other hand continued to create tension were the performance measurement of the business units. The interdependence between units in the production process and the standard cost-based price gave large profits to the unit in the end of the process. That unit continued to show great returns without giving credit to the units earlier on in the process. This concerned some of the business units' managers as they felt they could not control all matter on which they were measured.

Helden et al. (2001) goes on to discuss that even if each business unit were accountable for its own performance it was also part of the integrated production process and therefore have a collective responsibility in the common decision areas. Helden et al. suggest that multiple performance measures are introduced in such a situation, which include both operational and financial measures, in order to promote coordination and encourage the collection and use of market information. This needs to be reflected in the accounting information system so that it promotes lateral relations as well as automatization. However, Helden et al. mentions that such controls may not fully comply



with each other. Some control will focus on the individual nature and the financial performance of the business unit while other will promote integration and the financial performance of the company as a whole. At times these measures will conflict and it is up to the managers to resolve the conflicts or balance the demands of the units with the demand of the organization.

## 3 Methodology

*Presented thoroughly below is how this study was conducted and how the results were arrived at. The chapter ends with a discussion of the study's quality.*

### 3.1 Qualitative methodology

The methodology (Ahrens & Chapman 2006) chosen in this study is qualitative. Ahrens and Chapman state that qualitative methodology aims to explore a social order that is subjectively created through interaction between actors. By looking at how accountability is created and what it in turn creates, this study takes on the interpretative perspective that “social reality is emergent, subjectively created, and objectified through human interaction” (Chua, 1986, p 615). Qualitative research further allows the studying of a situation in which the use and meaning of management accounting is indefinite (Ahrens & Chapman, 2006) and is therefore considered to be favorable when studying transfer pricing.

This study was initiated by developing the theoretical framework since theory in qualitative studies assist in explaining events, making sense of the social reality, disciplines the interpretation of new data, and prevents the researcher from being overpowered by data (Ahrens and Chapman, 2006). This report followed an iterative process in the construction of the theoretical framework, the presentation of the empirical results and the research question. Ahrens and Chapman (2006) describe this iterative process as seeking a fit between problem, theory and data, as the research problem guides the choice of theory which in turn guides the data collection.

### 3.2 Case study

The case in this report was selected since it is expected to increase the knowledge about a specific interest (Stake, 1994), i.e. about accountability's relations to internal transactions. Due to the abstract nature of accountability, detailed in-depth knowledge is required to answer the research question set out in this report. A case study is an approach suitable when exploring a phenomenon in its natural setting and there is a need for deep knowledge (Collis & Hussey, 2014). The role of accounting information in creating accountability makes the context essential in this study, further motivating the choice of a case study which puts emphasis on the context (Collis & Hussey, 2014; Stake, 1994). In order for the writers of this report to get familiar with the specific case and its context, a workstation was set up at the case company.

#### 3.2.1 Selection of case

This case study has taken place within the Atlas Copco Group. In the annual report of 2015, Atlas Copco states that it is a world-leading provider of compressors, vacuum solutions and air treatment systems, construction and mining equipment, power tools and assembly systems. The company was founded in Sweden in 1873 and is today listed on the NASDAQ Stockholm stock exchange with revenue of 102 billion SEK in 2015 and more than 43 000 employees globally.

The reason for selecting Atlas Copco as the field of study is due to its complex organizational structure that gives internal transactions an important role in the company's control system. Figure 2 displays Atlas Copco's organizational structure of the group. The group is decentralized and divisionalized, putting further emphasis on the internal transactions. The group has 4 business areas which consist of 23 divisions. Each division in turn consists of one or more product companies and several customer centers which are sales companies. At group level, more than 490

units are consolidated. In order for the divisions to focus on their core business, the group has internal service providers which supply IT related services, financial services and HR-services with higher quality and at a lower cost. Products or services that go from one unit to another are considered as purchases, which can be within a division between the product company and the customer center, between units in different divisions or between units and the internal service providers.

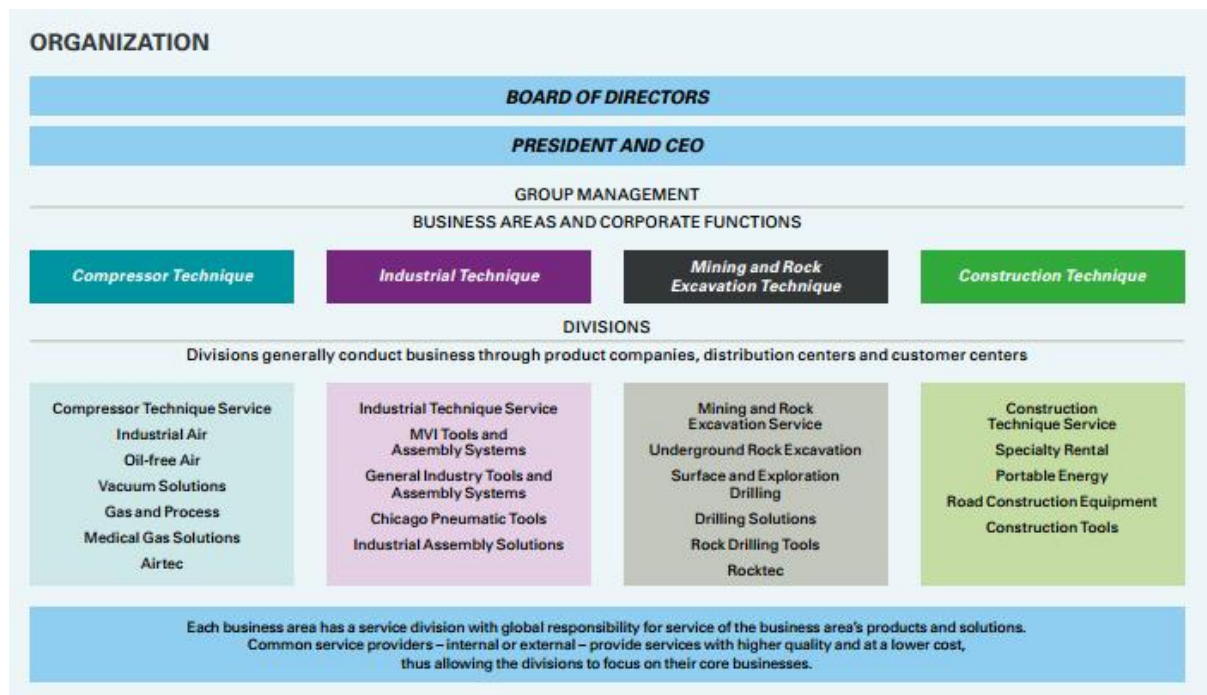


Figure 2. Atlas Copco organization in Atlas Copco annual report 2015 (p. 8).

### 3.3 Data collection

The qualitative data collected in this study consist mainly of primary data from interviews, and is complemented with secondary data collected from both internal and official documents of the case company. The data collection was guided by the theoretical framework and collected in a systematic way (Collis and Hussey, 2014; Yin, 2009) which is explained more in detail below. Before the data collection began, the researchers in this report spent time at the case company and gathered background information in order to become familiar with the specific context (Collis and Hussey, 2014).

#### 3.3.1 Primary data: Interviews

In this study, primary data was collected using interviews in order to gain data that explore understandings, opinions, attitudes, and feelings (Collis and Hussey, 2014). When possible, face-to-face interviews were conducted since it has an advantage when asking complex and sensitive questions and collecting comprehensive data (Collis and Hussey, 2014). All interviews but one could be conducted face-to-face, the final interview was conducted using a questionnaire due time limitations for the respondent. The face-to-face interviews were conducted by both researchers of this report which made sure that all issues of interest were explored during the interview (Collis and Hussey, 2014). Further, the face-to-face interviews were recorded when permission was given by the respondent to do so, which was the case in all interviews except two. During all interviews notes were taken which were subsequently transcribed along with the recordings to enable a more

thorough investigation of the material gathered. The recordings helped the researchers to focus on the respondents and their answers, making it easier for the respondent to feel confident enough to give honest answers but also to get a better understanding of their responses which according to Jakob (2012) makes them more likely to share information.

To further make the respondents rely on the researchers, each interview started with classification questions (Jakob, 2012) that were non-threatening (Collis and Hussey, 2014). The interview continued with “easy” questions and finished with the more difficult and sensitive questions in order to establish higher trust with the respondents (Jakob, 2012).

All face-to-face interviews took place in quiet locations so that the respondents wouldn't be distracted by others and to ensure the quality of the recordings. Further, the interviews were planned based on the schedule of the respondents, making the time of the interviews vary due to the respondents' schedules. (Jakob, 2012) When a shorter interview than desired was planned, the interview guide was reviewed beforehand and certain questions prioritized.

The researchers classified themselves as being perceived primarily as outsiders (Tinker and Armstrong, 2008) to the case company as it takes time to be included in a group, getting to know people and to get a complete understanding of a company's culture. As outsiders (Tinker and Armstrong, 2008), the researchers could ask questions that might be taken for granted by insiders, and critically assess the everyday assumptions within the organization. Being an outsider also gave the interviews a benefit of not demanding a “socially accepted” answer by the interviewees.

### ***3.3.1.1 The interview guide***

For this study, a semi-structured interview guide with planned topics derived from the theoretical framework (Jakob, 2012) was used to get more elaborative answers and to get a better understanding of the respondents' personal constructs (Collis and Hussey, 2014). Open ended, expansive and general questions were asked to get comprehensive answers, which allow for more than just the planned information to reveal itself (Jakob, 2012). These were complemented with follow-up questions (Collis and Hussey, 2014) during the interviews. The interview guide is attached in Appendix (Section 8.1).

### ***3.3.1.2 Selection of interviewees: Snowballing***

The selection of interviewees was made using the snowball technique, i.e. to follow the recommendations from the interviewees of more people with knowledge regarding the subject in question (Collis and Hussey, 2014). In qualitative research, snowball sampling is the most widely used method (Noy, 2008). The repetitive process of snowballing is considered an effective tool to access hidden populations (Noy, 2008), which was considered an advantage in this study to reach the people with an insight into the social accountability processes. The sampling technique of snowballing is interrelated to the interviews i.e. data accessing and data collecting are mutually dependent. This puts emphasis on the interaction and trust that exists between the researcher and the respondent as it relates to the quality of referrals (Noy, 2008). This was taken into consideration during the interview as an emphasis was put on building trust between the researchers and the respondents.

There is however a risk with using the snowball sampling technique in this study, which is that it might cause a biased view due to the recommendations of interviewees. Since the person recommending the next is aware of the subject, and what has been discussed during the interview,

the researchers risk being recommended a person with similar views on the research subject as the previous respondent. If the initiator of the sampling technique has a certain opinion, the researchers thereby risk missing out of a more comprehensive view of the phenomena since respondents with different opinions and experiences might be missed.

A contact person was used in this study, taking on the role of an informant (Fontana and Frey, 1994; Yin, 2009) and thus acting as both guide and translator of the case company's culture. This contact person was the first to initiate the snowballing process, and continuous communication was kept throughout the research process. As a final note, the contact person approved the publication of this document and its content.

The interviewees, their position within Atlas Copco and the length of the interviews are presented in table 1. In this report, all interviewees from the study are given anonymity to encourage a greater freedom of expression and more open responses (Collis and Hussey, 2014). This means they will not be named, but referred to using an alias.

Table 1. List of interviewees

<b>Interview order</b>	<b>Interview time (approximately)</b>	<b>Position</b>	<b>Organizational level</b>	<b>Alias</b>	<b>Sampling course (suggested by)</b>
1	50 minutes	Finance Manager	Legal Organization	FMLO	BCD2
2	45 minutes	Business Controller	Product Company	BCPC1	FMLO
3	45 minutes	Business Controller	Product Company	BCPC2	FMLO
4	45 minutes	Business Controller	Product Company	BCPC3	FMLO
5	45 minutes	Business Controller	Division	BCD1	BCD2
6	120 minutes	Business Controller	Business Area	BCBA	BCD2
7	60 minutes	Communicator	Internal Service Provider (Group)	CISP	BCBA
8	50 minutes	Tax	Corporate Function (Group)	TCF	BCBA
9	25 minutes	Accountant	Corporate Function (Group)	ACF	BCBA
10	-	Business Controller	Sales Company	BCSC	ACF
11	50 minutes	Manager	Internal Service Provider (Business Area)	MISP	BCD2
12	60 minutes	Business Controller	Division	BCD2	BCD2

### 3.3.2 Secondary data: Documents

In this report the internal documents, such as policy documents and organizational charts, confirm the hierarchical accountability present within Atlas Copco. According to Yin (2009), the role of documents in case studies is to confirm and enhance the evidence from other sources. Further,

such internal documents and public documents such as the latest annual report were used by the writers of this report to learn more about the context of the case company.

### **3.4 Data analysis**

All interviews were transcribed and then summarized according to the interview guide. A preferred strategy to analyzing case study data is to follow a theoretical orientation (Yin, 2009). Since the interview guide was derived from the theoretical framework, the guide has also functioned as a link between the empirical data and the theoretical framework when assembling the empirical results. After summarizing the main points from all interviews using the topics in the interview guide, the empirical results were written in order to present an as fair as possible view of the story of Atlas Copco. Thereafter, the analytical model presented in section 2.2 was applied to the empirical results and used to deduce the conclusions presented in chapter 6.

### **3.5 The quality of the study**

Golafshani (2003) suggest that the quality of qualitative research should be judge on measures such as the research's credibility, consistency, neutrality, transferability. Credibility depends on the research instrument. In qualitative research however, the research is considered to be the research instrument and the credibility of the research thus depends on the researcher's ability and effort (Golafshani, 2003). A detailed description of how the data were collected and how findings were derived using the analytical model during the study is presented in this report in an effort to facilitate a replication of the study and to ease the reader's' ability to assess its reliability, which aids to the consistency of the report (Merriam, 1995). Merriam states the real question for reliability in qualitative research is about the consistency between the results and the data, meaning that the findings should reflect the data collected to the best of the researcher's ability.

In qualitative research the validity is subjective rather than objective, and it is the plausibility of the conclusion that counts (Ahrens and Chapman, 2006). Merriam (1995) has the same view that validity is to ensure that the interpretation of reality is presented as true to the phenomena as possible, i.e. it should be neutral. Ahrens and Chapman (2006) states that the common threats to the plausibility are observer caused effects, observer bias, data access limitations and complexities. To gain validity, Merriam (1995) suggest that a multiple of data sources are used to ensure the authenticity of a phenomenon, and that the interpretations are taken back to the participants for verification. In regards to accountability, multiple sources are hard to get to confirm the phenomena as it is an individual's perception of his/hers reality. Data access limitations and complexities are therefore present but accounted for by doing in-depth interviews with observed caused effects being limited.

### **3.6 Generalizability**

This report has chosen to follow one of the approaches described by Merriam (1995), which implies that generalizability is determined by the users of the research and not by the researchers themselves. Therefore, a thick description of the study's methodology and method is presented, in order for the user to be able to determine if the findings are transferrable to their own situation (Merriam, 1995).

## 4 Empirical results

*This section will tell the story of Atlas Copco, based on interviews with the company's employees. A short presentation of the history and present features of the transfer pricing system is given, focusing on the actions and feelings that come as a result of the transfer pricing system.*

### 4.1 Background on the transfer pricing system

The transfer pricing system in Atlas Copco started around 1987-1988. Before that point no sales staff wanted to sell hand held tools since compressor machines were both easier to sell and more profitable. The management board of the company had earlier been discussing whether or not to divest these hand held tools since they were not considered to be contributing with enough value. However, a decision was made to break them out from the rest and make it into one separate unit that would only focus on selling its products. When corporate management noticed their mentality of living and dying with their local product, market, and customer, the opinion shifted towards instead realizing the value of their business model. This was the start of the divisionalization of Atlas Copco which is still present today, enabling a focus on developing and producing specific products. The first step was to move central functions to the operating divisions. A customer center, which is the company's name for a sales company, was created for each of the business areas and left on the corporate level were functions such as group accounting, legal, IT and the group's CEO and CFO which is still the structure today. There were several discussion regarding which models to use for this new structure and the CFO at the time stated: *"There should be no free services, all employees need to charge their time in some way"* (Business Controller Business Area, BCBA).

The basic idea with the divisionalized structure was to have a divisional president with full responsibility, feeling that it is their duty to make sure their division has a sufficient turnover. *"In the beginning it was not all clear and of course scary at times but the picture communicated by the CEO and CFO at the time was very clear; there should be no such things as central costs, everything is to be charged operationally"* (BCBA). The idea was to initiate a form of trading activity so that units within the company could decide whether to buy in house or use an external provider. *"There are no free lunches"* became the organizational wide accepted motto with a strong initial focus on removing all central costs. *"Make sure you charge all your expenses on the operating units, and the central functions that still remain - charge them too!"* (BCBA).

Nowadays things have become smoother internally regarding the charge of overhead costs, neither group legal nor group accounting charge their costs onto the operating units anymore. The company realized that it did not lead to any real advantages since it created both extra work and stress to keep track of who to charge and the correct number of hours spent on different projects. *"The central issue is always to try to find the balance between decentralization and what is most effective for the group as a total"* (Accounting Corporate Function, ACF).

The organization has internal service providers, for those services not directly connected to Atlas Copco core business. They often belong to a business area with the aim of creating synergies within their field (such as IT, HR and purchasing). Their purpose is to supply services and charge the costs to the units consuming them. It is considered more efficient to have a service provider due to efficiency gains, since if these services were produced by each individual unit it is believed to result in more inefficiency, vulnerability and a greater dispersion of knowledge. Regarding IT services, it is mandatory to purchase some of the services due to keeping a certain technical infrastructure throughout the company.



When using these internal service providers an invoice will be sent with the charge of the service. An issue in this is that the internal charges are not so specific since you assume that the recipient is aware of what has been requested. This causes problems when trying to understand what you are actually charged for and sometimes more effort is put into questioning these types of invoices than towards external suppliers. For example, an internal invoice might say IT-services and the amount. *“Then you start reasoning about what exactly is this? Is this price really correct? This leads many managers to debate and question these invoices in a more extensive way than with their external supplier invoices.”* (BCBA). As mentioned, the aim of having internal service providers is for them to supply services of higher quality and at a lower cost so that the units can focus on their core business. Since units still debate and question invoices, both due to intransparency and the charged price, this prospective efficiency gain has not been entirely successful.

#### **4.1.1 Tax’ role in the transfer pricing system**

*“Transfer pricing is the biggest and most continuous issue for the group tax at Atlas Copco”* (Tax Corporate Function, TCF).

The tax department’s responsibility is to set up policies to be followed by the rest of the group which means interpreting the OECD guidelines regarding transfer pricing. It is the responsibility of each division to make sure that the policy is complied with in the product companies and customer centers. This means charging a correct transfer price for the transactions between different legal units. *“Atlas Copco has about 50 product companies in the world which produce the machines and supply them to the customer centers who in turn sell them to external customers. The transaction between the product company and the customer center has to follow the transfer pricing rules, as the transfer price is only a tax issue. The transaction from the customer center to the external customer is not dependent on any transfer pricing rules, then it is all about making a profit”* (TCF). When the internal service provider supplies services to other legal units, they have to charge the unit a fee since having it for free would be an incorrect pricing according to the transfer pricing rules. The Business Controller Division 2 (BCD2) states that it is not always necessary to send invoices between the units but legal tax aspects often require them to do so.

For tax compliance reasons it is important where the profit is located and the tax rules thus create additional work which do not create any value for the division since measures are made on a consolidated level. From a group perspective however, it is necessary since *“It is not possible to disregard tax, then the tax authority will come after you, everywhere”* (TCF). Not all members in the customer centers understand that tax compliance means that profit levels need to be managed, and that traditional profit maximization is not the objective. Ten years ago profit maximization was the target, and it appears to be a habitual behavior which takes time to change. The customer centers’ profit is only a matter of tax compliance; they should stay within a given profit margin interval in order to comply to the transfer pricing rules. *“It does not matter how well they work because they are only allowed to make a certain profit. It is only the consolidated profit, which is an operative issue, that matters but not everyone understands that”* (TCO). The consolidated profit of the division is confidential, meaning that the customer centers do not have a full insight to the measures which they are evaluated and rewarded on. Since people cannot see what they are measured on, they instead strive to improve what they can see, i.e. their local profit.

## 4.2 Internal transactions today

The main reason for doing internal transactions today is so that the right cost can be allocated to the correct part of the process, to match income and cost, and to create synergies for the organization as a whole. The BCD2 states that the aim is to demonstrate the true profitability for each unit, market, or transaction between divisions in order to enable more informed decision-making, especially when investment proposals are present. In order to do this each unit must take responsibility for their costs to enable a fair representation. All managers are accountable for their performance which consists of two parts. One that they can directly affect consisting of what they choose to purchase from the other units, and one they can indirectly affect such as cost for property by using less square meters. To get at fair view of the units, and a correct value in the accounting, the price for the internal transactions is cost based with actual cost for products and standard cost for labor. *“Cost-based prices give a correct value of the inventory and diminishes the risk of discussions about going to the competitor to buy the products since you cannot get something to a lower price than the actual production cost in house”* (Finance Manager Legal Organization, FMLO).

The principles for the allocation of the internal transactions are established in a yearly plan based on consumption or allocation keys such as revenue, employees or utilized area with a yearly revision which usually works in a smooth way even though the allocation keys sometimes get questioned. The BCBA wonders why they need to do this and states that they are continuing with it due to old habit. The Business Controller Division 1 (BCD1) agrees in questioning the system’s validity but sometimes it can make sense to allocate the cost to where it originates. The system is somewhat successful in the aim of showing the true profitability for the units or markets. *“In some cases I can still feel that we have accomplished what we set out to do with increasing the awareness that everything has a cost when the local units can see how their profitability changes”* (BCD2). The system helps the company to focus on a correct cost allocation, but since it appears to be an everyday organizational practice not much emphasis is placed on the actual effects that the system might bring with it.

## 4.3 Taking responsibility

The units in Atlas Copco often co-operate which creates a scenario in which one unit’s result is dependent on another unit’s efficiency since these internal transactions are based on actual cost. The BCD1 state that the ambition is for all units to see the big picture and value belonging to the same company which is something that is continuously enforced throughout the organization. *“But if you are the manager of a local customer center you of course wish to improve those measures on which the variable compensation is based”* (BCD1) which are then partly dependent on the efficiency of other units. The BCBA however states that *“you are always dependent on other people, subcontractors etc. and you cannot put all the blame on them because then you are not in the clear about what your responsibility is”*.

*“People take more responsibility for their cost when they are measured on it. The thought is to make everyone more aware of resource utilization and to not consume more resources than they actually need. In that sense you can control behavior”* (BCBA). Upper management’s objective is thereby to control behavior in terms of these aspects which seems to be accomplished by this system. This control may in addition however bring with it other aspects than just reducing waste and overconsumption. No manager wants to take responsibility for someone else’s costs making them use invoices to charge the other units they consider the cost belonging to. According to the

BCBA, there are frequent discussions in line with: *“This isn’t part of my plan, how did this come up? Who decided on this?”* The BCBA testifies about a frustration regarding the internal charges but also mentions that they are important: *“I’m not sure if all of them are value adding, but if it’s free then people will take advantage of it”*. A solution employed by members is then to pass the costs further along according to the BCBA: *“When you are feeling pressured and need to cut costs you will try to find someone else to charge for this invoice”*.

#### **4.3.1 Managers’ ability to affect costs**

Managers care about the results they are responsible for but feel that the system is somewhat unfair and are at times frustrated that they cannot affect their results. *“Many of the overhead costs are just allocated according to certain keys. One can discuss for years about which key is the best but in the end one just have to accept the costs given to you. You don’t have a say in the matter if you feel it is too expensive. You need to bring that up with your management team and let them solve it”* (FMLO). The BCD2 is however concerned about the effect this might have on the managers with a financial responsibility: *“If you feel like you cannot control your cost, you just shrug your shoulders. The worst case scenario is if that kind of attitude spreads to other cost which you actually can affect”*. The system has thereby brought forward important aspects for the group in terms of taking responsibility for one's costs but since members at large don’t feel that they can control and effect these costs unwanted behavior might arise in the organization.

The BCD2 sometimes wonder what the objective of the system really is: *“If managers in general feel like it is just costs that they cannot affect, that are simply allocated by keys which they don’t have a say in, then it’s not optimal. It depends on what we want for this organization; do we just want to allocate cost or do we wish to direct behavior? In many cases the units hold the belief that they cannot influence anything so it has no effect on how they act. Overall my opinion is that you should be able to influence the costs you are charged.”* From the perspective of the customer centers the response is often resignation with the feeling that there is no use in trying since nothing will change anyhow. This has however opened up for other discussions. *“Our customers feel like they have no influence or say in the matter so instead they are pushing for having their own local staff which they can directly influence. This makes me feel resignation regarding the structure and the prices as they are now. I would much rather charge the business area directly since they are the ones setting the structure and leave it up to them if they wish to further allocate or absorb the cost”* (Communication Internal Service Provider, CISP). Since members feel resignation regarding their control and what they can affect it here becomes apparent that this dissatisfaction demonstrates itself in terms of actions from the customers to regain some of the control.

#### **4.3.2 Accounting as means of giving account**

The BCD2 states that the general level of understanding is scattered in the organization. *“It’s very mixed, sometimes you almost want to take out your own wallet and explain with actual banknotes what is going on. But one also has to remember that for 90% of organizational members, finance and accounting is not their main field of interest, so even if we try to educate them they probably won’t remember much a couple of months later”* (BCD2). The Business Controller Product Company 1 (BCPC1) states that *“most members of the organization understand somewhat but not how these costs are calculated and how they can affect them. Some managers are of course exemplary and understand it very well”*.

The company does not have any documentation at the moment showing how the system is constructed. The BCPC1 explains that internal education in accounting for managers has been an important process during the past four years, increasing their level of understanding greatly as opposed to prior the initiative. Their ambition has been to simplify accounting to make it transparent and understandable for members without a financial education. In this educational package internal transactions are included in order to increase the understanding regarding which basis they are charged or allocated upon such as internal rent charges, cost for computers and depreciation. The aim is for members to understand that these are not just cost thrown at them but actually costs they can affect. *“You need to educate in this matter since it’s very hard to see what lies behind the internal transactions in the accounting statements. They can see the receipts but not which allocation key that has been used or where this charge stems from”* (BCD2). Atlas Copco thereby tries to remedy the problematics of managers not feeling like they can affect the costs they are charged but since organizational members still testify about the systems intransparency this initiative does not seem to have been completely successful.

#### **4.4 Cost of internal transactions**

To some degree, the transfer pricing system leads to sub-optimization, a feeling of *“we and them”* (BCSC). Another issue created by the internal transactions is a misdirected focus. When a unit manager stops purchasing an internal resource, the cost for that resource still remains within the company at large, just at a different unit. No one bothers about lowering the actual cost, instead the focus lies on being allocated the smallest share possible of the joint costs. According to the BCSC, *“there is not much thought given to the system, it is a part of the organizational structure that has given the organization its success”*. This demonstrates how the system is effective in its overall aim but leads to unwanted effects such as sub-optimization which to some extent seems to be acknowledged by upper management. The BCBA questions the cost of the administrative work while the BCSC states there is not much thought given to the system and the organizational structure. This demonstrates how upper management seems to be focused on costs which lower level managers do not seem to question in its organizational form, but it also demonstrates their dissatisfaction with the system taking other expressions such as trying to minimize their allocation of joint costs.

The BCPC1 sees it as a tradeoff, one must weigh the benefits of cost awareness, responsibility, transparency, and not over-consuming resources against the internal bureaucracy it creates. The bureaucracy is a downside of the large organization of Atlas Copco and decisions made on corporate level that are beneficial for the group might not always be beneficial for the local unit. Regarding the internal services, CISP wish they could be more standardized since they would have much to gain in terms of efficiency, especially regarding financial services and IT. However, it is the flexibility and diversity of the group that made its success. The counter arguments from the customer centers regarding more standardized services is that finance and IT are too closely related to sales, which must be adjusted to the specific market or unit. *“The customer centers often argue that their local contexts require specific handling but that is rarely the case”* (CISP). This shows how local units sometimes have a hard time understanding what’s best for the group and instead focuses on how they directly will be affected. Since it is mandatory for them to purchase certain IT-services their response in terms of dissatisfaction displays itself in wanting customized solutions which is a view not shared by the service provider.

## 4.5 Evaluation

When evaluating performance, a number of financial KPIs are primarily used. The group also measures soft values but according to the BCBA these are neither as strong nor as grippable as the financial: *“The financial KPIs are considered more legitimate, shareholders will always want their dividend. The financial part is where emphasis lies when controlling the organization, it’s what is discussed, measured and subsequently rewarded on”* (BCBA).

The BCD2 states that they conduct both customer review meetings (CRM) and business review meetings (BRM) a couple of times each year. The BRM focuses on the business side and are conducted with each division and most of the customer centers with a thorough review of the market share, customer mix and how competitors act. The CRM instead focuses on the company as a whole regarding processes, financing, balance sheet reviews and more.

The BCD2 explained that most general managers in the customer centers have a variable compensation forming up to 20% of their annual salary. For 2016 some of the parameters included are market contribution, market efficiency, and 4% consists of individual targets depending what the group management wants to emphasize. Such individual targets can include increased customer satisfaction, increased margin on a specific product or the successful implementation of a new purchasing system. The group thereby seems to have the opinion that it is what is rewarded financially that gets prioritized. Although this might be true in many cases, some of the lower level employees affected by this reward system do not agree that it’s the best way to go. *“For some people it works fine, others consider it to be a lottery”* (BCSC).

When evaluating units, corporate headquarters claims to take into account local factors affecting results giving companies the possibility to explain and justify their performance. *“The president of each unit is responsible for following the set plan, if you follow your plan and still don’t reach your intended result you have to explain yourself. It’s very important to have a clear and open communication when circumstances prevent you from staying on track and I feel that our internal communication in these cases is sufficient”* (BCBA). The monitoring and follow-up within the business area is quite strong with a general understanding of external influences and a monthly meeting where these issues are discussed. *“If a unit is experiencing problems you of course have to take some sort of action to tighten up. This is usually when members start dividing their fixed costs in a less productive way but for them it’s important since they are measured on their costs”* (BCBA). Atlas Copco thereby tries to remedy the sub-optimization that could occur and take local conditions into account but it has not had an effect in a complete sense since members respond with a less effective dividing of cost to satisfy the hierarchical accountability pressures.

## 4.6 Internal service providers

One of the internal service providers have strict efficiency demands that today amounts to 4 percent yearly meaning it either have to lower its prices or absorb more costs. This complies with the efficiency pressures put on the service provider by the customers. When asked why they “sell” the service instead of just performing it the CISP states that they wanted to show initially that they were effective and setting a price was good for demonstrating this. Some local units however had a hard time accepting this in the beginning since they focused more on their direct costs increasing than the knowledge base and back-up that came along with purchasing the service from a large provider. The handling of the cost of the services provided by these units can be done in two ways according to the CISP, either you price them and charge the units consuming or you simply allocate

the cost evenly. *“The main advantage of pricing the services are that it encourages improvements, if you increase your efficiency it will be demonstrated in your prices. If we would simply allocate the costs evenly, no one would take responsibility for them”* (CISP). The service provider shares the group management's view that costs make members more prone towards taking responsibility but also demonstrates how it makes members cost-focused and hindered in seeing the overall benefits they could receive from a large internal provider making it necessary for them to show their effectiveness.

Earlier the prices were negotiated between the local units and the internal service provider. *“I had to sit down with each general manager and negotiate with them which was very time consuming and tough, but a decision was after some time taken that it was not plausible to negotiate anymore due to time constraints”* (CISP). It was decided that the prices are to be set by the service provider's board with representatives from each business area present. Once they have settled on which prices to use the local general managers cannot question or try to negotiate this directly with the service provider, instead the discussion needs to go through their respective business area. *“This eliminated much of the previous discussions but it did not mean they were satisfied and happy about it, many still feel that our prices are too high”* (CISP). The BCD2 agrees in that people are not satisfied with the service providers prices: *“Even if the service is in itself great, people feel it is too expensive which makes them think that it is no good after all”*. When the customers are dissatisfied, they need to bring their opinions to a higher level – *“and wait for nothing to happen”* (BCSC). This awareness of not being able to affect the prices due to a slow bureaucracy has resulted in there still being price discussions between the service provider and their customers, the very thing the change aimed at removing. *“I still spend a great deal of time discussing prices with clients even though we are not supposed to do that anymore”* (CISP). This can be seen as the customers' way of expressing their dissatisfaction over the internal service provider and the prices.

#### **4.6.1 The relationship between the service providers and their customers**

A customer-supplier relationship opens up for the ability to place demands in terms of quality and service level. *“If there is no customer-supplier relationship and instead just a colleague sitting next to you, it is not as likely that you would be open with your dissatisfaction”* (Manager Internal Service Provider, MISP). By having customer meetings, it is possible for the service provider to ask the customers what they can do to improve in order to make the customer more satisfied with their service. The internal service provider emphasizes their customer satisfaction measurement. More demands can increase quality, but it is dependent on how it is measured. The internal service provider prefers to include more services or increase the quality instead of lowering the prices, nevertheless such “additional” services must be demanded according to the BCD2. If there is no demand, then there is no point in creating those services. The services must contain some kind of value for the customers, and the deal needs at least to break even between the cost of doing it yourself or buying the service from the internal service provider since it otherwise demonstrates an inefficient organization. It might be better to work on efficiency but one of the internal service providers does not seem to share this view according to the BCD2. They have performed several operational investments but the efficiency has not improved as the prices stay the same along with charging the units the cost for the investments itself creating dissatisfaction among customers.

The internal service providers' belief is that customers often seem to want more but more services means a higher cost which is subsequently charged to the buying units. When the unit manager discovers that their cost from the internal service provider has increased they often go back claiming that the service provider need to stop with the new, additional services because the

increase in cost is too high. *“This is exactly what the system wants to accomplish, the managers are resource aware”* (BCBA). If the services were free of charge, the costs for the internal service provider would probably be much higher, which would be negative for the group’s financial performance. The system’s overall aim with cost awareness is thereby achieved but it does not necessarily come with all positive aspects for the continuing operations for the group since the service provider's aim is to enable the units to focus on their core business.

No division or unit is forced to purchase financial services from the internal service providers, but the option is instead to do it yourself or use an external provider. The alternative of performing the financial reporting yourself often results in non-standardized process, making the consolidation for the group more time consuming. The BCD2 states that is theoretically possible to do things yourself, but strongly questions if it is possible in practice due to both the costs of finding a new supplier or performing the service yourself and the difficulty in integrating it smoothly with the rest of the group. The MISP confirms that units in some cases have the possibility of using other external suppliers but also states that it is very difficult for an individual unit to change supplier in practice. For the customers this means that they in theory have a choice regarding the sourcing of services, but are in practice often only left with the option of using the internal service provider. The service provider does not see themselves as an authority and cannot control other units, they can only give their recommendation. This demonstrates the different views parties have on their relationship.

There is a pressure from the customers on the service providers to be efficient, have high quality and low prices. However, both the CISP and the MISP see it as a positive pressure. At annual meetings, the customers want to know what they have done to improve their efficiency to lower the cost of their services. As the customer centers and product companies are under pressure to cut costs themselves, they often turn to the internal service provider asking what they can do to help. *“The general manager comes to me and says: We need to lower our cost by 4 %, you are a large part of our cost, what are you doing to help us with this?”* (CISP). If the internal service provider can show that they have lowered the unit prices, the general manager is often satisfied. Since unit prices are used it may encourage general managers to consume fewer services. IT costs are per person, meaning downsizing staff will reduce the IT service cost. It is more difficult to reduce consumption of financial services since reports must be written and invoices handled, even if times are hard or if you reduce staff. This shows how managers are cost aware and how they are using their relationship with the service provider in a more hierarchical way. It also demonstrates the circumstances in which managers have no control but at rather forced to take on costs. Cost awareness is thereby highly visible in the organization but might lead managers to make decisions favoring a reduction of costs in the short run to reach targets that could have a negative impact on long-term operations.

There is a limited amount of people involved in setting the agreement of what should be included in the service supplied by the internal provider. Those not involved, meaning most of the employees in the division, are often not enlightened on what agreement has been reached. *“This is definitely a challenge for us as a service provider, how do we get everyone to understand what they have purchased? They don’t necessarily have to think it’s appropriate but they at least need to understand the set agreement”* (MISP). Frequent comments on the matter involve what the customers feel are missing from the service. *“In that case the shortage comes from the divisional managers signing the agreement without knowing what the divisional members are actually requesting. The service provider delivers with the aim of fulfilling the existing agreement, if*

*something is lacking from that agreement the responsibility does not lie with us” (MISP). The service providers’ stance is that it is their job to communicate the specifics of the services provided since their customers do not take responsibility for handling this internally to their divisional members. “It’s part of our job to make sure everyone understands what they can expect from us since as long as something is unclear you always expect more” (MISP). This shows another situation in which the customers are acting in a hierarchical manner, demanding as much as possible. This might originate from the previous social relationship between the customers and the service provider, in terms of having different expectations on internal suppliers as opposed to using an external provider.*



## 5 Analysis

*In this chapter the analytical model presented in the theoretical framework is used to discuss how the accountability pressures are present in Atlas Copco and what can be seen to be the outcome of these pressures.*

### 5.1 Accounting information as a basis for accountability

In accordance with Roberts and Scapens (1985) the accounting information created by the transfer pricing system becomes more important when there is no face-to-face interaction, which is often the case for the internal service providers but also between producing units and customer centers. The downside to this according to Roberts and Scapens (1985) is that subordinates can only rely on their results being the main source of the judgment of their managerial performance and competence, and not that the evaluators will take into account their local context and the specifics that shaped them. An example of this can be demonstrated by the use of cost based transfer prices in Atlas Copco and its impact on motivation. In order to be compliant to the tax rules regarding transfer pricing, units should strive to reach a predetermined profit level set by the transfer pricing rules. This logic is not fully understood by all members of the organization as it somewhat goes against “*common business logic*” in which profit maximization is the ultimate goal. This has a negative impact on divisional managers’ motivation and entrepreneurial spirit according to Cools and Slagmulder (2009). In the company, some counter actions have been taken to avoid this. The divisions regularly perform Customer Review Meetings (CRM) and Business Review Meetings (BRM) with their units in order to understand the specific local context and the various affecting factors which could explain why this is not considered a problem.

Regarding the internal service provider, they are being judged by their customers based on the price of the service since it is the service provider’s way of demonstrating efficiency. In Atlas Copco there appears to be a habit of exploiting the system of internal transactions when managers further charge costs to other units, thus avoiding taking responsibility for them.

### 5.2 The accountability process

As Kreiner (1996) states, it is the process of accountability itself that creates the action and identifies the actors and evaluators. Kreiner also believes that the process of accountability is to make individuals mutually accountable and can be seen as both authority and actor simultaneously. The transfer pricing system has created a situation of multiple relationships for all units in which they are both authority and actors at the same time. This further makes it difficult to determine who should be accountable for the financial results. Roberts and Scapens (1985) believe this difficulty to stem from the complexity of interdependent actions and since accountability pressures aren’t static but evolve in relation to the actors involved (Carnaghan et al., 1996) it further brings complexity to the issue which has been observed in the organization.

By looking at the accounting system as support to the relationship between institutional principles and the local context as Kirk and Mouritsen (1996) state, the internal transactions within Atlas Copco facilitate control and comparison of subsidiaries. However, Kirk and Mouritsen (1996) also state that accounting needs accountability in order for it to become important. By measuring units on their profit and holding the managers responsible for it, Atlas Copco have emphasized more accountability in the accounting system. Another thing that Kirk and Mouritsen emphasize are the expectations that an accounting system brings with it. The subsidiaries will have expectations on the actions from the management team based on the accounting information presented by the

accounting system. One of the concerns raised in Atlas Copco is that subsidiaries will have the expectation and feeling that the management team will behave and take actions no matter what kind of information the accounting system delivers. If managers feel resignation over their control of costs it is likely that it will affect their behavior in a negative way which can be seen through the unwanted side-effects organizational members display.

### **5.3 Accountability's role in shaping the organizational reality**

Lilley (1996) argues that the search for control eliminates the possibility for actual control. When trying to control, you can only control the control in itself and not the actual actions of the users. In Atlas Copco the system appears to foster sub-optimization, a feeling of we and them along with a misdirected focus in terms of costs. This demonstrates how the system has back-fired in some sense and that the actions taken in trying to control the behavior of members has not resulted in solely positive outcomes supporting Lilley's notion of only controlling the control. By holding both unit managers and lower level managers responsible for the costs Atlas Copco has affected the behavior by creating a greater consideration of consumption and reducing waste. However, there has also been some negative side effects to this, namely a misdirected focus. When examining the matter more closely it becomes apparent that negative effects of opportunism and sub-optimization by local managers to some extent appear. Since financial results are emphasized throughout the organization, and subsequently rewarded on, it leads managers to optimize the result of their units by lowering their costs. This can be done either by questioning the prices charged by the internal service provider, argue about the allocation keys for joint costs or trying to charge another unit with costs they believe belongs to them in accordance with the transfer pricing system. In short, the evaluations have led to a great awareness of costs but not necessarily a greater responsibility for those costs. It is also in line with Roberts and Scapens' (1985) thoughts about confusing the reflection of accounting information with organizational reality. Even though Atlas Copco has tried to remedy this in several ways it might be hard to do in a complete sense. The way the system is formed also creates distrust which legitimates the need to further control in line with Roberts' (1991) notions that distrust is not a display of human nature but rather a display of the accountability pressures that are present.

The organizational structure is not given much thought to by members of lower positions claiming that they accept it as the foundation for the company's overall success. This appears to be in line with Kirk and Mouritsen (1996) thoughts about allowing accounting to form a regime of truth, and a display of the institutionalization of transfer pricing that has occurred (Burns and Scapens, 2000). In Atlas Copco there is an understanding of the importance of correct cost allocation and having well-functioning relationships between the units. Roberts and Scapens (1985) however raise a word of caution when confusing the organizational reality with the picture presented in the accounting information, as it is selective and subjective. This phenomenon could be seen in one of the internal service providers who had the image of a high customer satisfaction rate in accordance to their measurements. As long as their customer satisfaction is above target, attention does not seem to be given to other measures of their service. A similar situation was described by Cäker (2007), when one of the units in his study prioritized the non-financial measures over the financial ones and that when the opinion of what the customers wants is picked up it can serve as a strong guidance for behavior that is hard to redirect through the management accounting system. In Atlas Copco internal service providers appear to be captured with delivering what they consider the customer truly requesting and needing, which serve as guidance for their behavior. It does however not appear to be in line with what the customers are truly requesting in terms of cost reduction and efficiency creating an unbalance.

The accounting system inserts the subunit into the context of the organization as a whole thereby using criterion from the inside as opposed to the units own local characteristics according to Kirk and Mouritsen (1996). In Atlas Copco consideration is taken in terms of the units' local contexts and current economic situations which are obtained through the CRM and BRM meetings held with representatives. It thereby appears that local characteristics are attempted to be accounted for. The CISP states that their customers' counter arguments towards more standardized services within finance and IT is that their local context require special handling, the internal service provider however argues that that is rarely the case. The units want their local context to be taken into consideration when performing the service in order for it to suit them seamlessly but the service provider's aggregated view instead sees the units' similarities. The desire for a specialized seamless adaptation of internal services might be the result of the set structure with the removal of price negotiations a while back. Since the units are no longer allowed to discuss pricing with the service provider directly, or in some cases their choice to purchase the service at all, they instead try to argue with what they believe they still can affect namely how the service is to be performed making their discontent with the system as it is today appearing in other ways. This displays how the transfer pricing system has moved focus away from the price of the services toward instead focusing on quality.

#### **5.4 Hierarchical accountability pressures**

Roberts (1991) sees acceptance and recognition as important to individuals since the desire for recognition makes us adhere to expectations set by others and we are therefore accepted for our ability to fit in with the required image. The self is thereby drawn towards meeting the demands of routine accountability in order to be successful. In Atlas Copco there are various KPIs and targets set up for members in order to control the organization with a linked variable compensation to motivate an intended behavior from its managers. The most important aspect according to the BCBA is however complying with the financial KPIs since they are considered the most legitimate and thereby the most important for seeming successful in the eyes of others members. This is in line with Roberts (1991) view on accounting information creating individualizing effects i.e. individuals identify themselves with results, and have an instrumental relationship with others. The units within the case company are forced to purchase certain services, such as IT, and with the current transfer pricing structure these mandatory IT-services enforces the customers to view the relationship with the internal service provider in a hierarchical manner.

#### **5.5 Social accountability pressures**

Roberts (2001) states that recognition can come from socializing processes of accountability based on conversations and sense-making between individuals of equal power. The reason for which Atlas Copco's internal service provider sell the service instead of just performing it was initially to show that they were effective and prices were considered a good way for demonstrating this. They needed to justify their existence to customers and demonstrate their processes, efficiency and the correlating prices charged. The problem with this is however the non-equal power aspect which is demonstrated in the relationship between the service provider and their customers. When choosing to price the services an internal market was created enabling more formal relationships between the members. The internal service provider however still promotes having a social relationship with the buying units since there is a strong focus on measuring customer satisfaction. Customers are on the other hand are overtaken by hierarchical demands due to the strong focus on financial targets, costs and the shape of the reward system. This has similarities to the situation

described by Cäker (2007) where the lateral accountability was not included in the formal accounting system making the lateral and hierarchical accountability unbalanced. In Atlas Copco, the service provider have a better match between social and hierarchical pressures, and the lateral accountability can therefore be argued to be included in the service providers' formal accounting systems. This is not the case for the customers. Another explanation to why hierarchical accountability is favored by the customers relates to the decreasing of social accountability when the communication between the service provider and their customers decreased (Jönsson, 1996). When price negotiations were lifted to a higher level in the organization as opposed to between customers and the service provider directly, it decreased the socializing processes described by Roberts (2001) which includes recognition through informal talks as well as sense making between people of equal power.

## **5.6 Conflicting demands of accountability**

The conflict present in Atlas Copco comes from units viewing their relationships in different ways and thus responding to accountability demands differently, rather than a direct conflict between the social, informal commitments and the hierarchical, formal responsibilities as described by Roberts (1991). When price negotiations ceased between the units and the service provider directly, it caused a shift in the accountability relationship making customers view it in a more hierarchical way. This shift in accountability causes problems since members are not certain about which relationship they are to have with each other, the appropriate correlating behavior that comes with it as well as how accounts should be given and demanded.

The internal transactions in Atlas Copco can be seen as creating social commitments between parties of equal power, the divisions are specialized in different activities and can support each other to maximize the output. The transfer pricing system also creates a formal responsibility which in turn makes the relationship between units more instrumental. In Atlas Copco a situation was described by the CISP about how local units had difficulties accepting the need to purchase something from a central service provider since their main focus was to maintain low costs. This point to units not knowing how to act in their relationship, much like the situation in Cäker's (2007) study when the two units did not know if they should treat each other like customer/supplier or as part of the same organization. The customers in Atlas Copco do not see much value in the additional knowledge a central service provider can supply. Many units still today complain about the price level at the service providers, meaning that the hierarchical pressures trump the social seen from the customer center and product companies' perspective. From the internal service providers perspective, the focus seem to be the opposite since they recognize their interdependence with the customers and focus on their customer satisfaction and value the communication between them. A possible explanation for this mixed view on the relationship is found in Munro and Hatherly (1993). They discuss how control technologies which contribute to social accountability and lateral flows of information, which the transfer pricing system to some extent does, might be subverted into the opposite and instead reinforce the hierarchical accountability. The main reason for such a transition is the strong hierarchical accountability pressures which are present for the buying units in Atlas Copco. Since the internal service provider and the buying units are evaluated differently by central management, the transfer pricing systems has different effect on their view of accountability. For the service provider, the hierarchical evaluation matches the social pressure to a much higher extent than what it does for the buying units. Therefore, the internal transactions create social accountability for the internal service provider, but instead reinforce the hierarchical accountability pressures for the buying units due to the strong financial focus by their superiors.

This hierarchical accountability has brought with it individualizing effects as explained by Roberts (2001).

Helden et al. (2001) observed that multiple performance measures are helpful in coordinating units but they saw that not all control measures complied with each other. When measures are conflicting it is up to the managers to resolve the conflict or prioritize between the different demands. Due to the individualizing effects (Roberts, 2001) that the internal transactions create for the customer centers and product companies there is a possibility that they will prioritize their own unit over the group. According to Messner (2009) the individual might however be limited in giving account due to several reasons. The different view on the relationships makes the service provider and the buying units limited in different ways. The service provider is limited in accordance with the exposed self due the hierarchical demands the customers place on them which they are forced to account for but cannot in the hierarchical way the customers are demanding due to their social view of the relationship. The buying units on the other hand are limited in accordance with the opaque self since implicit knowledge and practical consciousness and cannot be fully accounted for. For the company this means that the way the system is shaped, and the un-wanted side effects that unit managers present as a result, is an outcome from the organizational reality the operate in which they might not be able to fully account for.

## 6 Conclusion

*Presented below are the results of the study, suggestions for future research, the study's implications for research and practice as well as final reflections from the researchers.*

This paper set out to examine how the transfer pricing system within a company, Atlas Copco, affected the various accountability pressures within the organization. After conducting interviews with employees on various organizational levels, a display of a conflict between the hierarchical and social accountability pressures emerged. This conflict was not as much a direct conflict as described by Roberts (1991), but rather a conflict of different views on the accountability relationship between units within the firm. After changing the features of the transfer pricing system, a relationship previously defined by social accountability transformed into a hierarchical relationship for one unit, while the other still see the relationship in terms of social accountability. The reason that the view only changed for one of the two units is due to different accountability pressures present. It can further be explained by Munro and Hatherly (1993) who state that adding a new sort of accountability might instead only reinforce the existing accountability which can be hard to turn. A change in the transfer pricing system has thus lead to an uncertainty about how to view the relationship between units, something that Cäker (2007) also found in his study. Further, this conflict of accountability demands is troublesome for the individuals in the organization and affects their ability to give account. The study also found that the object of discussion has changed in the accountability relationships. The current shape of the transfer pricing system prohibits customers from discussing price directly with the service provider which instead makes them focus on the quality of the service. This shows how the object of accountability has changed and how members are finding new ways to rebalance the accountability relationships. This might have implications for both research and practice in terms of how members will strive to rebalance accountability and the current shape of the management control systems present in the respective organization will affect how this can be done.

The conflict of accountability demands has affected what the analytical model call the organizational reality. Several aspects related to the transfer pricing system points to sub-optimization. As the producing and selling units are experiencing a hierarchical accountability pressure, the transfer pricing system is creating individualizing effects (Roberts, 1991) and instrumental relationships. Since organizational members adhere to the hierarchical accountability pressures they are experiencing, in terms of meeting financial targets in order to qualify for their variable compensation, the organization risks local units sub-optimizing their short term result as opposed to favoring long term organizational success. The internal service units are however experiencing socializing effects which cause a clash between the two, as described above.

This study demonstrated from a system perspective that transfer pricing can reinforce both social and hierarchical accountability demands and which demand it will strengthen is dependent on the rest of the management accounting system. In this particular study the performance measurement in the organization had a strong impact on the accountability pressures, and the transfer pricing system reinforced the pressures present. This opens up for the possibility of studying which part(s) of a management accounting system that determines and controls the accountability pressures and which part(s) that has a more secondary role in supporting those pressures. Such notions could help to clarify which management accounting practices that should be in focus when wanting to change the existing accountability pressures. This study also found evidence supporting the notion that transfer pricing can be an institutionalized management accounting practice as discussed by

Burns and Scapens (2000) which could have implications for future research regarding change of transfer pricing practices.

## **6.1 Researcher's final reflections**

As a final comment by the researchers a reflection regarding the internal service providers will be put forward. In the organization of the case company these service providers have the aim to be competitive in terms of price and quality in the sense that customers are supposed to want to use them based on the superior result they can deliver as opposed to contracting an external provider or performing the service themselves. The company's basic notion is that units purchasing the service are in some cases free to switch to an external provider or perform the service themselves if not satisfied with the service supplied. This was however stated in the interviews as much easier in theory than in practice due to transaction costs, the culture of the company and the fact that certain services are mandatory for units to purchase in-house. As shown in this research paper this has caused the organizational members to view the relationship in different ways along with possible sub-optimization of local results. This has led the researchers to believe that these internal service providers are not used in the most optimal way. They should instead have a strategic focus enabling the most beneficial long term strategies for the group as opposed to being seen competitive by internal customers. The structure chosen by the case company does not seem to fully support the current aim of these internal service providers which opens up for a possible future research area within examining internal service providers in organizations and their role in supporting the business. Which variables that contributes to a successful use of these units, supporting the overall aim of the company, could be determined and how they correlate with the strategies present in the organization.

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# 8 Appendix

## 8.1 Interview guide

- Your role within the company including background
- What is your interaction with internal transactions?
- Tell us about how the internal transaction system is constructed and your overall knowledge about it
  
- What do you think is the main reason for doing these internal transactions?
- Do you think that the system is successful in what it aims to accomplish?
- How important do you think the internal transactions are?
  
- What kind of effects do you think the internal transactions might have on individuals behavior?
- How do you view the “relationship” between units that do internal affairs?
- How much emphasis is placed on accounting numbers (such as revenue, profit, costs) within the organization? Are there other non-financial KPIs to evaluate the performance of units/divisions? What is most important to look at when evaluating the performance?
  
- How is “accounting” understood by the rest of the organization? Do you need to adapt the language or your communication in order to be understood?
- How does it work when the superiors interpret the results? Are you able to explain, comment, justify it? How much knowledge (and understanding) do the superiors have of the local conditions leading up to these numbers?
  
- How is the overall cost culture within the company/division? Is there a difference in focus or action depending on the financial results/profitability?
  
- Tax incentives role in transfer prices