

What is a Professional Service Firm... and why does it matter? ¹

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Abstract

Professional service firms (PSFs) are increasingly seen as important objects of organizational research for two reasons. For one, PSFs represent a growing sector within modern economies, thus warranting research on how they are different from the prototypical manufacturing and high-tech firms more commonly studied. Perhaps more importantly, because PSFs rely almost purely on skilled human capital, they are often looked at as harbingers of organization forms in an increasingly human capital-intensive or knowledge-intensive economy. Many scholars suggest PSFs might represent models for firms throughout the economy (Lowendahl 1997; Scott 1998; Blair and Kochan 2000; Teece 2003).

Unfortunately, there is little consensus on what even defines a professional service firm. At best, definitions vary from scholar to scholar; at worst, they are left implicit and unexamined. Scholars would likely agree that law and accounting firms are the quintessential PSFs and should fit into any proposed definition. However, including any other industries raises important definitional questions. If consultancies or investment banks are included, as they often are, then we cannot distinguish PSFs by their adherence to an institutional logic of “professionalism”, marked by ethical norms, preferences for autonomy, and state-sanctioned entry barriers (Greenwood 1990; Lowendahl 1997; Greenwood and Empson 2003). If software development firms are included, as they sometimes are, then we cannot distinguish PSFs by the production of intangible services.

This lack of clarity on what defines PSFs is not just a nuisance for organizers of PSF-focused conferences. Rather, it creates two important problems for PSF research. It hinders communication *between* PSF researchers as well as *from* PSF researchers to the broader organization theory community. Among PSF researchers, low definitional rigor complicates comparisons or generalizations across studies in different contexts: do the results of a law firm study generalize to other potential PSFs? More importantly, if the definition of a PSF is ambiguous, then it is difficult to articulate how PSF research contributes to broader theories of organizations. In other words, whether and how the study of PSFs contributes to organization theory rests precisely upon explicitly identifying what makes PSFs exceptional in the first place.

This paper makes progress on this important task of clarifying the boundaries of the PSF universe. It does so first by reviewing, critiqueing, and synthesizing existing PSF definitions from organizational theory (e.g., Eccles and Crane 1988; Greenwood 1990; Maister 1993; Lowendahl 1997; DeLong and Nanda 1999; Lorsch and Tierney 2002; Greenwood and Empson 2003) as well as from organizational economics (e.g., Alchian and Demsetz 1972; Jensen and Meckling 1979; Rajan and Zingales 2001; Levin and Tadelis 2002; Teece 2003). However, it proceeds from the premise that progress will not come from a singular definition that excludes many realms of activity, but instead from identifying a range of plausible distinguishing characteristics, then discussing how the use of each definition affects (a) the scope of the PSF universe and (b) the generalizability of the insights derived from PSF research.

Secondly, the paper assesses the applicability of these various characteristics to a broad set of industries. Based on these assessments, it identifies and labels clusters of related industries that lie within an inclusive PSF umbrella: i.e., it maps a wide range of industries into regions within (and nearby to) the PSF universe. Lastly, the paper discusses the connection between alternative definitions and the types of research questions and organizational lessons to which they may contribute.

An example of the issues involved: researchers frequently distinguish PSFs primarily (although not exclusively) by their extreme knowledge-intensity (e.g., Lowendahl 1997; Greenwood, Li and Deephouse 2002). However, knowledge-intensity also applies to most high-technology firms that employ scientists and engineers, yet these types of firms are probably not ones we want to describe as PSFs. In addition to knowledge-intensity, PSFs are also characterized by a *lack* of capital investment. Yet the presence of large capital investment may radically improve the ability to exercise authority over knowledge workers because the firm can own important production inputs—making the management of scientists potentially very different from the management of lawyers. Thus, extending insights about PSFs to knowledge-intensive environments in general may be highly problematic.

This paper contributes to PSF research in several ways. It identifies points of consensus within the existing literature regarding the defining features of PSFs and challenges the validity of several oft-proposed definitions. It provides a language for labeling the differences and similarities between industries that feature PSF-like qualities. And it provides an inventory of industries with which to assess the validity of functional theories of PSF organization. For example, if a theory of the professional partnership is based on some exceptional condition facing law and accounting firms, the map in this paper can identify additional industries that share those characteristics and hence should also feature partnerships (along with those that do not and hence would not be expected to feature partnerships).

¹ Presented at the Clifford Chance 2006 Conference on Professional Service Firms, IESE Business School, Barcelona