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Collaboration and control: managing tensions in competitive inter-organisational relationships

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UNIVERSITY
of
GREENWICH

Jennifer Grafton
The University of Melbourne

Julia Mundy
The University of Greenwich

Key findings:

- Control mechanisms within alliances must maintain a delicate balance. Each firm must protect itself from appropriation threats while also co-operating with competitors in order to enhance its own opportunities for long-term success.
- The control mechanisms used to attain this balance between gains from co-operation and competitive threats encompass a range of formal and informal controls.
- These findings suggest that management accountants responsible for the design and use of inter-organisational controls must guard against the temptation to revert to traditional ways of thinking about control.
- Practising accountants should seek to understand the social relationships that exist between their firms and potential partners, and exploit these in order to capture gains from co-operation as well as to manage potential misappropriation concerns. Informal mechanisms, such as shared beliefs and trust between firms, are likely to be a more effective and efficient means than formal controls of monitoring the behaviour of partners.
- The use of such mechanisms is also more likely to facilitate collaborative activity over the longer-term and across other alliances.

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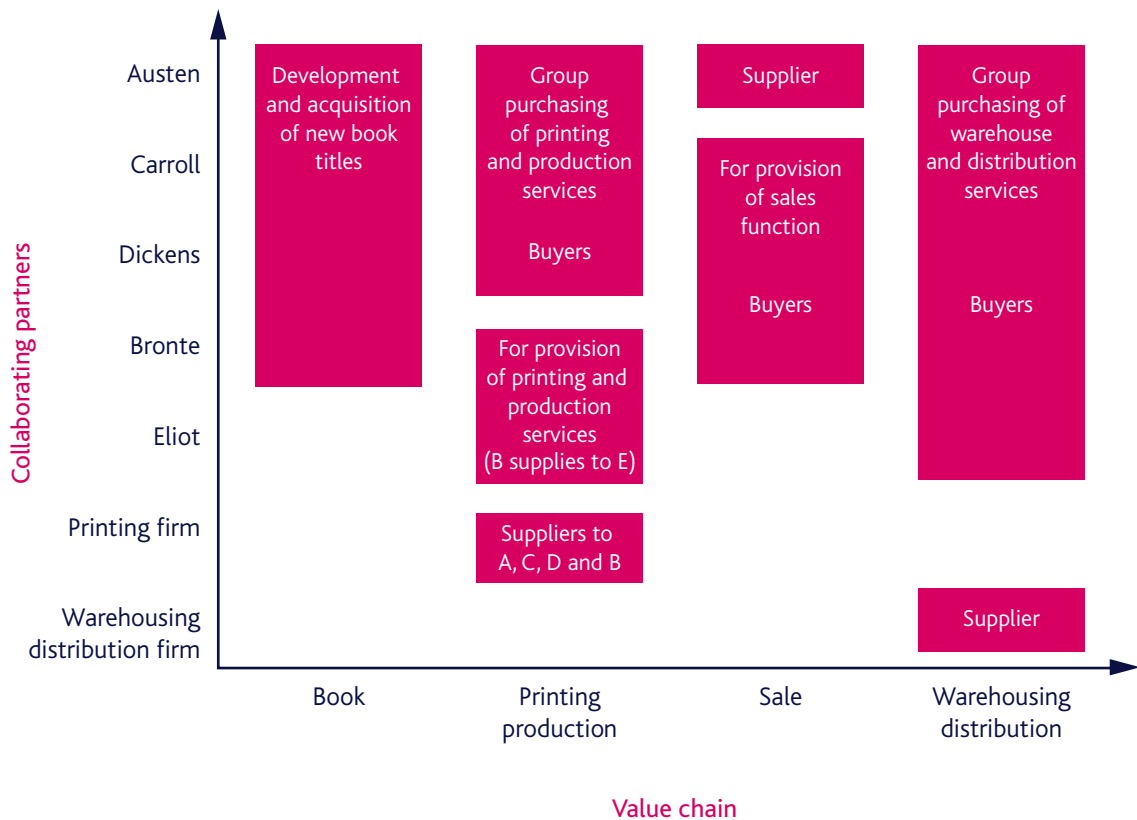
Overview of project

This project investigates the tensions, or control challenges, in competitive inter-organisational relations and analyses the type and use of control systems for the purpose of managing these tensions. The study was conducted in the independent trade publishing sector in the United Kingdom. This sector is an appropriate research site for this project because firms are direct competitors but also simultaneously collaborate in activities across various functions of the value chain. Furthermore, they collaborate when engaging in networks

with both suppliers and customers. This contemporaneous membership of different networks provides an interesting opportunity to explore the tensions arising in the pursuit of competitive collaborations and the use of controls to manage these tensions both within and between particular alliances.

Our study captures the perspectives of five inter-related independent publishing houses, plus a number of their common key suppliers and customers. We investigate four collaborations across the value chain in which these five firms co-operate. These collaborations include the initiation of new book titles (product development), production processes, sales, and warehousing and distribution operations. The network of collaborations between these five firms is shown in figure 1.

Figure 1: Summary of competitive inter-organisational collaborations studied



The project contributes to the extant findings on the governance and control of inter-organisational relations by providing rich accounts of the tensions arising in collaborations between competitors. Specifically, we draw on these accounts to develop insights into the interplay of controls employed to manage these collaborations.

Objectives

- To explore the control challenges that arise in collaborations between competing firms.
- To investigate how control systems are implicated in managing the tensions that arise from the simultaneous pursuit of co-operation and competition in collaborations between competitors. Specifically to:
 - investigate the role of control in ensuring gains from co-operation in such collaborations
 - investigate the role of control in managing appropriation concerns in such collaborations.
- To explore how the control systems of particular competitive collaborations are influenced by the broader nexus of activity within an industry network.

Main findings and their implications for practical application

The study provides evidence of control challenges and solutions in four co-operative alliances between five competing independent publishing houses. The alliances in which they co-operate are separately organised and managed, but collectively they create a broader network of activity between the firms.

The competitor firms in our study collaborate because of the potential for immediate and longer-term gains at the organisational, network and industry level. Gains are complementary and arise from a number of sources including access to skills and knowledge, and economies of scale and scope. Interestingly, while gains to be accrued at the organisational level are an overriding enticement to competitive collaborations, all of the participants in our study noted the importance of broader network and industry benefits. This mutually supportive environment creates a collective sense of camaraderie, uniting the independent houses in their constant battle against the power of the booksellers (their customers) and the mass-market approach of the conglomerate publishing houses that also compete in the area of trade publishing.

The collaborations investigated in the project present a range of complex control challenges at the inter-firm level relating to both promoting co-operation and managing appropriation concerns. For example, three of the firms outsourced their sales function to another firm in our study that has its own sales force. This presents the challenge of co-ordinating production schedules and exchanging information across organisational borders. Collaboration in the sales function also has the potential for lost sales through the use of a competitor's sales force, placing the reputations of the individual firms at risk in the event that the books are not ready for the planned publication date. In fact, loss of proprietary information is a significant risk that spans all the alliances, ranging from ideas or potential authors for book titles, to book covers and formats, to commercially sensitive financial and non-financial data. Each firm guards its intellectual property in relation to book titles and potential authors in order to maintain its unique identity and enhance its prospects for commercial success.

Control mechanisms within alliances must maintain a delicate balance. Each firm must protect itself from appropriation threats while also co-operating with competitors in order to enhance its own opportunities for long-term success. The control mechanisms used to attain this balance between gains from co-operation and competitive threats encompass a range of formal and informal controls.

Observed formal control mechanisms

We observe few formal control mechanisms in the four alliances we investigate, despite the potential for misappropriation and opportunistic behaviour. For example, in the context of joint purchasing of print services the absence of a formal contract between collaborating publishing houses increases the risk that one of the partners might pull out of the agreement at any time. This could leave the remaining firms no better off, or even in a worse position than when purchasing individually if it leads to a reduction in economies of scales and loss of reputation with printers. Similar incomplete contracting is observed in the sales alliance with entire sales functions being outsourced to a direct competitor without formally specified and monitored performance measures. In both of these examples, the contracts are used to define the nature of the alliance rather than as a tool for managing these processes. Other formal mechanisms evident in our case study include task planning and progress evaluation in the sales process, while an explicit specification of tasks characterises the alliances based around the printing and production process.

Observed informal control mechanisms

The use of incomplete agreements across the alliances reflects the strong influence of social controls that manage the various relationships between these firms. One important social control is an informal networking group constituted by the managing directors in our case firms. Membership of this group helps to nurture social ties and produces a strongly-held shared set of beliefs and values that define for participants the importance, nature and role of independent publishing houses. These values and beliefs are not unique to any particular collaboration but rather span and support all of the evident inter-connections between firms. A central shared value is the commitment by these independent publishing houses to the delivery of high-quality books that contribute to society's cultural activities. Subscription to this philosophy instils a sense of solidarity between these organisations against the commercialism and mass-market approach that predominates in the conglomerate publishing houses. Complementing the shared values is the widely held belief that each publishing house in this collaboration has its own *modus operandi*, an overall identity that contributes significantly to the sector and which ultimately justifies its continued independence. These shared beliefs, coupled with the ever present fear of financial failure, encourage the firms to co-operate with and support each other, despite the underlying potential threats to their competitive advantage.

Concerns about misappropriation are managed through the restriction of membership of the informal networking group to the managing directors, which reduces the likelihood that potentially sensitive information will be imparted to a competitor firm. Misappropriation concerns are further reduced because of the pervasiveness of shared values between the publishing houses. Loss of membership of any collaboration due to misappropriation could have potential ramifications for the offending publishing house in a range of other collaborative efforts. Misappropriation reflects a lack of support of the continued independence of the other firms and this belief is fundamental to continued collaboration between the publishing houses. While the continued commercial success of a publishing house may not be completely jeopardised by exclusion from one competitive collaboration, exclusion from collaborations across the value chain could place a house at a significant disadvantage. The firms comply with the collaborative objectives partly for fear of sanctions. Our findings suggest that increased network inter-connectedness increases the salience of this control mechanism.

A high degree of trust is evident in the broader relationships between the various partners. Trust between the alliance

partners originates in the collaborative efforts based around the initiation of new book titles; this further supports the strong social networking ties among its member firms. We find that trust between alliance partners mitigates the need for constant monitoring or detailed contracts and facilitates the expansion of collaborations across the network. In the current study, this trust takes several forms. In the cases of the third-party production and the sales alliances, trust is grounded in a belief that the firms supplying the service identify with the requirements of their partners because these reflect values and concerns identical to their own. Trust is cultivated over time as the purchasing firms continue to receive a level of service that matches exactly their own requirements. The existence of this 'identification-based' trust between the alliances' partners in the third-party production and sales alliances removes the need for more formal control mechanisms to manage co-ordination requirements and in particular appropriation concerns in these settings.

While prior research has drawn on broad notions of trust as a determinant of inter-firm collaboration, our observations shed light on the nature of the relationship between trust and other informal control mechanisms. Another form of trust, 'reputational' trust, is facilitated by the shared beliefs and values brought about by regular communication. This enables firms to develop an understanding of their competitors' behaviour, enhancing their ability to predict the likely reaction to events. In the context of the network of independent publishing houses examined in the current study, information and knowledge about the other group members enable each firm to make plans and investments based on what they think their competitors are likely to do, thus accelerating the decision making process.

Trust between partners can deteriorate when the opportunities for personal gain increase beyond those obtained through co-operation. We find that the concept of a 'calculative-based trust', in which close relationships between firms are based on a calculative economic rationale, helps to explain the extent of co-operation occurring in each alliance, as well as the mechanics through which such co-operation occurs. This means that the shared beliefs and values are supported by an expectation that each firm will abide by the unwritten rules attached to participation of the group for fear of future sanctions. Thus, the publishing houses believe that their partners will conform to the norms of co-operation because there exists sufficient benefits in doing so (or punishments for not doing so). For the firms included in the current study, sanctions might involve exclusion from future discussions or from other forms of collaboration that are vital to their continued independence. The firms 'trust' (i.e. have sufficient confidence) that their partners

will behave as desired to maintain the relationship as long it remains in their interests to do so. The behaviour of each partner can therefore be described as guided by enlightened self-interest, which is a 'precarious equilibrium between gain seeking and compliance with co-operation norms'. Thus, even when the primary goal is to maximise profits, firms are willing to sacrifice some short-term gains for the potential of greater benefits in the longer-term that accrue from their relationships with the other firms.

There exists a continual conflict between the desire to maintain the relationship with a partner versus the requirement to maximise profits. In order to protect the alliances, it is therefore in the interest of all the firms to constantly promote to each other and to themselves, the benefits of co-operation, and that they employ a variety of signals to do this. Each publishing house is alert to the signals generated by their alliance partners because they do not want to be the victims of opportunistic behaviour. First, the members use the social networks in which they participate to communicate and reinforce their shared belief in the importance of working together against the power of the booksellers and the conglomerate publishing houses. A firm whose attendance lapses or which voices doubts about this shared belief is signalling to its partners that its interests may no longer be aligned with the other members. The partners can use this information to decide whether they wish to continue their various relationships with the firm. A second signal used to promote the benefits of co-operation is the standard commission structure that the third-party sales firm (also a major competitor) pays to its sales people regardless of whose books they sell. This is tangible evidence of the firm's claim that third party sales is one of its key goals and thus signals its commitment to the alliance. Any change in the pay structure of its sales force would immediately indicate to its partners a shift in its attitude towards the alliance. Third, the absence of formal control mechanisms can be viewed not simply as the result of an inability to design such controls, but also as positive signals that indicate an alignment of interests and a willingness to co-operate.

The interplay between formal and informal controls

There are a number of explanations for the lack of formal controls. First, the informal controls appear to operate in an effective and internally consistent manner. The shared priorities and values of the firms bind them together across all of the collaborations and reduce the need to implement more expensive formal controls. The extensive use of informal controls signals a willingness to co-operate, whereas the presence of formal controls may negatively impact the good working relations between the firms. Our findings

suggest that their use would stifle creativity, impede the gains from co-operation, and inhibit the trust that binds the firms. Second, there are practical difficulties associated with engaging in short-term opportunistic behaviour. Firms self-regulate their opportunistic behaviour, not simply due to reputational reasons, but also because such behaviour is itself highly risky and can lead to unpredictable consequences. For example, if one firm misappropriates information obtained from another during the third-party production process, it might be excluded from the social networking group, thereby losing access to valuable comradeship and advice. The need for formal controls is therefore diminished because the potential loss to each firm in the event of undesirable behaviour or poor performance is so high.

In summary, the collaborations investigated in this study represent a close-knit network consisting of a relatively small number of firms in which the members know each other personally and possess a good understanding of each other's businesses. Network cohesion is facilitated by social ties underpinned by a strongly held set of beliefs and values. The significance of the social controls that permeate the network of firms lies in the absence of formal controls used to manage each individual collaboration.

Implications for practitioners

The project highlights some important implications for practitioners by producing valuable insights into the control mechanisms that are used to manage competitive collaborations. We find that observable control mechanisms do not always reflect fully the control problem that they are intended to manage, but that this does not necessarily signal either poor choice of controls or potential problems. In other words, the controls in place will sometimes be less complete than would be otherwise expected, and still operate effectively at lower cost. For example, the use of formal control mechanisms, particularly contracts, may inhibit collaborative efforts between competing firms. In contrast, social relationships between competing firms have the potential to generate an underlying set of shared values and beliefs from which collaborative activities can develop and continue. These shared beliefs provide the basis for entering into collaborations that benefit all participating parties, despite the competitive nature of the relationship. Shared beliefs between firms also play a crucial role in the subsequent management and control of these and other collaborations in which competing firms engage.

Together these findings suggest that management accountants responsible for the design and use of inter-organisational controls must guard against the temptation to revert to traditional ways of thinking about control.

Instead, practising accountants should seek to understand the social relationships that exist between their firms and potential partners, and exploit these in order to capture gains from co-operation as well as to manage potential misappropriation concerns. Informal mechanisms, such as shared beliefs and trust between firms, are likely to be a more effective and efficient means than formal controls of monitoring the behaviour of partners. The use of such mechanisms is also more likely to facilitate collaborative activity over the longer-term and across other alliances.

Conclusions - lessons learned from the research

- Collaborations between competing firms present a range of complex control challenges at the inter-firm level relating to both promoting co-operation and managing appropriation concerns.
 - The control mechanisms used to manage these challenges encompass a range of formal and informal controls, but performance measurement systems and detailed contracts between partners are less evident because their use would stifle creativity, impede the gains from co-operation, and inhibit the trust that binds collaborating firms.
 - Social controls are crucial to the successful management of competitive collaborations. In particular, shared beliefs and values, reinforced through regular communication, help to establish a high degree of trust between the various partners. This mitigates the need for constant monitoring or detailed contracts and facilitates the expansion of collaborations between firms.
- Firms engage in collaborative activities for reasons of enlightened self-interest. Short-term gains may be sacrificed for the potential of greater benefits in the longer-term that accrue from relationships with other firms.
 - Trust between alliance partners is grounded in a calculative economic rationale, in which firms believe that their partners will conform to the norms of co-operation because sufficient benefits exist in doing so (or punishments for not doing so).
 - Firms are alert to signals from their alliance partners that indicate their continued desire to engage in collaboration. Monitoring the behaviour of partners helps to manage appropriation concerns.
 - The observed controls that are used to manage collaborations between direct competitors are influenced by the broader network of relationships in which these competitive collaborations exist.
 - The reduced use of formal controls and corresponding emphasis on social controls presents particular challenges to management accountants used to traditional ways of thinking about control.

Authors

Dr Jennifer Grafton

The University of Melbourne

E. j.grafton@unimelb.edu.au

Dr Julia Mundy

The University of Greenwich

E. j.mundy@gre.ac.uk

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**Chartered Institute of
Management Accountants**

26 Chapter Street
London SW1P 4NP
United Kingdom

T. +44 (0)20 7663 5441

E. research@cimaglobal.com

www.cimaglobal.com

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