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Accounting in markets, hierarchies and networks: The role of accounting in the transnational governance of postal transactions

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A B S T R A C T

We examine the changing role of accounting in the development of the international postal system between 1840 and the emergence of the Universal Postal Union (UPU) in 1875. We use the distinction between mundane and opportunistic transaction costs to explain why accounting disappeared as a coordinating mechanism as postal transactions migrated from spot market exchanges, through bilateral contracts (treaties) between nations, into a network of domestic post offices coordinated by the UPU. Our analysis refines the application of transaction cost economics to the understanding of the role of management accounting in different governance mechanisms.

Introduction

Williamson (1996) suggests that there exists a set of discrete governance mechanisms through which transactions can be completed. Each governance mechanism has its own capabilities and limitations such that different types of transactions are handled by specific governance mechanisms at lowest cost. The polar types of governance mechanisms are markets and hierarchies but hybrid forms of governance are common. These hybrid governance mechanisms include relationships, alliances and networks. Hybrid governance mechanism may have different information and control requirements than markets and hierarchies. Hopwood (1996), among others, has expressed the need to understand the implications of these types of governance mechanisms for management accounting information and control systems:

> To date accounting research has largely ignored such changes and their implications for financial decision making and control. Having earlier given little or no consideration to the informational implications of matrix structures and the financial aspects of project oriented forms of organization, the accounting research community is largely continuing to be satisfied with its fixation on the traditional hierarchical organization (Hopwood, 1996, pp. 589–590).

In response to this call for a better understanding of the role of accounting in inter-organizational relationships, accounting researchers, drawing on a variety of theoretical perspectives, have examined how accounting information is used to facilitate "cooperative coordination" (Hakansson & Lind, 2004) within hybrid structures and the impact of these cooperative undertakings on management accounting practices. In doing so, some researchers looked at the constitutive role of management accounting information by probing into "*how* accounting is a 'force' – an actor – in establishing and developing inter-organizational relationships" (Mouritsen & Thrane, 2006, p. 242) or explored the enactment of accounting controls in alliances that are part of larger networks and the effect of these alliances on accounting practices (Chua & Habib, 2007). Others, drawing on economic theories, including transaction cost economics (TCE), have explored the governance role of the management accounting information and controls in alliances and networks (Anderson & Dekker, 2005; Dekker, 2004; Hakansson & Lind, 2004).

In studying the role of management accounting systems within specific governance structures, however, these studies do not problematize the change in use of accounting as

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transactions migrate from one governance mechanism (i.e. markets or hierarchies) to another (i.e. networks). To overcome this gap in our understanding of the existence and role of accounting techniques in inter-organizational relationships, we explore the effect of a series of changes in governance structure on the use of accounting information. We identify a setting, the international postal market, in which we are able to trace "longue durée" changes (Braudel & Matthews, 1982) in the use of accounting as transactions migrate from spot market exchanges to bilateral treaties/contracts between national postal providers and, finally, to a network of national postal providers coordinated by the Universal Postal Union (UPU). Unlike the empirical observations in extant accounting literature on networks, in this setting, accounting technologies are eliminated when transactions move from bilateral agreements to a network in an attempt to facilitate interaction among participants. Concurring with Dekker (2004) on the limitations of current interpretations of TCE to explain the use of accounting in networks, we expanded on the use of TCE in the accounting literature by introducing the concepts of "mundane" and "opportunistic" transaction costs (Baldwin, 2008). This distinction allows us to theorize the disappearance of accounting as transactions shift from the market into network forms of governance.

This paper is structured as follows. We begin with a discussion of current work on the role of accounting in markets, hierarchies and networks. A key assumption of this literature is that management accounting information emerges as a replacement for market prices when transactions migrate from the market to other forms of governance. We identify gaps in this literature: to date the literature has not examined changes in accounting when transactions shift from one governance structure to another and do not account for instances where accounting is eliminated as a result of this transition. We then identify a key elaboration of transaction cost economics that has not been used in the accounting literature: the distinction between mundane and opportunistic transaction costs. Next the use of the case method to explore accounting in the international postal system is discussed. In particular, we argue for the use of case analysis as a theory testing method when theories make non-probabilistic predictions and as a theory elaboration method through its emphasis on mechanisms and processes. We then describe our data set. Our main results are presented in three sections describing the state of the postal system in the time period 1840–1875, the transactional issues that arose, and, finally, the change in rules and accounting procedures that were implemented in the first UPU Convention in 1875. Our discussion and conclusion draw the lessons from this case for the application of TCE to accounting phenomena.

The role of accounting in markets, hierarchies and networks

Accounting in markets and hierarchies

Neo-institutional economics, and transaction cost economics in particular, provide an important framework for understanding many accounting phenomenon. This framework relies on two main insights. First, Coase (1937) developed the insight that markets and firms were alternative ways of completing transactions and that there are costs to the use of either mechanism. The idea that the market mechanism was not costless, in particular, provided Coase with a way to reconceptualize the nature of the firm. The firm would arise if it could complete transactions at lower cost than in the market. For example, where complex interdependent tasks are required to produce some good, it may be more effective to hire skilled craftsmen as wage labour controlled by a central authority (the firm) rather than have each craftsman attempt to contract with all others for specific work. However, there must be increasing costs to the use of the firm and authoritative control to complete transactions that limits the size of the firm (otherwise, a single firm would internalize all of some forms of transactions). Coase (1937) thus provides a role for management inside the "black box" production function envisioned by classical economics and provides a rationale for the existence and size limits of firms.[1]

Second, Williamson (1975) generalized these observations by suggesting that markets and hierarchies (i.e. firms/government agencies[2]) were alternative governance mechanisms that had a contingent cost advantage in completing transactions depending on the nature of those transactions (characterized by the "critical dimensions" of asset specificity, frequency, and uncertainty, Williamson, 1979, p. 239). This leads to the "discriminating alignment" hypothesis that transactions will be allocated to particular governance mechanisms in order to minimize the cost of completing those transactions.

> Transactions, which differ in their attributes, are aligned with governance structures, which differ in their cost and competence, so as to effect a discriminating—mainly a transaction cost-economizing—result (Williamson, 1996, p. 12).

Williamson's work proved to be particularly useful for challenging anti-trust laws by showing that vertical integration in some industries was economically rational rather than simply an attempt to create monopoly power. In general, empirical support has been greatest for the relationship between asset specificity and the choice of governance form but inconsistent for other dimensions of transactions (Shelanski & Klein, 1995). Williamson's (1975) insight has also been used in the accounting literature to suggest that management control systems, as a key aspect of governance systems, would also vary according to the characteristics of transactions (Anderson & Dekker, 2005; Spekle, 2001). It has also informed studies of the

[1] Santos and Eisenhardt (2005) provide a review of alternative conceptions of the formation of organizational boundaries.

[2] Williamson explicitly recognizes government agencies/departments as a valid governance structure subject to transaction cost analysis: "Transaction cost economics views the public agency as a candidate mode of governance that is well-suited for some purposes, poorly suited for others" (Williamson, 1999, p. 311). The term "hierarchy" is used to refer to both private and public sector bureaucracies in which resources are allocated by management.