



# Governing cooperation hazards of outsourced municipal low contractibility transactions: An exploratory configuration approach

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## ABSTRACT

Increasingly, public sector organizations (PSOs) outsource the delivering of important welfare services. This gives rise to important questions of how PSOs can control their suppliers. The purpose of this paper is to show how PSOs manage cooperation hazards of low contractibility transactions, i.e., activities expected to be difficult to govern. The paper applies a taxonomic configuration approach which means we apply a holistic view on the governance of suppliers and search for internally congruent governance packages that also are adapted to the context of the transactions. We find indications of the importance of internal congruence in governance packages in order to effectively deal with cooperation hazards. We also notice that the intensity in and types of controls in inter-organizational relationships are affected by the amount of cooperation hazards. A conflict between a relational and a bureaucracy-based governance package in one of the configurations is argued to be the main driver behind lower expectations about positive behaviour from suppliers.

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## 1. Introduction

In the 1990s prominent researchers called for more research on management control in inter-organizational relations (IORs), i.e., how companies coordinate activities and ensure cooperation across organizational boundaries (e.g., Otley, 1994; Hopwood, 1996). These researchers had noticed a trend where organizations increasingly cooperated in strategic alliances such as joint ventures, long-term outsourcing relationships, licensing agreements and franchising arrangements, all of which created new management control issues. In response to this call, the research on management control in IORs has grown extensively. This research is important since many IORs fail (Langfield-Smith and Smith, 2003) due to inappropriate

controls (cf. Groot and Merchant, 2000; Dekker, 2004, 2008).

One inter-organizational arrangement that has been dealt with to a fairly large extent in the management control literature is outsourcing, i.e., when organizations contract out the manufacture of goods or the supply of services to other organizations (see, e.g., Frances and Garnsey, 1996; Van der Meer-Kooistra and Vosselman, 2000; Mouritsen et al., 2001; Langfield-Smith and Smith, 2003; Dekker, 2003, 2004, 2008; Cooper and Slagmulder, 2004; Anderson and Dekker, 2005; Donada and Nogatchewsky, 2006; Cäker, 2008; Kraus and Lind, 2007; Free, 2008; Van der Meer-Kooistra and Scapens, 2008). However, most research on control in outsourcing relationships deals with private sector organizations and only to a lesser extent with public sector organizations (hereafter PSOs) (Broadbent and Guthrie, 2008; Samuel et al., 2009). This is somewhat surprising since outsourcing occurs increasingly both in the private and the public sectors (Langfield-Smith and Smith, 2003; Broadbent and Guthrie, 2008). The research on PSO

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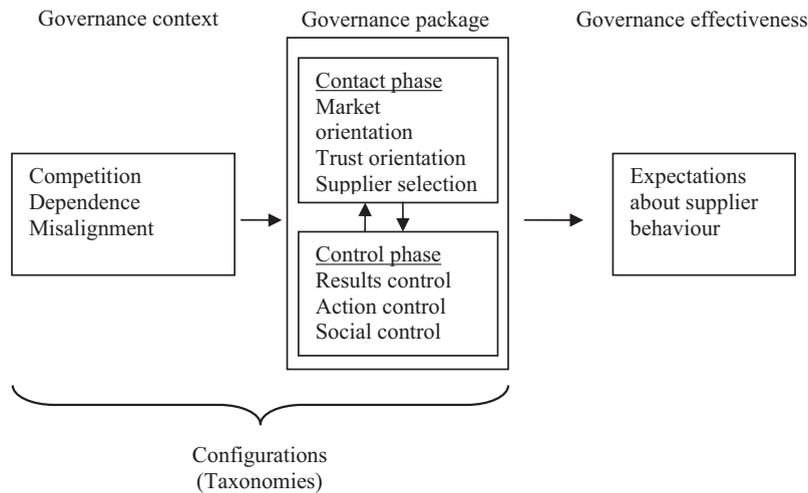


Fig. 1. Conceptual framework.

outsourcing deals mostly with the pros and cons of outsourcing per se or with the make-or-buy decision, and not explicitly with control issues (for an exception see Cristofoli et al., 2010). The majority of the studies yet carried out on outsourcing control in PSOs are about control of non-core activities or of 'technical' activities (see e.g., Seal, 1999).

In this paper we further complicate the picture by focusing on the governance of public sector activities that are theoretically assumed difficult to govern (cf. Groot, 1999; Cristofoli et al., 2010). Here we study inter-organizational control of suppliers engaged in 'soft' public sector activities, such as health care, social care and education. On a generic level, these activities are difficult to govern because of the low measurability of outputs,<sup>1</sup> poor knowledge of the transformation process (Ouchi, 1977; Hofstede, 1981), the typical high asset specificity (Speklé, 2001) and probity (Williamson, 1999), i.e., the contractual situation is characterised by *low contractibility* (cf. Domberger, 1998). Additionally, the governance of low contractibility transactions is often affected by political and institutional factors (Hofstede, 1981; Van Slyke, 2006; Johansson and Siverbo, 2009), not least by the legislation on procurement (Håkansson and Lind, 2007). This paper focuses specifically on one management control challenge that arises when organizations outsource activities: the cooperation problem. Our aim is to show how PSOs manage cooperation hazards of transactions characterised by low contractibility.

In doing so, we build on the extended transaction cost economics (TCE) approach often used in the inter-organizational management control (IOMC) research (Van der Meer-Kooistra and Vosselman, 2000; Dekker, 2004, 2008; Langfield-Smith and Smith, 2003; Anderson and Dekker, 2005). Besides the traditional TCE explanation to governance structures (Williamson, 1981, 1985, 1996) the

extended TCE-framework acknowledges the importance of relational and institutional factors. We use a configuration approach which means we apply a holistic view on the governance of suppliers and search for internal congruent governance packages that are adapted to the context of the transaction.

In Fig. 1 we describe the conceptual framework for the study. Taking the PSOs' perspective, we consider an important measure of the effectiveness of the governance of suppliers is the PSO's expectations about supplier behaviour. These expectations are presumed to be an effect of how the PSO designs the governance package, i.e., how the outsourcer acts in the contact phase (market or trust orientation and supplier selection) and the control phase (results control, action control and/or social control). The governance effectiveness is furthermore expected to be affected by how the governance package as a whole is aligned to the governance context (market competition, dependence of suppliers and misalignment, later to be described in detail). Consequently, the governance effectiveness is presumed to be dependent on internal fit within the governance package as well as external fit between the governance context and the governance package.

In the study we identify three theoretically meaningful and qualitatively different configurations which show the relevance of a configuration approach. We find strong indications of the importance of internal congruence in governance packages in order to effectively deal with cooperation hazards and that the intensity in and types of controls in inter-organizational relationships are affected by the amount of cooperation hazards.

The paper is structured as follows. In the next section we present our approach, key theoretical concepts and a theoretical discussion on the causes of cooperation hazards and how they may be managed. The section ends with the formulation of two research questions. In the following section we provide details about our study's data, variable measures and method. Then we present the study's results and a discussion of our findings. In the final sec-

<sup>1</sup> Perhaps 'outcome' would have been a more appropriate concept since the concept output does not capture the value or quality of a service.

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