

Collaboration between firms and NGOs: An agency perspective

Notes de séminaire

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PRÉSENTATION D'UN
PAPIER DE
RECHERCHE
CONSACRÉ AUX
NOUVELLES FORMES
DE COLLABORATION
REGROUPANT DES
FIRMES ET DES ONG
(PAPIER CO-ÉCRIT
AVEC MIGUEL
RIVERA-SANTOS ET
CARLOS RUFIN)

Most contributions on alliances tend to focus on partnerships linking two or more firms. Beyond these traditional agreements, we observe more and more alliances linking a firm and a not-for-profit organization. We call these agreements B2N alliances (B standing for business and N for not-for-profit organizations). These alliances raise specific issues and challenge frameworks used to understand traditional alliances. More specifically, we will explain how B2N alliances invite us to analyze differently the agency theory.

What are B2N alliances?

Contrary to B2B alliances that link two firms, B2N alliances encompass different forms of collaborations between for profit (i.e. firms) and not-for-profit (i.e. NGOs) partners. Behind this unique term, there is a wide variety of agreements with diverse levels of engagement, diverse motivations and diverse types of NGO partners. These B2N alliances can be observed in various settings and can link firms and NGOs either at the international or at the local scale.

For this project, we have decided to restrain our analysis to B2N alliances with a focus on providing goods or services of social value to beneficiaries distinct from alliance partners. In other words, what makes B2N alliances special comes from the fact that they create value for external beneficiaries (i.e. beneficiaries that are not one of the partners). They differ from transactional relationships such as the sponsorship of specific projects by involving a higher commitment of both partners. These alliances can target different goals such as community capacity building, economic development, health care, poverty alleviation, etc. For example, Timberland has decided to partner with SkillsUSA, a NGO offering training programs. In concrete terms, Timberland employees are invited to give a part of their time to help this NGO and contribute to the training offer.

Why are B2N alliances interesting?

In addition to the novelty of the object, what makes B2N alliances interesting to study? As more and more B2N alliances have been signed in the last years, the

number of research articles on this topic has increased significantly. Essentially, most articles have tried to extend existing core theories to B2N alliances such as transaction costs economics (King, 2007; Rivera-Santos and Rufin, 2011). However, other core theories have not been applied yet to B2N alliances and could give interesting insights on some specific mechanisms.

Among these theories, we have decided to focus on the agency theory. This theory has played a central role in management research. For instance, agency theory has been mobilized to explain and analyze diversification or acquisition strategies (Morck & Yeung, 1992; Shleifer & Vishny, 1991). It has also been used to address governance issues in strategic alliances (Balakrishnan & Koza, 1993; Mjoen & Tallman, 1997; Reuer & Ragozzino, 2006).

However, until now, no study has examined agency issues in B2N alliances, in spite of their unique agency configuration. Analyzing B2N alliances with the agency theory not only allows us to describe agency mechanisms in B2N alliances, it also gives us the opportunity to improve and challenge the agency theory by introducing new elements observable only in a B2N setting. Consequently, we develop two research questions:

1. How do firm and NGO differences impact the agency hazards faced by partners in B2N alliances?
2. How do these hazards affect the governance of B2N alliances and the benefits that the alliance delivers to the alliance's external beneficiaries?

The agency theory and its implication for NGOs and interorganizational collaborations

Before studying B2N alliances from an agency perspective, we remind some fundamental elements concerning the agency theory and its applications with NGOs and interorganizational collaborations.

The agency theory has been developed by Jensen & Meckling (1976) to explain the relationships linking shareholders and managers. Consequently, in a standard principal-agent (P-A) relationship, a principal, typically the shareholder, hires one or more agents, typically managers, to perform a task, typically maximizing the principal's return on his/her investment. Each actor has a clear role in this relationship and it is usually admitted that both the principal and the agent come from the same sector. However, this transfer of power from the principal to the agent can contribute to tensions between both actors. The agency hazards primarily stem from the principal's concern that the agent will not act in his/her best interest. To deal with these hazards, the principal creates a set of incentives and monitoring mechanisms specifically designed to mitigate this concern.

Concerning NGOs, the situation is different. NGOs can be defined as "private, voluntary, non-profit organizations whose members combine their skills, means and energies in the service of shared ideals and objectives" (Mawlawi, 1993). From an agency perspective, we can say that principals are donors and staff, such that we are in presence of a stewardship relationship (Van Slyke, 2007). The stewardship relationship aims at ensuring that the funds provided by donors are utilized in the way intended as conveyed in the agreement. However, we can adopt another perspective and say that external beneficiaries can also be seen as "principals" as they are influenced by the outcome of the NGO's work. The problem becomes even more complex in situations where the NGO represents the beneficiary's interests. In this case, the ability for the donors to monitor the NGO's actions is rather limited.

Finally, in interorganizational collaborations, the agency configuration gets even more complex. In fact, there is a multi-level agency structure within and outside the alliance. Outside the alliance, each firm faces its agency structure with managers hired to represent the shareholders' interests. In parallel to these agency relationships, the partners also recreate the conditions of a principal-agent configuration. Indeed, a partner A expects its partner B to do a part of the shared activity in the best interests of partner A. Consequently, partners implement a set of incentives to reduce agency hazards.

The agency configuration in B2N alliances and agency hazards

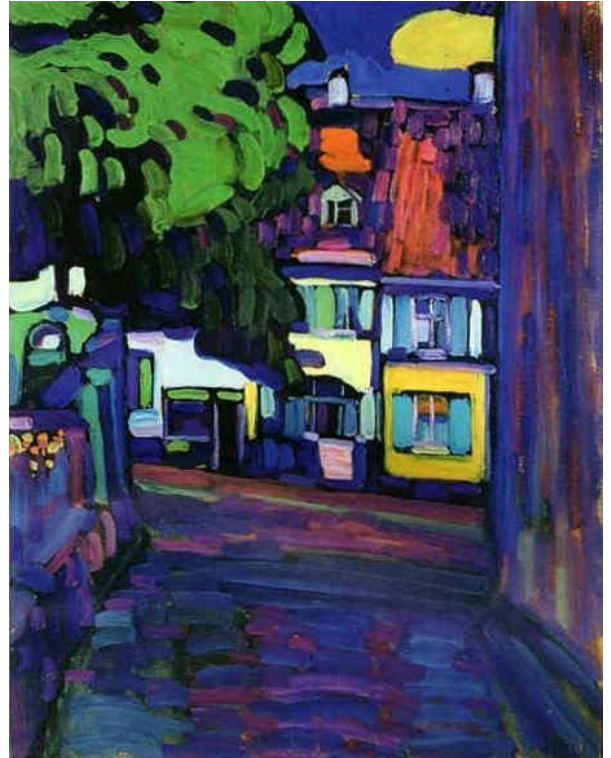
Considering the agency structures described previously, we understand easily that B2N alliances represent a unique but very rich configuration for the agency theory. The multi-level agency structure can be described as follows:

- The firm is in a standard principal-agent relationship in which the shareholders hire a manager to perform a task;
- The NGO is also in a standard principal-agent relationship in which the donors give to the NGO to perform a task (e.g. alleviate poverty);
- The alliance linking the firm and the NGO creates a situation in which both partners take simultaneous principal and agent roles;
- The external beneficiaries act as principals to the B2N alliance from which they expect results. However, they can't always express themselves their approval or disagreement as the NGO represents their interest as self-proclaimed agent.

Considering that agency hazards arise from the divergent interests of a principal and an agent (Mahoney, 2005), we investigate the implications of the B2N configuration. We observe that in addition to the traditional alliance configuration, B2N alliances requires taking into account external beneficiary's interests. But the real challenges come from the fact that the external beneficiary does not explicitly entrust a task to the B2N alliance, leading to a potential disconnect between interests and perception of interests. In addition, contrary to the ROI or the evolution of a market share, the measurement of interests and of fulfillment of needs is far more difficult in B2N alliances. We can then state: Agency hazards will be more severe in B2N alliances than in B2B alliances, *ceteris paribus*.

Developing a B2N alliance typology

As explained previously, the external beneficiary does not explicitly entrust a task to the B2N alliance. In fact, the NGO very often acts as a self-proclaimed representative of the beneficiary's interests. We can thus see that the agency will depend on the ability and the willingness of the external beneficiary to define and communicate its interests. The ability refers to the beneficiary's voice (Hirschman, 1970): does it have a low or a strong voice to complain in case of strong disconnection between its expectations and the reality? The willingness or publicness dimension is based on the idea that benefits can be either public or private (Samuelson, 1954) and



*Maisons de la Obermarkt à Murnau,
Wassily Kandinsky (1908)*

don't have the same impact within the community. The more public a good is, the less the external beneficiary has an incentive to express its dissatisfaction. Crossing these two dimensions, we can elaborate a typology of B2N alliances.

Based on this typology, some agency mechanisms are now investigated in the specific context of B2N alliances.

Agency hazards, governance issues and benefits in B2N alliances

The first question raised in an agency configuration is how severe is the agency hazard. If we observed previously that agency hazard is more severe in B2N alliances than in B2B ones, we must precise this result depending on the type of B2N alliance. As explained earlier, the more public the benefits, the less incentive the beneficiary has to express its interests. In addition, the less voice it has, the higher the risk it can't express its point of view. Combining these two dimensions, we reach the following conclusion: Agency hazards in B2N alliances will be more severe, the lower the external beneficiary's voice and the more public is the benefit delivered. Conversely, hazards will be less severe, the higher the beneficiary's voice and the less public is the benefit, *ceteris paribus*.

The agency theory has been extensively used to study interorganizational collaborations and to address governance issues. Governance issues can be analyzed through three dimensions: mutual monitoring, joint monitoring and the use of incentives. Concerning mutual monitoring, the NGO is generally in charge of monitoring the benefit flows to the beneficiary. The NGO consequently tries to avoid any misappropriation of the benefits by the beneficiary. This situation has greater chances to happen when the benefits are private and the beneficiary has a low voice. We can thus state: Mutual monitoring in B2N alliances will be higher, the lower the external beneficiary's voice and the less public is the benefit delivered. Conversely, mutual monitoring will be lower, the higher the beneficiary's voice and the more public is the benefit, *ceteris paribus*.

The joint monitoring of an alliance refers to the situation in which both partners engage in the monitoring of the alliance's progress as part of the ongoing joint alliance management. The joint monitoring is usually easier when the outcomes can be measured easily and at a low cost. Private benefits are easier to measure than public ones. In addition, the stronger voice of the beneficiary, the easier it is for the partners to measure the progress. Consequently, we can pose: Joint monitoring in B2N alliances will be higher and the reliance on external norms lower, the lower the external beneficiary's voice and the more public is the benefit delivered. Conversely, joint monitoring will be lower and the reliance on external norms higher, the higher the beneficiary's voice and the less public is the benefit, *ceteris paribus*.

Usually, incentives created by partners aim at ensuring that they share the same goals. Indeed, without these mechanisms, B2N partners respond to different types of incentives which is challenging. To avoid any conflict within the B2N partners, the external beneficiary (i.e. the principal) may ask them to use incentives. The more private the benefits are, the more interest the beneficiary has in asking the partners to implement efficient incentives. In addition, the more voice the beneficiary has, the higher the likelihood the partner accepts to use incentives. We can thus state: The use of incentives to mitigate agency hazards in B2N alliances will be higher, the higher the beneficiary's voice and the less public the benefit. Conversely, the use of incentives will be lower, the lower the beneficiary's voice and the more public the benefit, *ceteris paribus*.

Finally, the question of the benefits flowing to the beneficiary across the B2N alliance must be raised. The mechanisms are rather simple: the more voice the beneficiary has, the more benefits it should get from the B2N alliance. In parallel, the more public the benefits are, the lower the risk of misappropriation of the benefits. Combining these two mechanisms, we conclude: The flow of benefits to the external beneficiary will be lower, the lower the beneficiary's voice and the less public the benefit. Conversely, the flow of benefits will be higher, the higher the beneficiary's voice and the more public the benefit, *ceteris paribus*.

Contributions, limitations and future research perspectives

With this work, we have tried to develop an extension of the agency theory thanks to B2N alliances by adding complexity and nuances to agency-theoretic arguments through multi-level agency structure and role of external beneficiary. More precisely, with the introduction of the concepts of voice and publicness into the agency theory, we have been able to study more fine-grained implications on both governance and benefit flows.

This research is essentially limited by the use of single theoretical lens to understand B2N alliances. However, we have identified other directions for future research. Beyond the development of empirical tests for these propositions, we invite researchers to extend our results in other settings such as firm-government collaborations or NGO-government collaborations. The analysis of the different levels of collaboration and of the different rents generated could also be promising.

DÉBAT

Paul Chiambaretto: Thank you for this very interesting presentation. Could you come back on the difference between mutual monitoring and joint monitoring?

Ulrich Wassmer: In an alliance, the mutual monitoring essentially refers to the mechanisms implemented by the partners to keep an eye on the other one and avoid misappropriation of the benefits by one of the partners. On the contrary, the joint monitoring essentially means the mechanisms set by both partners to measure the progress of the alliance.

Jean-Philippe Denis: There are two points I don't really understand. First, in the agency theory, one of the main elements is "residual claims". The fact that the shareholder bears some risks or has something to lose when she gives her power to the manager. And here, you pose that external beneficiaries are principals. But they don't give anything to the NGO so they have nothing to lose. The only principals in this case are the donors to the NGO. Second, I don't understand how you use the voice concept developed by Hirschman. This concept is essentially linked with the notion of decline: "I express myself or I quit because I am in a decline situation". But here, there is no situation of decline. For instance, nature or the Indian tribes don't know they are in a situation of decline.

Ulrich Wassmer: These are very interesting points. In fact, in the agency theory, the principal is not only the one giving money, it is also the recipient of the benefits. In

this case, it is simply that both are different: the donors give money (and are consequently principals), but the external beneficiary receives the benefits (and is consequently a principal too). Your question is very interesting because we had this debate with the other authors to know if a pure or hard-core agency theorist would share our point of view with two different principals. It is something we will have to work on. It is exactly the same with the “voice” concept. Are we pushing it too far?

Alain Jeunemaitre: I found the paper very interesting and puzzling at the same time. To what extent is your situation different from a public-private partnership in terms of complexity? It is exactly the same for me.

Ulrich Wassmer: For us, it is a way to extend not only the alliance literature, but also a way to put forward new insights on agency relationships. To our knowledge, it has not been done even in the public-private partnership literature.

Jean-Philippe Denis: The problem with agency theory is that it is a theory of ownership. But here, there is no ownership issue. The beneficiary is not an owner and consequently has nothing to lose. And here comes again the problem of voice: if you have nothing to lose, you can never be in a decline situation and so can't use your voice.

Ulrich Wassmer: This is true. Here the beneficiary doesn't invest anything so he doesn't bear any risk. We will have to work on it.

Paul Chiambaretto: I don't really agree. If initially the agency theory has been developed to deal with ownership issues, it is now used in different contexts. For instance, you have many contributions in health economics dealing with patient-doctor relationships using this framework. Maybe some of these references could be useful and closer to your approach.

Ulrich Wassmer: That's precisely where the stewardship relationship comes in. You can have different interests between the patient and the doctor as we have between the beneficiary and the alliance. But still the crucial point is essentially for us to justify that these external beneficiaries act as a principal.

Benjamin Lehiany: I found it very interesting because the agency theory is well-suited to work with vertical relationships. While here, with these alliance issues, you extend it to horizontal relationships. I think it is something that you could stress more as one of your contributions.

Ulrich Wassmer: It is good you mention it. But we have to be careful and don't bring too many ideas at the same time, because it would change the structure of the paper and literature to which we refer.



Marie-Rachel Jacob: It is much more a vocabulary question. I usually say to my students that alliances are between competitors whereas partnerships are agreements between organizations that are not competitors. Do you share this point of view? What do you mean in your paper by alliances?

Ulrich Wassmer: As an alliance researcher, I came to the conclusion that the term “alliance” doesn't really mean much. It is very often misused. We essentially work on collaborations as developed by Gray. She essentially defines them as two or more organizations setting goals they try to achieve

*Charon traversant le Styx,
Joachim Patinir (1524)*

together. I prefer this term but the term B2N alliances is used and my co-authors actually coined it so we try to use it as much as possible.

Hervé Dumez: I have essentially two points I would like to raise. First, I have some difficulties to understand the agency relationship within the B2N alliance. I can see an agency relationship within firms; an agency relationship within NGOs; I can hardly see it at the level of the alliance. In an alliance between two car manufacturers, taking the form of a joint venture, there could be an agency relationship. There are heavy investments that lead to potential losses. But here, the structure of the B2N alliances is lighter. Potential losses are less important. Do you mean that losses could be non-financial? Maybe, we can see these B2N alliances through the concept of cross-legitimization and so the losses in a B2N alliance could be in terms of legitimacy or reputation. But I am afraid the agency theory doesn't give you the possibility to take into account this cross-legitimization dimension which is crucial to me. Second, I am not sure the firm and the NGO are in the same situation. In this B2N alliance, the firm has almost nothing to lose compared to the NGO (for which the agreement is crucial at least in terms of resources). And NGOs can also lose their souls in partnering with capitalist firms. How do you take this asymmetry into account?

Ulrich Wassmer: Concerning the agency relationship within the alliance, we think it is important to describe it and not to consider the alliance as an organization. In fact, if we don't describe it, we miss something and we hide an important part of the agency hazards. Concerning the cross-legitimization, in this kind of alliances, this is essentially one of the main drivers of formation. We haven't thought a lot about it but it may be interesting to add it.

Benjamin Lehiany: I think it would be good to highlight more precisely the risks faced by all the actors in the relationship. It would allow us to understand more precisely what is at stake.

Ulrich Wassmer: That's true. We haven't talked enough in the paper about these risks. By doing so, we could link it more to the notion of loss which is central in the agency theory.

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