

## SUPPLY CHAIN GOVERNANCE AND MULTINATIONAL CORPORATIONS' GOVERNANCE – A THEORETICAL COMPARISON

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**Abstract:** Globalization is measured by the number of countries where companies have subsidiaries. Being present on different markets, owning manufacturing capabilities in countries with inexpensive labor force or ensuring the direct supply of raw materials are decisions made by all companies which consider the expansion and the power of their business. The goal of this article is to discuss about choosing the best alternative for expansion if governance mechanisms are considered.

Two alternatives exist: one is to expand by acquisition; the other is to enter another country through partnerships. Considering simple corporate governance, both alternatives contain supplementary elements, creating in this manner more complex environments.

Multinational companies (MNCs) add to the simple - domestic corporate governance the next elements: multi-national governance systems characteristics and forms of expansion, but also local business cultures. Supply chain governance contains the elements presented for MNCs, while other should be considered: forms of collaboration, partner's power within the relation.

Both these complex governance forms are further presented. The main conclusion is that MNCs governance practices can be borrowed for supply chain governance. Some authors consider that supply chains are forms of outsourcing and so avoiding corporate governance.

**Keywords:** governance, supply chains, multinationals

### Introduction

With As the influence of international business systems grows, supply-chains and multi-national companies expanding alike within the world, researchers and practitioners are interested to understand the relations that exist between headquarters and subsidiaries on one side, and between supply chain partners on the other.

The goal of this article is to present differences and similarities between these two forms of governance. A literature review is performed, following the next structure:

1. Within the first part of the article governance is defined, extending the simplest approach of corporate governance to multi-level governance, in this case the hierarchical paradigm of governance;
2. Supply chain governance characteristics are presented within the second part of the article;
3. Details regarding MNCs governance are presented within the third part of the article and conclusions are made at the end.

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### Defining governance

During the last decade, governance, as a new scientific field, was dominated by corporate governance. The concept refers to organizations as single entities, comprising as a basic element the relation between shareholders and managers [1], called the principal – agent problem or the shareholders' perspective [2]; a more advanced view on corporate governance refers to the relation between organizations and stakeholders [2], called the stakeholders perspective.

One hypothesis we consider within this article is that even the most advanced view on corporate governance is useful for single entities only. It is a framework for companies, which have headquarters and manufacturing capabilities within one country. This framework is outdated in comparison to reality, ruled by globalized companies, with supply chain partners placed all over the world. Economic organizations act nowadays as inter-organizational entities.

For this paper, governance is defined as the rules, the structures and the institutions that guide, regulate and control social life, features emanated from power [3]. Governance is a superior system for decision making, for management. It is the framework where decision making is made, for any system.

Considering the systems to be governed, there are several levels of governance. If we take into account the seven levels of living systems [4], we consider that the last five system levels can be governed, and we give examples:

1. Cells – cannot be governed;
2. Organs – cannot be governed;
3. **Organisms** – humans;
4. **Groups** – teams, departments, units;
5. **Organizations** – companies, public and non-profit organizations;
6. **Community and or society** – communities, cities, regions within countries, nations;
7. **Supranational systems** – formed by various countries, earth.

Within literature, we find several details regarding each system' governance: for the third systems level (organisms) exists national governance; fourth and fifth systems levels (groups and organizations, profit, public and non-profit) are affected by corporate governance; for the sixth level (community and or society) exists international, national, regional and community governance; for the seventh level – global governance.

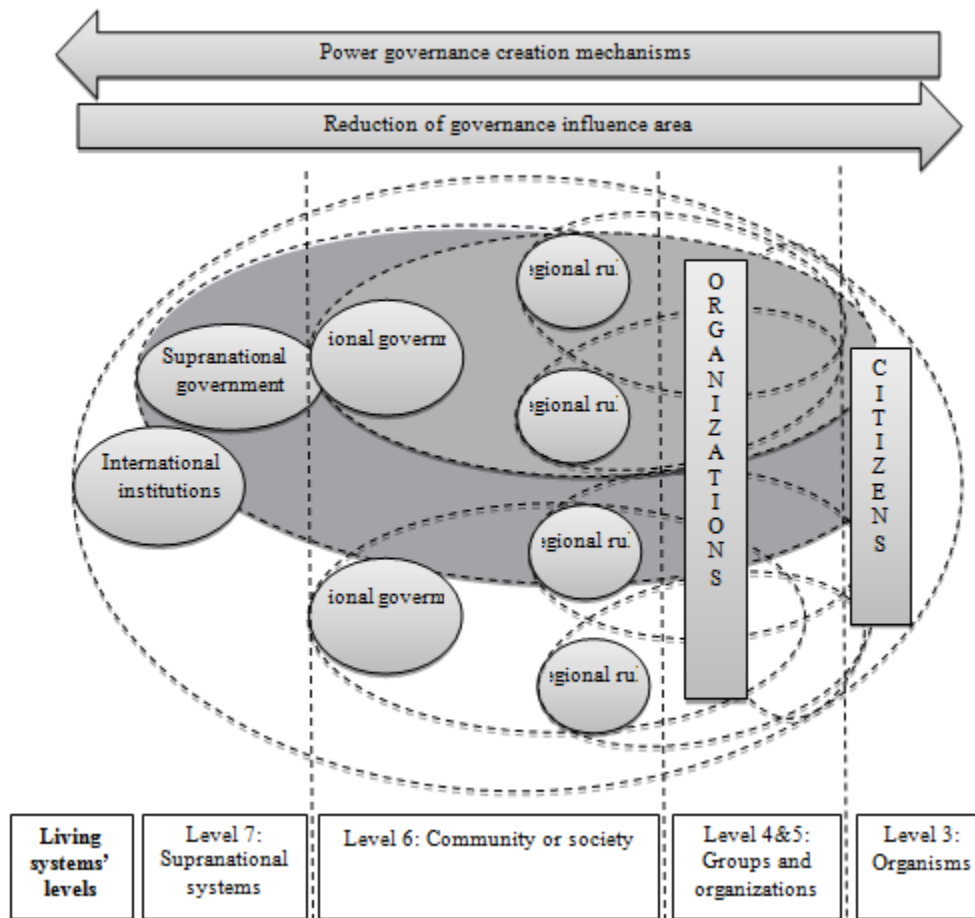


Figure 1. Governance hierarchical levels

However, the enumerated forms reflect the hierarchical view of governance. There are many concerns during this crisis for reducing the level of malfunctioning within companies over the world. A common quest whether actual national and international governance is capable of ensuring the control and the right path for both companies and individuals is always reflected within economic journals. For each systems' level there can exist institutional, structural or productive power, which generates governance, creates written or non-written rules, or guides and controls the actors. It is much confusion between national governance and governance in general. The truth is that the government is only one of the rulers, which acts at the fourth level of living systems. At the rural level and community level other actors such as farmers associations, scientific institutes, religious leaders, finance providers or even individuals can be the real governors if they own one power force. As we can deduct, all these systems are functioning following the same rules. The government parties may be different, but the power rule is

reflected at each level. It is very important to observe that these systems interact and there are some dependencies between them. The governance process is reflected in Figure 1. This figure is a static representation for governance levels. Each governance level is addressed to a specific living system. There is a hierarchy between systems and their ruler. Every system is commonly governed at a superior level.

### **Supply chain governance**

Most researches performed within governance area refer to political or corporate governance, without covering the complexity of supply chain governance. Supply chains are conglomerates formed by several corporations, in order to respond to customers' demand [5]. Supply chain is a concept with many understandings. We shall define for this article a supply chain as a group of companies creating the supply for a product or service. This definition is given considering the fact that the term supply chain has evolved from Porter's value chain, and that supply chain should be used by specialists from several research areas but logistics researchers [6]. As a field of governance, supply chains are complex systems with different structures and power proportions between partners.

The groups of organizations are the real structures which create products in this new economic order of the world. There are few companies being able to realize products by themselves. That's why the governance of companies' interactions is necessary. A supply chain is more than multiple dyadic relations between several companies. Governance has been commonly considered the framework for a two-party relationship. This case is impossible for supply chain governance. Our understanding for supply chains is that real supply chain function as a whole extended organization. Based on specific contracts, a group of companies create a supply for a product, but if there the continual relationship is missing, there is no supply chain.

#### *Sources for a supply chain governance framework*

It is obvious that corporate governance models insist on holding the balance between individuals' and organizations' goals [7], while supply chain models should focus on the relations between several companies participating to create the supply. There are few studies concerning inter-organizational governance because scholars are more organizational oriented or that the study of this multi-organizational governance is costly and time consuming [8]. A common assumption is that governance is not a proper approach for collaborative networks.

There are many names used within literature when it comes to the governance of groups of organizations, such as network governance, inter-organizational governance [9, 10], inter-firm governance [11], trans-organizational governance [12]. Supply chain governance framework is composed from elements imported from international, global, national, regional and corporate governance. The multitude of names is generated by the different types of relations established between the firms forming a group.

*Supply chain governance reflects the relation between supply chain partners*

Supply chains are structures with equal partners or with non-equal partners. Within literature, there are distinguished symmetric (or equilibrated) supply chains, and asymmetric (disequilibrated) supply chains. Gereffi [in 13] has identified five types for value chain governance: hierarchy, captive, relational, modular and market – ranging from high to low levels of power asymmetry. One company can have total control over another, here we face a hierarchical relation – it is a hierarchy. The opposite situation is the market relation.

*Hierarchical governance*

An asymmetric supply chain, having as coordinator the producer or the buyer is commonly run as a hierarchical system. **Hierarchical supply chain governance** seems to be the right term for it. The coordinator implements an extended corporate governance structure, without taking into account partners' interests. It is the case for hierarchy and captive governance between partners.

*Market governance*

Market governance implies a short-term relation between equal partners. The costs and barriers to leave the chain are low. In this case, there are no coordinators, while all companies function autonomously. Supply chain governance exists at a low level. There are probably no structures for coordinating the whole chain. It is the case for modular and market governance among partners. The framework for supply chain governance has been many years dominated by the **transaction cost economics theory**. Transaction cost economics is concerned with the management of transactions in an efficient manner through the least cost form of governance and is based centrally on the assumption of firm opportunism [14]. There are several elements which influence the efficiency of a relation; there are factors which inhibit a relation and create supplementary costs (barriers), or others which increase the efficiency of a relation. At an inter-organizational level, this theory gives the opportunity to a firm to choose from a contractual relationship with an external supplier to hierarchy based governance – i.e. firm integration. There are several intermediary forms, such as joint ventures and franchises. Transaction cost economics theory suggests that **relationships between companies are transactional**, and they exist at arm's length [15]. In this case, an organization changes suppliers very often and supplier dependency is avoided.

*Relational governance*

The last case proposed by Gereffi implies relational governance between partners. Implemented at the supply chain level, it could reflect governance definition. Rules, structures and institutions that guide, regulate and control the chain can be developed. This is the **relational supply chain governance**. Why would a wealthy company opt for such a model? There are reputational benefits; the company has the opportunity to align to the current international governance practices. Fair-trade includes new governance elements, such as accountability, transparency, inclusivity, duty in order to ensure that the interests of the poorer are considered by

chain coordinators [16]. There are also economic benefits generated from a long-term relationship: priority to producing specific parts, better coordination.

While transactional relations are based on contracts and rules, the partnership type is based on risk and benefit sharing. Lambert suggests that a supply chain partnership should include several main elements: joint planning, joint performance management tools, balanced two-way multilevel communication, risk and reward sharing, trust and commitment, the scope of the partnership, reciprocal investment [17].

Some aspects have to be clarified in the supply chain terminology. The aspects suggested by Lambert et al. are not governance processes, but management processes. Partnership in Lambert's view is in our opinion only a management process for supply chains. The same opinion is considered by Fawcett [18] et al.: governance is not management, but an infrastructure which enhances communication and coordination, which should also drive operational excellence and corporate competence.

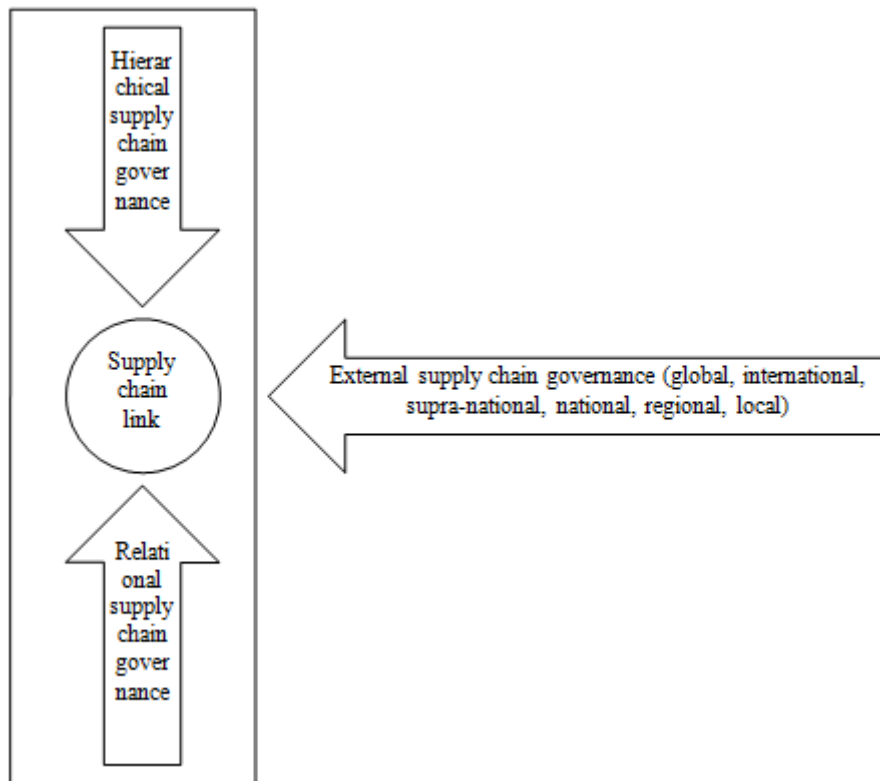
All these aspects can be implemented through executive governance councils, supply chain steering committees, partner advisory councils and senior executive supply chains positions. However, the functions of these structures are not very well established [18] at a supply chain level.

#### *Network governance*

Another model which can be adopted for supply chain governance is **network governance**. This model exists as a policy network - instead of regional governments these networks are formed by several actors who share common interests and who consider that cooperation is the best way to achieve them. There exist state or non-state actors (civil society, private companies); they can include multi-level actors (from regional, national or international level). Instead of market or hierarchical governance, there is a durable bargaining system linking independent actors based on trust for long term relationships (Messner and Meyer-Stamer 2000). There is the equalitarian network, where all partners have the same rights and obligations. There are equal partners, the cooperative character of their relation is very strong, and they are usually called networks [8].

#### *A dual governance framework for supply chains*

A complete framework for supply chain governance should contain both elements presented in this paper: the influence which is generated by supply chain partners, and that one which states, international institutions, regional structures create through distinct mechanisms. The dual framework is presented in the next figure:



**Figure 2. A framework for supply chain governance**

Though there is a trend for developing partnership-type relations with supply chain partners, there can exist hierarchical governance. We think that the governance provided by external institutions for the supply chain act as independent waves affecting the existence of an organization. More than that, there is an interaction between rulers and agents and this interaction generates a continuous process of adaptation of governance practices at each level and at a supply chain level.

A supply chain link receives specific governance inputs from different organizations. In conclusion, these influences have to be included by a framework for supply chain governance. In order to obtain better results for the supply chain as a holistic system, all influences are considered. The above framework considers the characteristics of all supply chain links, and considers the variation generated by supply chain internationalization process.

By comparison, corporate governance is interested only to the benefits of few stakeholders. This framework considers the interests of both supply chain partners and international or global organizations.

### MNCs Governance

MNCs are great geographical business systems built by powerful companies all over the world. They are complex to manage and to govern. Geographical diversity is reflected by great variance in legal systems, other non-market institutions, and MNC governance and CSR approaches across country units [19]. There are no international standards for governance and reporting, enforcement is commonly made by stock exchanges and national jurisdictions. Single-tier governance systems (US and UK) and two-tier governance systems (German and Japanese systems) co-exist all over the world.

One governance tendency is to have a **tightening of governance systems** for all MNCs' subsidiaries. Tightening has the next definition [19]: it means increased MNC compliance with specific standards and practices recommended in national and international governance codes and guidelines. Tightening involves reducing entrenchment and discretion of top managements and governing boards, and increasing both formal and willing compliance of executives and directors with internal and external governance codes and guidelines. Complying with best governance prescriptions should be a source of competitive advantage such that no MNC can afford to fall too far behind in the adoption of best governance prescriptions.

Anyway, there are three possible scenarios for the evolution of international governance and reporting standards [19]:

1. One scenario is the voluntary adoption of best practices, scenario which would continue the pre-2008 situation. This alternative is the most flexible for businesses; but also is the least reliable and trustworthy. The freedom of the markets shall divide between winners and losers through competition. Bad practices should tend to disappear in competitive conditions. Early movers might gain competitive advantage. However, whether markets are sufficiently competitive is not well established empirically. Compensation systems tend to work against best governance practices. Dramatically increased government intervention in markets following the beginning of the crisis undermines the possibility of appearance of this scenario. Scandals and crises tend to erode investor and public confidence and to threaten the foundations of the market system. Failures of integrity tend to provoke increased government regulation. Voluntary adoption of different practices (such as CSR, but also transparency mechanisms) might be evaluated not as succumbing to social pressures but as a cushion against reputational effects of weak performance;

2. The second scenario is the appearance of government regulation. FCPA and SOX are instances of reaction to scandals and crises. Evidence on whether earnings management has become more conservative post-SOX is divided and disputed. Evidence on whether SOX has tended to move companies to non-U.S. exchanges seems mixed: it has had no clear effect on large companies but may have affected small companies. This alternative is the least flexible from a business perspective; but also likely now to prove popular with politicians and public



sentiment. This approach tends over time to increased detail and rigidity. Companies must expect to comply regardless of immediate cost. On the other hand, the external governance over companies increases as a reaction to the actual lack of intervention mechanisms for the state. There are more independent directors and wider practiced separation of the Chair and CEO positions. Internal control and the strategic role of the supervisory board are improving. A strategic issue is making use of hard law for competitive advantage;

3. Between company voluntarism and hard law lies “soft law.” The term covers national and international codes that involve voluntary adherence but are promulgated by bodies such as stock exchanges, securities dealers associations, NGOs, and intergovernmental institutions such as the OECD. IFRS voluntary adoption is of this character. Soft law retains flexibility of company voluntarism while benefiting from the external legitimacy and pressure of supra-company promulgation. MNCs can adhere but not implement in some instances; or look for operating locations with weaker standards. Management should set a strong standard of adopting best practices, bearing in mind the difficulty to date of establishing reliable empirical relationships with performance measures of various types. The influence of the society over companies increases while the soft law is adopted.

### **Summary**

Considering the presentation of supply chain and multinational companies’ governance, there are some ideas which should be underlined. Both systems are at the beginning, while corporate governance is the current practice within the business world. The development of this new field, inter-organizational governance, is important for practitioners and scientists, there are already many studies presenting possible scenarios for the evolution of this complex field.

Given the incipient phase of these governance systems, there are low transparency and low predictability regarding the development of practices within inter-organizational environments. Great companies were considered by citizens as poles of attraction for politicians and poles of power, being able to influence political decisions. If we recognize the new governance systems, there could be manifest transparent influence actions from supply chains and multinational companies to state governments.

Regarding governance research, supply chain research seems to underline on the importance of the relation between partners. Governance is a reaction obtained from the interaction of several partners. MNCs governance studies insist on the differences which exist within the same company in different countries: corporate governance systems, business cultures or business practices.

In conclusion, there are similarities between these two governance systems: the multitude of actors, of countries where economic activities are performed. Though, there is a great difference between how these multi-organizational structures are formed. We consider that this article provides one hypothesis, which should be

considered: if you are to study supply chain governance, there are several models and issues which are already studied within the MNCs governance field. For the future, our efforts will be focused on the study of supply chain governance, models and practices from MNCs governance can be considered.

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#### ZARZĄDZANIE ŁAŃCUCHEM DOSTAW I ZARZĄDZANIE W MIĘDZYNARODOWYCH KORPORACJACH - TEORETYCZNE PORÓWNANIE

**Streszczenie:** Globalizacja jest mierzona przez liczbę krajów, w których firmy mają oddziały. Obecnie na różnych rynkach, posiadanie zdolności produkcyjnych w krajach o taniej sile roboczej, lub zapewnienie bezpośrednich dostaw surowców, stanowią decyzje podejmowane przez wszystkie przedsiębiorstwa, które uwzględniają rozwój i siłę ich działalności. Celem niniejszego artykułu jest omówienie wyboru najlepszej opcji dla ekspansji jako mechanizmu zarządzania. Występują tutaj dwie alternatywy: po pierwsze jest to rozszerzenie przez przejęcie, po drugie, aby wprowadzić inny kraj w ramach partnerstwa. Biorąc pod uwagę prostotę ładu korporacyjnego, obie alternatywy zawierają elementy dodatkowe, tworząc w ten sposób bardziej złożone środowiska. Przedsiębiorstwa wielonarodowe (MNC) można dodać do prostego - krajowego ładu korporacyjnego w ramach kolejnych elementów: wielonarodowych systemów zarządzania, jego cech i form rozwoju, ale także lokalnych kultur biznesowych. Zarządzanie łańcuchem dostaw zawiera elementy przedstawione w MNC, inne należy natomiast uwzględnić jako formy: współpracy lub partnera władzy w związku.

Obie te złożone formy zostały zaprezentowane. Głównym wnioskiem jest to, że praktyki w zakresie ładu MNC mogą być wypożyczone do zarządzania łańcuchem dostaw. Niektórzy autorzy uważają, że łańcuchy dostaw są formą outsourcingu i unikają ładu korporacyjnego.

### 供應鏈治理模式及跨國公司的治理 - 理論比較。

摘要：全球化是衡量公司擁有子公司的國家。在不同的市場，廉價勞動力的國家或擁有強大的製造能力，確保直接供應的原料是所有公司考慮他們的業務擴展和功率做出的決定。這篇文章的目的是討論有關治理機制的擴展，如果被認為是選擇的最佳替代品。

存在著兩種替代方案：一種是通過收購擴大，另一種是通過夥伴關係進入另一個國家。考慮簡單的企業管治，這兩種選擇含有補充元素，打造以這種方式更加複雜的環境。

跨國公司（MNCs）的簡單-

國內公司治理的下一個元素：多的國家治理系統的特點和形式的擴展，但也當地的商業文化。供應鏈治理中包含的元素為跨國公司，而應考慮：各種形式的合作，合作夥伴的內部權力關係。

這兩個複雜的治理形式。得出的主要結論是可以借用的供應鏈治理，跨國公司治理實踐。一些學者認為，供應鏈外包的形式，從而避免了企業管治。