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CONTROL ISSUES IN MULTINATIONAL ORGANIZATION

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ABSTRAK

Globalisasi di dunia usaha bisnis meningkatkan peran penting pengendalian di organisasi atau perusahaan multinasional karena perbedaan yang dimilikinya dibanding dengan yang lokal atau domestik. Perusahaan multinasional mempunyai lingkungan usaha yang berbeda di dalam hal-hal tertentu, misalnya: cara mereka berkomunikasi untuk mengatasi perbedaan lokasi dan waktu, perbedaan cara pengukuran kinerja di antara kantor cabang perusahaan, dan budaya yang akan mempengaruhi cara berinteraksi. Faktor-faktor tadi akan tampak dalam hal pemilihan bentuk perusahaan, mekanisme pengendalian dan tingkat pengendalian di dalam kantor cabang. Hal yang penting bagi perusahaan multinasional dalam memilih bentuk kerja sama adalah tingkat kepercayaan, dan tingkat pemahamannya terhadap situasi dan kondisi kantor cabang atau anak perusahaan.

Keywords: MNC, Control, Organization Form

INTRODUCTION

There are many reasons for the company to do the business outside national boundaries. Looking for a new market is one example. Those business expansion are triggered by deregulation, cheaper transport, better communication systems and information technology development (Goodwin, 1998). Nevertheless, the last two factors have significant role which enable business globalization. Those factors eliminate time gaps and geographical distance. It is now possible to run a business as a worldwide network that enable individual task i.e. research and development, engineering, testing and manufacturing is done transnational (Drucker, 1998). Thus, such entity can design such product in USA and make certain parts or manufacturing in some Asian countries simultaneously by using that technology.

Nevertheless, globalization trend in business has impact in certain factors such as control and organizational form. According to Goodwin (1998), there is important issue in control of multinational company whether it is semi autonomous or strongly controlled by headquarter. Indeed, Rosenzweig and Singh (1991, p. 346) quote Caves (1971) and Hymer (1976) argument that control on foreign subsidiaries is prerequisite for foreign direct investment and become ongoing concern of the MNC.

The topic of control in multinational context has been becoming source of research and discussion. The recent studies provide better framework of control especially in international joint venture. Therefore Ricks et. al. (1990) assert that it is possible to assume that (a) a majority ownership does not reflect greater control, (b) high level of control does not assure succeed of joint venture (c) informal control mechanism is important.

This paper discusses the environment of MNC, the form of multinational organization and those factors that influence of choosing that form. It also illustrates relationship between trust and control in organization. Then describe the difference between MNC and local firm as well.

ORGANIZATIONAL ENVIRONMENT OF MNC

Multinational Corporation has unique position since it may be a single organization that operates in network systems around the world. However, it can not deny the influence of different national environments (Rosenzweig and Singh, 1991). The domains of the international environment are global competition, a global technology, and so forth. Rosenzweig and Singh (1991) argue that MNCs are facing two different requirements. As a part of worldwide network environment, they have to be consistent with the others. However, as the entities that operate in the national boundary they have to adapt the local institutional environment. The similar point of view is taken by Ghoshal and Nohria (1993) who call it as "forces for national responsiveness" and "forces for global integration".

Rosenzweig and Singh (1991) state that there are three approaches on the nature of organizational environment encountered by MNC. First approach sees MNC as a single entity that face global environment. This approach has weaknesses on assumption of homogenous and monolithic environment that unrealistic in nature.

The other approach thinks that MNC is sub-unit that operates entirely within a single nation. Therefore, this kind of MNC is very independent which rely on resource within national boundaries. The last approach in between those mentioned approaches. It stresses between global integration and national responsiveness.

The local environment has significant role on MNC operation in terms of technology transfer. The MNC tend to transfer its technology in the country that has high skilled labor, and high level fixed investment (Blomstrom & Lipsey, 1996). In the Mexican case, the role of local economic policies and market competitiveness have significant impact on the degree of technology transfer.

In term of adaptation of MNC into local environment, organizational theorists believe that organizational structure and the task environment are stable among those countries (Rosenzweig and Singh, 1991). Based on the research upon American, British and Canadian companies, Rosenzweig and Singh (1991) cite Hickson, Hinings. McMillan, and Schwitter (1974: p. 59) opinion that there is "culture free context of organizational structure".

Rosenzweig and Singh (1991) state that there are two factors that influence the consistency among entities in MNCs. The first, organizations structure replication. According to Brooke & Remmers (1970) cited by Rosenzweig and Singh (1991), there is a tendency for similarity between parent and foreign subsidiary called "mirror effect1. However that tendency has disadvantage in which the headquarters may force the foreign branch manager's to follow the other branch that perform well. Headquarter seems to omit the possibility of deviation due to local situation. The second factor, the important of control of foreign operation. The need to control foreign subsidiary has been prerequisite for foreign direct investment. Furthermore, it will become concern during the firm's life. Sometimes headquarter will somewhat loose their control toward foreign subsidiaries in case of the local government imposes law or regulation. The local authority may force MNC subsidiaries to adopt such portion of ownership or adopt such specific form of financial reporting (Rosenzweig and Singh, 1991). Therefore, according to Chowdurry (1992) contractual and inter-firm arrangement done by MNC is often aimed to overcome the restriction issued by host government.

ORGANIZATIONAL FORM OF MULTINATIONAL CORPORATION

According to Osborn and Baughn (1990, p.504), there are two common organizational forms of multinational relationship. Firstly, joint ventures that involving shared equity for both parents. Thorelli (1986) cited by Osborn and Baughn calls it as hierarchical dominated form. Secondly, contractual agreement that not involving shared equity. The last one can be found in the form of licensing, distribution, technical assistance, supply, and marketing agreement. Thorelli (1986) calls it as market-dom inatedform.

Kogut and Singh (1988) cited by Osborn and Boughn (1990) remark that joint venture has advantage in reducing opportunism possibilities may be found in contractual agreement since it provides share of ownership and control over the use and results of assets. The joint venture form also gives opportunity for better monitoring mechanism. Therefore, according to Harrigan in Osborn and Baughin article, in short term joint venture gives better protection and control, although at significant administrative cost.

Nonetheless, joint venture has disadvantages as well since it is considered as more difficult to establish, terminate and fundamentally difficult to change (Osborn and Boughn, 1990). Furthermore, multinational joint venture may need more effort and time in building a common hierarchy that relates the gaps of culture, linguistic and traditions of partners (Anderson & Gatignon, 1986; Hayashi, 1987; Moroi and Itani, 1987; Zimmerman, 1985 in Osborn and Boughn's article).

Some firms in high-tech area may choose joint R&D before move to more important commitment in the longer term. Then, both partner and parent will learn each other before make a decision to use it for other purpose (Osborn and Boughn, 1990).

According to Osborn and Boughn (1990), there are two different alliances based on the size of partners. First is neither or only one partner is great multinational. This condition brings the need of control, coordination, and protection since the economic success is important for the parent. The last, both partner and parent are giant multinational enterprises. They use the alliance to get potential market from both sides.

Das & Teng (1998) classify alliance into equity and non-equity. Equity alliance means that parent has role as shareholders of the joint venture. Non equity alliance means is more in the technical assistance, joint R&D, joint marketing, joint production, and so forth. In addition, some scholars (Das & Teng, 1998) categorize alliance structure into joint venture, minority equity alliances, and nontraditional contracts (non-equity alliances). Joint venture is known as new independent company that may run under parent's network. Parent's firms own several of the joint venture shares. Minority equity alliances involve share taking of the one of the partner. Whereas non-equity alliance has been described earlier.

THE REASON FOR CHOOSING FORM OF ALLIANCE

In term of relationship between technological intensity and the governance form of alliance, uncertainty and control have significant influence (Osborn and Boughn, 1990). Firms probably choose more hierarchical form as technological intensity increases as a result of higher cost for monitoring, enforcing, and regulating market-dominated mechanism (Jones, 1987; Williamson, 1985 cited by Osborn and Boughn). Therefore, Osborn and Boughn (1990) state that quasi-market arrangement would be the least preferred mode for transaction in technologically intensive product areas. Hopefully, in that form, the firms try to protect and control their technology in terms of knowledge, product and service. However, the parent companies may want to control what knowledge is transferred by using arm-length contractual agreement which seems to reduce possibility of transferring more technology than intended.

The other factor that is considered in choosing particular form is transaction cost. According to Chan (1995) transaction cost include the cost of negotiating and transferring information and capability to another firm, cost of personnel training, cost of losing opportunity to having direct sales or getting full amount of the agreement. Indeed, wholly owned subsidiaries are preferred when transaction cost is high. On the other hand, joint ventures are favored when transaction cost is low.

Kogut and Zander (1993) quote Hill, Hwang and Kim (1990) argument that decision to transfer technology in joint venture or wholly owned subsidiary depend upon the nature of knowledge to be transferred. The choice of wholly owned subsidiary may result in the lower transaction cost and earns more gain from technology owned.

According to Casson & Buckley (1998) the transaction cost relate to flexibility. More flexible the firm, higher transaction cost indeed. Flexibility means transitory relationship among suppliers and customers. This condition may encourage cheating conduct since their relationship is more remote. Indeed, Strong and Weber (1998) article states that probability partner may look for individual opportunity or will do moral hazard exist in all transactions.

TYPE OF CONTROL

In term of object of control, control in particular joint venture may be more complicated since joint venture operates separately from its parents. The object of control is not just how the joint venture will meet the partners' interest, also it has to make sure that the partners will not behave opportunistically. Das & Teng (1998) cite Hamel (1991) and Hennart & Reddy (1997) argument that many joint ventures are used by partners to cover their real aim that is to learn know-how and new technology from the other partners. According to Robinson (1998) the parent or technology provider want to protect its intellectual property right even setting a limit how and in what extent that technology can be used. In the other form of alliances, the object of control can be reducing by cutting opportunistic behavior from the partner. They tend to be simpler than joint venture since there is no new independence firms formed.

The type of control imposed in that kind of alliances are different. In joint venture case, it is possible to use both hierarchical control and ownership control. Hierarchical control is seen in the staffing, reporting structure, meetings and few more. Whereas ownership control is related to equity owned by partners. More equity owned means more voting power. However, according to Das & Teng (1998) the control level is not equivalent to one's equity share. In the minority equity alliance context, the ownership control has important role. Since there is no new separate firm formed, the hierarchical control can not be implemented. In the non-equity alliances neither hierarchical or ownership control is possible, since their relationship is more contract base. Therefore, they can use their contract (contractual control) to control the other partners behavior.

The case of exercise of ownership between partners in the join venture can be found in the Maruti Udyog case, a joint venture between Suzuki Corporation of Japan with Indian government (Robinson, 1998). Both partners hold 50% of company's equity that control 80% car market in India. They had conflicted on the new managing director appointment. The Indian government assigned that job to the person that is not qualified in the Suzuki's opinion. The Indian government thought that it was their right to appoint anyone they want, however Suzuki wanted to be confirmed beforehand. Finally, Suzuki brought this case into the International Court of Arbitration in Paris. This case bring the lesson to other parties who want to do business in India should have majority control unless they will face difficulties to control the joint venture.

TRUST AND CONTROL IN ALLIANCES

Das and Teng (1998) state that the partners' alliance should be confidence enough since there is a risk of opportunistic behavior from the partners that will reduce cooperation satisfactory. Das and Teng (1998) define the confidence as "firm's perceived certainty about satisfactory partner cooperation". A low level of confidence will create suspicion relationship that will effects on the level of succeed of the alliance.

The confidence has two sources, trust, and control (Das and Teng, 1998). In terms of control, according to Beamish (1988), and Sohn (1994) in Das and Teng (1998) article, the firms tend to be more confident to make an alliance when they have control on subsidiaries. Das and Teng (1998) distinguish control into control mechanism and level of control. In this case, control is considered as "any process in which one party affect the behavior of others". Whereas Sohn (1994) defined it as any process in which a firm determines or intentionally affects what others will do.

According to Das <fc Teng (1998) who cite some scholars, the second source of confidence is trust that is defined as "the degree to which the trustor holds a positive attitude toward the trustee's goodwill and reliability in a risky exchange situation". Furthermore, Das & Teng quote Luhman's opinion (1979) that trust can be used for eliminating transaction complexity and gaining positive expectations. Strong

and Weber (1998) argue, that in international business transaction, trust is preconditional aspects of cooperation.

Das and Teng (1998) state that there are three reasons why trust and confidence is different. First, trust concerns to expectations about positive motives, on the other hand confidence refers to certainty about cooperative manner. Second, trust is part of the confidence, since there is other important part which is control. Both are complementary. Therefore, it is possible for the firms to cooperate even with low level of trust since they can use and develop appropriate control. The last, as implication of its difference, both have different ways to develop. Confidence can be improved by using control mechanism. On the other hand, trust. will be strengthening by looking for the track record of those who perform well and by using objective evaluation.

KNOWLEDGE AS A CONTROL TOOL

Even the equity position has important role as described above, there is another tool for control mechanism. Sohn (1994) argues that social knowledge can be used as complementary control mechanism for MNC in managing foreign subsidiaries. Social knowledge is defined by Tolbert (1988) in Sohn's article (1994) as "one's ability to understand and predict other's general pattern of behavior". Therefore Sohn (1994) cites Ouchfs argument (1980) that social knowledge relates to trust which can be close to clan. If control using social knowledge available thus it will allow MNC to reduce equity ownership as means of control. Research, shows that Japanese foreign direct investment tend to hold lower equity involvement than other countries (Sohn, 1994). To get lower share, they will gain from financial resources that can be invested in more subsidiaries. Moreover, some host governments propose local partner as a requirement for foreign direct investment. Therefore it is well accepted by host government to invest in some, subsidiaries or affiliates shared with local partners. To do so, the host government often gives economics an/or political concession to the MNC (Sohn, 1994). Thus the social knowledge can be used to accommodate host government demands without losing control.

Krackhardt (1990) quoted by Holm et. al. (1995) shows that accurate understanding of subsidiaries network will gain possibilities of a control network action. How important the subsidiaries for headquarter will influence level of control as well. (Holm etal'., 1995). Subsidiaries may have different network context since they operate in the different environment. Nevertheless, control problem will depend on the long-term network importance. Headquarters' knowledge of subsidiaries tends to be accurate on the most important subsidiaries.

THE DIFFERENCES BETWEEN MULTINATIONAL COMPANY AND DOMESTIC FIRM IN TERMS OF CONTROL ISSUES

Some people argue that they multinational company have some differences toward the local entity. One argument comes from Johnson and Scholes (1998) who state that in term of product and geographic market, coordination of operational logistic across national and across different business. Rosenzweig and Singh (1991) quote Mascarenhas (1982) argument, state that multinational enterprise has different complexities compare to the domestic company in maintaining control. It has difficulties in areas of communication, performance evaluation and culture gap between headquarter and subsidiaries.

Communication

Due to different geographic and language among headquarter and subsidiaries, it needs communication tools that enable them to keep in touch each other. Headquarter can obtain up to date information from the subsidiaries which help them to make appropriate decision in timely manner. In this case, the advanced technology of computer and communication has significant role behind the trend of globalization (Goodwin, 1998).

Another problem of communication is language. Since the MNC operate throughout the world with different languages, the problem of communication both oral and written will exist.

Performance Evaluation

Subsidiaries can be evaluated by using financial indicator gathered from their financial report. According to Goodwin (1998) the standardization of subsidiaries financial reporting is needed as way of unifying financial reporting process and reduce IT support cost since it can be replicated in some subsidiaries without addition of support team.

However in case of currency conversion into one strong currency such as US dollar, it has weakness of exchange rate fluctuation. The presence of this factor certainly influences the performance of the subsidiaries financial report in positive or negative way. Therefore when the currency is converted (time of conversion) is critical point on performance evaluation.

The manager of subsidiaries that operate in Asian countries may not show good performance since the currency crisis in those areas makes their revenue fall towards USD.

Though they sell those products exceeds the planned budget, if it is converted into USD, it will look very disappointing. On the other hand, the manager of subsidiaries that use strong currency will look better although they can not fulfill amount targeted. Then this case brings message to managers that their reward in unfair since they have to bear uncontrollable factor that is currency fluctuation. As suggested by Atkinson and Kaplan (1998, p.682) reward measurement system should reflect fairness unless it will fail to motivate the managers. Thus, performance evaluation in the MNC is more complex than the domestic entity.

Culture Gap

Cultural differences between headquarter and subsidiaries may influence the way of interaction, and control as well. Subsidiaries are likely to adapt to local condition when internal consistency is not critical (Rosenzweig and Singh, 1991). Some people argue that national culture has impact on the behavior of organization and individuals within (Pavett and Morris, 1995). That difference will lead to uncertainty that is important consideration whether or not the firm would engage in multinational business (Weinzimmer, 1996).

Pavett and Morris cite Addler and Doktor (1989) statement, argue that culture induces the subsidiaries through societal structures such as laws, politics, values, and behavior. Indeed, Adler and Bartholomew (1992) quoted by Pavett and Morris (1995) assert that "culture makes a difference". The same idea is stated by Kleinberg (1991) in Pavett and Morris (1995) article who call it as "culture matters". Furthermore, parent nationality affects what types of organization structures, management processes, personnel practice and managerial culture predominate (Johansson, et.al., 1997).

CONCLUSION

Multinational corporations are influenced by the environment where they live and the headquarter policy. Rosenzweigh and Singh (1991) and Ghoshal and Nohria (1993) argue that MNC is facing two different requirements. First, the need to be consistent with network and the other is adaptation to the local environment. There are some forms of Multinational Corporation. Osborn and Boughn (1990) distinguish it into hierarchical dominated form and market dominated form. Furthermore, Das and Teng (1998) classify alliance into equity base and non-equity base. The reasons for choosing form are influenced by technological intensity, transaction cost and the nature of knowledge to be transferred (Osborn & Boughn, 1990; Chan, 1995, Kogut & Zander, 1993).

Confidence that comprise of trust and control has important role in partner relationship. Lack of confidence may result on the failure of alliance (Das & Teng, 1998). Indeed, knowledge of subsidiaries business context can be used as complementary control mechanism (Sohn, 1994).

Some people argue that there are differences between multinational and domestic company. Johnson and Choles (1998) underline product and geographic market differences. Furthermore, Rosenzeigh and Sings (1991) state that they differ in the area of communication, performance evaluation and culture.

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