Network Governance and Organizational Forms: Captive to the Past or Rational Reconstruction? A Framework for Assessing what Works Best!

Abstract

This paper provides an overview of key factors to consider in assessing the merits of alternative network governance structures for inter-jurisdictional alliances and networks. The analysis draws on transaction cost economics, strategic management theory, social network theory and agency theory to propose a comprehensive framework for assessing the relative merits of various organizational forms and governance structures. It reports on the application of the analytic framework to one case and applies it retrospectively to an earlier case study. This analysis suggests that for a governance form to emerge and thrive, it must address problems of adapting, coordinating, and safeguarding exchanges and fulfilling accountability expectations more efficiently than other governance forms. Exchange conditions interact with local needs, social and accountability mechanisms to inform a decision as to whether a network is better governed by a particular organizational form.

The primary determinants of organizational form, in which two or more organizational entities govern their combined or collective efforts to advance common interests or objectives, should be the efficiency and effectiveness of the particular organizational form and governance structure in managing and governing those collective efforts, the transactions between them, the frequency of those transactions, the enduring nature of their common interests, the degree to which they interact with common or shared third parties, the degree of responsiveness to local needs and changing business environments, the range of social mechanisms necessary to safeguard the assets, exchanges and reputation of the organization and provide proper accountability to stakeholders. Organizational forms commonly used to advance collective interests range on a continuum from loosely knit 'horizontal' coalitions of independent organizations with informal links, to tightly knit 'vertical' organizations with 'wholly-owned' subsidiaries or satellite/branch offices.

Literature Review

Oster (1996) surveyed 61of the largest national U.S. networks. She found, among other things, that two-thirds operated with a franchise model (e.g. UW, YM/WCA, Red Cross, Scouts) as opposed to a wholly owned subsidiary (corporate) model (e.g. Save the Children, Amnesty, many International Aid Agencies). The franchises contributed an average of 1.2% of their revenue to the national umbrella organization, sometimes based on a sliding fee schedule related to budget and type of revenue. Among the largest twenty, the use of the franchise form was even more common, at close to 90% of the total. She also found an average of 461 affiliates in franchise models compared to an average of 9 branch offices in corporate models. Oster compared the relative advantages of the franchise model versus the corporate model on five traits: reputation, fundraising, access to capital, managerial performance and reliance on volunteers. She found that the corporate model performed somewhat better than the franchise model on safeguarding reputation and fundraising, while the franchise model significantly outperformed on the other three traits.

Jones, et.al. (1997) conducted an extensive review of the literature on network governance including a review of definitions of the term from the perspective of different disciplines. They adopted the following as the working definition for development of a general theory of network governance: "Network governance involves a select, persistent and structured set of (*relations between?*) autonomous firms (or nonprofit agencies) engaged in creating products and services based on implicit and open-ended contracts to adapt to environmental contingencies and to coordinate and safeguard exchanges. These contracts are socially, not legally binding." (Jones et. al. 914) They offer a theory of network governance that integrates transaction costs economics and social network theory. They argue that the interactions of exchange conditions (demand uncertainty, task complexity, human asset specificity, frequency) interact with social mechanisms (restricted access, macro culture, collective sanctions) to determine the degree of 'structural embeddedness' in the relationships between autonomous partners.

Widmer and Houchin (1999) surveyed 55 national U.S. networks. They found, among other things, that 54% had organizational members only (e.g. Boys and Girls Clubs, United Way, Mental Health, Planned Parenthood, YM/WCA), 32% had both organizational and individual members (e.g. Big Brothers/Sisters, Girl Scouts, Gray Panthers), and 14% had only individual members (e.g. Red Cross, Boy Scouts and Lung Association). They identified a "continuum of 'affiliations' in which member organizations' very existence is dependent on and extensively proscribed by their relationship with the national organization. Affiliates' identity and mission are established by the national organization and member organizations could not continue work under the same name if they were no longer affiliated. On the other end are "associations" whose members could continue to exist under the same name and with the same mission whether they belong to the national organization or not." (p.12)

Edgar (2002) consolidated the findings from reviews of eight umbrella or network organizations (three of which were conducted by this author). The organizations that were examined include the Canadian Council for International Cooperation, the National Action Coalition on the Status of Women, the Canadian AIDS Society, the National Audubon Society, Amnesty International Canada, New Brunswick Environmental Network, the First Nations Environmental Network and the government – Environmental Non-governmental Organization (ENGO) relationship in the Netherlands. The organizations were reviewed with the objectives of identifying effective network governance structures and practices, and identifying means of achieving mutually satisfactory links between government and the ENGO sector on policy issues.

Sauve (2002) developed a framework for analysis of network governance drawing on transaction cost economics and strategic management theory incorporating principles of efficiency and effectiveness. He defined network governance as "the institutional matrix that encapsulates the configuration of multi-stage business arrangements between autonomous partners within a strategic network." He then applied the analytic framework to two stylized agrifood businesses. He concluded that the unique contribution of network governance to management, production and supply is the combination between a configuration of decentralized decision rights unified around strategic purposes guided by principles of efficiency and effectiveness.

Gill (2004) reports on a literature review on partnerships. I adopted a three-dimensional typology of partnerships developed by Torjman. *Consultative* relationships are established to seek advice or input from experts, other stakeholders or the public. *Operational* partnerships are work-sharing arrangements in which the components of a given task are delegated to specific parties. *Collaborative* partnerships are set up to share resources, risks and decision-making.

In Gill (2005) I offered a classification system for organizational form and ownership structure, based on board selection, as one of several factors that influence governance practices. This typology included collectives, self-regenerating boards, funder appointed boards, chartered or affiliate organizations, membership elected boards (co-operatives and federated models), constituency elected, publicly elected and mixed selection processes in which the board selection process is critical to identifying organizational ‘ownership’ and appropriate lines of accountability.

Mollenhauer (2006) surveyed twenty-one national non-profit networks in Canada to identify key characteristics of successful network governance. She defined a not-for-profit federation “as a network or partnership that includes a national or provincial organization, affiliate branches and/or some form of local and/or regional bodies that share a mission, brand and program model and have some legal independence from one another”. She did not distinctly categorize different organizational forms, but placed the sample organizations on a continuum from loose, autonomous to highly centralized governance structures. She ascribed the benefits of federations, regardless of where they fit on the continuum, as consistency in services and products; greater accountability; increased synergy; higher levels of corporate/donor support and stewardship; stronger advocacy; reduced duplication; increased credibility; shared best practices; and national and international connection and affiliation. She, like Widmer and Houchin, concluded that a continuum of loosely knit to closely held organizations, rather than a distinct typology, best expressed the nature of the complex forms of networks or federations.

Renz (2006) draws attention to the decreasing autonomy of individual organizations and boards in local service delivery as community agencies form alliances or partner in collaborative networks that guide and coordinate services across organizational boundaries. He describes this emerging phenomenon as individual organizations exercising their mandates from multiple centers of activity…within a broader strategic framework in pursuit of a common, community rather than organizational, overarching vision. They are “linked via a web of strategic relationships in which power comes from non-formal relationships among the various people playing leadership roles in the multiple centers of activity. These are systems of organized (but not hierarchical) influence and engagement…that moves the locus of control beyond any one organization. Consequently boundary-spanning simultaneously causes boundary-blurring where it becomes increasingly difficult to tell where one organization’s work ends and another’s begins.”

Discussion

The governance of networks is perhaps one of the least studied fields of nonprofit governance. While Oster’s work draws a clear distinction between franchise and corporate organizational forms, the end of the continuum with the most formally embedded structures, it does not extend the typology to the other end of the spectrum represented by loose coalitions and points in between. Nor has there been much attempt to examine governance of networks in local communities or regions, where some of the more loosely structured networks evolve to coordinate services and resources to those jurisdictions or to specific target populations. This paper is an attempt to move the yardsticks forward in development of a typology that identifies the specific points on the continuum that are sufficiently distinct to warrant separate categorization. Like most typologies, the boundaries between them will not always be so distinct as to entirely avoid overlap.

Definition of Key Theoretical Constructs

A **transaction cost** (as contrasted with cost of production) is a cost incurred in making an economic exchange. In modern economies, transaction costs have become equally (and perhaps more) important than production costs (Williamson) as noted in the increasing business preoccupation with supply chain management. Transaction cost economics (TCE) is concerned with understanding how transaction costs affect organizational structure and governance arrangements. "The driving force affecting the choice of governance arrangements is the desire to economize on the total cost of services, including costs associated with contractual hazards and the costs of institutional arrangements designed to address such hazards." (Joskow: 96)

Strategic Management Theory is about scoping the environment (SWOT analysis) to provide a foundation for the formulation and implementation of strategies and structures to gain competitive advantage in the pursuit of objectives, products, markets and profits or consumer benefits. (Wikipedia references)

Social Network Theory views social relationships in terms of nodes and ties where the attributes of individuals are less important than their relationships and ties with other actors within the network. Nodes are the individual actors within the networks, and ties are the relationships between the actors. There can be many kinds of ties between the nodes. In its most simple form, a social network is a map of all of the relevant ties between the nodes being studied. The network can also be used to determine the social capital of individual actors. (Wikipedia references)

Agency Theory in economics is the problem of motivating one party to act on behalf of another, known as 'the principal-agent problem'. The principals do not know enough about whether (or to what extent) a contract has been satisfied. The solution to this information problem is to ensure the provision of appropriate incentives so agents act in the way that the principals wish. It involves changing the rules of the game so that the self-interested rational choices of the agent coincide with what the principals desire. Agency theory is concerned with resolving two problems that can occur in agency relationships. The first is the agency problem that arises when (a) the desires or goals of the principal and agent conflict and (b) it is difficult or expensive for the principle to verify what the agent is actually doing. The second is the problem of risk sharing that arises when the principal and agent have different attitudes towards risk. (Eisenhart 1989)

Networks

Networks, for the purposes of the framework presented here, are defined as being generally comprised of autonomous or semi-autonomous organizations engaged in selective relationships formed to create products or services or accomplish specific goals. They may be based on agreements that range from the morally or socially binding to more formal legally binding agreements that either guide or regulate patterns of interaction, power relationships, decision-making authority, incentives and control mechanisms, dispute resolution, response to environmental contingencies, and the contribution, use and exchange of resources. "Networks can be seen as a combination of governance structures, with multilevel relationships between horizontally or vertically-related entities. Network governance is an institutional structure for defining a process for collective action (or strategy)…enabling the assurance, at the lowest cost, that the individual behavior of partners follows the rules for collective action…and mitigates the contractual hazards between them." (Sauve:2)

Networks may evolve organically or be developed intentionally for a variety of purposes. These may include one or more of the following:

- Sharing information, ideas, insights, experiences and skills through a broader network than may be available to individual partners
- Consultation on matters of common interest
- Building consensus on matters of common interest
- Partner, member, community or public education
- Coordination of services, research, policy positions or advocacy
- Achievement of more widespread reach than can be achieved by the participant members independently
- Accomplishment of objectives beyond the scope of individual members
- Generating greater effectiveness and strength through broader constituencies
- Providing greater credibility and/or profile around a particular issue or cause
- Increasing solidarity and mutual moral and psychological support among members
- Division of tasks and responsibilities in pursuit of mutually agreed goals
- Sharing or pooling of resources (adapted from Cecchini et. al. 2000:11)

They may encompass a broad array of organizational forms that range on a continuum from informal coalitions to more formal legal 'partnership', charters or affiliation agreements, franchises and even corporate subsidiary forms. They do not usurp, or intrude upon, the essential independence or autonomy of the participant organizations in the more loosely knit networks. However, at the other end of the continuum (franchises and corporate subsidiaries), there are distinct constraints on the autonomy of local units. This paper provides an overview of key factors to consider in assessing the merits of alternative organizational forms and network governance structures for inter-jurisdictional networks. The analysis is based on transaction cost economics, strategic management theory, social network theory and agency theory.

Factors that influence organizational form

Gill (2005) identified board selection processes (organizational ownership), legislative mandate, mission and values, developmental stage, size and complexity, financial circumstances, geographic scope and critical events or transitional phases as key factors influencing the form or structure of individual organizations. This paper introduces additional important determinants that need to be considered in constructing the governance of networks.

Key determinants of organizational form, in which two or more organizational entities govern their combined or collective efforts to advance common interests or objectives, should be the ***efficiency and effectiveness*** of the particular organizational form in managing and governing those collective efforts, the nature of transactions between them, the frequency of those transactions, the enduring nature of their common interests, the degree to which they interact with common or shared third parties, and the range of social mechanisms necessary to safeguard the assets, exchanges and reputation of the organization. *Efficiency* is a ratio of input to output assessed against some industry standard or performance benchmark. *Effectiveness* is a measure of goal attainment, with service providers/producers and consumers or other stakeholders often having different perceptions about whether or to what degree goals have been achieved.

"For a governance form to emerge and thrive, it must address problems of adapting, coordinating, and safeguarding exchanges more efficiently and effectively than other governance forms." (Jones et. al. 917) This current paper inserts the concept of local needs into the framework developed by Jones, et. al. so that exchange conditions interact with local needs and social mechanisms to inform a decision as to whether a network is better governed as an informal coalition, alliance or partnership, or a more formal federated, franchise or corporate organizational structure.

Alternative Structures for Network Governance

Organizational forms commonly used to advance collective interests range on a continuum from loosely knit 'horizontal' coalitions of independent organizations with informal links to tightly knit 'vertical' organizations with 'wholly-owned' subsidiaries or satellite/branch offices. These forms are commonly known as ***coalitions, alliances, partnerships, federations, franchises*** and ***corporations***.

Coalitions are typically loosely knit, informal agreements among separate, independent organizations struck for the purpose of cooperating or collaborating in a joint action, each in their own self-interest, to advance a particular common cause or interest. It is an *ad hoc* grouping of organizations united for a specific purpose…usually to coordinate efforts around a ***single issue or cause***. The collaborative efforts may be a temporary matter of convenience or endure for some time, but the agreement is not entrenched in a formal legal structure. There may or may not be a fee to join, and a requirement to commit to certain principles. Members are free to leave the coalition at any time. Sometimes, such groups are quite diverse in mandate but hold some degree of passion or conviction about a specific matter of common interest. Sometimes, their differences might make them appear to be 'unlikely bedfellows'. Each entity within the coalition uses its own resources to advance the cause, often within a generally agreed strategic framework developed through frequent communication, thereby gaining the synergistic effects of collaborative action without inter-organizational exchange of resources.

Alliances are more enduring *informal agreements* between organizations to collaborate in their efforts to advance a ***range of specific interests*** based on common values and goals. Resources are pooled on an ad hoc basis but not exchanged between members. In an early stage of development, leadership and administrative support may rotate between members. As the alliance matures, a single member may host administrative support and coordinate activities. Leadership typically rotates based on expertise, resource capacity and interest in a particular aspect of the alliance's pursuits. Administrative and secretarial support may rotate with the leadership, or be hosted by a single 'sponsoring' organization that may also receive and hold funds in trust for the alliance.

Partnerships may be defined simply as 'collaborative ventures between two or more organizations that pool resources in pursuit of common goals and objectives, share risks and rewards (benefits), and share authority, responsibility and accountability (in and for decisions and actions)'. (Cecchini, et. al. 7) Members of a partnership retain their separate identity but are committed by informal or legal agreement that describes certain rights and obligations, the nature and purpose of the partnership, the relationship of partner organizations to the partnership, the distribution of power, rewards and liabilities as well as the terms of withdrawal from or dissolution of the partnership. Partnerships may be consultative, operational or collaborative. They often occur in local communities with a limited number of partners…the type of network or alliance that Renz (2006) described as emerging in local communities or regions and which I would refer to under this framework as consultative, operational or even sometimes extending to collaborative partnerships within the context of the Torjman typology (Gill 2004).

Partnerships, like all relationships, are organic by nature. They evolve and change over time depending on the common interests or issues that bring partners together, the level of trust, the constellation of leadership and commitment at a particular moment, the immediacy of issues that are their focus, the resources that are available to support their efforts and the shifting priorities of the respective partners. Partnerships may be the most appropriate characterization of network governance at the local community level. They may take the form of interagency agreements, implicit or explicit, to coordinate services. Coordination may be arranged through coordinating/planning committees that involve board representatives or management committees with executive staff of the agencies, or both.

A recent example of a successful partnership can be found in the joint fundraising efforts of the Toronto Canadian Opera Company**,** the Art Gallery of Ontario**,** the Royal Ontario Museum**,** the Royal Conservatory of Music and the Gardiner Museum which have together raised $742.2-million (85% of their combined goal) for their simultaneous expansion and renovation projects.

Federations (Latin: *foedus*, covenant) typically emerge from an initial agreement between one or more separate and autonomous organizations to contribute (usually through membership fees) to the advancement of certain common interests and accomplish together, what they cannot achieve as efficiently or effectively alone. They might, for example, support research, education, advocacy, development of professional or practice standards. This organizational form is a formal ***association*** of independent organizations that incorporate a new legal entity whose 'ownership' is vested in the member organizations (or individuals), and is exercised through a board of directors that is elected or appointed by that membership. They are bound together for specific purposes by reciprocal obligations and benefits, in an umbrella organisation which has rules identifying conditions of membership and its termination, distribution of power and resources, and how they will be governed and financed.

Members may be autonomous provincial/state, regional or local branches/chapters or special interest constituencies of a provincial or national organization or association or some mix of these. These organizations are typically created ***bottom up*** by members who may be grassroots (e.g. environmental networks), local (e.g. service providers), provincial/state (e.g. industry, professional or service associations), or national umbrella groups such as associations of other multi-member associations (e.g. Canadian or American Society of Association Executives).

The umbrella federations may be provincial/state, national or international governing bodies. The independence of the component organizations is constitutionally entrenched and may not be altered by a unilateral decision of the central body. Members are free to discontinue that membership at their discretion, sometimes with a specified notice period.

Franchise (Chartered) organizations are comprised of a provincial/state, national or international organization that establishes or creates local affiliates – chapters or branches – '***top down***' under the umbrella of the constitutional documents/bylaws of the provincial, national or international entity defining how it is organized and governed and its rights, duties, privileges and obligations. They share a mission, brand and program model and have some legal independence from one another. Local affiliates may hold their legal status solely through the umbrella organization or may incorporate and attain nonprofit and charitable status within their own jurisdiction. The central organization may be governed by a self-regenerating board, election of directors from individual members of the organization, or elections based on some jurisdictional formula for representation of the local affiliates. In some instances, provision may be made for election or appointment (by the board) of 'members-at-large' to complement the skill sets of representatively elected directors.

The component or member organizations may have exclusive decision-making authority or jurisdiction with respect to certain matters…such as local service needs identification, service delivery, staffing and fundraising…that may not be exercised by the umbrella (national, provincial, or state) body. The central governing body may have exclusive jurisdiction to represent the interests of its members to outside organizations or governments, may set minimum standards for services by it constituent organizations, approve or withhold the use of its trademark and name, offer certain administrative, procurement or professional services (e.g. pensions, information technology, equipment purchasing, referral services, best practice standards, information sharing and networking) that may be more economically delivered through a central body. (e.g. United Way, Planned Parenthood, international service clubs like Lions and Kiwanis, Amnesty International, United Negro College Fund, and many international aid agencies.)

This organizational form is favored because of its enhanced capacity to attract volunteer support, donor commitment, and to respond with flexibility and nimbleness to changing environmental influences and challenges within the smaller local, regional or provincial/state jurisdiction. "National operations invest in system-wide activities: the development of a national brand and reputation, creation and supply of administrative systems, communications, and standards (or best practices) supports. Local affiliates conduct the operational work of the organization." (Oster, 85) The franchise system has been described as a form of organizational structure that 'weds a knowledgeable big-time operator with an entrepreneurial (more nimble) local operator'. (Oster, 87)

The franchise system has four basic characteristics (Oster, 84):

1. "The franchiser transfers to the franchisee the exclusive right to use a trademark or sell a particular product (or service), usually within a specific geographical jurisdiction.
2. In exchange, the franchisee pays the franchiser a fee that may involve some initial lump sum and typically an ongoing fee keyed to the level of business.
3. The franchiser provides some assistance, typically on technical or operating matters, and maintains some control on the way in which the business is operated.
4. Any residual revenue surplus or shortfall from the franchise operations accrues to the benefit or responsibility (detriment) of the franchisee."

Corporate model networks have 'wholly owned' subsidiaries…satellite or branch offices. They are characterized by a single-tier governing body, sometimes elected by representatives of local operational units, with full authority for all decisions, determination of products and services, establishment of standards, quality and administrative systems, collection of all revenues, payment of all costs, and allocation of all charitable revenues. There is typically no local governing or advisory body and less local management discretion than in a franchise operation, although there may be a continuum ranging from entirely central decision-making and operational/asset control to some delegation of responsibility for local needs identification, fundraising and advocacy to local advisory committees. The corporate model tends to offer less flexibility for response to local conditions and is often encumbered by slower hierarchical decision processes. (e.g. VON Canada, MS Society of Canada, Sierra Club)

Mixed Organizational Forms

Then, of course, there is the ubiquitous mixed organizational structure often combining franchise and corporate model features, straddling the line between federation and franchise structures, and sometimes even blending features of federations and partnerships. In organizations that have a mixed membership model (both individual and organizational members) this adds to blurring of direction, authority and lines of accountability.

Much of the confusion around network governance has resulted from failure to distinguish between discreet characteristics of organizations at various points on the 'federation' continuum. The next section of this paper examines the characteristics that differentiate between the franchise and corporate organizational forms at the more centralized end of that spectrum, in which local operations relinquish certain aspects of their autonomy.

Comparative Analysis of Franchise versus Corporate Structures

"Environmental uncertainty triggers adaptation, which is the 'central problem of economic organization' because environments are rarely stable and predictable. Asset specific (or customized) exchanges involve unique equipment, processes, or knowledge developed by participants and exchanged between them. This intensifies the need for coordination between parties. Customization of exchange commodities, combined with uncertainty, requires safeguarding exchanges through reducing behavioral (compliance) uncertainty.

"For a governance form to emerge and thrive, it must address problems of adapting, coordinating, and safeguarding exchanges more efficiently than other governance forms. Exchange conditions interact with local needs and social mechanisms to inform a decision as to whether a network is better governed by a federated, franchise, corporate or some other model." (Jones, et. al. 916-917)

Exchange Conditions

1. A large number of local delivery sites;
2. Demand uncertainty combined with stable supply;
3. Exchanges high in customized or specialized products or services;
4. Complex tasks integrating diverse specialists; and,
5. Frequency of exchanges between parties comprising the network.

Local Needs

1. High dependence on volunteers;
2. Product, service or management flexibility;
3. Assessment of managerial performance;
4. Access to capital;
5. Dependence on fundraising to support local operations; and,
6. The kind and quality of product or service and its association with trademark (brand) reputation.

Social Control Mechanisms

There are several social control mechanisms, short of structural integration, that can accommodate local needs while still recognizing the importance of exchange conditions that influence the need for interaction between components of a national organization. These are:

1. Common values;
2. Common goals and objectives;
3. Restricted access to membership;

4. Development of a macro culture of shared commitment to common values, objectives, behavioral norms and performance standards;
5. Collective sanctions for transgression of norms; and,
6. Reputation and trademark of the national body

Analysis

Exchange Conditions

1. The **number of local operational or delivery sites** is an important consideration in determining the degree of structural integration. Oster offers strong evidence that the larger the number of local community (branch or affiliate) operations necessary to deliver a product or service, the stronger the arguments in favor of a franchise model as opposed to a vertically integrated corporate model.

2. **Demand uncertainty** "can come from customers, suppliers, competitors, regulatory agencies, trade agreements, unions, financial markets" or other environmental influences. Stable supply combined with high demand uncertainty is cause for avoiding vertical integration. "Under conditions of demand uncertainty, firms disaggregate into autonomous units, primarily through outsourcing or subcontracting. This *decoupling* increases flexibility—the ability to respond to a wide range of contingencies—because resource bundles, now exchanged or rented rather than owned, can be cheaply and quickly reallocated to meet changing environmental demands." (Jones, et.al. 918-9)

3. **Labor supply: "**Network governance is found in industries with high levels of demand uncertainty but a relatively stable supply of labor. Demand uncertainty is generated by unknown and rapid shifts in consumer preferences; rapid changes in knowledge or technology which results in short product lifecycles and makes the rapid dissemination of information critical; and, by seasonality which makes vertical integration inefficient. *"In essence, demand uncertainty with stable supply provides conditions amenable to networks and markets but inimical to vertical hierarchies." (Jones, et. al. 919)*

4. **Task complexity "**refers to the number of different specialized inputs needed to complete a product or service. Task complexity creates behavioral interdependence and heightens the need for coordinating activities. Differing specialists and inputs may result from an increased scope of activities, number of business functions needed, number of products created, or number of differing markets served. Task complexity under time pressures makes coordinating through a series of sequential exchanges between network affiliates unfeasible. Time pressures are due to the need to reduce lead-time in rapidly changing markets." (Jones, et. al. 921)

Highly customized (specialized) products, services or staff derive from participants' knowledge culture, skills, routines, and teamwork often acquired through 'learning-by-doing'. "Such exchanges create dependency between parties. For example, if the buyer decides not to purchase the customized product or service, the seller cannot sell or transfer the product or service easily to another. Customizing products or services increases demands for coordination between parties. It also raises concerns about how to safeguard these exchanges since customizing products or services makes both seller and buyer more vulnerable to shifts in markets." (Jones, et.al. 919)

Exchanges of highly customized products or services may require an organizational form that enhances cooperation, proximity, and repeated exchanges to effectively transfer knowledge and resources among parties. Cooperation among exchange parties is necessary because parties must work together to gain knowledge or market advantage. "Since 'human assets' may quit the exchange or diminish their efforts, they are more dependent upon one another's cooperation to complete the exchange. Demand uncertainty pushes firms toward dis-aggregation while customized or specialized products intensify the need for coordination and integration among parties. *Network governance balances these competing demands by enhancing the rapid dissemination of knowledge across organizational boundaries."* (Jones, et. al. 920)

5. Frequency of Exchanges Among Parties

Frequency concerns how often parties exchange knowledge, human assets or other resources or services. "Due to the costs of specialized governance structures, TCE assumes that they are used only when there are recurring exchanges. However, frequent exchanges not only justify, but enable using inter-firm networks as an alternative governance form." (Jones, et. al. 922)

Interaction Effects of Exchange Conditions

"No single exchange condition propels the emergence of network governance. A combination of specific conditions is required for network governance to emerge and thrive as an organizational form that offers comparative advantages over markets and hierarchies.

These conditions involve high adaptation needs due to changing product demand, high coordination needs due to integrating diverse specialists in complex tasks, high safeguarding needs due to overseeing and integrating parties' interests in customized exchanges.

These exchange conditions inhibit use of market mechanisms because complex, customized exchanges are not adequately safeguarded or efficiently coordinated among parties. The exchange condition of flexibility needed in rapidly changing markets inhibits use of hierarchies, even though they may facilitate complex, customized exchanges. The central point is that network governance balances competing demands of these exchange conditions." (Jones, et.al. 923)

Local Needs

1. **High dependence on volunteers –** A major determinant of voluntary effort is the volunteer's perception of influence over the composition and allocation of the organization's output…very remote in a centrally controlled organization.

2. **Product, service or management flexibility –** is greater in autonomous or franchise structures than in hierarchical, corporate models.

3. **Assessment of managerial performance**. There is greater capacity to assess managerial performance with a local governing body that is closer to the action…to the services and to their impact on the community. A local governing body can provide a more effective interface between the service and the community than a more remote, centrally governed corporate hierarchy. Local 'advisory' bodies do not meet the test of local governance and often confuse accountability relationships.

4. **Access to capital**. Local sources of capital financing tend to favor organizations with local governance accountability.

5. **Dependence on fundraising to support local operations.** Although local donors may favor locally controlled organizations, their contribution decisions may also be influenced by the reputation of a national brand. Solicitation of contributions from national corporations, foundations, grant makers, government contractors, or donors seeking national profile is likely to be more effectively coordinated through a national structure.

6. **The kind and quality of product or service and its association with trademark (brand) reputation.** Local organizations gain substantial prima facie credibility from association with a highly reputed national brand. This may be an important factor in gaining an initial foothold in a local market, but may be less critical for an established organization with a credible local presence. Nevertheless, dissociation from a national brand may have a deleterious effect, at least in the short-term, in a highly competitive market.

Interaction Effects of Local Needs

Oster (p. 87) compared the corporate and franchise models on five 'local needs' factors. She rated the performance of the corporate model as 'good' at safeguarding reputation and 'coordinating fundraising activities'. The franchise model was rated as only 'fair' on these factors. However, the difference on the other three factors: 'access to capital', 'assessment of managerial performance', and 'encouragement of volunteers' was more significant. The effectiveness of the corporate model on these factors was rated as poor, while the franchise model was rated as good. She also concluded that the latter offers substantially greater flexibility than the former.

Social Mechanisms

Common values are the filter through which goals are established and the glue that brings organizational leaders together and maintains their solidarity in the face of external challenges.

Common goals and objectives establish the basis for coordination of efforts in mission-driven organizations. These are critical to the development of common interest alliances but provide less incentive for collaborative action than other social mechanisms that follow in this discussion.

Restricted access is a limitation in the number of exchange partners within a network. Fewer partners who interact more often reduces variance in expectations, skills, and goals that parties bring to exchanges. This facilitates mutual adjustment and permits exchange partners to learn each other's systems, develop communication protocols, and establish routines for working together, all of which enhance coordination. "*Restricted access reduces coordination costs for parties with customized, complex exchanges and enhances safeguarding of customized exchanges for parties in rapidly changing markets and therefore the likelihood of network governance emerging and thriving in rapidly changing markets for complex, customized tasks.*" (Jones, et.al. 928)

Macro culture is a "system of widely shared assumptions and values comprising industry, occupational, or professional knowledge that guide actions and create typical behavior patterns. This knowledge base is derived from fundamental assumptions about customers, competitors, suppliers, and society. It specifies roles, role relationships and conventions — accepted approaches and solutions to problems. The presence of a macro culture reduces coordination costs for customized, complex exchanges." (Jones, et. al. 929-31)

Collective sanctions involve group members punishing other members who violate group norms, values, or goals. They safeguard exchanges and define and reinforce the parameters of acceptable behavior by demonstrating the consequences of violating norms and values. (Jones, et. al. 931-32)

Reputation "involves an estimation of an organization's character, skills, reliability, and other attributes important to exchanges. Reputation is important under exchange conditions of uncertainty and customization. As environmental uncertainty increases, exchange parties' become more concerned with information about their own and others reputation. (Jones, et. al. 932-3) "*Reputation is the central strategic asset, embodied in the name and trademark, that national organizations either franchise or hold corporately, and that the reputation of the whole is quite vulnerable to malpractice by a local affiliate or franchisee.*" (Oster, 88)

Interaction Effects of Social Mechanisms

"The congruent and mutually reinforcing interaction of these social mechanisms in network governance promotes cooperative behavior. Restricted access, macro culture, and collective sanctions act to preserve and enhance reputation, decrease coordination costs and safeguard customized exchanges in rapidly changing markets." (Jones, et. al. 933-4)

Oster (87-94) provides some evidence that the corporate form is, at least marginally, more effective in preventing loss of reputation and coordinating fund-raising but that the franchise model is significantly more effective in improving access to capital, monitoring and assessing the performance of local management, and encouraging volunteer support.

Structural Integration

"The interaction of exchange conditions — demand uncertainty with stable inputs, customized goods/services requiring high levels of specialized products, services and staff, complex tasks requiring diverse specialists, and frequent exchanges — promotes greater structural integration among exchange parties." (Jones, et. al. 923-4)

"Structural integration provides the basis for social mechanisms to adapt, coordinate, and safeguard exchanges; thus, its presence enhances the likelihood of network governance emerging and thriving in rapidly changing markets for complex, customized tasks.

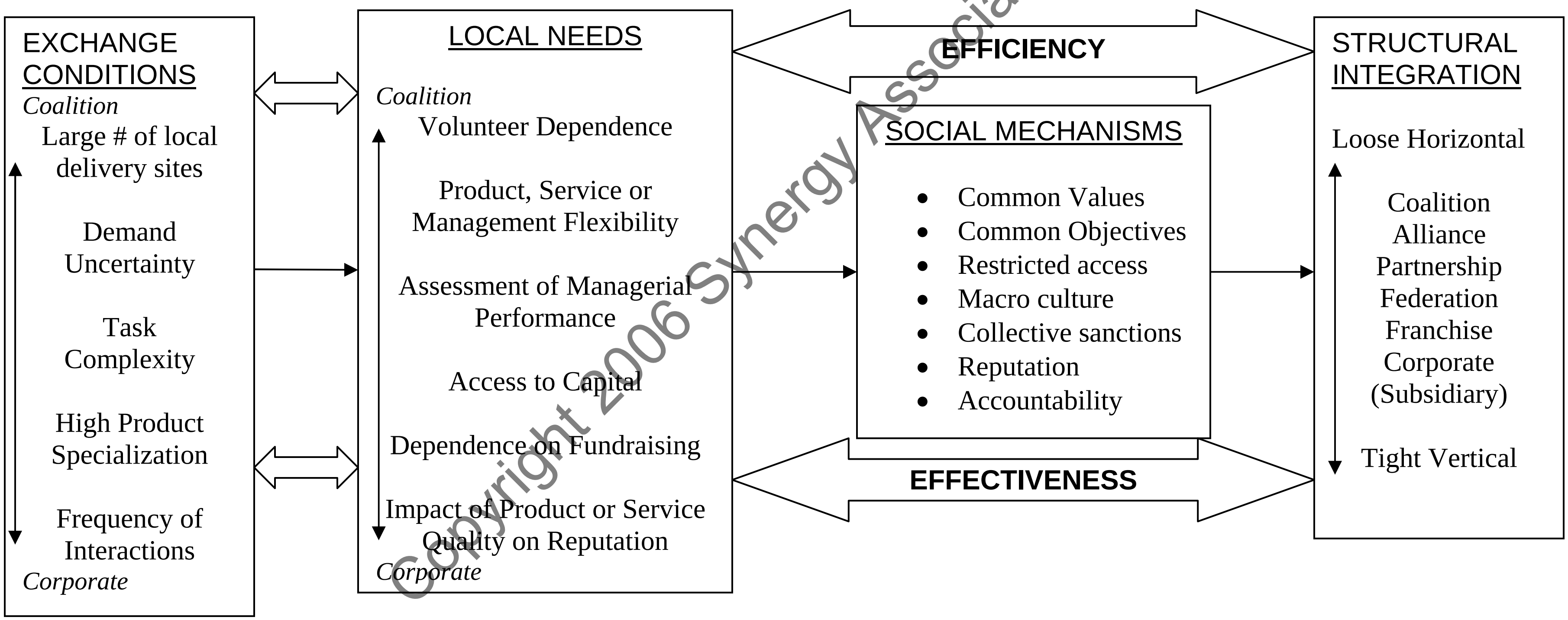
"Too much or too rigid structural integration may create its own set of problems…feuding, choking off of novel information from other parts of the industry, and welfare-like support of weak network members.

The optimal level of structural integration in terms of overall fitness of the network may be in an intermediate range where parties are neither too tightly connected to fragment social connections nor too loosely connected that they are unaware of who has information to provide, or who knows whom in order to request the information. The optimal level of structural integration may be determined by network size." (Jones, et. al. 925)

An Integrating Framework

This framework was developed in response to a request from a client to research the advantages of a franchise structure over a corporate structure. It seemed to me that the TCE/social network framework developed by Jones, et. al. could be adapted to incorporate concepts from the work that Oster had done on the comparative advantages of a franchise versus wholly owned subsidiary model in responding to specific (local) needs. A further overlay of Sauve's work integrating TCE with strategic management theory, thereby placing efficiency and effectiveness solidly within the analytic framework, also seemed to make some sense. My own additions to these concepts are modest, with the exception perhaps of presenting them somewhat more concisely and creating the resultant synergy. The following chart outlines the framework that developed out of this work.

Chart 1 – Efficiency and Effectiveness in the Interaction of Exchange Conditions, Local Needs, Social Mechanisms & Structural Integration[1]



[1] Adapted from Jones, Hesterly & Borgatti (1997) and Oster (1996).

This framework was then applied to the circumstances that my client was confronting. An outline of those circumstances and our analysis along with a retrospective application of the framework to one of my earlier organizational consultations follows.

Case Studies

Ottawa Branch, Victorian Order of Nurses of Canada

The Victorian Order of Nurses of Canada was incorporated in 1897 in Ottawa to provide nursing services in the community. During the next two years branches were also established in Toronto, Montreal and Halifax. VON Canada evolved from an early partnership between theses branches to a franchise structure with branches across the country. The central body provided support for branding, training, practice standards, pensions and government relations, and over time acquired the right to disenfranchise branches. Local boards governed the franchises, employed management and staff, managed their own payrolls, planned and operated services, raised funding locally for capital and ancillary operations, and nominated a representative to the national body. By 2005 VON Canada had annual revenues of approximately $250 million, about 8% of which emanated from service contracts held by the Ottawa branch.

In the late 1990's a number of branches verged on insolvency because of revenues lost as a result of a strike of their nursing staff. VON Canada dissolved the boards of those branches and took over their operations as wholly owned subsidiaries with local advisory committees. In the ensuing years they decided to transform their organizational structure and implement a corporate model in which all branches would be directly operated as subsidiaries with all revenues flowing to the national body, which would employ all staff and direct operations through regional management teams. The remaining 'franchises' were asked to conform to this direction, with a considerable additional financial contribution to the national to cover revenue shortfalls resulting from the earlier insolvencies, or signal their intention to give up their franchise rights.

The board of the Ottawa branch analyzed its options with the assistance of this framework. They concluded that the move to a corporate organizational form with centralized governance and administration would not serve the best interests of current and future clients of the local operation on the basis that the franchise model would have been preferred due to the large numbers of local delivery sites, high demand uncertainty over time, strong needs for volunteer engagement (in services or fundraising[2]), managerial flexibility, management oversight, and access to capital funds.

They concluded that the conditions that might have favored the corporate model (high product specialization, high adaptation needs due to changing product demand, high coordination needs due to integrating diverse specialists in complex tasks, high safeguarding needs due to

[2] They had in fact been raising as much or more money locally as had all of the rest of VON Canada.

overseeing and integrating parties' interests in exchange of specialized products or services and protecting reputation) were not consistent with their perception of local needs and efficient, effective operations.

They consequently opted to abandon their VON franchise, maintain local control and re-incorporate as Carefor Health and Community Services.

Canadian Environmental Network (CEN)

The CEN is a national environmental non-governmental organization (ENGO) with some 700 organizational members in its affiliates. It functioned until 2002 with a federation structure with eleven provincial/territorial affiliates and a national 'First Nations' affiliate. Membership in the provincial/territorial affiliates was organizational, but the members of affiliates also received membership status in the CEN. The First Nations affiliate[3] had only individual memberships. The CEN operated on a core contribution agreement from Environment Canada, project revenues and modest membership fees. The core contribution agreement accounted for two-thirds of its revenues in the worst of years and as little as twenty percent in the best of years. The national body transfers a substantial portion of its core funding to affiliates to support their operations.

Financial struggles at the national and affiliate levels, internal divisions, high executive turnover and eroding credibility caused the organization to restructure in 2002. It eliminated individual memberships causing the withdrawal of the First Nations affiliate. First Nations people now participate through the member organizations of the remaining affiliates. The CEN continues with a federation structure which has elements of a franchise model, with central influence (rather than control) based on memorandums of understanding regarding use of the 'pass-through' funding for core operations. Affiliates operate with a federation model uncompromised by transfer of funds from the provincial body to its members.

Analysis of the current structure through the lens of the framework provided in this paper might lead to the conclusion that the CEN and its affiliates have, under the circumstances, struck a reasonable balance between local (regional) needs and efficient/effective operations in which social controls operate to bring cohesion to a grassroots movement in pursuit of common objectives based on common values, a large number of local delivery sites, demand uncertainty and the need for frequent transactions/communications combine to favor a federation structure.

Conclusion

In my experience as a member of many boards, as CEO of a large nonprofit and as a consultant I have found little interest in theory and theoretical frameworks unless they hold the promise of practical application and utility. The integrated framework presented in this paper is an attempt to move theoretical constructs a little closer to practical use.

[3] See Edgar 2002 for more detailed cases studies on the First Nations affiliate and the New Brunswick provincial affiliate.

It was used successfully to guide the deliberations of the board of a local VON franchise operation confronted with a gut-wrenching decision about abandoning a one hundred year historical relationship with a brand it had helped create and grow…versus abandoning local control in responding to local needs. If not instrumental in the final decision-making then it certainly helped the board members' conceptualization of the issues and affirm their instincts on the matter. Retrospective application of the framework to the CEN revealed nuances that I had not seen as clearly when I was engaged in my organizational development work with that organization.

Further research and practical application will be necessary to test whether the typology of organizational forms is sufficiently comprehensive or unnecessarily elaborate, and whether the analytic framework can be used to guide nonprofit networks in determining an organizational form appropriate to their circumstances. It will then stand or fall on its merits and assessment the many members of our national and international network neighborhoods.

One of the other important issues that has surfaced again in some of the works cited in this paper is whether mixed membership models (individuals, organizations or larger groups of organizations) actually create the ambiguity in mandate, roles and accountability relationships that I believe they do. Again, further research will be necessary to test this hypothesis and examine whether there is a place for that variable in this integrated framework.

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NOTE: This was presented in summary form as a keynote address at the "*Networks, Stakeholders and Nonprofit Organization Governance: Whither (Wither?) Boards*", Conference for Practitioners *and* Researchers, Convened by The Midwest Center for Nonprofit Leadership, University of Missouri - Kansas City and The Nonprofit Quarterly, April 26-27, 2007

Network Governance & Organizational Form:

Captive to the Past or Rational Reconstruction?

A Framework for Assessing What Works Best.

2008 Congress of Humanities and Social Sciences:

Association for Nonprofit and Social Economy Research

Vancouver, June 4 to 6, 2008

Mel Gill, President, Synergy Associates

Network Governance

OBJECTIVES of Presentation & Paper

- Advance understanding of network forms and governance structures
- Describe pertinent theoretical constructs
- Develop typology of primary network forms
- Examine key factors affecting network structures & their inter-relationships
- Articulate a framework for integrating these concepts into an analytic tool of practical value

Background

- VON Canada > Ottawa Branch
  - •Founding member 1897
  - •Four original partners
- National franchise network: 2005 $250M
  - •Ottawa 8% of total
  - •Insolvency of some branches > nurses strike
  - •Corporate shift: wholly owned subsidiaries
- Request for advice for Ottawa Branch

Theoretical Foundation

Transaction Cost Economics

Strategic Management Theory

Social Network Theory

Agency Theory

Transaction Cost

- Cost incurred in making an economic (or any other) exchange to which a cost can be attached
  - In contrast to costs of production
- How these affect organization structure and governance arrangements
  - Economy & Efficiency in achieving aims & controlling contractual hazards in relations between members of a network

Strategic Management

- Environmental scan as foundation for
- Formulation of strategies and structures
- In pursuit of objectives
  - Products
  - Markets
  - Profits
  - Consumer benefits

Social Network Theory

- Focus on relationships between, rather than attributes of organizational leaders
- Social network mapping
- Social capital
- Gladwell > ‘Connectors’

Agency Theory

- **Principal / Agent**
  - Motivating one party to act in interests of another
- **Problems**
  - Goals/desires of the principal and agent conflict
  - Agent has more information than principal
  - Insufficient information for principal to verify
  - Different attitudes or incentives related to risk

Networks

- Autonomous or semi-autonomous multi-level (vertical/horizontal) organizations
- Forming selective relationships to create products, services or accomplish goals
- Beyond the reach of individual orgs
- Socially to legally binding that
- Define process for efficient & effective
- Collective action

Networks Regulate

- **Power relationships**
  - Decision-making authority
- **Incentives and control mechanisms**
  - Dispute resolution
- **Response to environmental contingencies**
  - Patterns of interaction
- **Contribution, use and exchange of resources**

Collective Action >

- Information sharing
- Consultation
- Consensus building
- Education (member or public)
- Coordination of tasks, services, policies, research, advocacy, etc.
- Strength in numbers
- Division of tasks and responsibilities
- Sharing or pooling of resources

Network Structures

Coalitions

Alliances

Partnerships

Federations

Franchises

Corporate

Coalitions & Alliances

- **Coalitions**
  - Bottom-up morally or socially binding
  - Loose knit collaboration
  - Single cause with common self-interests
  - Discretionary membership
  - No pooling of resources
  - Action within broadly defined strategic framework
- **Alliances**
  - More enduring informal agreements on range of issues
  - Ad hoc pooling, but no exchange, of resources
  - Rotating leadership and administrative support
  - May be single organizational sponsor/host to hold funds

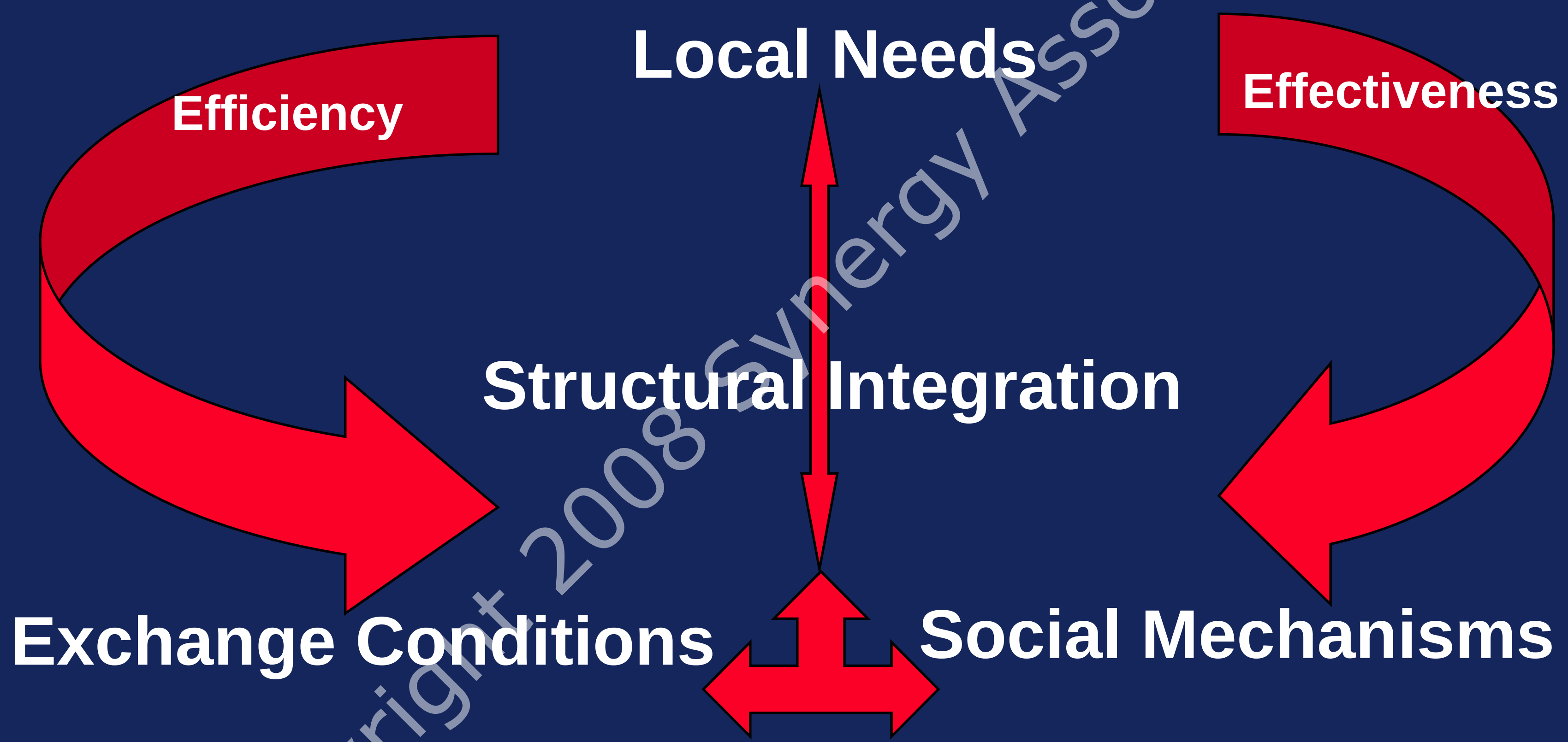
Partnerships & Federations

- **Partnerships**
  - Shared authority, responsibility, accountability & risk
  - More enduring morally or legally binding agreements
  - Clear terms of participation and termination of membership
  - Limited number of partners
  - Consultative, operational or collaborative
  - Community service planning/coordination
- **Federations (covenant)**
  - Autonomous organizations incorporate new legal entity
  - Formal ‘bottom-up’ democratic governance structure
  - Voluntary membership (terms of participation/termination)
  - Membership fees support collective activities
  - Grassroots, local, regional, national, international umbrellas

Franchise & Corporate

- **Franchises**
  - ‘Top-down’ chartered branches/chapters/affiliates
  - Affiliates incorporate under umbrella or in own right
  - Constitutionally entrenched, terms of trademark use, operational standards, rights, responsibilities and obligations
  - Center (network-wide) vs. affiliate (local operations) division of responsibilities
  - Representative governance
- **Corporate (wholly owned subsidiaries)**
  - Central governance, standards & operational guidance
  - No local governance
  - Less local management discretion
  - Slower hierarchical decision processes
- **Mixed Models**

Analytic Framework



Local Needs

Coalition

Volunteer Dependence

Product, Service or Management Flexibility

Assessment of Managerial Performance

Access to Capital

Dependence on Fundraising

Impact of Product/Service Quality on Reputation

Corporate

Exchange Conditions

Coalition

Large # of Local Delivery Sites

Demand Uncertainty

Task Complexity

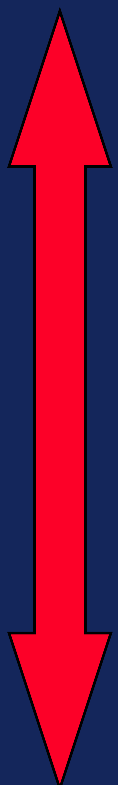
High Product Specialization

Frequency of Interactions

Corporate

Social Mechanisms

Coalition



Corporate

Common Values

Common Objectives

Restricted Access

Macro-culture

Reputation

Accountability

Structural Integration

Coalition

Corporate

Coalitions

Alliances

Partnerships

Federations

Franchises

Corporate Subsidiaries

Mixed Forms

Structural Integration Premises

- *"Demand uncertainty with stable inputs, customized goods/services requiring high levels of specialized products, services and staff, complex tasks requiring diverse specialists, and frequent exchanges promotes greater structural integration*

- *Structural integration provides the basis for social mechanisms to adapt, coordinate, and safeguard exchanges*

- *Too much or too rigid structural integration may create its own set of problems…feuding, choking off of novel information from other parts of the industry, and welfare-like support of weak network members"*

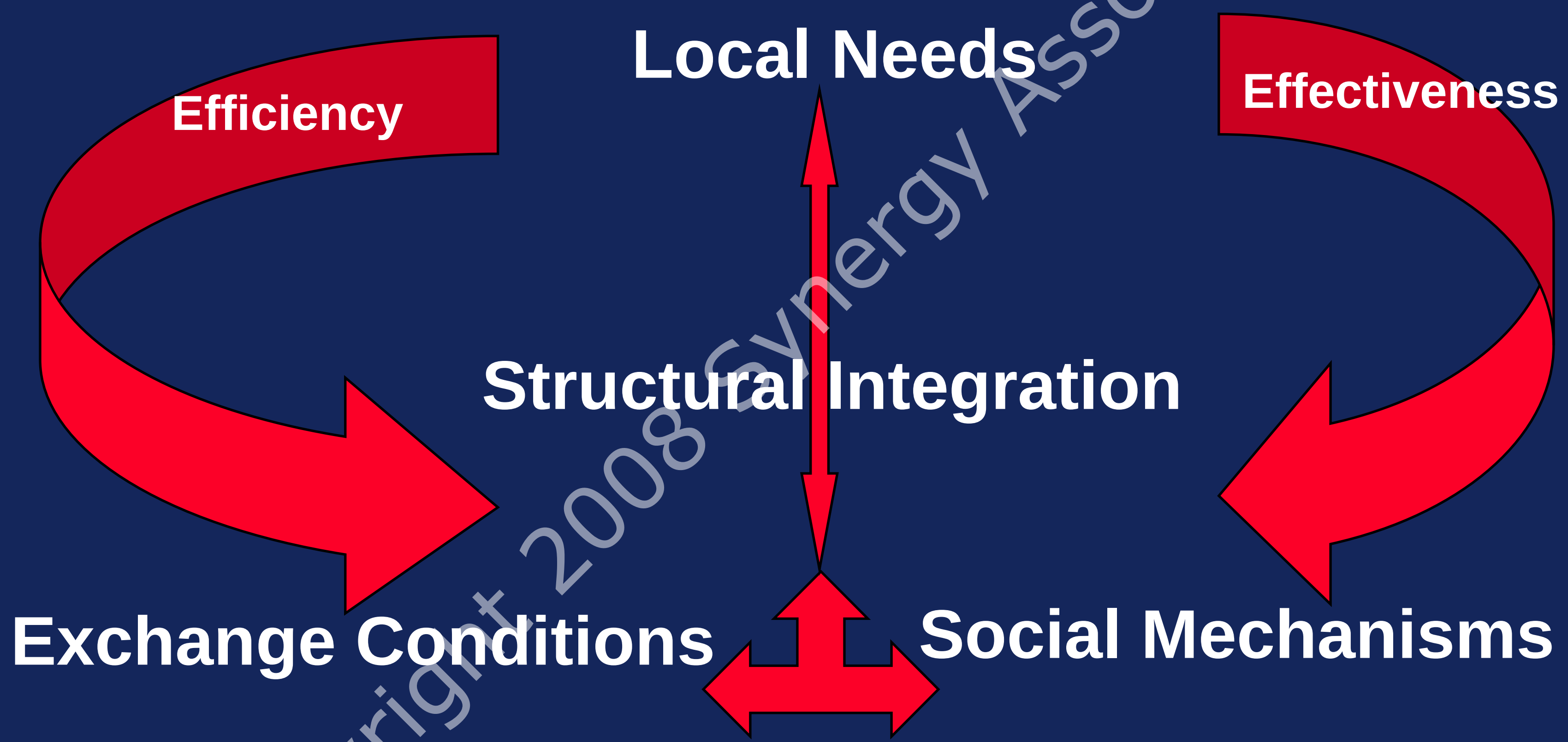
Jones, et. al.

Structural Integration Premises

- ***The optimal level of structural integration in terms of overall fitness of the network may be in an intermediate range where parties are neither too tightly connected to fragment social connections nor too loosely connected***

- ***'For a governance form to emerge and thrive, it must address problems of adapting, coordinating, and safeguarding exchanges more efficiently than other governance forms. Exchange conditions interact with local needs and social mechanisms to inform a decision as to whether a network is better governed by a federated, franchise, corporate or some other model.' (Jones, et. al.)***

Integrating Framework



Carefor Health & Community Services

● Franchise pros

- Large # sites
- High demand uncertainty
- High volunteer needs
- Management flexibility
- Management oversight
- Fundraising (capital & operational)

*** Preferred option**

● Corporate pros

- High product specialization
- High need to adapt to changing demands
- High need to coordinate diverse specialists & complex tasks
- High safeguarding needs

*** Not consistent with local needs**

Thank You!

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