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1

Introduction: Governance and Contracts in Strategic Alliances

Africa Ariño¹ and Jeffrey J. Reuer²

Alliance research and practice have developed considerably in the last decade, and this book focuses on the governance and contractual foundations of alliances. This general topic has always been central to the alliance literature (Reuer, 2004; Shenkar and Reuer, 2005) and has been the subject of many of the seminal writings in the field. It is also an area that has recently seen interesting contributions as scholars have developed new theories on the design and management of collaborative agreements, and as empirical evidence has accumulated from progressively more detailed investigations of strategic alliances.

While alliance governance and contractual forms are very much related, they are also distinct in scope as well as in the purposes they serve. *Governance* refers to ‘alternative institutional modes for organizing transactions’ (Williamson, 1979: 234), and prior research in the alliance literature has developed many insights into the problem of governance in this business context. Considerable research, for instance, has been devoted to the question of when firms should use alliances over acquisitions in order to enhance organizational efficiency. A second, related stream of research has examined when various forms of non-equity, or purely contractual, alliances are preferable to equity alliances such as joint ventures or partial acquisitions. By contrast, a *contract* determines ‘the specific exchanges negotiated by trading partners and the allocation of risks and trading gains resulting from them’ (James, 2000: 48). Governance form solves the broader boundary of the firm problem, whereas contractual form specifies terms of trade and the allocation of decision rights.

Although related, there is not necessarily a one-to-one relationship between governance and contractual forms, although this is commonly the assumption in alliance and other studies on organizational governance over the years. On the one hand, there is substantial contractual heterogeneity within particular governance forms. On the other hand, some contractual clauses are as likely to appear in some governance structures as in others, such as in equity and non-equity alliances. Furthermore, it appears that

alliance governance and contractual forms share few determinants (for a revision of empirical work that supports these statements, see Ariño and Reuer, 2005). The two are distinct features of alliance design that deserve more research attention, and only recently have scholars begun to assemble the data necessary to understand the details of alliances' contractual foundations and consider how dimensions of alliance contracts relate to broader governance modes, informal mechanisms of governance, and other aspects of alliance design and management.

This volume results from a conference on 'Strategic Alliances: Governance and Contracts' held in Barcelona, Spain at IESE Business School, University of Navarra, in June 2005. The aim of the conference was to gather a group of distinguished scholars to discuss papers and ideas around firms' investment decisions related to alliances as well as the design and management of collaborative agreements. The conference followed a format that provided more room for extended, focused discussion than is often the case at large conferences. The call for papers was deliberately centred around a few major themes related to the governance mechanisms and contractual underpinnings of alliances. We invited a group of scholars known for work on these topics across a wide array of disciplinary perspectives.

The conference was kicked off with a practitioner panel on the content and process issues associated with alliance contracting. This panel offered managerial and legal practice perspectives to which subsequent discussions related. So as to incite discussion around the conference's themes, we decided to depart from the customary format of paper presentation followed by discussion. Instead, the paper presentations were grouped around common themes and had a panel-like format. One person served as a facilitator for each panel, setting the stage for a fruitful discussion of the papers presented, and offering an integrated view of the set of papers that highlighted the intriguing aspects the papers offered when considered jointly. Twenty-three papers were presented at the conference. After a process of self-selection and revision overseen by the facilitators, this volume includes twenty of the papers. Aiming to reach a broader audience than specialized journals, we asked the authors to remove technical details that would be appropriate in other outlets and – within space limits – to be more extensive in discussing their research questions and theoretical ideas.

Overview of the volume

The structure of this volume reflects the two major conference themes: alliance governance (Part I) and alliances' contractual underpinnings (Part II). The different weight of the two parts is but a reflection of the relatively less research attention that alliance contracts have received. Below we offer some highlights from these two parts of the volume and point out some of the broader themes that emerged from the conference.

Chapters in Part I on the governance of strategic alliances reflect a number of important topics, or sub-themes, that exist in the alliance literature and are topics of considerable on-going research. The first one that is explored in Chapters 2–4 concerns alliances as discrete governance structures. All three chapters focus on the alliance itself and the project underlying the collaboration as the unit of analysis:

- Garrette, Dussauge and Castañer reflect on the case in which firms' overall resource endowment is too limited for them to undertake a desired project on their own. The opportunity for collaboration through scale alliances stems from the existence of potential partners with similar needs. They suggest that scale alliances are most likely formed by weaker firms for whom the alliance is an alternative to carrying out a project autonomously. Their chapter is part of a series of papers that carefully distinguish alliance types and motives rather than aggregating together very different types of collaborations.
- Mulotte, Dussauge and Mitchell consider the project of entering a new business domain, be it a new industry or a new geographic market. In line with the previous chapter, the authors argue that the choice between autonomous and alliance-based entry is affected by pre-entry resources. Because alliance-based entry requires a lesser effort, it may inhibit a firm's ability to create a full set of the new resources required to succeed in the long run, however.
- Grandori and Furlotti broaden the spectrum of governance choices and suggest that strategic, project-based alliances involve a nexus of legal, organizational and social mechanisms. They argue that alliances are not well framed along the continuum of hierarchical versus market governance or along the continuum of relational versus obligational contracting. In line with our earlier claim that there is not necessarily a one-to-one relationship between governance and contractual forms, they propose that contracts are not necessarily coordination devices that are close, similar or consubstantial to markets; rather, contracts contribute to defining and protecting important features of interfirm organizational configurations.

A second sub-theme revolves around the governance mechanisms underlying strategic alliances. Chapters 5–8 are related to this topic. While the first two chapters focus on factors driving the choice of ownership level, the latter two examine how governance choices influence technology exchange and knowledge transfer:

- Kale and Puranam assess the extent to which choice of equity ownership level in exchange partners is influenced by considerations related to resource and exchange attributes. Their findings show that the influence of the former is stronger than that of the latter.

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- Richards and Indro also consider ownership characteristics in the context of alliances that involve the government as a partner. In addition to offering empirical evidence of conditions under which a government is more likely to be a partner in a joint venture, they suggest that when governments do get involved in alliances, those in developed countries are more likely than governments in emerging economies to take a dominant role.
- Tallman and Phene examine characteristics of partners and alliances in order to explain the choice of governance mechanisms in the biotechnology industry. Coordination issues appear to be more relevant than appropriation concerns, maybe because of the strength of intellectual property protection mechanisms in this sector. Cooperative arrangements with technologically similar partners may be an effective way to exchange technology in industries with characteristics similar to those of biotechnology.
- Oxley and Wada provide evidence that indeed alliance governance and contract structure have a significant influence on knowledge flows. Interestingly, while alliance-related knowledge transfers increase the more hierarchical the alliance structure is, unrelated knowledge flows are reduced when licensing occurs within the context of a joint venture.

The discussion naturally moves into the dynamics of governance choices, the third sub-theme around which Chapters 9–12 revolve. Governance-related choices constitute a sequence, and early choices influence subsequent ones:

- Agarwal, Anand and Croson assess the effect of previous alliances on acquisition performance based on an experiment they reported. On the one hand, they find that alliances may not be beneficial to a subsequent acquisition because replacing confrontational routines that develop in an alliance setting is more difficult than creating appropriate new routines once an acquisition has taken place. On the other hand, they find that the prior social contact that an alliance enables has a positive impact on acquisition performance.
- Vlaar, Van Den Bosch and Volberda challenge the notion that alliances are a discrete governance decision. They introduce the concept of *governance trajectories*, which implies that partners align firm and transaction characteristics with a series of governance decisions in order to optimize alliance performance throughout its entire lifetime.
- Cuypers and Martin look at international joint ventures from an options perspective. They discuss empirical evidence that real option logic applies when uncertainty is exogenous, but not when uncertainty resolves endogenously. They compare real options arguments about the role of exogenous uncertainty with other theories (e.g. transaction cost theory, agency theory and bargaining).

- Koenig and Mellewigt argue for the need to clarify the relationships between uncertainty and governance. Toward this end, they provide a classification of uncertainty types, uncertainty effects, and governance mechanisms, and this classification allows them to offer a number of propositions on how uncertainty affects governance choice using transaction cost economics, real option theory, and the resource-based view of the firm.

Finally, the fourth sub-theme concerns relational governance. Chapters 13–15 relate to the emergence and use of relational norms:

- Poppo and Lambe explain the development of relational norms as a mechanism that eases adaptation to unexpected changes and events. They argue that the processes and factors that influence perceptions of relational norms change over time. They propose and test a theoretical framework that considers the differential influence of uncertainty reduction factors and emotional factors in the development of relational norms in younger and older exchange relationships.
- Hoetker and Mellewigt examine the conditions under which the use of formal, contractual mechanisms and the use of relational mechanisms are preferable. The nature of the assets involved in an alliance – in terms of property-based versus knowledge-based assets – is a key contingency that determines the optimal configuration of those mechanisms. They find that while the two types of mechanisms may coexist, they are not interchangeable as the most effective means of governing an alliance depends upon the type of assets involved.
- Svejenova, Koza and Lewin propose an enforcement framework that differentiates between trust and trust-like mechanisms that can generate reliability and predictability of partners' cooperative behaviour. These mechanisms include partners' social and legal embeddedness, and the existence of ownership relationships, and may allow the initiation of a relationship in the absence of a common relational history.

Chapters in Part II take up the contractual underpinnings of strategic alliances. This set of chapters collectively suggests that reliance on relational norms is compatible with reliance on detailed contracts, and the papers examine some of the implications of the interplay between relational and formal governance:

- Ring identifies a number of economic and psychological dimensions that define different kinds of contracts, and he discusses the contracting processes that produce these kinds of contracts. Given the uncertainty involved in strategic alliances, the contracts that govern them have

to provide for means for governing conduct in the uncertain future, as well as evidence of the intentions of the parties about these matters at the time of contracting.

- Mayer suggests that the role of contracts goes beyond protecting the parties and ensuring enforcement of an exchange, as conventional views of contracts would emphasize. Contracts allow the parties to share enough information that they can understand each other's needs and ensure that their interests are protected. In this way, more detailed contracts can help facilitate relationship development.
- Wakeman focuses on patent rights in the context of alliances involving biotechnology start-ups. He examines how the strength of patent rights affects the timing, choice of partner, and structure of the alliance contract as reflected by financial terms and allocations of control rights.
- Ryall and Sampson examine the question of whether prior relationships complement or substitute for formal governance. They do so by exploring if and how formal terms in technology alliance contracts vary with prior alliances – either with a specific partner or more generally. Their empirical results suggest that the informal governance inherent in interfirm relationships has different effects on formal governance depending upon whether these relationships are on-going or past.
- Argyres and Mayer discuss how firms learn to design their contracts, a process that can take a long time for firms in young, high-technology industries. Patterns of learning to contract are reflected in the evolution of contractual provisions over time, and this learning may result in the development of firm-specific contract design capabilities that may become a source of competitive advantage.
- Ariño, Ragozzino and Reuer examine the experiences of small firms in renegotiating their alliance contracts. Their findings show that although small firms are no more or less likely to renegotiate alliances than other firms, they tend to adjust their alliances less in the face of governance misalignments. In addition, small firms make higher levels of transaction-specific investments without introducing appropriate contractual safeguards, which can trigger contractual renegotiations at later stages of an alliance development.

Conclusions

Several themes emerge from this collection of papers, and they all deserve more attention in future research. First, we see more and more studies that offer detailed investigations into the governance mechanisms supporting interfirm collaborations. This partially reflects growing maturity in the alliance field more generally, and it contrasts the comparatively broad treatments of alliance governance in some of the seminal works in the field. As noted earlier, alliance governance was typically examined through the use

of coarse categories such as alliances versus M&A, equity versus non-equity alliances, and the like. Addressing these alliance investment and design choices has been, and will remain, very important in the literature, yet studies are increasingly examining specific features of alliance governance such as ownership levels, allocations of control rights, and so forth. Studies appearing in this volume have begun to examine what explains why firms use particular governance mechanisms in alliances, and in future research scholars might examine the implications of these choices and how they relate to other alliance phenomena such as process dimensions of collaboration and the organizational and managerial context of alliance formation and management (e.g. the structure of the alliance group, knowledge management tools, use of third party experts, etc.).

Second, we see a greater emphasis on the dynamic aspects of alliance governance decisions. For instance, in this volume several chapters examine a number of questions such as how alliances might be used as sequential investment vehicles to enter new markets or acquire another firm, how governance mechanisms change as partners develop multiple alliances over time with each other or others, and how individual dyads are renegotiated in the face of governance misalignments or opportunities to hold up a partner who has made investments specific to a relationship. Several opportunities to extend this research stand out. This work might be connected to process studies of alliances in order to study alliance contracting as well as its effects on the costs of negotiating alliances and the evolution of collaborations. There is also a question of whether the dynamics of a single alliance reflect or prompt changes in the direct and indirect ties a firm has through its interorganizational network, so it may be important to situate individual alliances' governance dynamics in this broader context. There is a dearth of studies on alliance implementation, so studies by scholars studying human resource management or organizational behaviour would be welcome to examine the causes and consequences of various types of alliance dynamics at the individual or group level by investigating managerial capabilities to manage alliances, career considerations, and the functioning of teams within and across organizations, to name a few.

Finally, research on relational governance and work on formal governance have often been conducted by different authors with different assumptions about managerial behaviour, and we are seeing the benefits of studies that empirically investigate the interplay between formal and relational governance mechanisms supporting alliances. Conventional wisdom has held that the two substitute for one another, yet there is emerging evidence presented in this volume that there are opportunities for complementarities, and longitudinal research is beginning to show how formal governance mechanisms might stimulate relational norms or vice-versa. Future research would be valuable that disentangles the benefits or costs of the various mechanisms underlying relational governance such as different forms of trust,

the development of interorganizational routines, reduction of information asymmetries, expectations for future exchange, and so forth.

Let us close by thanking several people without whose help this volume, and the conference that helped develop the ideas contained in it, could not have been possible. Generous financial support for this project was provided by the Anselmo Rubiralta Center for Globalization and Strategy at IESE Business School, University of Navarra. We would also like to thank John Bell (Philips International BV) and Antoni Valverde (Freshfields Bruckhaus Deringer) for sharing their experiences and expertise on the managerial and legal aspects of alliance contracting. During the conference and preparation of the book, a number of staff members and doctoral students at IESE offered their assistance, for which we are grateful: Gemma Golobardes, Elena Golovko, Kerem Gurses, Caterina Moschieri, Guillermo Nesi, Giovanni Valentini and Hugo Zarco. We also wish to offer special thanks to several scholars who served as facilitators during the conference and offered developmental reviews on the chapters contained in the volume: Tina Dacin (Queens' University), Estaban Garcia-Canal (University of Oviedo), Carlos Garcia-Pont (IESE Business School, University of Navarra), Arvind Parkhe (Temple University), Brian Silverman (University of Toronto) and Stephen Tallman (University of Richmond). Last, but not least, we are especially grateful to Francisco and José M^a Rubiralta whose generosity has made this project possible, as well as other activities of the Anselmo Rubiralta Center at IESE.

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