

Governance costs

Chapter 3

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Governance costs

- We call impediments to collaboration “governance costs”
- They prevent synergies and act like taxes
- They depend on governance structure

Where do they come from?

- They are costs for achieving effective collaboration
- If the ownership is common, we call them ownership costs
- If they arise from transaction with external actors, they are transaction costs
- They are impediments to collaboration and to control the process

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- A typical example is given by different rewards or incentive between collaborating units/actors: to stimulate cooperation there are additional costs such as monitoring suppliers; resolving disputes; etc..
- Other: freeriding; cheating; misrepresentation
- Another problem is difficulty in coordination for geographical matters; different professions; etc..: they cause lengthy meetings; costs for manuals or coordinators; etc..

The link between governance costs and synergies.

- Governance costs are higher for synergies that require massive modification or of the one-sided type.
- All costs for preventing issues during transactions (within or without the organization) are governance costs.

The link between governance costs and governance structure

- Eg. Common ownership vs separately owned business.
- In the first case, the ultimate control is entirely in the hands of CEO, therefore transactions costs between divisions are reduced and coordination problem are more easy to avoid.
- However, this could cause a dilution of managers' incentives in case of synergie and other negative behaviors such as free-riding on other business customers

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- Decision making results slowed from adding layers to hierarchy
- The greater are modifications needed for implementing synergies; the less effective is the synergy itself due to governance costs.
- Model for choosing governance structure: see theories/readings from Coase and Williamson.

The three conceptual pillars of corporate strategy

- Corporate advantage through joint ownership
- Synergies through joint operations
- Governance costs and governance form

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- In the absence of governance costs; the governance structure has no effect on collaboration

Explainer video

- [collaborating](#)