Governance costs

Chapter 3
Beatrice Orlando
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
• 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 diluition of managers’ incentives in case of synergie and other negative behaviors such as free-riding on other business customers
• Decision making results slowed from adding layers to hierarchy
• The greater are modifications needed for implementing synergies; the less effective is the synergie 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
In the absence of governance costs; the governance structure has no effect on collaboration
Explainer video

• collaborating