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Forms of Organizing

Background

In order to explain different organizational forms, the four main perspectives networks, communities, markets and hierarchies have been used to explain the nature of organizations and why organizations might exist as they do. These have included Oliver Williamson's transaction cost economics in its response to neoclassical economics emphasis on markets, Walter Powell's network form of organization, Ouchi's work on clans, Granovetter's discussion of business groups, Adler and Hekscher's communities. While each of these perspectives leads to the support of different organizational forms, together they provide an explanation of organizations in our society.

Scott's chapter 13 provides us with a background of the rise of the corporate form. The corporation in North America can trace its roots to guilds from the Middle Ages in Europe, through to the corporate charters of the European empires (such as the Hudson's Bay Company in Canada, and British and Dutch East India Companies in India), to privately owned railroad firms in the second half of the nineteenth century in North America, and mass-production manufacturing facilities at the turn of the century shaped the way we know of corporations today.

However, the attempt to understand the organizational form as a variable and the underlying assumptions of these claims have persisted to form the larger social science question of the purpose of organization in society. In fact, the issues of independence, power, relations and benevolence can be traced back to earlier philosophers such as Aristotle who in *Nicomachean Ethics* asked in 350 BC: "Even the rich and those in possession of office and of dominating power are thought to need friends most of all. For what is the use of such prosperity without the opportunity of beneficence, which is exercised chiefly and in its most laudable form towards friends". The literature on markets traces back to Adam Smith and David Ricardo, while Coase and Williamson's work on transaction cost approaches is seen as a response to earlier neoclassical assumptions in microeconomics. Williamson's emphasis on the transaction builds on Commons (1934) earlier emphasis on the transaction as the unit of analysis, while he follows his doctoral advisor Simon in his assumption of bounded rationality. Granovetter's (1985) problem of embeddedness which was positioned as a critique of transaction cost also connects the issue of rationality and opportunism to Hobbes' *Leviathan*, and more recently to debates between Polanyi and Hayek. The networks approach also finds a key precursor in Georg Simmel's early work where he claims that individuals can freely migrate across intersecting circles. For communal approaches, Marx, and Weber discussed the issues of power, control and communities, clans and professions, while Tönnies introduced the term *gesellschaft* and *gemeinschaft*. The background of our perspectives on forms of organizing are deeply embedded in the broadest questions of economic sociology.

Central claims

Markets and Hierarchies:

The general claim by neoclassical economists is that markets provide the most efficient form of transaction. However, Coase asks the question if markets were the most efficient form of transacting why would firms exist? Thus, the transaction cost approach became a comparative theory of economizing transactions through the market versus internalizing the transaction within the firm. TCE's conjecture regarding the different forms of firms relate to its unit of analysis, the transaction. Firms are different because there are many different types of transactions.

Network and community forms of organizing:

Network and community approaches to organizing make similar claims: transaction cost levels are not the only considerations for determining forms of organizing; markets or hierarchies are not the two only types of social organizing. In fact, both approaches posit that there exist intermediate and cross-boundary forms of organizing, based on value-rational considerations and regulated by reciprocity norms.

Networks are intermediate types of binding and a relation form of organizing, taking the middle ground between markets and hierarchies (Powell 1990). They emerge recursively, through repeated, "reciprocal, preferential, mutually supportive action" (Powell 1990) between multiple actors. They consist of nodes and relations between these nodes.

The community concept is based on Ferdinand Tönnies' distinction between *gesellschaft* and *gemeinschaft*. Community forms of organizing are regulated by shared values and beliefs, and a moral ethic of behavior. They are characterized by interdependence and create structures that are identity-building.

Reasons

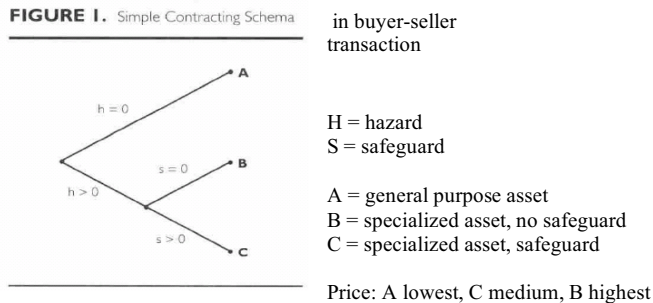
Markets:

Under market conditions that provide the most economical way of transaction the following conditions are argued to exist: large numbers bargaining (enough sellers are available so that the buyer is not constrained by holdup with one seller), the price serves as the information signal, this information provides the required information so that the decision maker is rational. These assumptions Williamson refers to as benevolence, omniscience, and omnipotence.

Hierarchies:

Transaction cost economics presents the dichotomy between markets and hierarchies and further organizational forms between these two. Based on a simple calculation of governance costs less transactions costs, a firm can choose the most appropriate method to complete a given transaction. Coase assumes that the market is the default way of organizing, there are decreasing returns to management of internalizing otherwise you would see one big corporation. In the transaction cost approach there are two main assumptions that go against the traditional neoclassical understanding of markets, bounded rationality (actors have limited information but are intendedly rational) and opportunism (deceit with guile). Williamson also is credited with making transaction cost approaches empirically viable by adding the following dimensions for transactions: uncertainty, frequency and asset specificity.

Williamson presents the alternative choices between markets and hierarchies in a decision tree diagram. In Figure I. below, a firm would consider hazards of each position (h) and the potential safeguards(s) and then calculate the costs of each position (A, B or C) and determine whether the firm would decide to organize the transaction in the market, or within a hierarchy.



Network and community forms of organizing:

Both network and community forms of network approaches to organizing ground their claims in the importance of reciprocity norms and ‘interorganizational trust’ as coordinating principles (Zaheer, McEvily and Perrone 1998). They posit that mutuality and interdependence can emerge from repeated interaction, even in the absence of hierarchical command chains, as well as exact evidence of performance.

> Networks

From a functional perspective, networks can increase flexibility over hierarchies and increase reciprocal information sharing over markets. Trust is a mechanism that binds without formal obligation or commitment. In this sense, it leaves enough flexibility to accelerate information flow (no tedious control mechanism) and therefore, learning and innovation.

> Communities

According to Adler and Heckscher (2006), collaborative communities emerge, when neither markets nor hierarchies are dominant. They are stabilized through shared values and purposes. In a similar fashion to Adler and Heckscher, Ouchi (1980) argues that communal organizing in the form of clans emerges, when neither markets nor hierarchies can address high uncertainty about performance. In such a situation, highly congruent objectives (through complete socialization) can help overcome the organizing blockade. Again, commonality of values, reciprocity, and legitimate authority are emphasized. Another phenotype of communal association is put forward by van Maanen and Barley (1984), who describe occupational communities as bounded work cultures, across organizational boundaries and with (some) self-control of the occupation. Some shared characteristic between the conceptualizations of communal organizing described here is that they cross organizational boundaries, are based on reciprocity and trust and are more rule-prescriptive than networks. Similar to networks, knowledge flow and creation are the primary benefits of this form of organizing.

Evidence

Markets:

Empirical research supporting the markets form of organizing has mainly been used to break up monopolies and create situations of large numbers bargaining where the market would be seen as most effective. Most frequently used in strategy is the logic from the Structure-Conduct-Performance Paradigm by Mason and Bain has been used by Porter to advise firms of ways in which they can create situations of small numbers bargaining in an attempt to gain a sustainable competitive advantage. Alchian and Demsetz work to create large numbers bargaining in order to prevent monopolies from taking hold inspired Williamson to approach the small numbers bargaining problem, although the two differed in their approaches.

Hierarchies:

Williamson claims that his contributions to the transaction cost approach have made it an empirical success story. Some recent studies have been able to keep to the narrow bounds of the transaction cost approach by combining it with population ecology, resource based view and relational theories of the firm. By combining these approaches the authors have been able to find support for the notion that firms that make the right choice in economizing transaction costs are performing better (Nickerson & Silverman, 2003; Mayer & Nickerson, 2005; Hoetker, 2005).

Network forms of organizing:

Network forms of organizing have gained increasing importance over the last two or three decades, although there are examples of such forms existing even before that (e.g., Business houses in Pakistan, Keiretsu in Japan). In fact, the flexible structure of traditional small firm networks may have prepared them in a unique way for new, more competitive market conditions (e.g., networks of SME furniture makers in Emilia Romagna, Italy). More recent forms of networks are strategic alliances and innovation networks, created with the explicit goal of innovation and knowledge transfer (Freeman 1991).

Community forms of organizing:

Community forms of organizing abound and often transcend organizational boundaries, as described by van Maanen and Barley (1984) in their conceptualization of occupational communities. They cite various examples of occupations (e.g., fishermen, firemen, also classical 'profession' like medical doctors or lawyers) that constitute the primary frame of reference for their members, as opposed to the formal institutions they may belong too. Ouchi (1980) cites school systems as an example of an organizing form that follows symbolic rules.

Qualifiers

Markets:

The boundary assumptions of markets are clearly articulated yet often criticized for their stringent assumptions. Neoclassical economists believe that in market transactions people have rational preferences among outcomes that can be identified and associated with a value. Firms act to maximize profits. Actors operate independently on the basis of full and relevant information. Yet, these conditions only hold in situations of large numbers bargaining, when actors do not have access to full information and behave opportunistically which is especially prone in situations of small numbers bargaining.

Hierarchies:

Many scholars also find the boundaries of the transaction cost approaches limiting. Comparison is drawn on the basis of the transaction within the market vs. subsumed within the firm not a comparison amongst firms of which one uses the transaction most effectively; the unit of analysis

is the transaction not the firm or a field of firms. The transaction cost also assumes that actors are farsighted and prospecting, previous interactions are not addressed. While markets fail under conditions of unbearable transaction costs, bureaucracy fails under high uncertainty about performance measurement when tasks become so unique and ambiguous that they can no longer compare their behavior in order to control.

Network and community forms of organizing:

Network forms and community forms of organizing are subject to a number of boundary conditions. First of all, these perspectives presuppose a positive concept of mankind (unlike Hobbes' *homo hominem lupus est*), since it is based not on control, but on trust. Empirically, network forms, by relying on trust and reputation as control mechanisms can be destabilized by power play and misuse of trust. Theoretically, since nodes and relationships are presented as fundamentally equal and similar, the approach runs into difficulties conceptualizing the effect of power differentials. Another fundamental problem is related to the fact that network boundaries are not clearly defined, jeopardizing the descriptive power of the approach. Both approaches are also unclear about their relationship to markets and hierarchies. Some authors conceptualize networks or communities as complementary to markets and hierarchical transactions, others seem to argue that we are moving towards a system where these new forms will become dominant.

Reservations

Markets and Hierarchies:

Granovetter and Powell make similar criticisms of the markets and hierarchies approaches. Powell argues that markets and bureaucracies are shaped by dense webs of political, religious and social affiliations. Transactions do not take place in a vacuum and actors work in cooperation with others. Markets are subject to institutionalized rules that have been shaped by society, furthermore these relationships contain elements of power and hierarchy, which creates inequity that determines who is able to enter transactions and determines the suitability of their behavior. There are further issues with the assumption of opportunism, Ghoshal and Moran (1996) argued that transaction cost is not useful as a normative theory because it prescribes to managers a wariness of opportunism that will become a self-fulfilling prophecy of more opportunistic behavior. Similarly, Granovetter (1985) argues that the transaction cost approach lacks the use of trust as a governing mechanism and does not account for those who use trust to seek information.

Network and community forms of organizing:

The network approach, by overemphasizing relations, neglects actors and all aspects internal to them (e.g., emotion, satisfaction). Network approaches are also difficult to test empirically, because the direction of causality may run both ways, or even be circular. As to the community form of organizing, van Maanen and Barley's (1984) concept of internal membership in communities (as opposed to externally attributed) causes serious problems. Since social meaning is created through interaction, it is unlikely that self-perceived membership is merely internally caused. Rather, there is likely some form of external attribution of membership roles, as evidenced by job titles and descriptions, as well as educational degrees. Theoretical approaches to network forms and community forms of organizing are also subject to some of the same reservations. Both approaches to describing forms of governance outside markets and hierarchies over-emphasize harmonious cooperation. In reality, networks are difficult to build and maintain and community forms of organizing, while more stable, can be sources of role conflict (van Maanen and Barley 1984).

While network approaches emphasize structure and community approaches emphasize norms and values, the approaches seem complementary in many aspects. It may be argued that they could be integrated. In that respect, they violate Karl Popper's principle of theoretical parsimony.

Conclusion:

The different types of organizing presented above do not per se constitute a theoretical perspective in organizational research. Each perspective emphasizes a different dimension, as illustrated by Powell's (1990) summary of the market, hierarchy and network approaches (with an addition of communities). However, they put forward important descriptions of what forms organizing can take under which circumstances and for what goals certain forms are more likely to emerge and more adequate to choose.

Table 1. Stylized Comparison of Forms of Economic Organization.

Key Features	Forms			Communities
	Market	Hierarchy	Network	
Normative Basis	Contract— Property Rights	Employment Relationship	Complementary Strengths	Traditional
Means of Communication	Prices	Routines	Relational	Collegial
Methods of Conflict Resolution	Haggling— resort to courts for enforcement	Administrative fiat—Supervision	Norm of reciprocity— Reputational concerns	Clan/work Identity
Degree of Flexibility	High	Low	Medium	Medium
Amount of Commit- ment Among the Parties	Low	Medium to High	Medium to High	Medium to High
Tone or Climate	Precision and/or Suspicion	Formal, bureaucratic	Open-ended, mutual benefits	collective
Actor Preferences or Choices	Independent	Dependent	Interdependent	Peer Control
Mixing of Forms	Repeat transactions (Geertz, 1978)	Informal organization (Dalton, 1957)	Status Hierarchies	Expertise Trust
	Contracts as hierarchical documents (Stinchcombe, 1985)	Market-like features: profit centers, transfer pricing (Eccles, 1985)	Multiple Partners Formal rules	Appropriate Moral Behavior

It may be argued that the level of uncertainty has the strongest influence on the adequacy of a form organizing. Market transactions are chosen when uncertainty about performance is low: Prices contain all information necessary to distinguish between uniform goods and expectations of performance are clear. Under circumstances of intermediate uncertainty, hierarchies become more attractive. For instance, labor contracts between employees and firm contain an element of uncertainty as to what the exact tasks to be fulfilled are (performance evaluation is difficult, see Ouchi, 1980). Finally, when uncertainty about performance is extremely high, organizing efforts tend towards trust-based modes of communal governance, which help surmount transaction barriers that can neither be solved by hierarchical structures, nor by bargaining transactions.

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