Corporate Governance in an MNC: Towards the View of Culturally Determined Agency

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Abstract
This study is positioned to contribute to the subject area of corporate governance in multi-national corporations (MNCs), which represents a substantial void in the literature both on corporate governance and international business. The new theoretical proposition of culturally determined agency is suggested. It builds on the recently put forward behavioural theory of corporate governance. This novel theoretical lens in corporate governance merges the under-socialized agency theory, as the dominant institutional logic in corporate governance of domestic firms, and the behavioural theory of the firm, which is probably the only theory of the firm that explicitly treats firms as complex social systems. Finally, three exemplifications of application of this new theoretical construct of culturally determined agency to the analysis of contemporaneous business issues in MNCs are briefly discussed: meta-national governance, use of expatriates, as well as knowledge and innovation management.

Keywords: Agency theory; Culture; Multinational Corporation; Power/Politics

Introduction
The financial crisis that erupted and infected the world economy in the years of 2007 and 2008 has sparked vigorous debates about the social order, problems of allocation of scarce resources, and the lack of distributive justice in wealth-distribution across different societal groups. This leads to an increasingly widening gap between the elitist and poorest strata of the society. Implicit to this discourse are the phenomena of power in social relationships and politics that are played out not only in societies, but also in large corporations, and especially the multi-national corporations (MNCs).

Such entities generate financial streams of the magnitude that often exceed the Gross Domestic Products (GDP) of the small-sized, albeit well-developed, national economic systems (e.g., Walmart’s or Exxon Mobil’s revenues exceed the GDP of Turkey or Austria; Rugman et al. [1]). The current degree of internationalization of businesses, and the high volume of international trade and exchange have led to the situation, where MNCs at different managerial levels have commenced resembling ‘transnational societies in miniature’, with increasingly international and diverse managerial teams and task groups (Beck, 2008: 797), [2]. At the same time, there have been voices articulated in the international business scholarship that the field suffers from the lack of a big research question that would serve as a catalyst for its development [3]. Yet, there is a substantial void in the international business literature: the problem of corporate governance in MNCs [4-9]. Therefore, in an attempt to start addressing that gap, the theoretical framing that I adopt in this paper is corporate governance in MNCs.

I build on the recently suggested theoretical proposition of the behavioural theory of corporate governance [10]. It merges the under-socialised agency theory [11-14] with the behavioural theory of the firm. The former represents a main institutional logic informing corporate governance of domestic firms, whereas the behavioural theory of the firm treats companies as complex social systems and arenas of organisational politics in a comparatively most explicit way [15-17].

In devising my theoretical proposition, I recognise the phenomenon of culture as a distinctive feature of MNCs, which differentiates them from their domestic counterparts. It is equally specific for the entire area of international business research and makes it a separate field of study within managerial science [18,19]. The new theoretical construct of culturally determined agency is to serve as an analytical tool that will allow for the rigorous scrutiny of the socio-cognitive processes of the perceived individual agency formation at the interface of boardrooms across the two governance levels in MNCs, i.e. at the parent- and subsidiary-level.

Finally, I discuss the three exemplifications of the application of this theoretical construct to the study of important contemporaneous topics in MNC governance and management of high relevance for the business practice.
Corporate governance in an MNC

An MNC represents a traditionally conceived for-profit stock-exchange listed organization, and hence its long-term objectives are no different to the domestic firms. Therefore, the principles of corporate governance are equally applicable to an MNC. Since the UK Cadbury Committee [20] corporate governance movement evolved into practically an autonomous field of study within managerial science and grapples with ways of directing and controlling companies to the benefit of their stakeholders. However, the specificity of governance in MNCs is that it is subject to additional influences of culture and institutions of countries, in which its operations are located. This adds further layers of complexity to the analysis of the governance systems in MNCs as compared to their domestic counterparts. As a result, corporate governance in MNCs represents a relatively unchartered territory in terms of academic contributions [6,7,9,11,21-24].

Among the corporate governance mechanisms, scholars have been paying particular attention to a board of directors. It represents an internal institutional mechanism of shareholders’ indirect control over company management. Board structures vary between countries due to their different legal and socio-economic legacies and path-dependencies. Accordingly, we can distinguish between Anglo-Saxon (common law) and countries in continental Europe together with for instance Japan (civil law), which is characterized by the stock market and relational/welfare capitalism, respectively. In the former case, companies typically install one-tier/monistic boards, where differently contractually obliged non-executive and executive directors meet to form a single collegial body at the apex of organizational hierarchies. In the latter variant, there typically occur two-tier boards with a separate executive segment in the form of a management board and a non-executive segment construed as a supervisory board [6,11,21,24-26].

Regardless of the ultimate board structure, the most crucial aspect of this governance mechanism is derived from the fact that the contractual scripts for particular board roles determine a chain of accountabilities, and hence power distribution, among them. So, the CEO and other executive directors are accountable to the Chairman of the board (provided that it is a non-executive function) and other non-executive directors. The non-executive directors are in turn accountable to shareholders, who, if it is an institutional shareholder, are further accountable to their clients and their own shareholders, if such an institutional investor represents a stock-exchange listed company itself [27-30]. Such a configuration of accountabilities and power distribution among the main corporate actors, in the sense of their responsibilities for the decision-making process, sounds complex. Furthermore, their implications and consequences cascade down the organization, and have direct influence on the strategy-making process, which determines the long-term direction of company development. This is so, even if this complex set of relationships describes only a domestic company and not an MNC.

The picture becomes much more complicated, when we add multiple foreign subsidiaries with their own boards of directors, and even more so, when those subsidiaries are listed on the stock exchanges, and hence have their own shareholders. As a result, we have separate circuits of configurations of accountabilities for an MNC headquartered and for its all pertinent subsidiaries. Luo [6,7] refer to them as the 1st tier and 2nd tier governance, respectively. The extant academic research recognizes the importance of the headquarters-subsidiary relationships for the overall successful governance of an MNC e.g. [4-9,19]. However there has been a paucity of especially empirical research that would examine the interface and interactions between the headquarters’ and subsidiary boards in an MNC. The existing contributions were largely confined to either the 1st-tier e.g., [31] or 2nd-tier e.g., [32] governance only.

One conceivable explanation for this substantial void in both international business and corporate governance literature is the difficulty involved in rigorous conceptualization of this complex set of relationships at both governance levels, and especially at the interface between them in the MNC. Drawing from the dominant institutional logic in the Anglo-Saxon corporate governance system, i.e. the agency theory, we need to recognize that such a chain of accountabilities in an MNC, involving both headquarters’ and subsidiary boards, de facto constitutes an agency framework with multiple layers of agency relationships [6,7,11,21]. Accordingly, for instance non-executive directors on the subsidiary board are, in addition to their accountability to the subsidiary shareholders, also accountable to both executive and non-executive directors on the headquarters’ board, and indirectly to the headquarters’ shareholders. So, they act as principals towards the executives on the subsidiary board, and as agents in relation to all aforementioned board members at the headquarters level as well as indirectly to the headquarters’ shareholders. There are many conceivable combinations of the agency relationships between different corporate actors at both headquarters’ and subsidiary governance levels. However, I have illustrated just one case for the subsidiary non-executive directors as a matter of depicting the complexity in-built in governance structures in MNCs. Nevertheless, such an exercise could be carried out for other board members and/or shareholders at either of the governance levels in the MNCs. The MNC two governance levels together with the chains of accountabilities in the boardroom are illustrated in Figure 1.
A new theoretical proposition: A view of culturally determined agency

There have been repeated calls in the academic literature to increase the theoretical pluralism in the international business research, and hence adopt multi-theoretical perspectives. In recognition of this opportunity, scholars have documented a substantial degree of infiltration of the international business research by the paradigmatic framework of the strategic management literature, i.e. the resource-based view of the firm, in the last two decades of international business scholarship. This Penrosean perspective [33] allows researchers to disentangle the nature of the firm-specific advantage (FSA) that MNCs transfer across borders in terms of their resources and capabilities. It also helps identify the challenges ahead of MNCs that are inherent to the balancing act of responding to countervailing pressures resulting from enacting global integration, while maintaining a sufficient level of local responsiveness. This framework of global integration versus local responsiveness has in the meantime become the core analytical tool for scrutiny of the MNC operations, viewed through the lens of the firm internationalization strategy [1,8,34,35].

As discussed earlier, there is a dearth of academic research on the governance models and processes in MNCs in the international business field coupled with under-utilization of the agency theory in this type of research endeavour. Given the prominence that the agency perspective has gained in studies on corporate governance of domestic firms, scholars duly recognize the research potential that can be triggered and realized by the adoption of this theoretical lens in studies on corporate governance in MNCs [4-7,9].

Agency theory as a dominant institutional logic in corporate governance

Contributors to the scholarship based on the institutional theory stipulate that organizations tend to exhibit a high degree of institutional isomorphism in terms of design and enactment of organizational hierarchies and architectures. This is in pursuit of social legitimacy for their existence and functioning, while maintaining a reasonable level of technical efficiency [36-38]. Such institutional uniformity implies the existence of the dominant institutional logic, which informs both the academic research and the work of regulators. Its findings are then translated into managerial practice. The role of such a theoretical leitmotif in the area of corporate governance in the Anglo-Saxon capitalism has been played by the agency theory. It has been so since the revival of interest in the new institutional economics (NIE) in the mid-1970s, marked by Williamson’s (1975) contribution on markets and hierarchies [12-14].

Taxonomically, the agency theory belongs to the research stream of NIE. It regards the notion of contract as the main analytical tool to explain market mechanisms. This is in opposition to the neoclassical economics, which concentrates on price as a solution, based on which market clearances occur [39]. As Eisenhardt [40] duly elucidates, there are two main streams of scholarly work on the agency theory. What the corporate governance researchers typically use is the Positive Agency Theory (PAT). A more mathematically advanced principal-agent framework, which mainly focuses on problems of the agent’s incentive alignment, represents the latter research strand. The limited rigour in applications of the agency theory predictions to the analysis of the corporate governance phenomena has led to the situation, where the agency theory has become practically synonymous with all deficiencies of the corporate governance scholarship e.g., [27,28,41-44].

In the stock-exchange listed company, we have to do with de facto separation of ownership and control. PAT suggests dividing the decision-making process into two main components. The first one is the decision management, including decision initiation and im-
plement, for which company executives are responsible. The latter is the decision control, encompassing decision ratification and monitoring. It is supposed to be enacted either by shareholders directly (e.g., through voting at the AGM), or indirectly through the board of directors, the significant part of which is meant to be composed of independent, non-executive directors. This last element of the depicted governance structure, i.e. a significant fraction of independent, non-executive directors on the board, has become symbolically synonymous with what corporate governance arrangements should be, based on the agency theory logic. However, such a limited view has largely ignored the other elements of the corporate jigsaw [12-14,25,40].

The principal-agent framework in PAT is probably best illustrated with a shareholder- manager dyad. The former, as capital owners, hire the latter, who possess the specialist knowledge and managerial skills that the shareholders do not have themselves. This classic agency situation is characterized by information asymmetry, in favour of management, which supports their power potential in this bargaining game over the distribution of the ex-post quasi-rents. Moreover, since managers, unless the performance-related executive pay contingency is applied, are not capital owners, they may have higher proclivity towards risk-taking, compared with shareholders, who are the residual risk bearers. From this description, it becomes apparent that the agency situation is de facto underpinned by a certain power distribution, which leads to organizational politics and can be easily depicted as a bargaining game between these two corporate actors. This means that shareholders, as principals, endeavor to install safeguards in the corporate governance system that are intended to curb potential managerial self-serving behavior. It can take a form of shirking or unjustified empire-building and is formally encapsulated in PAT with the notion of the ex-ante risk of adverse selection and the ex-post risk of moral hazard [12-14,40,45].

PAT predictions, as a dominant theoretical lens in the field of corporate governance, have been widely translated into managerial practice. This process was accompanied by the intense regulatory work, taking a form of principle-based governance codes, such as the UK Corporate Governance Code (2014), which predominantly drew from PAT suggestions. Examples of such recommended institutional arrangements included the establishment of boards with the substantial representation of non-executive directors, performance-related executive pay contingency, or avoidance of the CEO duality, i.e. the situation, where the same person is both the CEO and Chairman of the board.

Yet, immediately after the inception of the corporate governance movement in 1992, which across the world is symbolically associated with the proceedings of the UK Cadbury Committee, critical voices concerning the explanatory power of PAT started to be raised. Equally symbolic in this respect was [46] call for unveiling the boardroom reality and increasing the realism of context in corporate governance research. This sparked a number of contributions involving greater theoretical pluralism and adoption of multi-theoretical perspectives, as well as in its most radical form ‘dismantling the fortress of the agency theory’ [27,28,41,42,44]. Ghoshal’s [47] assertion that bad theories destroy good managerial practice has become almost a canonical argument that PAT critics have been articulating.

In this work, I adopt the stance of a PAT apologist. However, I admit that some criticism of this theory is justified and well-grounded, such as the line of PAT criticism that accentuates that PAT represents a strongly under-socialized perspective [9-11,43]. Implicit to this statement is the recognition that board proceedings do not unfold in the social vacuum. On the contrary, board members act in the boardroom in strong connection with the role and social identities that they bring with themselves. They indulge with certain behavioral strategies and tactics, which PAT leaves not described, whereas other theories can account for them [10,18,43,48,49]. This creates scope for a fruitful theoretical hybridization between PAT and the behavioural view of the firm in the form of the behavioural theory of corporate governance [10]. Such a theoretical hybridization can generate additional insightful predictions, and thereby increase the realism of context in corporate governance studies, without unduly compromising the generalisability qualities of PAT.

Socially Situated and Socially Constituted Agency

The behavioural view of corporate governance is derived from the behavioural view of the firm, which arguably rests on more realistic assumptions than the economics-rooted PAT with regard to the heuristics of managerial action. In addition to the bounded rationality condition, the principle of satisfying and the assumption on routinisation in the decision-making process, the behavioural view treats organizations as complex social systems. They constitute venues of power battles among the coalitions of corporate actors realizing often conflicting goal agendas [15-17,50,51]. It is therefore probably the most explicit about the existence of phenomena of power and politics in the corporate settings among all theories of the firm.

Westphal [10], in their recently published work, suggest enriching the under-socialized agency perspective with the predictions of the behavioural theory of the firm. They refer to this cross-theoretical hybridization as the behavioural theory of corporate governance. Within that framework, they distinguish two main mechanisms that impact on behavior and actions of actors involved in governance processes in corporations, i.e. the socially situated and socially constituted agency.

PAT, as an under-socialized and actor-centric theory, concentrates on examining patterns, according to which individuals voluntarily, however rationally, realise their own goal agendas. They are motivated by self-interest and differential personal risk preferences, as well as are subject to informational and incentive constraints. In effect, PAT governance mechanisms tend to be formal in nature. They take a form of either incentives for managers as agents or means of monitoring/controlling them. They are construed to provide safeguards against such actions of managers, who driven by their self-interest may be potentially deviating from the desired organizational and/or societal outcomes. This unfolds by aligning
managers or disciplining managers as agents [12,14,40].

Westphal [10] infuse the agency relationships with the social context. They emphasize that corporate leaders do not operate in the social vacuum. On the contrary, they act in the socially constructed and interpreted reality. In the methodological sense, they enrich the heuristics of the individual human action in corporate governance, as posited in PAT, with the social fabric of norms, values and beliefs, and point towards the socio-cognitive processes as actual frames, within which particular board members enact their decision-making processes. In other words, in this cross-theoretical framework, [10] conceive the missing link between the macro-social explanations of well-functioning corporate governance practice, as offered by the economics-rooted PAT, and the micro-behaviour that is most likely to actually unfold in the boardroom reality.

The notion ‘socially constituted’, in turn, is conceived to capture a deeper kind of influence of the social context on the perception of the individual agency than it is the case with the socially situated agency. This concept emphasizes ways in which individuals’ socialization into social relationships, networks, as well as institutions, which have influence on their perceived individual agency (e.g., a manager being accountable to non-executive directors directly, and to shareholders indirectly). Therefore, they represent crucial contingencies that ultimately shape the behaviour of individuals. The notion ‘socially constituted’, in turn, is conceived to capture a deeper kind of influence of the social context on the perception of the individual agency than it is the case with the socially situated agency. This concept emphasizes ways in which individuals’ socialization into performance of their particular roles (e.g., as a manager, a Chair- man, a non-executive director), as well as their cumulative personal experiences to date, determine what they regard as possible or realistic in a given situation. The perceived individual agency, shaped through these processes, ultimately precipitates in a specific socio-cognitive orientation that particular board members adopt in their socially constructed boardroom reality [10].

There have emerged an entire stream of empirical research, which, even if it does not fully explain the theoretical rationale of the suggested behavioural theory of corporate governance, explicitly examines the socio-cognitive processes and behavioural tactics that are likely to unfold in the boardroom reality. They act as contingencies that shape decision-making processes by particular board members. For example, Westphal [52,53] predicts the likely board outcomes as a result of competition and collaboration between the CEO and non-executive directors in the boardroom. [54] research pluralistic ignorance on boards. Westphal et al. [55] scrutinize favour rendering, ingratiating tactics and norms of reciprocity. Westphal et al. [56] analyze the processes of symbolic and impression management, together with organizational/ institutional decoupling. Finally, Westphal et al. [57,58] look at the social distancing tactics as a means of disciplining and/or demonstrating ostracism towards those minority coalitions, which step out of the line dictated by the dominant board fraction. Culturally determined agency

The notions of social situatedness and constitution [10], fall close to Bourdieu’s [59] concept of habitus. He coined it in elaborating on his view of power as internalized constraints. His perspective is methodologically akin to the conceptualizations of power by Lukes [60] and Foucalt [61], who regarded it as a ubiquitous abstract and subtle force that is impacting on individuals in such a way that they actually act as their own over-seers. They discipline themselves and the existing social relationships thus arise as the natural order. These arguments suggest that the individual agency as perceived by particular social actors is de facto socially constructed, whereby this process is hugely influenced by the position of a given actor in the existing structure of social relationships.

In corporate governance of domestic firms, the socio-cognitive processes that shape board members’ perception of their individual agency are described in the aforementioned contributions by James Westphal e.g., [52,53,56,58]. However, such developments can also occur on MNCs’ boards. There is one characteristic, though, which makes corporate governance in MNCs distinctively different from corporate governance in their domestic counterparts. This is the phenomenon of culture and cultural differences between nation states. It is also the distinctive feature of the entire international business research, and hence we have it as a separate field of study in management science [3,18,62].
Why do I use the word determined, rather than situated or constituted, as Westphal et al. [10] do? The reason is that the cultural influences are slightly ontologically different than those primary socio-cognitive processes that [10] describe. First of all, the fact of the sheer existence of the cultural differences does not necessarily mean that they are triggered or activated in terms of their relevant impact on processes of shaping the agency perception at the interface of boardrooms at two governance levels in MNCs. For example, as Lau et al. [63] and Chrobot-Mason et al. [64] demonstrate for the notion of faultlines in the group effectiveness literature, such within-unit fractures can exist, and yet remain dormant, if they do not have cognitive task-relevance for the team proceedings. Therefore, one should not assume that the existence of cultural differences between the MNC headquarters and subsidiary boards is automatically translated into their material impact on the agency relationships. Second, in connection with the first argument, one cannot pre-determine the quality of this impact of cultural differences on agency relationships. The negative influence does indeed seem to be more likely than the positive impact from the point of view that cultural differences are deeply ingrained in human beings’ mindsets, potentially encompassing not only the cognitive and affective sphere, but also language and value systems [65-67]. However, on the other hand, in the scenario, when the MNC headquarters and the foreign subsidiary in question are located in culturally related countries, such as Germany and Austria, which share the language and belong to the same Germanic cultural zone as distinguished by Ronen et al. [68] the odds are that the impact of cultural differences on agency relationships can be neutral. However, one cannot preclude the positive effects, either. This observation brings us to the point that the quality and magnitude of impact of cultural influences on the agency relationships at the interface between boardrooms at two governance levels will be highly contingent on the size of cultural distance between the country of the MNC headquarters and the country where a given foreign subsidiary is located [69,70]. Finally, referring back to Bourdieu’s [59] notion of habitus, cultural differences and their bearing for the agency relationships across levels of governance in MNCs mainly result from the different geographical locations of the MNC headquarters and a given foreign subsidiary. This implies substantial structural determinacy, however, does not preclude some amount of behavioural voluntarism on the part of the corporate actors involved. For example, there exists such a theoretical possibility, where subsidiary executive and non-executive directors may resemble more intrinsically ‘good’ stewards of the entire MNC organisation, as described in the stewardship theory e.g., [71], rather than the self-interested and opportunistic agents, despite the existing cultural differences. Ultimately, this argument comes back to the point that cultural influences on the agency relationships in the MNC corporate governance are ontologically secondary to the processes of social situatedness and constitution [10].

Another question that may be posed is why I utilize the notion of culture rather than the concept of an institution, which covers a wider spectrum of phenomena than culture with regard to the setting of a given foreign country? The advances in the contextualization of the international business research, such as in the form of more accurate operationalization of the country of origin and the host country effects than before, were possible thanks to the development of the international comparative institutional theory. It stipulates that the development of idiosyncratic national management systems in different countries represents a largely path-dependent process, which is shaped by the legacy and interplay of political, economic and social institutions e.g., Kostova [72]. In this vein, the institutional theorists suggested the term of institutional distance as opposed to cultural distance, which is construed as a measure of cross-country differences in terms of the MNC home country and host country institutional contexts. It captures the degree of similarity or dissimilarity between the regulatory, cognitive and normative institutions of the two compared countries [69]. Kostova [72] elucidated that the cognitive and normative dimensions of the country institutional contexts are conceptually not far from culture, whereas regulatory aspects are. This is exactly the reason, for which I believe that the term culturally determined will be more appropriate than the phrase institutionally determined. The regulatory aspects of the agency relationships are typically regularized in the contractual agreements specifying particular board roles. So, this would result in a degree of overlap between the contracts as such and the discussed additional influences on the perception of individual agency by particular board members. In addition, the term culture is conceptually much closer than the notion of an institution to human mindset, i.e. our cognitive, affective, linguistic and value system spheres [65-67]. And they are actually most relevant for the socio-cognitive processes arising from differences in mindsets among the involved corporate actors. So, coining the phrase culturally determined rather than institutionally determined more accurately reflects the actual phenomena that are intended to be captured with that phrase.

International business scholars also indicate that the classic framework of global integration as opposed to local responsiveness still holds a great potential for new findings and insights, especially with regard to its second dimension. In particular, Meyer et al. [62] suggested a phrase of multiple embeddedness. It is construed to account for the multiplicity of local contexts that an MNC in its most developed form, i.e. present in a number of countries, has to internalize. In consequence of such high breadth of internationalization, the MNC headquarters will have to grapple with a number of variants of culturally determined agencies between the headquarters and the whole spectrum of foreign subsidiaries. Those agencies will predominantly differ in terms of intensity of cultural influences, depending on the magnitude of cultural distance. Such a scenario reflects how complex and intricate the task of the MNC governance can become. This is likely to lead to the Penrosean effect, i.e. resource constraints, in this example mainly in terms of the headquarters’ boards’ cognitive and cultural awareness potential. It will be expressed in a limited capability of managing increasing complexity from each increment of added cultural distance arising from each expansion to a new country [73]. Moreover, in the
spirit of the predictions of the Scandinavian school of international management of incremental internationalization [74,75] one has to recognise that the most profound managerial challenges crop up from internationalization moves into culturally distant countries. For example, those into new, culturally unrelated zones, e.g. from the Anglo to the Arab cultural zone in Ronen et al. [68] nomenclature, or from the North American Free Trade Association (NAFTA) to Japan/ the Association of Southeast Asian Nations (ASEAN) countries (between two of the three main economic systems in the triad/regionalisation view of the internationalisation of the world economy; [1,35,76]. The academic literature documents the likely organizational antecedents and consequences of internationalization in big leaps in terms of, for instance, TMT composition and the incidence of foreign nationals on TMTs. This is construed as a means of increasing the cognitive and cross-cultural awareness on this MNC key decision-making body for the TMT to be able to navigate through complex and uncertain foreign territories e.g., Barkema et al. [77] Barkema et al. [78]. Finally, the increased appreciation of the local context sheds new light on the governance challenges that foreign subsidiaries are confronted with. In pursuit of social legitimacy in their countries of operations [79] subsidiaries have to emit credible messages to local communities of business practice and opinion leaders, such as local shareholders, customers, suppliers, governments, regional self-governments, universities. However, at the same time, foreign subsidiaries have to maintain their allegiance to the MNC headquarters, and comply with the MNC policies, its adopted business model and organizational culture. This is necessary in order to uphold the MNC headquarters’ internal legitimacy, or in other words the MNC-issued license, for their operations. This situation of foreign subsidiaries being subject to two, conceivably often countervailing pressures originating from their embeddedness in the local environment and their allegiance to the MNC hierarchical authority is referred to as dual embeddedness [62,80,81]. The corollary of the strong impact of the local milieu on the foreign subsidiary management is that this force will act as a catalyst activating cultural differences at the boardroom interface between the two governance levels, i.e. the MNC headquarters and a given foreign subsidiary. This will result in such socio-cognitive formation of individual agency perceptions that will aggravate MNC governance challenges and problems, which ultimately will be translated into increased agency costs. In sum, the dual embeddedness condition underscores the argument that cultural influences on the agency relationship are more likely to be negative rather than positive from the point of view of their impact on the overall MNC governance effectiveness.

This view of cultural differences having exacerbating influence on the governance hazards in MNCs that are somewhat in-built in the agency relationships tends to dominate in the academic literature to date. The agency problems arising from cross-border separation of a principal and agent are assumed to magnify the information asymmetry condition, in the sense that the foreign subsidiary management as an agent becomes an even more informed party than the MNC headquarters as a principal. The local and specialist knowledge with regard to the local environment, in which a given subsidiary is embedded, in terms of the legal, regulatory and normative institutions, as well as culture, are often beyond the reach for the MNC headquarters management from the confines of their frequently culturally distant location. This condition of information asymmetry further reduces the task programmability, agent behaviour observability, and ultimately raises causal ambiguity of the agent’s managerial action. Accordingly, the scores for the criteria, based on which we infer the agency costs of managing far-flung cross-border operations, are likely to increase [6,7,23,37,82-84]. So, according to this theoretical reasoning, the organizational politics in MNCs at the interface of boardrooms at the two governance levels, the MNC headquarters and a given foreign subsidiary, put the foreign subsidiary management as an agent more on par with the principal, the MNC headquarters, compared with the governance of domestic firms. However, given that there exist theoretical possibilities for cultural influences not to have a negative impact on the agency relationships across governance levels in MNCs, such as when the cultural distance is low, my theoretical proposition is more moderate than the presented view of predominantly exacerbating influence of cultural differences on the agency relationships in MNCs. Nevertheless, the common denominator of both standpoints on the subject matter is the recognition that the specificity of the MNC governance, similar to the specificity of the entire field of international business, is attributable to the phenomenon of culture. In this spirit, as well as in appreciation of the explanatory potential of the behavioural theory of corporate governance, which draws from the research traditions of PAT and the behavioural view of the firm, I propose a view of culturally determined agency. This notion is construed as a descriptor of the factual governance setting that occurs at the boardroom interface across two governance levels in MNCs.

Proposition 1: In an MNC the relationship between the 1st- and 2nd-tier governance is framed with the notion of the culturally determined agency.

Proposition 2: The culturally determined agency stipulates that the cultural influences on the processes of social construction of the perceived individual agencies by particular board members at both governance levels in an MNC constitute a significant portion of the overall variance of all types of factors influencing these processes.

Exemplifications of Application to International Business Research

Buckley et al. [3] were warning the academic community that the international business field suffers from the lack of a big research question that would drive it forward. At the same time, there is such a big literature void as corporate governance in MNCs, which touches upon the ultimate raison d’etre of MNCs. Moreover, recent contributions to the international business field discover and report new phenomena that occur in the organization of MNCs, which require new and/or better scholarly explanations. For example, MNCs do not cease to compete for managerial talent. In addition, there is notable scarcity of engineering cadre in the US, which is pivotal for
maintaining high quality R&D departments that have been traditionally identified as key in terms of developing a transferable FSA by the MNC [4,85,86]. Radical innovations in electronics as well as information and communication technologies have profoundly impacted on the viable business models, with e-commerce creating an additional dimension for the cross-border investments. As a result, we witness what scholars refer to as ‘fine-slicing’ of the value chain by MNCs. This leads to the situation, where for instance a few subsidiaries located in one country all share the same MNC mandate in terms of being responsible for one particular activity located in the same stage of the value chain, such as inbound or outbound logistics (Rugman, Verbeke & Yuan, 2011: 257). In the similar vein, the new approach to MNC governance, e.g., meta-national governance, was suggested as a more appropriate organizational response to the changing demands of international markets than the traditional multi-divisional governance approach [87,88]. Finally, on the theoretical front, a new envelope concept of bounded reliability was coined, which allows for more comprehensive accounting for PAT-stipulated ex-post risk of moral hazard. In addition to the pejorative texture inherent to Williamsonian concept of opportunism that implies intentional deceit [89], it suggests the mechanism of benevolent preference reversal, which is not negatively value-laden and is meant to signify good faith re-prioritization on the part of subsidiary managers [35,90]

Business practice can therefore be in many respects ahead of scholarship, which is a corollary of rapid acceleration and enormous dynamism in the development of and changes in international markets enabled by large-step technological advancements in especially the last two decades. Hence, the new theoretical construct of culturally determined agency may not only be utilized in studies on the MNC governance, but also in research on other important aspects of the MNC functioning. In the following sub-sections, I briefly discuss three of such conceivable applications.

Meta-national governance

Doz et al. (2001) suggest a new concept of meta-national governance as an arguably better alternative to the traditional multi-divisional form of governance in the face of an increasingly dynamic and knowledge-based economy of today. This view implies that knowledge is scattered around the world and hence the MNC competitiveness predominantly hinges upon processes of knowledge creation and management, which encompass knowledge development/acquisition, absorption, diffusion and exploitation. Therefore, it has become a strategic imperative for MNCs to operate a flexible, sensitive and where needed flat organisational structure that will facilitate knowledge exchange between the MNC and its external environment. In lieu of the traditional structure and management processes between headquarters and subsidiaries, as well as among subsidiaries, the meta-national governance view suggests that MNCs of today need three distinct, albeit inter-connected activity levels: sensing, mobilising, and operations.

Sensing means proactive search for emerging knowledge and innovations. Mobilising involves the use of the so-called magnets, i.e. flexible and adaptable organisational forms, such as virtual teams, which will enable effective translation of new knowledge into innovative products or specific market opportunities. Finally, operations are conceptually the closest to the traditional multi-divisional form of governance, and the operations divisions are tasked with a target of effectively and efficiently bringing innovative solutions to market ahead of competitors [88,89]. Although Verbeke et al. [88] do not find any evidence that the meta-national approach to governance is likely to be superior to the traditional multi-divisional form of governance, we can still conclude that important modifications to the MNC structures are being repeatedly ventured today. They can take a form of meta-national governance, fine-slicing of the value chain [90,91], or off-shoring as a form of a cross-border value chain disintermediation [85]. This has enormous implications for the accurate understanding of the demands of effective governance in MNCs.

MNCs organisational structures change, however, one variable stays the same, i.e. culture and cultural differences. That is why we consider these developments in the international business field. The strategic imperatives resulting from increased importance of knowledge management processes are tipping the balance of power towards those subsidiaries that are most innovative and hence critical for the success of the MNC entire value chain. The view of culturally determined agency can then serve as a tool for identifying ways, in which a workable modus operandi between the managerial elite of those critical subsidiaries and the MNC headquarters’ board can be elaborated. First of all, the cultural awareness related to the country or a number of countries, in which those critical subsidiaries are located, can be developed on the MNC headquarters board by introducing directors who hold nationalities of the countries in question. Alternatively this can be achieved by launching extensive training programmes for the domestic directors on the culture(s) of those relevant countries. Second, training and staffing of domestic directors on boards of those critical subsidiaries as expatriates can be considered. Finally, the MNC headquarters can resort to such behavioural tactics as favour rendering, ingratiation, or building well-conceived norms of reciprocity.

Proposition 3: In meta-national governance of an MNC the notion of culturally determined agency can explain ways in which the critical subsidiaries can be identified and managed.

Use of expatriates

The academic literature documents that MNCs adopt a specific organisational response to the increases in their internationalisation posture. It consists in introducing foreigners to the executive and board ranks. Such moves are intended to increase the cross-cultural awareness and sensitivity among the members of the key decision-making bodies at the apex of the MNCs’ hierarchies in order to facilitate the company navigation in uncertain, complex, and often culturally distant countries. In Gupta et al. [92] language this practice constitutes the MNCs’ well-grounded strategic impera-
tive of embarking on ‘the quest for a global mindset’. It represents a crucial strategic capability allowing MNCs to appreciate the diversity across cultures and markets, and ultimately to synthesize across this diversity [93-95].

This technique of enhancing the TMTs and boards’ cognitive potential with regard to cultural diversity issues also constitutes probably the most rational response to the governance problems in MNCs, as captured by the suggested view of the culturally determined agency. Well-constructed boards comprising foreign nationals from countries of the MNC’s operations at the level of the parent-firm are more likely to alleviate and solve problems resulting from cultural differences as well as potential misunderstandings due to such differences at the interface of boardrooms across governance levels in MNCs. Boards uniformly composed of only parent-country domestic directors may be less capable of doing so. The situation turns more problematic, when we consider the question of whether or not the MNC headquarters should influence the composition of boards in its foreign subsidiaries. This dilemma is probably best illustrated by the notion of dual embeddedness, i.e. the subsidiary management being subject to countervailing pressures resulting from their embeddedness in the local milieu and their allegiance to the MNC internal structures, policies, and organisational culture [62]. The presence of the subsidiary country nationals on the subsidiary board may seem to be a rational corollary of the need for establishing its social legitimacy in relation to the local communities of business practice and regulatory environment/bodies [79]. However, MNC parents have to then weigh pros and cons of enacting a proactive approach of ensuring that the pursuit of the efforts legitimising subsidiaries to their local stakeholders do not unfold at the expense of the well-conceived interest of the MNC as a whole.

One possible solution is to install parent-country nationals on the subsidiary boards as a governance safeguard against moral hazards on the part of the subsidiary management. There is evidence in the academic literature that the policy of staffing foreign operations at different managerial levels with expatriates can be effective, however it is typically an expensive practice [96]. This is because expatriates, before they commence their international assignments, need to undergo extensive cross-cultural training so that their psychological adjustment to living and working in a different culture is maximally facilitated and eased. Moreover, they also need to be incentivised to want to leave their home country and live abroad for a substantial period of time. This means that the relocation schemes offered represent another significant cost component of enacting the policy of staffing foreign subsidiaries with expatriates.

So, the view of culturally determined agency can serve as a theoretical vantage point for studies undertaking an economic cost-benefit appraisal of the policy of using expatriates. This can be done in comparison with alternative options, such as winning the loyalty of the subsidiary management by the parent-company with the fully transparent policies of resource allocation based on the procedural justice principle within MNCs [97], organising virtual teams involving participation of the board members from both the MNC headquarters and subsidiaries, or calling into existence an international advisory board as an auxiliary collegial body for statutory boards, in the spirit of cross-cultural capability enhancement on an organisation-wide basis.

Proposition 4: The view of culturally determined agency can serve as a vantage point for the cost-benefit analysis of the expatriate staffing policy in an MNC.

Knowledge and innovation management

The modern, knowledge-based economy, characterised by rapid information transfer and exchange, as well as extremely shortened product life-cycles, have enormously raised the bar for companies with regard to generating and sustaining their competitive advantages. The corollary of these developments is the necessity for companies to organise their knowledge and innovation management processes in an extremely effective and efficient way. Indeed, knowledge as a resource and innovation as a capability have become the most critical and, at the same time, coveted strategic capabilities, the possession of which endows a given economic party with power, and hence strong ability to influence organisational politics. Therefore, in the international business literature of today, there has been an increasing emphasis put on implementing flexible and adaptable organisation structures that would allow MNCs to tap knowledge in different geographic locations, because knowledge is increasingly scattered around. In the similar vein, the subsidiary autonomy has to be seen in a new light, in the sense that the subsidiary ability for self-determination and self-government should not be strangled, if a given subsidiary has mastered the activity that is pivotal for the success of the MNC entire value chain. And even more so, if it is able to generate reverse knowledge flows to the MNC parent and other subsidiaries, based on the non-location bound competitive advantage [19,35,76,87,88,91,95,98,99].

The emphasis on knowledge and innovation as key strategic capabilities is not new in the MNC studies. The very early accounts on the subject matter have recognised and accentuated that the non-location bound FSA, as the basis of the MNC establishment and international expansion, is typically knowledge-based. It takes the form of either the R&D expertise or the marketing know-how [100,101]. What is important, however, is that knowledge-intensity of the economy has further dramatically increased and there has occurred a profound reversal of or rather an overall deep change in the patterns of knowledge flows within the MNC’s structure. This means that subsidiaries are increasingly able to generate a non-location bound FSA of their own, and to transfer it either to the MNC parent or other subsidiaries. In consequence, the pendulum of power balance has a tendency to swing away from the corporate core and the power scripts determined d’etre in contractual agreements are not congruent with the de facto distribution of power.

This factual state of affairs in the realm of MNCs leads to a new strategic imperative in the MNC parent-subsidiary relations. Mana-
gerial dexterity of the MNC corporate elite is now reflected in their ability to coordinate and manage the relationships with subsidiaries and among subsidiaries without power or at least with less power than it used to be in the past. In such a setting, the importance of the cross-cultural awareness and sensitivity on the part of the MNC parent’s TMT and board of directors, as accentuated in the view of culturally determined agency of the MNC governance, further gains in salience and prominence. There is imaginably the entire scope of socio-cognitive processes and behavioural tactics that are likely to unfold at the interface of boardrooms at two governance levels in MNCs that can be unveiled in well-designed and well-conducted studies of MNC governance [102-110].

Proposition 5: The view of culturally determined agency can explain the socio-cognitive processes at the headquarters-subsidiary interface as part of the knowledge and innovation management in an MNC.

Conclusion

In this work, by considering the problems of MNC governance I touch upon the raison d’etre of MNCs. There is a substantial void in the literature on both corporate governance and international business. Both these ample and rich research streams have greatly developed over a few last decades, however somehow there is a paucity of contributions that would address research questions that arise at the interface of these fields of research. In recognition of this opportunity for a contribution, I propose a novel theoretical construct of the culturally determined agency. It draws from the behavioural theory of corporate governance and allows for the accommodation of the cultural factors in the analysis of the governance practice. I also discuss the exemplifications of potential applications of this theoretical concept to the state-of-the-art topics of the MNC governance and management that are of high managerial relevance. It is my hope that this theoretical proposition can serve as a useful analytical tool for scholars that will decide to explore this almost unchartered research territory, or that it will at least provoke further discussion and debate on this subject matter.

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