International master franchise agreements: An investigation of control from operational, relational and evolutionary perspectives

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Abstract

Purpose – This paper examines the inter-organisational processes used to control international master franchise agreements from operational, relational and evolutionary perspectives.

Design/methodology/approach – The research is undertaken through a qualitative, in depth case study in the international hotel industry. The case comprises an international master franchise agreement between a large US-based hotel franchisor and its European master franchisee.

Findings – The study identifies the inter-related nature of operational and relational control processes and how these evolve over the life of a master franchise agreement. It reveals how the perceptions of franchise members serve to enhance or inhibit the development of relational norms and how these, in turn, impact on the predominant type of control and the specific inter-organisational processes employed.

Research Limitations – The research is based on a single in-depth case study within one industrial context and the universality of the findings may therefore be limited.

Practical Implications – The paper offers insights to managers of international master franchise agreements on the interaction between members' perceptions, relational norms developed and the inter-organisational processes used to control the agreement. It also reveals how the use of contractual controls can inhibit the development of relational norms and negatively impact on relationships between franchisors and master franchisees. The findings presented may have relevance to managers of other types of international alliance agreements.

Originality/value – By drawing on both the alliance and franchise literature and employing a qualitative approach, the study helps to close a gap in the current international franchise literature through the identification of specific inter-organisational processes for control within international master franchise agreements, how these evolve in respect of relational norms and how these are underpinned by perceptions of franchisor and franchisee members.

Key words - international master franchising, inter-organisational control, relational norms, hotels

Paper Type - Research paper

Introduction

Within retail and service industries, international expansion through franchising has become increasingly popular (Altinay and Wang, 2006; Doherty and Alexander, 2004). In any franchise system, the importance of maintaining a tightly controlled and integrated system that supports a defined brand name and image is well-recognised (Fladmoe-Lindquist, 1996; Quinn, 1999). However, whilst empirical studies on domestic franchising are abundant, international franchise systems have received less attention (Sashi and Karuppur, 2002). Research has tended to focus on the rationale for internationalising, the internationalisation process, or the factors that influence the choice of franchising as an international market entry strategy (see Quinn and Alexander, 2002 or Doherty, 2007a; 2007b for a detailed review). Modal choice studies have subsequently given rise to investigations of operational control and support within international franchise systems (Quinn, 1999; Quinn and Doherty, 2000; Doherty and Alexander, 2006). While this latter stream highlights the importance of inter-organisational processes for control, the research area is still relatively underdeveloped (Doherty, 2007a). Other researchers have identified the relevance of franchisor and franchisee relationships to the control of franchise systems (Perry *et al*, 2002; Doherty and Alexander, 2004; Monroy and Alzola, 2005; Clarkin and Swavely, 2006; Weaven and Frazer, 2007a). Nevertheless, there have been few attempts to consider control concurrently from both operational and relational perspectives.

The link between control and inter-firm relationships has received more attention within the alliance literature. While the importance of clear inter-organisational processes to maintain control is well documented, researchers have also recognised the significance of social controls to manage relational behaviour between alliance partners (Larsen, 1992; Spekman *et al*, 1998; Kauser and Shaw, 2004). Furthermore, empirical studies have highlighted the evolutionary nature of relationships in alliance agreements (Kanter, 1994; Buono, 1997; Batonda and Perry, 2003; Poulymenakou and Prasopoulou, 2004) and the potential impact this might have on the control systems used (Ring and Van de Ven, 1994; Das and Teng, 1998; Gulati, 1998; Dekker, 2004). This research suggests that operational and relational control systems may change over time, yet there is a scarcity of empirical research that examines control simultaneously from operational, relational and evolutionary viewpoints.

Researchers have also identified fluidity in franchisor and franchisee relationships over time (Connell, 1999). However, within the international franchise literature, it is not currently clear whether control systems evolve over the life of franchise agreements or how operational and relational controls impact on each other during this process. This paper reports the findings from an empirical study that addresses this knowledge gap through an investigation of control in international franchise systems from operational, relational and evolutionary perspectives. The research context is international master franchise agreements; a particular type of business format franchising that entitles the franchisee the rights to open franchised units and to grant these rights to third parties as sub-franchisors, usually over a defined geographical territory (Connell, 1999; Quinn and Alexander, 2002). As such, they are contractual agreements that are distinct in their own right, yet bear resemblance to other types of inter-organisational alliances. Given this characteristic, the study examines control from both franchisor and franchisee perspectives, drawing on the alliance literature where dyadic inter-firm perspectives have been incorporated. While business relationships have also been examined within the marketing literature, much of the research has been conducted from a single organisation perspective (Athanasopoulou, 2009).

The paper aims to make a two-fold contribution to the international franchise literature: firstly, investigating operational, relational and evolutionary control in international franchise systems and secondly, by increasing our knowledge and understanding of the use of master franchises as specific franchise system phenomena. It begins with a review of the two literature streams- control in alliance and control in franchise systems- and then draws these two streams together, identifying the specificities of master franchise systems. The research design and findings from a case study are then presented. The conclusion highlights the contributions of the study and offers recommendations for further research and implications for practitioners.

Control in alliance agreements

Although there are a variety of different types of alliance agreements, they are generally considered to be mutually beneficial contractual agreements with a defined purpose and shared resources between two or more firms (Gulati and Singh, 1998; Arino, *et al* 2001; Parise and Casher, 2003; Todeva and Knoke, 2005). The design of effective inter-firm processes to control and coordinate the activities of alliance partners is important (Arino and de la Torre, 1998) as the contract does not provide sufficient control for every future eventuality (Ring and Van de Ven, 1994; Ivens, 2005). Geringer and Herbert (1989:237) suggest that in inter-organisational agreements control is,

‘the process by which one partner influences, to varying degrees, the behaviour and output of the other partner, through the use of power, authority and a wide range of bureaucratic, cultural and informal mechanisms.’

The authors also identify three dimensions of inter-organisational control: focus, extent and mechanisms. Respectively, these refer to the scope of activities monitored, the degree to which control is exercised and the means by which it is achieved. Kauser and Shaw (2004) argue that any investigation of inter-firm control needs to consider all three dimensions.

Geringer and Herbert’s (1989) definition also reflects the role of behavioural, outcome and social controls in alliance management. Other researchers add that these types of control are important both before and after contractual agreements are signed (Das and Teng, 1998; Gulati and Singh, 1998; Dekker, 2004). Behavioural control refers to the actions by and between individuals and partner organisations and their impact on alliance results, whereas output control concerns assessment against these results (Gupta and Govindarajan, 1991). Mechanisms to achieve behavioural control include direct supervision, training, job descriptions, standard operating procedures, formalised policies and the processes used to ensure adherence to these (Cardinal *et al*, 2004; Das, 2005). Outcome control mechanisms include the decision-making processes and tools employed to set budgets, allocate resources and determine quality, and the reporting procedures to monitor performance against targets set (Chang and Taylor, 1999; Cardinal *et al*, 2004). In contrast, social controls are designed to engender interpersonal relationships within and across alliance partners (Ring and Van de Ven, 1994; Arino and de la Torre, 1998). Social control processes include those that influence partner selection and the setting of joint goals to identify potentially long-lasting relationships as well as those used for shared decision making after contracts are signed (Das and Teng, 1998; Gulati and Singh, 1998; Dekker, 2004).

There is some consensus within the literature on the importance of behavioural control to achieve alliance goals (Das and Teng, 1998; Gulati and Singh, 1998; Dekker, 2004; Kauser

and Shaw, 2004). However, Larsen (1992) argues that social controls are the most important to manage the relational behaviour of alliance members. While Spekman *et al* (1998) suggest it would be naïve to rely solely on these, there is a good deal of support for the use of social control processes. Buono (1997) notes that they can add to the development of shared ways of operating to better coordinate the activities of different firms. Social processes are also reported to break down organisational boundaries, increase the permeability between organisations (Martinez and Jarillo, 1989; Dess *et al*, 1995) and thus improve inter-organisational coordination.

Coordination considerations are extensive in inter-firm arrangements (Gulati and Singh, 1998) and need to be carefully considered for any inter-firm learning to take place (Mohr and Sengupta; 2002). Typical mechanisms include communication and information-sharing routines, rules and procedures, liaison and integration roles, cross-functional teams and task forces (Grandori, 1997; Gittel and Weiss, 2004; Tuomela and Salonen, 2005). These coordination mechanisms are reported to be more difficult to manage and potentially more costly without the benefit of some formal and hierarchic control procedures (Gulati and Singh, 1998; Dekker, 2004). However, Gulati and Singh (1998) conclude from their research on buyer-supplier relationships that firms will balance the cost of coordination against the risk of partner firms behaving opportunistically. Furthermore, Ring and Van de Ven (1994) warn that control processes that incorporate excessive legal structuring and hierarchical monitoring of the relationship can be detrimental.

Other researchers suggest that the need for formalised and hierarchic control processes diminishes over time (Foss, *et al*, 2000; Arino *et al* 2001; Dekker, 2004) as the development of trust between firms drives a change to the use of more informal self-enforcing safeguards (Dyer, 1996; Dyer and Singh, 1998; Barringer and Harrison, 2000). Trust relates to both capability to perform required tasks and to goodwill, the expectation that a firm will act in the best interest of the agreement and not behave opportunistically (Cullen *et al*, 2000; Dekker, 2004). Within the literature there is a continued debate as to whether trust acts as a substitute or complement for formal control as it emerges (Ring and Van de Ven, 1994; Das and Teng, 1998; Gulati, 1998; Dekker, 2004) and the need for further research is recognised (Arnott, 2007). Arino *et al* (2001: p111) suggest therefore that relational quality or 'the extent to which the partners feel comfortable and are willing to rely on trust in dealing with one another' is a more relevant construct. Relational quality reflects the sense of unity and balance of power in the alliance. As such, it incorporates other alliance characteristics such as degree of compatibility of corporate cultures, decision-making styles and communication. As alliances evolve (Kanter, 1994; Buono, 1997; Batonda and Perry, 2003; Poulymenakou and Prasopoulou, 2004), the relational experiences between members are reported to drive the development of shared norms of behaviour (Ahuja, 2000; Ivens, 2005) that serve to control the agreement more informally, yet still inhibit opportunistic behaviour.

Research on alliances suggests therefore, that a combination of behavioural, outcome and social controls is important in the management of alliance agreements. These controls comprise formal procedures and mechanisms for decision making to define and monitor financial and quality targets and the inter-organisational processes for communication to share information and coordinate the activities of the different firms. Furthermore, the literature suggests that the combination of these processes may change over the operating life of the agreement. However, empirical findings are mixed, particularly in relation to the impact of the different control processes and mechanisms on each other as alliances evolve.

Control in franchise agreements

As with alliance agreements, control is a fundamental issue within any type of franchise system. Agency theorists have long argued that there are often divergent interests between principals (franchisors) and agents (franchisees) and that franchisees may behave opportunistically to pursue their own interests at the expense of those of the franchisor (Brickley and Dark, 1987; Lafontaine, 1992; Elango and Fried, 1997; Dant and Nasr, 1998; Dahlstrom and Nygaard, 1999; Quinn and Doherty, 2000). Maintaining a tightly controlled and integrated system that supports a defined brand name and image is deemed essential to gain competitive advantage in any type of franchise system (Fladmoe-Lindquist, 1996). However, system-wide growth in international markets is frequently at odds with maintaining a consistent brand image and uniform product and service standards (Wang and Altinay, 2008). Franchisors are faced with the challenge of maintaining uniformity across the franchise system to protect the brand, while at the same time facilitating local responsiveness to meet the demands of different markets (Bradach, 1997; Weaven and Frazer, 2007a).

Hoffman and Preble (1991) identify three different types of control in franchise systems; legal, economic and administrative. The extent to which the contract is the main source of control in franchising has been the subject of a number of investigations (Felstead, 1993; Stanworth, 1991; Stern and El-Ansary, 1992; Fulop and Forward, 1997). As with alliances, there are limitations to its effectiveness in franchising. Some studies suggest that contractual controls are only used when there are serious breaches of agreement (Connell, 1997; Quinn, 1997) or when the franchisor wishes to establish structural system changes (Connell, 1997). The franchisor's willingness to use the contract as a source of power also impacts upon the effectiveness of this control mechanism (Quinn and Doherty, 2000). Furthermore, in international franchising, contracts cannot be standardised and are more difficult to enforce due to the geographic distances involved (Fladmoe-Lindquist, 1996, 2000). Nonetheless, franchisees' fear of losing their investment and their willingness to engage in opportunistic behaviour is based upon the threat of potential expulsion from the system and the associated economic risks (Hopkinson and Hogarth-Scott, 1999) and thus on the franchisor's willingness and ability to enforce the contract. However, in master franchise agreements, the few empirical studies conducted suggest that economic control may be higher. For example, it is suggested that by raising reward expectations, economic control is increased as self-enforcing mechanisms that reduce opportunistic behaviour are created (Kaufmann and Dant, 1996; Bradach, 1998; Bercovitz, 2002; Skalins and Mayer, 2002).

Administrative controls comprise the operational processes used to achieve goal alignment and monitor adherence to these (Hoffman and Preble, 1991). These control mechanisms include decision-making processes and the mechanisms used to monitor financial and quality targets and are similar to output and behavioural controls identified in the alliance literature. Training and brand manuals are frequently used to support franchisees, maintain quality control (Doherty, 2007a) and control brand uniformity (Quinn and Doherty, 2000). Inter-organisational processes for communication and information sharing are also important to the control of international franchise systems (Dant and Nasr, 1998; Quinn, 1998). However, the effectiveness of administrative control is related to the geographical distances involved and the different environments of the host countries (Hoffman and Preble, 1991; Fladmoe-Lindquist, 1996; Elango and Fried, 1997; Quinn, 1998) and is therefore potentially more limited in international franchising. There are further limitations identified in master franchise agreements where responsibility for quality control may be devolved to master franchisees who are also reported to filter franchisor communication (Ryans *et al*, 1999). The

evidence from research is mixed however, with some studies suggesting master franchisees are more likely to behave opportunistically given their unique status (Weaven and Frazer, 2007b); and others suggesting they are more likely to conform to franchisor practice than franchisees operating single units (Dant and Nasr, 1998; Doherty and Alexander, 2006). However, Quinn (1999) argues that many studies have addressed the issue of control superficially and Quinn and Doherty (2000) report the need for further research to determine the mechanisms used to control international franchise systems, master or otherwise.

The control challenges faced by international franchisors have led researchers to consider the importance of franchisor-franchisee relationships, similar to alliance researchers. Hopkinson and Hogarth-Scott (1999) argue that control in franchise systems can be developed through effective relationship management. Managing franchisor - franchisee relationships has also been linked directly to the success of franchise systems (Weaven and Frazer, 2007a) although the factors that influence cooperation in franchise relationships are not well understood (Clarkin and Swavely, 2006). However, Connell (1997) concludes from his study of international master franchising in the hotel industry, that franchisor and master franchisee relationships have an ongoing fluidity and that support structures and communication channels are important to these relationships. Monroy and Alzola (2005) also recognise the evolutionary nature of master franchise agreements and argue conceptually that the quality of relationships in franchise systems develops over time as trust, mutual commitment and relational norms develop. The authors advise that these norms, in turn, reflect the flexibility of franchise members, the perceived mutuality of the agreement, the sense of unity amongst franchise members and the spirit of cooperation. While this argument suggests that relational controls become more important over the life of a master franchise agreement, there is a need for empirical evidence to support it.

Control in alliance and franchise agreements

The review of these two streams of literature highlights a number of similarities in the research findings on control in alliance and franchise agreements, despite the different terminology employed. The limitations of contractual or legal controls are recognised in both literatures, albeit for different reasons. In addition, within both types of agreements, operational and relational control processes are reported to be used in combination to achieve behavioural, outcome and social control. The literature also suggests a good deal of similarity in the control mechanisms and processes used within both types of agreements, despite the differences in how these are labeled. Key control mechanisms in alliance and franchise agreements include inter-organisational processes used to maintain financial and quality control, and inter-organisational processes for decision making, coordination and communication. The relevance of formalised documentation such as brand or training manuals and standard operating procedures is also identified. Table 1 draws together the two streams of literature to summarise the inter-organisational processes used to maintain operational and relational control and the effectiveness of these as reported in the literature.

Table 1 provides evidence of the maturity of research on control within the alliance literature compared to that within franchising, and suggests that a greater understanding of the latter could be gained by drawing on this literature. The shaded areas highlight clear gaps in our understanding of control in international franchising and master franchise agreements that could be better understood through this approach. In particular, Table 1 identifies that there is a need for further research to identify the factors that influence cooperation in international

franchising; the impact of relational controls on operational controls in international and master franchising; and the use and effectiveness of relational controls in master franchise agreements. In an effort to address these knowledge and empirical gaps, this study investigates control in international master franchise agreements from operational, relational and evolutionary perspectives through an investigation of the inter-organisational processes identified in Table 1. In so doing it also extends our understanding of master franchise systems and of international franchising. The design of the study is explained in the following section.

Research design

Research context and case

The research was conducted within the context of the international hotel industry, where master franchise agreements have a long history and continue to be a popular expansion strategy (Strauss, 2007). In addition, this industrial context serves to build on a growing number of empirical studies undertaken within international retailing where academic interest in international franchising is similarly in its infancy (Doherty and Alexander, 2006). Alexander and Lockwood (1996) suggest that there are strong similarities between these two industry sectors and much potential for learning by combining research experiences. The case is an international master franchise agreement for one hotel brand that has been in operation for over 10 years. The length of the agreement is important in exploring how inter-organisational processes and relationships evolve over time.

The case comprises a US franchisor, part of a multi-divisional conglomerate, which owns the hotel brand, and a European master franchisee of that brand, also part of a multi-divisional conglomerate. At the start of the agreement, the franchisor had approximately 270 hotels with over 60,000 rooms in its predominantly North American brand portfolio. The master franchisee operated 29 hotels with around 11,000 rooms in 11 European countries. At the time of the research however, the franchisor's brand portfolio had grown to 450, mostly 3-star hotels with almost 100,000 rooms in 60 countries. Part of this growth was achieved through the master franchisee whose portfolio had grown during the course of the agreement to 110, mostly 4-star hotels, with 29,000 rooms in 38 countries.

Research strategy and data collection methods

In order to fully explore control within international master franchise agreements a qualitative case study was employed. Qualitative studies are increasingly used within international franchise research so that a better understanding of operational issues can be determined (Doherty, 2007a; Weaven and Frazer, 2007a), particularly in studies of retail franchising (Doherty, 2009). The single case study approach was deemed appropriate given that the authors were given exceptional access to those executives involved on both sides of the partnership since it was established and over the extended period of time as it developed. As a leading and long-established brand, the single case enabled 'certain insights' which 'other organizations would not be able to provide' (Siggelkow, 2007: 20). Similarly, Altinay (2004) and Alexander (2009) demonstrate the value of in-depth single case study strategies in franchise and retail research.

Table 1: Control in Alliance and Franchise Agreements

Type of Control: Terms Used		Effectiveness of control		
		Alliance Agreements	International Franchise Agreements	International Master Franchise Agreements
Operational Alliance: Behavioural Outcome Franchise: Administrative Economic	<ul style="list-style-type: none"> • Training, brand manuals, job descriptions, standard operating procedures, formal policies • Inter-organisational processes used to ensure adherence to standards set • Inter-organisational processes for decision making and information sharing used to set budgets, allocate resources, determine quality, monitor performance against financial and quality targets set 	<ul style="list-style-type: none"> • Behavioural controls considered more important than outcome control; relevant pre and post contract • Some hierarchical operational controls required • Operational controls may be replaced by or complimented with relational controls over time 	<ul style="list-style-type: none"> • Administrative controls reduced in international franchise agreements due to geographic distances and market differences; • Economic controls based on threat of expulsion from franchise system and franchisor willingness to use contract 	<ul style="list-style-type: none"> • Administrative controls may be reduced due to degree of quality control devolved to master franchisee and by master franchisee filtering franchisor communication • Economic control potentially greater due to greater financial investment of master franchisee
Relational Alliance: Social Franchise: Relational	<ul style="list-style-type: none"> • Processes for partner selection (pre contract) • Inter-organisational processes for joint goal setting (pre and post contract) • Inter-organisational processes for coordination including communication and information sharing, liaison and integration roles, cross-functional teams and task forces (post contract) • Shared norms of behaviour (post contract) 	<ul style="list-style-type: none"> • Social controls can help to coordinate the activities of different firms in alliances, break down organisational barriers and lead to development of shared norms • Social controls may replace operational controls over time; empirical findings mixed as to whether they complement or substitute operational controls 	<ul style="list-style-type: none"> • Factors that influence cooperation in franchise relationship not clearly understood • How relational controls impact on operational controls not currently identified 	<ul style="list-style-type: none"> • Operational controls underpin franchisor-master franchisee relationships • Evolutionary nature of relationships identified but use and effectiveness of relational controls untested • How relational controls impact on operational controls not currently identified

Primary data was collected using semi-structured key informant interviews; a practice frequently used in organisational studies as it provides an economical approach to gaining 'global' data on organisations (Bryman, 1994:49). The interview schedule was organised according to the inter-organisational processes and mechanisms used for quality and financial control, decision-making, coordination and communication as identified in Table 1. The interview focussed on how these different processes were designed when the franchise agreement was established, how these changed over time and the factors that influenced the decisions that were undertaken and the changes to inter-organisational processes that were implemented.

Multiple interviews were conducted with corporate level franchisor and franchisee informants in North America and in Europe to provide cross-checking opportunities and increase the reliability of the findings. Eight interviews in total were conducted over 20 hours with the Brand CEO and corporate members responsible for strategy, development, marketing and financial management in both the franchisor and franchisee organisations. At least two respondents from each organisation had been involved in the original development of the master franchise agreement thereby providing longitudinal perspectives that are considered important in inter-organisational research (Buono, 1997). For both franchisor and franchisee organisations, three interviews were held within a relatively short space of time and a further interview with an additional respondent was conducted at a later stage to allow the main researcher to look for gaps in the data and to identify issues that needed further clarification.

Additional data was gathered in the form of archival analysis and document review (Yin, 2003) that included:

- organisation charts,
- brand standards and operating procedures,
- job descriptions,
- annual and interim accounts and reports,
- company newsletters and employee magazines,
- press releases,
- internal memos and
- analyst and investor reports.

The resulting triangulation of data helped ensure reliability of the overall findings.

Data was analysed using NVivo according to the 'three concurrent flows of activity' (Miles and Huberman, 1999, p. 16): data reduction, data display and conclusions drawing. Data reduction took place through both descriptive and interpretive coding (Gibbs, 2004). Descriptive coding was undertaken based on the inter-organisational processes investigated. Interpretive coding then took place according to the themes that emerged from the informants. Data was displayed by individual firm and then across the dyadic relationship in order to facilitate comparison across the franchisor and franchisee firms involved. The extant literature was then used to draw conclusions from this study (Perry, 1998), the findings of which are presented in the following section.

Control in international master franchise agreements

The data reveals that inter-organisational mechanisms and processes used to control the master franchise change over the life of the agreement. Three distinct stages of evolution

were identified and drawing on informant responses, these stages have been labelled as formation, development and maturity. The inter-organisational processes for quality and financial control, decision-making, coordination, and communication within each stage are displayed in Table 2. The factors that underpin the decisions for the specific processes employed are discussed below.

Stage one: formation

This first stage began with the identification of the need for a partner firm and lasted throughout the negotiation process. Each firm had a clearly defined purpose for seeking a partner that reflected their organisational growth strategies. Whilst the franchisor was seeking further international expansion through one of its preferred entry modes, the master franchisee sought to grow by 'access to new markets' and senior managers decided they

Table 2 The Evolution of Inter-Organisational Processes in Master Franchise Agreements

Process	Stage One: Formation	Stage Two: Development	Stage Three: Maturity
Control	<ul style="list-style-type: none"> • Negotiated as devolved to master franchisee, including diagnostic systems for quality control • Formal financial controls such as development targets included and monitored centrally 	<ul style="list-style-type: none"> • Control processes become hierarchical • Control dictated by power in the contract to franchisor • Emphasis on control through diagnostic systems including financial contribution to the system and quality indicators • Master franchisee also allowed to use diagnostic mechanisms to monitor output of franchisor 	<ul style="list-style-type: none"> • Control processes became more devolved • Diagnostic systems used to evaluate quality control but monitored by master franchisee or third party organisations • Financial control processes altered and more financial information was shared • Trust reported as essential for this to work • Control enhanced through the development of shared norms
Decision Making	<ul style="list-style-type: none"> • Negotiated to include involvement of master franchisee through formal vehicles such as Global Brand Council 	<ul style="list-style-type: none"> • Decision making becomes more centralised • Master franchisee had very little input, even through formal vehicles due to way they are managed • Tensions between franchisor and master franchisee reported 	<ul style="list-style-type: none"> • Input once more by master franchisee • Some formal vehicles disbanded and replaced by more informal mechanisms and processes • Master franchisee has freedom to adapt initiatives to suit local market conditions
Coordination	<ul style="list-style-type: none"> • Negotiated to include formal vehicles for lateral communication and participative decision making with master franchisee 	<ul style="list-style-type: none"> • Limited coordination processes between franchisor and master franchisee • Master franchisee working towards own goals and not shared goals of franchise network • Differences between franchisor and master franchisee portfolios, operating systems, goals and cultures were emphasised 	<ul style="list-style-type: none"> • Coordination processes increased to include shared conferences, interlocking directorates, greater socialisation and more informal communication • Strong networking between individual members of franchisor and master franchisee firms • Norms of practice develop across franchise network • Members proactively sought areas of commonality to improve integration • Evidence of all working towards the goals of franchise network and beyond extent of original contract
Communication	<ul style="list-style-type: none"> • Frequent and face-to-face communication deemed essential by franchisor and master franchisee, but was limited to senior organisational members involved in negotiating contractual agreement 	<ul style="list-style-type: none"> • Becomes more formal as a result of control and decision-making processes • Becomes less frequent between franchisor and master franchisee • Takes place predominantly at senior organisation levels 	<ul style="list-style-type: none"> • Frequent, informal and through different hierarchical layers • Personal and voice communication essential to reinforce individual relationships • Members willing to share confidential information outside of contractual requirements • At unit level communication remained limited to formal networking opportunities

needed 'a big brother' to gain access to global distribution channels. As one informant from the latter explained,

'we realised very fast that the [proprietary] brand name which is very strong in [the home market] was very weak outside of [the home market]. We needed to have a different brand in order to grow market share.'

However, both firms had previous inter-organisational experiences, not all of which were deemed successful. Maintaining control was therefore important to both parties as they realised that 'who your cousins are is as important as having cousins'. As a franchisee informant explained,

'We wanted to be in the driver's seat and actually control the thing....and in the back of the head was only one thing that we wanted, to keep our own independence'.

Given their previous experiences, both firms were also clear about what contribution they brought to the agreement and the risks they were taking by signing the franchise contract. The mutual recognition of this by both firms was therefore critical in the negotiation process. Whether the risk was deemed acceptable however, was reported to be down to the 'personal chemistry' between the individuals involved in the negotiation process and it was this that kept communication channels open between the respective members. Similarities in organisational goals, values and cultures between the franchisor and franchisee firms were assessed through communication at this stage.

The mutuality of the relationship was also reflected in how the inter-organisational agreement was defined. Despite the fact that the contractual agreement was technically a master franchise, corporate press releases and internal documentation referred to it either as an 'alliance' or 'partnership'. This definition suggests a balance of power in the relationship and this in turn, encouraged the decentralised inter-organisational processes identified in Table 2. While the contract stipulated adherence to brand standards as a quality control process, the franchisees were not subject to detailed operating and brand manuals that dictated formalised policies and procedures. As one franchisee informant summarised,

'we could basically develop our business the way we thought it should be done without any interference or any big hurdles to jump in the relationshipwe retained total operational control of our product....nobody would be throwing any manuals at us'.

Inter-firm processes for financial control were really rather limited at this stage as the franchisee maintained complete control over their capital and operating budgets. However, the contracts did dictate the fee structure and the franchisor set annual revenue targets for the franchisee. Decision-making processes were also decentralised and a number of formal inter-organisational vehicles, such as a Global Brand Council for marketing and human resource decisions, were created to facilitate this process. The limited degree of formalisation also supported this decentralised approach reflecting the control that the franchisee maintained over its portfolio. Once these decisions on operational control were agreed, the contractual agreement was signed. According to informants, the implementation of the agreement was the starting point for the second stage where changes to the agreed inter-organisational processes took place.

Stage two: development

The development phase began with the implementation of the master franchise agreement. Informants referred to this stage as the ‘honeymoon period’ that was ‘painfully slow’ and ‘hugely lacking in trust’. Within the case, a number of problems materialised due to the more tangible differences between the hotel portfolios of the franchisor and master franchisee and their administrative and technological systems. These differences were reported to create a number of ‘territorial issues, cultural issues, technology issues and priority issues’ as more members of both firms began to work together. The way in which the franchisor tried to deal with these issues however, only served to exacerbate them. The franchisor reportedly began to use the contract to govern the agreement, despite the decentralised arrangements agreed upon in the formation stage. The contract clearly depicted that the balance of the power lay with the franchisor that began to use its contractual authority to increase the degree of centralised control, hierarchical decision-making and the degrees of formalisation as illustrated in Table 2. Informants suggested that the franchisor,

‘had a sense of “we must control the brand everywhere in what they do”
.... if you own a brand you really want to have as much control centrally
as possible to ensure that there is consistency.’

There were also financial issues that arose at this stage. The contracts clearly indicated the master franchisee’s contribution to revenue targets as measured through the franchisor’s electronic distribution channels. However, the changes to inter-organisational processes led to the franchisee monitoring the performance of the franchisor to determine whether their fees were justified through the number of reservations derived through these distribution channels. This way of thinking served to further emphasise the differences between the firms and it was suggested that ‘we were still thinking me, you, us, prove your incrementality!’ The situation led each firm to focus upon its own organisation goals, rather than those of the franchise system. As one informant reported,

‘.. having joined the club, you behave very badly. ...which is; [you] don’t
really want to play by the rules of the club.’

Decision making processes also changed at this stage. For example, within the Global Brand Council, originally designed for participative decision making, one informant explained that when it came to sorting out the issues, ‘nobody was under any illusions, it was led by [the franchisor]’ who adopted a centralised approach to decision making. This led to the latter dictating through its ultimate contractual authority what should be done according to the home-country practices.

Communication became predominantly one-way and top-down. However, in the face of the escalating issues and ‘tensions’, that went on for ‘a year, 18 months’ between the firms, the franchisor recognised the need to ‘step up communication’ practices which became more, ‘frequent, informal, verbal and frequently face-to-face’ especially between the senior management of the different firms. Better understanding of the differences between the firms and their markets developed and the franchisor began to fully recognise that they needed to draw on the strong local market knowledge of the franchisee in order to achieve the goals set for the development of the brand. A senior franchisor member reported,

‘it wasn’t necessarily a re-negotiation, it was a realisation’ [of the
differences] and the need to ‘do business differently.’

Face-to-face communication, in particular, was reported to have shifted the perceptions of managers from one of 'recognising the differences' that were a root cause of the inter-firm issues, to one of 'accepting the differences' and learning to work around them. This required franchisor members to, 'listen with the intent to understand, not with the intent to reply'.

Once the franchisor realised the 'need to do business differently', the agreement moved into the third stage. Informants reported that the franchisor realised that using the contract to manage the relationship was not the best approach. With hindsight, one informant reflected that,

'The implication is the second you define your relationship as the terms in your contract, you have a real problem. You know you have to have a legal document that defines how the relationship works and why, but that almost needs to be put in the desk drawer.....If you start pulling out the documents and pulling out specific things, sub paragraphs, you know you are in for a bit of a battle.'

Stage three: maturity

The third stage, described by informants as one of 'maturity' began when the different firms worked collectively for the good of the brand. Prior to this stage, the relationship between the firms had not,

'quite gelled' [and that] 'the heart of the problem was we were still thinking in terms of "me" and "you" and not "us"'.

With this realisation, further changes were made to the inter-organisational processes as identified in Table 2, which once again began to reflect the mutuality in the inter-firm agreement. However, the franchisor still maintained some centralised control over the brand and there were 'certain core elements that [were] sacred', particularly within marketing. Nonetheless, the franchisee was given greater freedom to run marketing programmes and introduce concepts that were not available in the franchisor's home country. In addition, brand standards were replaced with wider brand values, which enabled greater degrees of local variation that reflected market and portfolio differences. The responsibility for monitoring adherence to these values was also devolved to the master franchisee.

There was also greater use of inter-organisational coordination processes at this stage. Annual conferences were reported to have changed from being 'a bit of a jaunt' to an opportunity to 'share success and best practice'. There was also greater movement of staff members between organisations and an interlocking directorate was created. These changes also led to greater franchisee involvement in decision-making as the franchisor, 'stopped hitting us over the head with a baseball bat'. Another informant explained,

'now when it comes to development, it is joint development. It's no longer they go and redevelop and present to the world, they would rather get us involved and we co-develop'.

This approach was reported to incorporate 'the grass root experience from multiple markets' and lead to an approach where the franchisor questioned, 'what is best for the brand and what is best for the partners?'

Communication between the firms devolved down to lower organisational levels at this stage. Formal communication vehicles were superseded to some extent by more informal communication practices used to manage the inter-organisational relationship. For instance, the Global Brand Council was reported to have 'literally petered out', and become an 'anachronism' 'because we get things sorted out by a phone call' and through 'face-to-face meetings'. An informant explained that 'our relationships are such that we have this ongoing dialogue anyway'. This dialogue led to the emergence of acceptable practices between the firms. For example, if there was an issue or query concerning new policies or initiatives, it was deemed poor practice to go to a counterpart's senior manager instead of the counterpart. This practice was considered a 'relationship status thing'. One informant suggested that as a result of these new processes,

'we have a healthy debate about how things are done and a very good exchange of information.'

When these changes in inter-organisational design processes were implemented,

'a watershed was reached' and 'we were seriously able to stop the engagement and get married, really get married'.

Informants reported becoming more 'customer focused', rather than 'proprietary' and to work proactively beyond the terms of the initial contractual agreements. For example there was a greater willingness to share financial and other performance data beyond contractual requirements. As one informant identified,

'you no longer think about "us and them", rather you think about the most cost-effective and customer friendly way of distributing our product'.

Another informant suggested that this required members to move beyond 'accepting the differences' between the different firms, to 'valuing the differences' and the strengths it brought to the brand. The reason for this change was, 'because it is a strong relationship and we trust them and vice versa'.

However, informants also recognised that this new approach could potentially 'open up anarchy and chaos' and a mature relationship was necessary to make this workable. Informants indicated that there had to be,

'trust in the relationship [and that] it is about having the integrity to know there is no hidden agenda'.

The next section applies the findings of this study to the extant alliance and franchise literature to examine the use of operational and relational control through the evolution of master franchise agreements.

The evolution of control in master franchise agreements

The findings presented above clearly identify the evolutionary nature of international master franchise agreements, supporting Connell's (1999) findings and previous empirical studies on inter-firm alliances (Kanter, 1994; Batonda and Perry, 2003; Poulymenakou and Prasopoulou, 2004). Consistent with these previous works, the study reveals that evolution is driven by the need to develop better or more workable inter-organisational designs. However,

by examining control concurrently from operational, relational and evolutionary perspectives, this research builds on the previous body of knowledge by identifying the specific inter-organisational processes for quality and financial control, decision-making, co-ordination, and communication and how these change over time in master franchise agreements. It reveals that these inter-organisational processes are decentralised in the formation stage, centralised in the development stage and decentralised once more when a stage of maturity is reached. These three stages are discussed, in turn, below.

Alliance researchers have previously identified the importance of social or relational controls in the partner selection process (Das and Teng, 1998; Dekker, 2004). This study identifies that these controls are also important in master franchise agreements in the formation stage. The importance of communication in the maintenance of franchisor-franchisee relationships has also been identified (Perry *et al*, 2002; Doherty and Alexander, 2006; Connell, 1997) and that interpersonal interaction facilitates the creation of social relationships (Doherty and Alexander, 2004). Whilst supporting these previous works, this study also identifies the impact these relationships have on the development of control systems and on operational controls used in master franchise agreements. The interactions and communication that takes place between senior members of franchisor and franchisee organisations help to shape perceptions of similarities between firms. These perceptions, in turn, serve to establish a sense of unity between the franchisor and franchisee. As such, the relevance of relational quality to the development of franchisor-franchisee agreements is clearly identified. Relational quality is reflected by what Hopkinson and Hogarth-Scott (1999) refer to as a balance of power between the franchisor and franchisee and hence the mutuality in the inter-firm agreement, previously identified in alliance research (Buono, 1997) and conceptualised in the franchise literature (Monroy and Alzola, 2005). In the case study, relational quality influenced the adoption of decentralised operational control processes without the reliance on standardised operating and training manuals. This study therefore supports previous arguments for the need for both relational and operational control processes in alliance agreements (Gulati and Singh, 1998; Dekker, 2004). However, it adds to our current understanding of master franchising by identifying that perceived mutuality is a factor that influences cooperation and relational controls used in international franchising, a gap identified in Table 1.

In the development stage, this mutuality is undermined when there are difficulties encountered in implementing the agreement. Alliance researchers have previously identified the potential for inter-firm conflict in the development of alliance agreements (see, for example, Kanter, 1994). However, this study builds on this research by identifying the impact of operational control systems on relational quality at this stage. In the case study, more extensive and centralised operational control processes are introduced by the franchisor through the power in the contract. These findings differ from those of Connell (1997) and Quinn (1997) who found that franchisors only use the contract as a control tool when there are serious breaches of agreement or when the franchisor wishes to establish structural changes. This research suggests that perceptions of differences between franchisor and master franchisees can also influence decisions to use contractual control in international franchise agreements.

Differences were noted in portfolios, administrative and technical systems and contractual power was used coercively to centralise operational controls and the decision-making processes and monitoring systems. These served to create resentment amongst franchisee members and encourage opportunistic behaviour. Ring and Van de Ven's (1994) have

argued that control processes that incorporate excessive legal structuring and hierarchical monitoring of the relationship can be detrimental to alliance relationships and this study suggests that this argument also applies to master franchise agreements. The operational control processes introduced reflect a lack of flexibility on the part of the franchisor and led to a lack of cooperation or sense of unity amongst franchise members. As a result, the relational quality (Arino *et al.*, 1997) built in the formation stage deteriorated. However, through enhanced communication and information sharing between the senior members of both firms during a transition period, a greater understanding was developed and members of both organisations started to accept the differences between the two organisations. With this acceptance, relational quality began to recover, and the relational norm of mutuality was reinstated. The franchisor also demonstrated the willingness to be more flexible in the operational control processes used. This study therefore adds to our understanding of relational quality in master franchising by identifying that it is the perceptions of franchise members, not the actual differences between firms, which influence cooperation, further closing this gap identified in Table 1.

As relational quality improved, operational control processes became decentralised again by the final stage of maturity. As these processes were adapted, relational ties increased between franchise members, who started to value the differences between the two organisations and the strength that it brought to the franchise system. In addition to the relational norms of mutuality and flexibility, there was a greater spirit of cooperation amongst these members and a greater sense of unity. Previous alliance and franchise research identifies the role of trust in the development of relational quality (Arino *et al.*, 1997; Doherty and Alexander, 2006) and cooperative behaviour in franchise relationships (Doherty and Alexander, 2004). The study provides empirical support for these findings as it identifies that trust leads to the emergence of shared norms of behaviour, that serve to enhance relational control in master franchise agreements. At the maturity stage, many of the formal operational control processes were deemed unnecessary as members of both firms expected that the other would act in the best interest of the agreement and not behave opportunistically. Previous alliance researchers have also argued that the need for formalised and hierarchic control processes diminishes over time in alliance agreements (Foss *et al.*, 2000; Arino *et al.*, 2001; Dekker, 2004) as self-enforcing safeguards emerge (Dyer and Singh, 1998; Barringer and Harrison, 2000) and this study supports this contention within master franchising. However, as there are still some operational controls used at this stage, this study suggests trust acts as a complement to, rather than substitutes for, formal operational control as it emerges in franchise agreements, as argued by some alliance researchers (Ring and Van de Ven, 1994; Das and Teng, 1998; Gulati, 1998; Dekker, 2004).

The case study highlights the importance of relationship management within master franchising, as did Doherty and Alexander (2004); Clarkin and Swavely (2006), Doherty and Alexander (2006) and Weaven and Frazer (2007a). Furthermore, it provides evidence to support Monroy and Alzola's (2005) conceptual argument that relational norms and controls are developed over time in master franchise systems. However, given the findings from the development stage, this is not necessarily a continual process. The study also offers evidence of the role of trust and balanced power in the development of relational quality in franchising, a finding consistent with empirical alliance studies (Arino *et al.*, 2001; Parise and Casher, 2003; Kauser and Shaw, 2004). Additionally, it supports the findings of Perry *et al.* (2002) who found that trust enhances commitment to the agreement. However, this study adds to our understanding of how these norms are developed through the identification of the perceptions of franchisor and franchisee members and how these influences the relational

norms developed and the type of control used. Four clear and distinct perceptions were identified based on similarities and differences in the two firms.

In the formation stage, the negotiations were brought to a close based on members' mindsets that reflected 'perceptions of similarity' between the franchisor and franchisee organisational goals, values and cultures. In the development stage, relationships waned when the members' focussed on the differences between the franchisor and franchisee organisations. The relationship hit a roadblock at this stage that was characterised by a mindset of 'us and them'. It began to recover when members learned to work through these differences and more specifically, learned to accept them. Franchise members perceptions were thus characterised as a mindset of 'us and them is okay'. This, in turn, led members to develop more ties between the firms and to value the differences between the two firms. As the relationship progressed to the benefit of both franchisor and franchisee a mindset of 'us' developed. These perceptions serve to influence the relational norms developed and these in turn, influence the specific operational and relational inter-organisational processes used to control master franchise agreements and their evolution throughout the life of the agreement. Table 3 depicts how these evolve throughout the three stages identified in this study.

Conclusion

This study sought to address a gap in our knowledge of control in international franchising, and master franchise agreements in particular. By drawing together previous research on alliance and franchise agreements and by examining control concurrently from operational, relational and evolutionary perspectives, it makes a contribution to the literature by identifying the inter-related nature of operational and relational controls and how these evolve throughout the life of master franchise agreements. It provides empirical evidence of the use of both operational and relational controls throughout the life of master franchise agreements, and the specific processes and mechanisms used to achieve these types of control thereby narrowing a gap identified in the international franchising literature. The study also identifies a greater reliance on relational controls in both formation and maturity stages. However, as some operational controls are used as well, it provides empirical evidence that relational controls act as a compliment to, rather than a complete substitute for, operational controls in master franchise agreements. As such it contributes to the current debate in the alliance literature, and to our understanding of how relational controls impact on operational controls in international franchising. Within master franchise agreements, the study suggests that relational controls can serve to overcome implications of reduced administrative operational controls through devolved quality control processes. In addition, given the reliance on relational controls in both formation and maturity stages, there is also empirical evidence that relational control can be effective in master franchise agreements.

The study further identifies that trust between franchisor and franchisee members is a key ingredient in the development of relational quality and franchisor and franchisee willingness to use relational controls. However, trust and relational control can be undermined through the use of hierarchical operational controls, providing further evidence of how operational and relational controls impact on each other. The study reveals how operational controls can in fact, encourage, rather than inhibit opportunistic behaviour by franchisees. Furthermore, it identifies the importance of franchisor and franchisee members' perceptions of the similarities and differences in franchisor and franchisee organisations to the development of

Table 3: The Evolution of Control in Master Franchise Agreements

Stage of Evolution	Members Mindsets	Relational Ties/ Relational Norms	Type of Control	Mechanisms Employed
Formation	Characterised by <u>'perception of similarities'</u>	<ul style="list-style-type: none"> • Positive but limited relational ties • Norm of mutuality 	Operational & Relational	<ul style="list-style-type: none"> • Decentralised quality control processes • Financial targets set & monitored centrally • Participative decision making • Multi-directional communication
Development	Characterised as <u>'us and them'</u>	<ul style="list-style-type: none"> • Relational ties tested • Relational norms inhibited <p>[Transition....]</p>	Contractual & Operational	<ul style="list-style-type: none"> • Centralised quality and financial control processes • Centralised decision making • Management by contract (power) • Formal and less frequent communication <p>[Transition....]</p>
	Characterised as <u>'us and them is okay'</u>	<ul style="list-style-type: none"> • Relational recovery as relational ties resumed • Norms of mutuality and flexibility 	Operational & Relational	<ul style="list-style-type: none"> • Communication increased • Control and decision making processes start to be adapted
Maturity	Characterised as <u>'us'</u>	<ul style="list-style-type: none"> • Relational ties increased and strengthened • Relational norms of mutuality, flexibility, cooperation and trust 	Relational & Operational	<ul style="list-style-type: none"> • Decentralised financial and quality control • Participative decision making • Multi-directional communication through different organisational levels • Shared norms and culture

relational quality and the use of relational controls. The study therefore adds to our current understanding of the factors that influence cooperation in franchise relationships, another gap identified in the international franchise literature.

The findings from this study have important implications for members of master franchise systems. When designing control systems, international master franchisors should consider how relational and operational control processes can be used from the outset of the relationship and how any operational and relational controls implemented might negatively impact on each other. They should also reflect on the degree to which perceptions of similarities and differences in franchisor and franchisee organisations and markets influence the specific control processes adopted. Both franchisors and master franchisees should also try to understand the factors that influence perceptions of similarities and differences to ensure a move to accepting organisational disparities as quickly as possible before relational quality is destroyed. Keeping communication channels open is important to ensuring that organisational members move to value any benefits that organisational differences can bring to the franchise system. In this way, communication can also serve to enhance relational norms and the relational quality developed. Whilst it may be tempting to use contractual controls when inter-firm differences are encountered, these may encourage, rather than prevent opportunistic behaviour and undermine relational norms developed. Franchisors, in particular, are advised to consider the use of relational controls if and when franchise members perceptions are focused on the differences between firms.

Despite the contributions of this study, further research which investigates factors underlying franchise member perceptions and the impact these have on relational quality is very much warranted. Previous research that examines relationship quality within the marketing literature (see for example Athanasooulou, 2009) may be beneficial in informing any further investigation. In addition, research into the effectiveness of economic controls in master franchise agreements and the extent to which they support other operational and relational controls would also be valuable. As a single case study in the hotel industry, there are limits to the generalisability of the findings to other master franchise agreements which may have their own relational dynamics. Therefore, further empirical research, also taking a dyadic and longitudinal perspective, but drawing on a more extensive sample (perhaps comparing the experience of different master franchisees in the same franchise system) and within different industry sectors, would help to validate the findings from this study.

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