

Building Alliances Across Differences?

Center for Gender in Organizations
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Negotiating the Spirit of the Deal: Economic and Social Contracts in Longer-Term Agreements

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Presenter:

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In the presentation summarized here, James Sebenius described observations and hypotheses concerning what he referred to as the social contract and its relationship to the economic contract in the context of long-term interorganizational partnerships. He referred to these as twin contracts. The observations and hypotheses were developed from a detailed analysis of approximately 20 case accounts of strategic alliances and joint ventures. His major claim was that “when you are looking at longer term agreements it can be descriptively accurate, as well as both conceptually and prescriptively useful, to think about negotiating and re-negotiating ‘twin contracts’.” The summary below describes his central ideas, along with hypotheses and observations about them. It also highlights questions that were raised by the presenter and by the audience, respectively.

Central ideas

Dr. Sebenius began by describing the problem that gave rise to this project, and the question that he and his colleagues set out to answer. He also defined the key terms of “social” and “economic” contract more precisely.

The problem and the question

This research began from the observation that the literature does not fully explicate what distinguishes long- from short-term contracts. From an economic perspective, long-term agreements are distinguished by the repeated nature of the transaction between the parties. From a socially-oriented and psychological perspective, what is significant about long-term contracts is the existence of a relationship. This research stems from the view that there are aspects of long-term contracts that need to be considered that are not explained by either the repetitive nature of the transactions or by the relationship. The effort in Dr. Sebenius’ and his colleague’s on-going work is to try to articulate these other aspects.

In order to begin unraveling this problem, there was an initial review and analysis of case studies of about twenty joint ventures and strategic alliances in a broad array of industries. The result of

this analysis was the identification of several categories that distinguished long-term relationships from short-term contracts beyond the repetitive nature of interactions between players and the relationship. These were:

- A potential for significant shift over time in the agreement (e.g., information and knowledge, opportunities that arise).
- The unfolding of events that alter the agreement.
- Complex contracting (e.g., contingencies, risk sharing).

These items, Sebenius noted, are well studied by economists. However, the case analysis also revealed another aspect of long-term contracts not addressed by economists. This aspect, which came to be called the “social contract” by Sebenius and his collaborators, had to do with the expectations jointly held about the nature, extent, and duration of the agreement, and the implicit process norms between the parties. The social contract was illustrated through the following story.

Rover-Honda Joint-Venture Story:

The joint venture between Rover, the British car company, and Honda started in 1979. Rover was in trouble with labor relations, productivity, and market share, and so decided to look to a foreign partner for help. At the time, Honda, was interested in gaining access to markets in the European Community. From Rover’s point of view, Honda was an attractive partner because it had production expertise and interesting technology. The relationship between Rover and Honda began with a licensing agreement. Rover would buy production, tooling, assistance, and exclusive rights to market cars in the European community, and Honda could go elsewhere. By 1981, Honda and Rover had jointly collaborated in building a model that involved some cross-licensing agreements. By 1988, the British Government sold Rover to British Aerospace. The change in partners did not affect Honda negatively. In fact, the relationship between them became very strong. They swapped stock and exchanged board members, and from Honda’s point of view, this was a very important relationship. At Honda, the term “marriage” was often used to characterize the relationship. Eventually, British Aerospace became tired of funding losses, and it decided to sell Rover. Analysts at BMW began to eye Rover, finding it to be very attractive for a whole host of reasons. The problem, however, was that Honda had cross-share holdings with Rover, furnished the technology and design, and, from Honda’s perspective, the two companies were involved in a “marriage” relationship. BMW knew they could not approach the partners directly because there would be a lot of resistance from Honda. So they went to British Aerospace in secret. British Aerospace, in turn, sold Rover to BMW on the sly. The analysts thought the sale was great; the British government and unions thought it was terrible; and Honda thought it was atrocious. But Honda could not stop the sale from happening, because British Aerospace had the legal right to divest itself of its holdings. At this point, the social contract turned very sour. Sebenius noted that what is not captured by extant ideas is the evolving character of relationships exhibited in the Rover-Honda story.

Key Terms Defined

Dr. Sebenius then distinguished and defined the notions of economic and social contract more precisely.

Economic contract:

The economic contract generally refers to the written legal contractual agreements between the parties. It includes financial terms, the required contributions of each party, the mandated governance process, termination provisions, and the allocation of decision rights.

Social contract:

The social contract refers to the set of unarticulated expectations among the parties relating to:

- The nature and extent of the agreement (e.g., opportunistic or open-ended).
- The duration of the agreement—endgame specified and foreseen.
- Process norms guiding interactions (e.g., consultation, decision-making, operation, disclosure, conflicts).

Conceptual clarification—the social contract is not always:

- Simply the working relationship;
- Just trust;
- An implicit contract;
- Democratic and positive—it can be hierarchical;
- Fully shared;
- Purely a psychological contract; or
- The result of fully compatible cultures and values.

Economists have studied most of the aspects of the economic contract in detail. Therefore, Sebenius focused on elaborating on the notion of the social contract. In particular, he discussed and illustrated hypotheses and observations culled from the analysis of cases of joint ventures and strategic alliances in the literature.

Observations and hypotheses

Dr. Sebenius framed the illustration of the following hypotheses and observations with two questions. He indicated that each party in a relationship needs to ask: What is my view of the social contract? What is the other's view of the social contract?

Observation 1

The first observation concerned a question about how social contracts actually work and what it is about the nature of the social contract that either helps or hurts the relationship.

Observation 2

The second observation was that social and economic contracts affect each other bi-directionally. That is, bad social contracts can make the economic contract go badly, and a bad economic contract can hurt the social contract. On the other hand, a good social contract can help the economic contract. Sebenius gave the following examples:

Honda and Rover:

The disjuncture between the operational and holding levels of this joint venture had the consequence of turning a good social contract sour. At the operational level, Honda and Rover had developed a strong working relationship and a positive social contract. Each side invested heavily in the relationship. A new economic contract was forged when BMW was able to persuade British Aerospace to sell Rover, and this sale turned the social contract sour.

Ford and Volkswagen in Brazil:

Ford and Volkswagen formed a joint venture motivated by very attractive economic incentives. Volkswagen was going to make small cars, and Ford was going to make big cars. Due to a shift in economic circumstances, the market was there for small cars, but not for big cars. Ford and Volkswagen were sharing the profits despite the fact that the Ford brand was suffering economically. This alliance concluded with an unforgettable image of a high, barbed wire fence built down the middle of the plant with Ford on one side and Volkswagen on the other. Here the economics had the effect of hurting the social contract.

Observation 3

The third observation was that twin contracts are not static. The social and economic contracts evolve through negotiation and renegotiation as circumstances evolve. For example:

Honda and Rover:

Here there was a very strong social contract, but it turned sour because, from Honda's perspective, the way the new economic contract was forged with BMW was deeply flawed.

Ford and Mazda:

The relationship started as small and opportunistic with some licensing agreements. Then there were lots of twists and turns. Over time, Mazda got in economic trouble, and its Bank asked a senior Ford officer, Henry Wallace, to become Mazda's president in Japan. This act would be unthinkable under normal circumstances. But if you look at it as an evolving series of economic contracts with an elaborated social contract, the act becomes sensible. This is a situation where something small becomes big.

Pediatricians and investors:

A group of pediatricians decided to develop interactive CD-ROMs on family health issues. A venture capitalist "angel" backed them. They agreed to a 50/50 profit sharing deal. The investor

helped the doctors make prototypes of the CD-ROMs, and used industry experience to make contacts. The idea caught on and publishers became very interested. The doctors then turned to the investor and sought to change the terms of their agreement. They argued that the investor's contribution of contacts and money did not justify a 50/50 profit sharing deal. They argued that their investment in training and their profile justified a change in the profit sharing agreement. The investor reacted very negatively, a conflict ensued and escalated, and each held the other in a stalemate. Ultimately, no business ever happened and no profit was generated.

Observation 4

The fourth observation was that the involved parties' view of a social contract may not be shared. This problem is particularly salient in cross-border, generational, cross-industry dealings. The social contract is often implicit, very different, and very problematic. The consequence of this can often be misunderstandings, conflict, and exploitation.

Observation 5

Structural characteristics of the parties can greatly affect the working social contract. For example, in the case of Rover and Honda, there was a strong relationship at the operational level, but not at the holding level. The disjuncture between the holding and the operational levels was so great that it gave an opening to BMW to come in and disrupt the relationship. In order to deal with this problem, it is critical that the right set of people are involved.

Concluding questions raised by the presenter

- Is the notion of the social contract sufficiently robust? Or is this a restatement and repackaging of other well understood phenomena, such as trust?
- How should the concept of social contracts be studied?
- What are the conditions under which strong and weak social contracts arise?
- What are the effects of the social contract on economic performance?
- Will this idea yield empirically grounded prescriptive theory?

Questions raised by the audience

Below are questions raised by the audience that have direct relevance to the theme of working across differences. These questions fall into two thematic categories as indicated below.

Emergent qualities of the social contract

Question:

The example of Rover and Honda suggests that the social contract is emergent. There is likely to be a process by which the parties negotiate a social contract as they work through the things that come up in the relationship. Applying this to the issue of working across differences, we are wondering what has to happen relationally to enable people to form alliances with each other? Do these things get negotiated and are they emergent? How do people from different identity groups know they are at a particular stage of the evolving social contract?

Response:

The social contract is emergent. Generally it is not named, but in some instances it can be very clearly discussed ahead of time.

Further thoughts:

Groups involved in a social contract might also need to deal with unanticipated problems. For instance, a conflict could arise, and a third party could be needed to intervene in order to help the group think about what is going on and to help the parties go on from there.

Context specificity

Question:

To what extent is the process of bringing the social and economic contracts closer together specific to the context, culture, and power relationship between the parties? The example that comes to mind is from Pat Williams' work, where she was describing her experience as an African-American woman trying to foster a relationship of mutual respect and trust with her white male colleague, who was also trying to create with her a relationship of mutual trust and respect. The way he would do this is through a handshake and a pat on the back, which for him was the way to build a trusting relationship. If they had tried to make explicit the terms of the social relationship, they would have changed the terms in ways that he would have found problematic. She, on the other hand, as an African-American woman, was concerned with establishing her credibility, demonstrating her willingness to stand by a bargain, and creating an equal power relationship. It was extremely important to her to negotiate the social relationship as part of the economic relationship; that is, to be explicit about the nature of the social contract. Both had the same end. You could not come in advance with ideas about how to make the twin contracts match without knowing something about the previous set of relationship of the parties.

Response:

Yes, social contracts are context-, person-, and culture-specific, but the dynamic is often the same. Here is a cultural example of a relationship, very self-consciously developed, between a Mexican and a North American partner. The US partner in particular did a lot of work to try to locate the relationship historically. They agreed on terms, and going forward, the U.S partner wanted to write down the agreement. This punctured the deal. Making it explicit by writing it down could destroy the social contract. Before making a contract explicit, partners need to explore whether or not their individual expectations match.

Further reflections on the theme of “Building Alliances Across Differences”

CGO’s learning task is to look at challenges and strategies for building alliances across different identity groups in organizations as a means to promote dual agenda change that fosters both equity and effectiveness. There are many challenges to building these kinds of alliances. Below we suggest places where we felt that Dr. Sebenius’ work on twin contracts has helped us, as well as some observations about where we see some differences when the notion of a “social contract” is applied to working across identity groups.

Negotiating the social contract up front

The notion of dense and multifaceted relationships of the sort that Dr. Sebenius described is critical in our work. That is, we found the notion that boundaries are fluid and people work in each other’s space to be very helpful. However, we questioned the applicability of specifying social contracts up front in our work. When groups or individuals speak from different identities, it is often quite difficult to know enough about one another to specify a social contract up front. Indeed, doing so may even exacerbate conflict by assuming certain ideas or norms we understand across groups. The multiplexed relationships that would allow individuals or groups to even have such a conversation have, in fact, to be negotiated within the context of “creating” a social contract. That is, they must occur in tandem. It is here where it may be useful to think about where there are possible “turning points” in the process of negotiations, and to explore what interventions might be possible in order to renegotiate social contracts.

Motivating factors for change in a social contract

We were also interested in the motivating factors for how a change in the social contract gets started. We thought that the idea that efficiency factors seemed to motivate a change had application, but also thought about who could make that argument, and how that argument could be made in a compelling way, especially when one is talking about different power relationships across groups.

The role of power in negotiating social contracts

Power is a key consideration for us, and so we wonder how it plays out in these case studies. CGO Affiliated Faculty member Karen Proudford’s work on intergroup relations seems to serve as a nice framework for understanding what happened in the Honda-Rover-BMW story. By focusing only on its relationship with Rover, Honda failed to see the key other relationship with BMW.

Social and economic contracts between for-profits and not-for-profits

We were interested in how the notion of “social and economic” contracts plays out when the organizations that are negotiating or establishing some kind of alliance are quite clearly different from one another. Dr. Sebenius referenced Jim Austin’s work on alliances between for-profit and not-for-profit organizations. Austin lays out the different kinds of alliances that these organizations make: basic “check-writing,” explicit transactional (AMEX-Charge for Hunger), and a third, which is a relationship in which the organizations are much more caught up with each other and their relationships much more organic. The partnership between Timberland and

City Year was cited an example of the latter. We were wondering what those third kinds of relationships look like. Is it the case that, in these relationships, it is often assumed that the non-profit holds the “social” end of things and that the for-profit holds the economic end of things? How do they negotiate their relationship, given that one may clearly be in it to get money from an organization, and the other may be in it to gain social capital (e.g., AMEX wants to be seen as a company that “gives back”)? What kinds of “bumps” in the road do these negotiations have? What happens when a non-profit, for example, feels that the for-profit company is “unethical”? Or a for-profit feels that a non-profit is “too radical”?

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