

## **The Influence of Multinational Enterprises on Subsidiaries: Context Matters**

### **Abstract**

**Purpose** – This paper examines how differences in the institutional environment of a multinational enterprise (MNE) shape the role of management control systems (MCSs) and social capital in the headquarters-subsidary relationship of an emerging economy MNE.

**Design/methodology/approach** – A case study design was adopted in this research. Data was gathered by means of semi-structured interviews, document analysis and observations. Interviews were conducted at the Nigerian headquarter (HQ) and United Kingdom (UK) subsidiary of the Nigerian multinational enterprise.

**Findings** – The study found that the subsidiary operated autonomously, given its residence in a stronger institutional environment than the HQ. Instead of the HQ depending on MCSs as a means of coordination and control, it relied on social capital that existed between the HQ and the subsidiary to coordinate and integrate the operation of the foreign subsidiary studied.

**Originality/value** – The reliance on social capital as a means of coordination and control of the foreign subsidiary in this study is significant, given that previous studies have indicated that multinational HQs normally employ MCSs as a means of control of foreign subsidiaries. Also, while previous studies have suggested that MNEs HQs have better expertise which enables them to design and transfer MCSs to foreign subsidiaries, this study found that such expertise relates to the institutional environment from which the HQ is operating from. Through the lens of institutional sociology theory and social capital theory, these findings directly contribute to the literature on the transference of practices and control systems in accounting and international business literatures.

**Keywords:** Emerging multinational enterprises; Multinational enterprises; Management control systems; Social capital; New institutional sociology; and Headquarter-subsidary relationship.

**Paper Type** Research paper

## **Introduction**

The literature on management control systems (MCS) in multinational enterprises (MNEs) suggests that controls are normally designed and transferred from the headquarters (HQ) to the subsidiaries (Hyvonen, 2008; Coates et al., 1992). This argument is predicated on the conventional understanding of MNEs having their HQ in developed countries, which possess stronger institutional and operating environments as well as better expertise than their subsidiaries, which are often based in less developed countries (LDCs). This understanding is however increasingly challenged, given the growing number of MNEs having their HQ in LDCs and subsidiaries in developed countries (Guillén and García-Canal 2009; Mathews, 2006; Yadong and Huaichuan, 2009; Yadong, 2005). The dynamics of this type of HQ-subsidiary relationship raises issues about the design and transferability of controls from HQ to subsidiaries. However, less is known about how developing country based MNEs influence management control in their developed country based subsidiaries. This paper addresses this gap in the accounting and international business literatures.

MNEs are business corporations that operate (have facilities and other assets) in more than one country (Chang and Taylor, 1999). An MNE “consists of a group of geographically dispersed and goal disparate organizations that include its HQ and the different national subsidiaries” (Ghoshal and Bartlett, 1990, p.603). The dispersal of assets, however, comes with the critical tasks of the coordination, control and integration of the activities across geographically dispersed subunits (Roth and Kostova, 2003; Mathews, 2006; Kostova et al., 2008). Furthermore, the complexity in operating an MNE increases because different cultural values, norms and ethnicities are intertwined (Buckley and Ghauri, 2004; Cantwell et al., 2010). For example, the employees of an MNE bring into the organisation different attitudes, values, and goals, which create a complex relationship that may cause interpersonal conflicts and uncertainties (Tan and Mahoney, 2006; Harzing and Feely, 2008; Cantwell et al., 2010).

Chang and Taylor (1999) argued that conflict and uncertainties can be reduced if the HQ of an MNE tries to increase control over foreign subsidiaries. They noted that MCSs “ensures that the behaviours originating in separate parts of the organisation are compatible and support common goals” (p.542). Foreign subsidiaries of MNEs are thus subjected to internal organisational pressures to adopt structures and controls that have been designed at the HQ; however, they may adopt the controls to varying degrees (Kostova and Roth, 2002) depending on their operating environment. Thus, the subsidiary’s response is influenced by the external institutional environment as well as the internal environment of the enterprise (Kostova and Roth, 2002).

Kostova and Roth (2003) suggested “informal approaches” to the coordination of organisational activities where the capacity of formal structures as the elements for coordination and integration of HQ-subsidiary operations is constrained by the institutional environment. Such might be the case where the HQ is based in a weak institutional and operating environment. However, the different dynamics of the HQ-subsidiary relationship with regards to how the subsidiary’s operations are coordinated and controlled by the HQ remains a largely unexplored area of research, despite its potential to enrich the debate in this space. This area of study is even more insightful, given the evidence which suggests that MCSs in organisations in LDCs are politicised, shaped by ethnicity and hardly used as control and coordinating mechanisms (Hopper et al., 2009; Tsamenyi et al, 2008; Efferin and Hopper, 2007; Wickramasinghe and Hopper, 2005). Factors such as culture, religion and the socio-political attributes of a LDC’s institutional environment have been

suggested as having the potential to shape MCSs (Tsamenyi et al., 2004; Hopper et al., 2003). Yet, the design and use of MCSs between developing country HQ and developed country subsidiary has received almost no attention in prior literature. This research attempts to fill this gap by answering the following questions:

- i. To what extent are controls that are designed and used by the HQ of an MNE based in a LDC transferred to the subsidiary in a developed country?
- ii. What is the role of social capital in the coordination and control of the subsidiary by the HQ?

Relying on the theoretical lens of the new institutional sociology and social capital theory, we examine the determinants of the transference of MCSs from a LDC based MNE to the subsidiary in a developed country. This study is contextualised in Nigeria, Africa's largest market for goods and services. A case study of a Nigerian financial services company pseudo named *Nigerian Service Multinational Enterprise (NSMNE)*, which is headquartered in Nigeria, and with a UK based subsidiary was specifically examined. The financial services context in Nigeria, which is characterised as poor in regulatory quality, high in corruption and low in government effectiveness (Kaufmann et al., 2008), provides a useful case study to examine MCSs in weak institutional contexts (Amaeshi, Adegbite and Rajwani, 2016). It further provides a good case study because it requires balancing local (Nigerian) and international (UK) demands (Amaeshi, et. al. 2016). Furthermore, the contrast between the UK's strong institutional environment and Nigeria's weak institutional environment (Adegbite, 2015), offers an interesting case for exploring how differences in institutional environments shape the relationship between the HQ and subsidiary of emerging developing country MNE. The rest of this paper is structured as follows. Next, we provide a review of relevant literature and theorises our research exploration. We then present our methodology, findings and discussions, and finally conclusions.

### **Literature Review and Theory**

The extant literature on accountability in international businesses suggests that for traditional MNEs with HQs in developed countries and subsidiaries in LDCs, controls are mostly designed and transferred from the HQ to the subsidiary (Norreklit and Schoenfeld, 2000). This is justified on the grounds that the HQ operates in a much stronger institutional environment (Elbashir, 2011, Hyvonen, 2008), and controls in LDCs are weak and politicised (Chang et al., 2009; Ferner, et. al., 2005).

Hence, studies of MCSs in MNEs have focused largely on the rational/technical view of controls, with the assumption that controls are designed for the purposes of efficiency and coordination (Canonica, 2010; Woolcock, 1998; Gordon, 2008). MCSs are designed to provide managers with information for decision-making and control, in an effective and efficient way (Anthony and Govindarajan, 2001; Canonico, 2010). MCSs from this perspective are formalised bureaucratic systems such as budgets, performance evaluation systems, formal investment appraisals, and decision-making processes (Ferner, 2000).

However, scholars have argued that MCSs could be designed and used for purposes other than control (Davila et al., 2009; Gomez and Sanchez, 2005; Tsamenyi et al, 2008). Proponents of this perspective posit that MCSs do not necessarily lead to efficiency and coordination (Efferin, 2007;

Wickramasinghe, 2005; Hopper et al., 2009). They suggest that MCSs are not necessarily objective or outside the influence of managers, but are rather socially constructed and context determined (Tsamenyi et al, 2008). Thus, the literature on MCSs in MNEs is increasingly suggesting a broader scope of controls, including formal and informal controls (Chenhall, 2003; Malmi and Brown, 2008; Davila et al., 2009). The pressure on the subsidiary to conform to HQ norms/controls while embracing the local institutional context results in a complex iterative and interactive level of controls that may require an integration process to make them mutually supportive (Yadong, 2005; Norreklit and Schoenfeld, 2000). As a result, a multinational subsidiary is likely to operate with two sets of controls: a set of formal control systems designed and transferred by the HQ, and a set of controls designed internally and shaped by factors at the subsidiary level (Rowley et al., 2000; Woolcock, 2001; Busco et al., 2008). Thus, an interesting question to ask is what shapes the extent to which MCSs in a subsidiary is locally driven or HQ driven. It will be particularly insightful to also know the extent to which controls that are designed and used by the HQ of an MNE based in a LDC are transferred to the subsidiary in a developed country. To shed light on these queries and to understand how differences in an MNE institutional environment shape the role of MCSs, we rely on the new institutional sociology theory and the social capital theory.

The new institutional sociology (NIS) theory argues that organisational systems are influenced by factors from the institutional environment. Hence, organisations may adopt certain processes and procedures as a response to the environment to appear legitimate. It seeks to provide answers to “old questions about how social choices are shaped, mediated, and channelled by institutional arrangements” (Powell and DiMaggio, 1991, p.2). It explores how these actions constrain or encourage the capacity optimisation abilities of managers and privileged others, securing their interests by prevailing rewards and sanctions (Powell and DiMaggio, 1991). While most organisation theorists emphasised the differentiated and diverse world of organisations and tried to provide explanations of the variations in organisational behaviour and structure, the new institutionalism as espoused by DiMaggio and Powell (1983) emerged with a different agenda, to explain homogeneity among organisations rather than seek to explain the variations in patterns (Fernández-Alles and Valle-Cabrera, 2006; Battilana et al., 2009).

Scott (1995, 2001) presented a different perspective of institutionalism. He suggests that organisations, when impacted upon by external environmental factors, may respond in different ways to the influence being exerted on them. This is relevant in this research, since institutional theorists suggest that the external factors impacting on organisations can shape the behaviour of organisational actors as well as the design and use of control systems within the organisation. The new institutional sociology theory in this framework provides the medium for analysing the influence of what Powell and DiMaggio (1991) described as exogenous factors.

However, a major criticism of new institutional sociology theory is that it is too externally focused and ignores the internal (endogenous) factors that shape organisational characteristics. Critics have argued that it fails to recognise that organisations and their systems are shaped by the values, norms of behaviours and beliefs that are held by individuals and groups that work in them. Kotsova et al., (2008) for example criticised the NIS notion that organisational survival is dependent on the extent to which they are aligned with their institutional environments (p.997). They also noted that organisational fields “do not exist in MNC” and the concept of organisational field does not apply to MNCs. Philip and Tracey (2009) have challenged this criticism of institutional theory arguing that it refers to a dated version of institutional theory. However, these criticisms highlight the lack

of consensus in the institutional approach and the call for more studies. Greenwood and Hinings (1996) for example proposed that the combination of the new and old institutional theories would “provide a model for change that links organisational context and intraorganisational dynamics” (p.1024). Hopper and Major (2007) confirmed criticisms of early NIS research for neglecting internal organizational dynamics. They extended the model of Dillard et al. (2004) by incorporating features such as the role of boundary spanners across social levels and how intra-organizational factors play a part. As a result, we broaden the scope of the framework used in this study to capture the internal environment of the organisation and especially, how social capital and interactions between key actors may influence the way MCSs are designed and used.

Social capital theory enables us to do this. The attributes of social capital theory which includes the boundary spanning concept that was incorporated by Hopper and Major (2007) as well as elements that have been highlighted by authors that advocates for a combination of the new and old institutional theories makes it appropriate for this study (see Abrutyn, and Turner, 2011). Social capital is facilitated by interactions with and between networks of actors (Adler and Kwon, 2002). Staber (2006) argued that social capital theory offers a useful foundation and “a process-oriented perspective” which helps to examine the dynamics embedded in managerial practices (p.190). He contended that the theory does not only “seem ideally suited” to explore the issues involved in multinational operations but adds to the understanding of these issues and how they shape practices by emphasising the role of “agency and intentionality”.

Social capital constitutes the resources that actors can access due to there being in a network or structure of social relations (Adler and Kwon, 2002). It is the “benefits that social actors derive from their social structures” (Kostova and Roth, 2003, p.297). From a multinational perspective, Staber (2006, p.190) defined social capital as the “benefits that accrue to a collectivity for maintaining cooperative relations between its members”. It refers to the “social relational properties and processes of the organizational system” (Staber 2006, p.190) that enable coordination and support innovative practices. Social capital is an attribute of successful organisations and is reflected in trust, reciprocity and norms of social behaviour that enable cooperation and integration of activities by regulating social behaviour (Kostova and Roth, 2003).

Scholars however, share different opinions on the sources of social capital and have evaluated the concept from different perspectives. One perspective views social capital as being generated from the collective interactions and shared interests of those within a dense network of strong ties. This implies that social capital is a property of close ties or cohesiveness and can be accessed by being able to mobilise resources within a network of close relationships (Adler and Kwon, 2002, Coleman, 1990). Another view of social capital is a resource that is inherent in actors bridging ties with other actors in other networks (Adler and Kwon, 2002; Bowey and Easton, 2007). Here, social capital is facilitated by interactions with other groups which an actor has direct or indirect contacts with, and it shapes the actions and outcomes of groups or sets an individual, unit or firm apart from competitors (Adler and Kwon, 2002). As Adler and Kwon (2002) suggest, we view social capital in this study as encompassing both bridging and bonding elements.

Thus, we use social capital theory in this study to explore how ongoing social relations combine with the institutional factors of the environment to shape the relationship between the HQ and the subsidiary of an MNE. As Granovetter (1985) argued, institutions that shape organisations are themselves so “constrained by ongoing social relations that to construe them as independent

is a grievous misunderstanding” (p.481-482). Understanding the above argument is becoming more pertinent as the structure of MNEs is changing, with a growing number of these organisations now having HQs in LDCs and subsidiaries in developed countries (Guillén and García-Canal 2009; Mathews, 2006). Yadong and Huaichuan, (2009, p.49) noted that MNEs are emerging from LDCs with “business attributes, dominant motivations, evolutionary trajectory, and strategic behaviours that are in contrast with those of older (North America, European and Japanese) MNEs”. These MNEs from developing countries are not the most advanced in technological and managerial expertise, but are increasingly becoming prominent and occupying strategic places in the global business arena (Yadong, 2005). It is therefore imperative to investigate the extent to which controls that are designed and used by the HQ of the NSMNE based in a LDC were used to control and integrate business operations and the role that social capital may play in such a setting.

## **Methodology and Analysis**

### ***Research Environment***

Understanding the context of the research sets the background and helps to explore, analyse and interpret the key issues discussed by interviewees during the data collection. This is important, especially as qualitative research is constructed based on the meanings that social actors make of their social contexts (Saunders et al., 2008; Smith and Ragan, 2005). The contexts of this research are Nigeria and the UK. On the one hand, Nigeria is a former colony and creation of Britain (Falola and Heaton, 2008). While the legacies of British rule remain influential (Ijeoma, 2002), the Nigerian society is very culturally different. For example, the notion of “kinship” is dominant in the Nigerian society. Kinship is the extension of the responsibility of care to extended family members, a situation described as Nigeria’s form of the UK’s social security by Limbs and Fort (2000). The responsibility to protect kinsmen poses a challenge to the formal systems and structures of controls in organisations. Besides, the cultural difference, customs and values of the Nigerian people make it challenging for enterprises that are structured per the western legacies left by Britain to establish locally viable control systems. As a developing country, Nigeria is faced with many of the problems common to such countries. Prominent among these is the level of illiteracy, poverty, political tensions and corruption (UNESCO, 2015; Kaufmann et al., 2008; Adegbite, 2015).

Corruption is one of Nigeria’s biggest challenges (Olu-Adeyemi, 2012, Olotu and Ogunro, 2013). According to KPMG’s Africa Fraud Barometer (2012), Nigeria, Kenya, Zimbabwe and South Africa are responsible for 74% of fraud cases in the continent. Government officials and senior management staff of MNEs were among the worst perpetrators of fraudulent activities in Nigeria (Randle, 2012). Corruption in the private sector has been conventionally problematic, owing to weak regulation of the governance and conduct of businesses. This is especially the case in the financial services industry, which is regulated by the Central Bank of Nigeria (CBN) (Tahir, Adegbite and Guney, 2016; Adegbite, 2012). The state of the financial services’ regulatory environment and the effectiveness of policy-making bodies are important to this study because they shape the control structures and behaviours prevalent in companies (Child and Tsai, 2005).

The United Kingdom, on the other hand, has a well-established and stable system of government. In comparison with Nigeria, the UK has a strong institutional context, with stable politics and polity, government and regulatory effectiveness and lower levels of corruption (Kaufmann et al., 2008). Furthermore, the British common law principles have become the applicable standard of legal practice in most of its former colonies and a point of reference in other countries (Huntington, 1984, Lijphart, 1991). The separation of power between the judiciary, legislative and executive arms of government is important for the effectiveness of the system (Halliday, 2011). The institutional profile of Britain reflects a contradiction to Nigeria. Understanding the institutional contexts of the research is important because institutional contexts shape social meaning and become reflected on how people make sense of social reality (Meyer and Rowan, 1977) and employ social capital. It is from this understanding that we attempt to address our research questions.

### ***Method***

This paper adopted a qualitative approach that involved semi-structured interviews, observations, and document analysis. This enabled the triangulation of evidence and increased the reliability of the data collected. This approach is useful because elements such as beliefs, norms, and culture are part of the institutional environments and are better captured qualitatively. Furthermore, Alawattage et al. (2007) argued that it is sensible to rely on qualitative methods, in sites where access to reliable data from quantitative methods may prove difficult. Our methodology is consistent with the broad accounting and international business literature in developing countries, especially Nigeria (see Adegbite, 2015; Amaeshi et. al. 2016).

### ***Case study***

To anonymise our case study, we refer to it as the Nigerian Service Multinational Enterprise (NSMNE). The NSMNE has over 700 branches that provide a comprehensive range of retail and corporate financial services in Nigeria. It has international subsidiaries and representative offices in many African countries, as well as in Europe and in Asia.

As one of the leaders in the sector, the NSMNE has played a key role in the financing of private investments in infrastructure development in the Nigerian economy. The NSMNE's contributions to the Nigerian financial services sector have been recognised by international publishers such as The Financial Times Group. It has a primary listing on the Nigerian Stock Exchange, where it is one of the most capitalized companies. The NSMNE is owned by over 1 million shareholders across the world and has an unlisted Global Depositary Receipt (GDR) programme. It has strong ratings from Standard & Poor's and Fitch and attained Information Security Management Systems (ISMS) certification from the British Standards Institution (BSI).

The organisation has been operating nationally in Nigeria for over 50 years and has over 5 million customers nationwide. It has now become international; with a wholly-owned subsidiary in the UK and operational presence in other parts of Sub-Saharan Africa and the Middle East. It is a "full-spectrum" financial services provider, a conglomerate whose operations rank among the most diversified on the African continent. The NSMNE has a strong capital adequacy ratio of 20.04% which is twice the CBN mandated minimum of 10%. Customer deposit is worth over \$9.4 billion and the value of total assets is over \$12.6 billion. The NSMNE is one of the largest corporate and

retail financial institutions in sub-Saharan Africa and pride itself as a reputable enterprise with good corporate governance and effective risk management.

The foregoing highlights our rationale for the choice of the NSMNE as the case study for this research. It is also one of the few emerging MNEs from Africa that has international presence in Europe. An MNE that operates in the UK was imperative for various reasons. First, policies and practices of the Nigerian institutional environment have been largely shaped by the colonial past that Nigeria shares with the UK. Second, the institutional environment of the UK as a developed country is in contrast with Nigeria as a developing country in terms of culture, norms and values and other practices. The contrasting nature of the two institutional environments offers an ideal setting for exploring how the institutional environment shapes the relationship between the HQ and the subsidiary of an MNE. Third, the researchers understand the socio-cultural, political and economic environments of both countries and can communicate with participants in their languages.

### ***Data Collection***

Data collection spanned four months at the Nigerian HQ and UK subsidiary of the NSMNE in the last quarter of 2012. Data was collected at all management levels at the headquarters (in Nigeria) and the UK subsidiary office in London. Non-managerial staff were also interviewed.

NSMNE staff members working at various levels were interviewed. This approach ensured that the data collected were more reliable and objective. It further ensured that rich data that represented the different views of participants were assessed and compared. An understanding of the role of staff members, and an observation of reporting activities, were crucial in the selection of staff members for interviews, since the interview process targeted the key decision-makers in NSMNE. Data was gathered from managers of different departments in the organisation, the directors they reported to, and any superior officer in the hierarchy that the directors may also report to. The interviewees were asked to comment on how differences in the institutional environment shaped the nature of MCSs in the organisation. Questions focused on the design and use of MCSs, the institutional and social capital factors that shape the process and the resulting implication for the HQ-subsidiary relationship.

A similar set of questions were employed in the interviews with directors and the managers, but with variations to the structure of questions, particularly, to fit their job descriptions. This gave an understanding of staff's impact and social capital on the organisation, and how that shapes the design and use of MCSs. It also helped in understanding the relationship between the headquarters and subsidiary of the NSMNE.

A total of 35 participants were involved in the research. Out of the 35 participants, 10 were from the UK subsidiary, while the remaining 25 were interviewed at the Nigerian headquarters. Interviews were tape-recorded, in cases where participants gave their consent. Where participants objected, notes were taken. To ensure anonymity, codes were developed based on the job functions

of interviewees. Codes<sup>1</sup> like BOM1, AOM1 and HBS<sup>2</sup> were used to identify interview participants and indicate the positions they occupy in the company. Participants from the UK were identified using the prefix UK. The interviews lasted between 50 minutes each, on the average. We note that interviewees' responses may be subjective and only recount their views of events which may emphasise aspects that interest them (Shotter & Gergen, 1994). To deal with the potential bias of interviews, documentary evidences were requested where possible and were analysed for consensus (Saunders et al., 2008).

### ***Data Analysis***

Partial analysis of the data collected early in the empirical stage was started while more data were being collected. This was done to enable an understanding of the key issues arising from the process that may not have been put into consideration in the initial design of the data collection instruments. Analysis at the initial stage was focused on the notes taken and not recorded interviews.

The actual analysis of data was a five-stage process. The first stage involved transcribing the tape-recorded data from the empirical process. The second stage involved reading through the data and making notes to aid easier coding. The third stage was the coding of data. The NVivo 10 software was used for this process. Data coding followed an open coding process. Key themes upon which the interview guide was design were used to form the structure (parent nodes) for the NVivo codes. During the coding process, emerging themes that did not fit into the initial classification of nodes were set up either as sub-nodes of existing nodes or as parent nodes. However, not all the data collected during the empirical study could be fitted into nodes. Cresswell (2014) argued that qualitative data are "so dense and rich, not all of the information can be used in a qualitative study" (p.195). Hence, only information relevant to the subject of the research was coded. Our inter-coder reliability was over 80%. We conducted a timeline to answer our two main research questions, using developed nodes to support the development of theoretical logics from our data (see: Amaeshi, et. al. 2016). The next part discusses our findings, using anonymised data from our case study.

### **Findings and Discussions**

Our findings are divided into 5 sub sections. We first discuss the role of MCSs in the HQ-subsubsidiary relationship. We then discuss the institutional factors shaping the extent of subsidiary autonomy and the business relationship with the HQ. The third section discusses social capital as a means of coordination and integration in the absence of imposed controls. Next, we consider the significance of the subsidiary to the NSMNE and organisational social capital. The fifth section discusses subsidiary staffing and potential social capital risk.

#### ***The role of MCSs in the Headquarters-subsubsidiary relationship***

Dacin et al. (2002) suggests that the differences in institutional environments between the HQ and subsidiary of MNEs may determine the relationship between them as well as the strategy that

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<sup>1</sup> Corresponding author will on request provide further information on the interpretation of the codes that have been used in this research to refer to the different interviewees.

<sup>2</sup> BOM and AOM stand for Branch manager and Area manager respectively, while HBS stand for Head of Business strategy.

would be followed to implement the HQ strategic objectives, including MNCs (see also, Rozkwitalska, 2013). Given the differences between the institutional environments of the HQ and subsidiary in our study, our findings indicate that the subsidiary of the NSMNE is operating autonomously. This means that rather than integrating HQ-subsidary strategies through imposing structures and controls, the LDC HQ seeks to benefit strategically from the developed country location of the subsidiary. An interviewee expressed it in the following words: *“What we integrate is not the strategy, what we integrate is what I call the aspirations. So, we may not align the content of the strategy, but the expected result is what we align together”* (HBS).

This finding is consistent with that of Hunschild and Chandler (2008) who argued that institutional pressures could lead to divergent practices rather than similarities in practices, as the mimetic isomorphism of DiMaggio and Powell (1983) suggests. Given the challenges of the Nigerian institutional environment, the HQ seeks to establish its international reputation through the UK subsidiary. The stability and advancement of the UK institutional environment, gives companies more confidence dealing with the NSMNE. An interviewee maintained that:

*“There are several reasons why operating in the UK is of such strategic importance to us (NSMNE). Companies may consider the level of risks associated with dealing with a UK firm more acceptable than dealing with a firm that is operating from Nigeria. For example, there is economic and political stability in the UK and a functioning legal system (in comparison to Nigeria) which might give companies the assurance that they can seek legal redress and get a fair hearing if a contract has not been enforced as agreed”* (AOM1).

The UK environment is in contrast with Nigeria, where the rule of law may be disregarded and a fair hearing difficult to get if legal actions are taken because of the weak legal and regulatory system (Innocent, 2011). As new institutional sociology (NIS) theory explains (Collier, 2001), the NSMNE depends on the subsidiary to gain external legitimacy and to be perceived as an enterprise devoid of the negatives of the institutional environment in which it is headquartered. Dacin et al. (2007) argued that the type of legitimacy that a firm needs and constituent to which a firm must appear legitimate are shaped by the objectives that a firm intends to achieve in an environment, as well as the firm’s characteristics and the characteristics of the environment. Powell and DiMaggio (1991) argued that if organisations are perceived as being like other successful organisations that are operating in the same environment, this gives legitimacy (credibility and acceptance) to the organisation. Our findings indicate a general perception that the actions or activities of the NSMNE were desirable within the socially constructed system of beliefs, values and norms of the UK institutional environment, helping the MNE to detach from the negative institutional perception of its HQ. Our findings also reveal that this divergent path was not only necessary for the subsidiary’s success in the UK, but was only practicable for the subsidiary and not the HQ in the short-term. This is because the challenges of the Nigerian institutional environment which were impacting on operations at the HQ were beyond the control of the HQ. Thus, the HQ could not try to be like the subsidiary. Hence, divergence rather than making efforts to appear like a single-unit enterprise became *“the main motivation for having the UK subsidiary and the reason why controls were not imposed on the subsidiary”* (UK01).

Our findings contribute to existing discourse in this space (Scott, 2005; Greenwood and Meyer, 2008; Dacin et al., 2002; Lounsbury, 2008; Kostova et al., 2008). For example, it supports the heterogeneity perspective of the NIS theory which suggests that variation in practices originates

from the need for organisational actors to act strategically in resistance to institutional forces (Lounsbury, 2008).

An interviewee maintained that:

*“what the subsidiary offers us is expertise at the international level. We have been successful domestically, but lack the experience at the international level. That is why the crop of experienced staff members that we have at the subsidiary are very important in the current scheme of things that management is pursuing” (HBS).*

This assertion is supported by an interviewee at the subsidiary who noted as follows:

*“... don't get me wrong, there are very competent people at the plc (HQ), but most of them have not worked outside Nigeria before. There is the usual saying that experience is the best teacher, and that is why our being here (UK) is important to the plc (HQ)” (UK2).*

From a regulatory perspective, the Financial Services Authority (FSA), which is the UK regulator, was perceived by the HQ as a pace-setter in formulating regulations in the industry. The FSA's regulations are far-reaching and impact on global practice. The experience of operating in such an environment was considered valuable to the NSMNE. An interviewee noted that:

*“...the UK people are ...very important to us (NSMNE). Even if what they may be requesting for will end up on our tables, having the UK people involved gives them (clients and customers) confidence that it will be properly done” (AOM3).*

The HQ is able to retain and attract businesses by referring them to the UK subsidiary, as such businesses seek to avoid the challenges of the Nigerian institutional environment and deal with more stable foreign enterprises. Hence, without being directly involved in the search for opportunities, the subsidiary can contribute to the results of the HQ, which is why the HQ seeks to align results, as noted by interviewee (HBS) earlier. That is, the HQ is more concerned with the strategic role of the subsidiary; hence, it has limited interest in imposing any financial controls.

Nohria and Ghoshal (1994) described the situation where the HQ adopts a strategy to match the subsidiary context rather than integrating the strategies as “differentiated fit” (p.491). Boeker (1989), in their study of factors affecting institutionalisation, found that the prevailing institutional factors at the time an organisation is founded, influence the strategy that is adopted. While the impression from the interviewees indicates that the strategy adopted by the HQ of the NSMNE to allow the subsidiary to operate autonomously was deliberate, a regulation requiring all foreign branches of foreign companies in the UK to be registered as subsidiaries was the reason why the UK subsidiary was incorporated in the first place. This suggests that the UK regulation and its timing may have influenced the strategy of NSMNE, and is consistent with the findings of Boeker (1989). Scott (2001) argued that organisations respond strategically to the impact of the institutional environment, “either by decoupling their structures from their operations or by seeking to defend themselves in some manner from the pressure experienced” (p.152). The reaction to the institutional environment by decoupling structures is consistent with the approach adopted by the HQ of the NSMNE.

A reporting structure that enables the HQ to have representatives on the subsidiary's board of directors serves as a channel through which important information about the subsidiary's activities

are relayed to management at the HQ. This can be regarded as a substitute for the direct use of MCSs. In explaining this, an interviewee noted as follows:

*“So, we have our own board which allows us to be autonomous to a degree, because obviously when we have board meetings every quarter, everything is reported to the board and the representatives of our parent then take that to the management. So, there is a communication link across, so the board interrelates to main board in PLC” (UK2).*

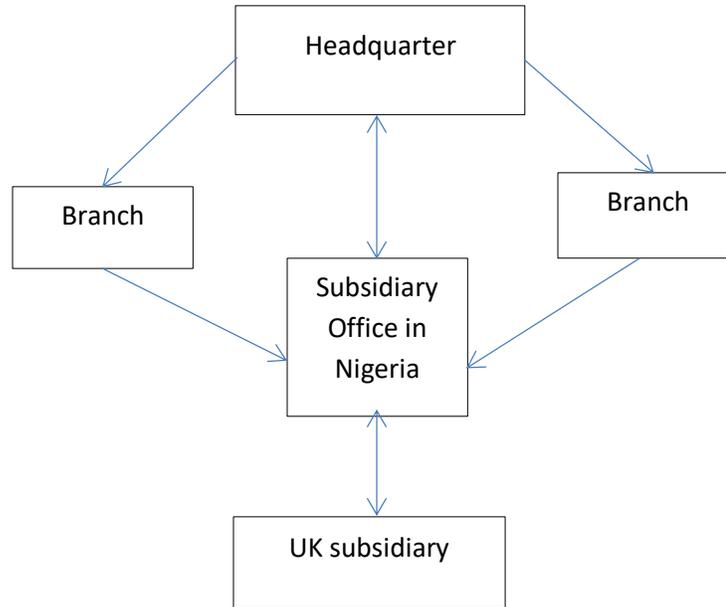
By autonomy, the interviewee (UK2) meant that the subsidiary managers are allowed to use their discretion to make decisions regarding the operations of the subsidiary (see for instance, Birkinshaw and Morrison, 1995). With the subsidiary able to choose how it uses the resources at its disposal (technology, human resources, knowledge and finance), controls from the HQ such as budgetary and performance targets are not imposed on the subsidiary. In the next section, we examine how this subsidiary autonomy shapes the business relationships with the headquarters.

### ***Institutional factors, subsidiary autonomy and business relationships with the HQ***

The business relationship between the HQ and the subsidiary of NSMNE was also shaped by the autonomous status of the subsidiary. While the HQ desires to be seen as a reputable international enterprise able to operate in developed economies such as the UK, direct business dealings between the HQ and the subsidiary was avoided. For this reason, daily business relationships between the HQ and the subsidiary are intermediated through a Nigerian representative/liaison office of the subsidiary. Staff from the representative office are accountable to the subsidiary but work closely with the HQ to bring business to the subsidiary. Interviewee (UK3) acknowledges the representative office role in connecting the subsidiary to the headquarters, as follows: *“You know we have a Lagos representative office, and they work for us and introduce Nigerian customers to London”*. However, in some instances, direct relationships involving communication of business transactions with branches and the head office at the headquarters do occur. These are, however, rare as described by an interviewee below:

*“Basically, the way it works is that, if the transaction originates from a branch, the branch will have to ensure it has been successfully executed for the client and that will require communicating directly with the subsidiary. For example, if someone sends a mail from the subsidiary, and the mail concerns a transaction originating from my desk, I will respond to it. It doesn't happen regularly; it's been more of a one-off event” (FT1).*

Figure 1 illustrates the business relationship between the HQ and the subsidiary of the NSMNE. It shows the representative office in Nigeria, through which customers are referred to the subsidiary and business relationships maintained with the headquarters. However, there may be instances of direct dealings with the subsidiary. The HQ through one of its branches may also have dealings with the UK subsidiary when the services they have rendered to a customer require the attention of the subsidiary. In some cases, the HQ may be required to facilitate transactions for a customer that has had previous dealings with it and is now referred to the UK subsidiary to proceed or take up a different business for the customer.



**Figure 1- The business relationship between the headquarters and subsidiary of the NSMNE**

Thus, the Nigerian representative office provides mutual commercial benefits for the HQ and the subsidiary. Interviewee (UK5) states that: *“this is why it is good to have a big parent as we do, they can introduce us to customers - our parent is the best friend that we have because its size sort of provides what we call open doors for us into customers. And they can help us. Say for example our parent is dealing with a company in the UK - I mean big level, they could in effect say, hang on, let’s introduce our London subsidiary because they can do some stuff for you”*. In the NSMNE, the network of relations created between the HQ and the subsidiary through the Nigerian representative office provides opportunities for the subsidiary to access customers in Nigeria, and provides the HQ with the opportunity to build its profile as an international enterprise and gain external legitimacy. Meyer (2008) argued that a “network relation between actors is a simple form of organisational institutionalisation, and that such relations may ... provide opportunities for their activities” (p.793). For example, the UK subsidiary also improves local legitimacy and reputation in Nigeria, based on the perception that UK-based enterprises possess the capabilities to deliver better quality services than Nigeria (see Agbonifoh and Elimimian 1999; Agboli and Ukaegbu, 2006).

Interviewee UK1 attested to this as follows; *“...we may not be generating as much returns to the plc ..... but, our presence here give customers a higher level of assurance that I can say has enhanced the reputation of the plc”*.

This notion was supported by interviewee HBS who noted that:

*“The value of the UK subsidiary to us (HQ) cannot be overemphasised. As the head of business strategy, my team was involved in the development and implementation of the plan that led to the establishment of the subsidiary and this plaque (shown to interviewer) is a testament to value that management places on what we achieved. The move did raise our*

*profile and it was a smart one because, just after we achieved it, our competitors followed suit”.*

Scott (2001) noted that organisations usually have many network connections and have to “decide what criteria to employ to assess similarity” if pressured by the institutional environment (p.168). He argues that scholars who take an interest in exploring, how organisations choose to be similar and with what organisations, adopt ‘network approaches’. In the next section, we employ the social capital theory in understanding the impact of networks of relationships on organisational processes.

### ***Social capital as means of coordination and integration in the absence of imposed controls***

The NSMNE exhibits a form of organisational social capital in the relationship between the HQ and the subsidiary. Organisational social capital according to Leana and Van Buren (1999) is a resource reflecting the character of social relations within the organization. Our findings show that staff members in the NSMNE share relational ties that are useful in addressing individual differences and self-interested behaviour. Chenhall et al. (2010) noted that relational ties between staff enhance bonding and the flow of information and exchanges between actors, which generates social capital. These relationships may also be shared with those external to the NSMNE (external networks).

In this study, it was found that the benefits of such external networks of relationships, went beyond the subsidiary network to the HQ. An interviewee explained how ideas and information are sourced from external ties as follows:

*“If it is something that has to do with operations, for example, you will get all the like-minded people like me all going to the same place, and we will go and say hi to each other, and it is very useful for various reasons because, .... And we talk to others, our peer group, similar size, similar business, what are they doing, do you know anybody on there, of course you find them and say, guys what are you doing on this issue?” (UK2).*

Another interviewee (UK4) suggests that “*information from external sources does not only help (the subsidiary) to be better informed about regulations and policies, but is also useful to the HQ to get better insight about the policy changes by the regulator and how such policies may affect the NSMNE operation as a whole*”. Also, positive information from external networks of relationship may not only benefit the focal actor that receives the information, but may in some cases benefit the broader aggregate (the subsidiary and the HQ in this case) that are able to make informed decisions based on such information (Adler and Kwon 2002).

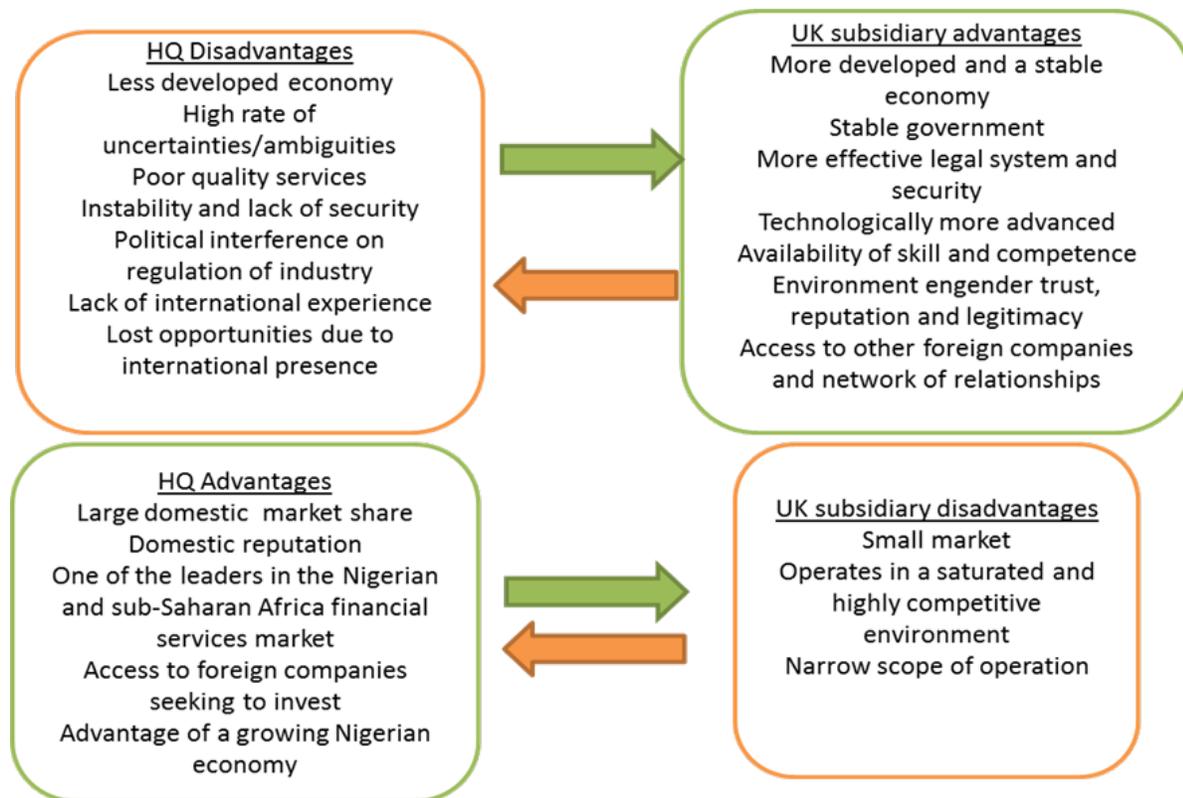
Furthermore, apart from the external information that was beneficial in the pursuit of organisational objectives, the bonding form of social capital between the HQ and the subsidiary also helped the NSMNE to regain its market share, which was consistently threatened by local competition. An interviewee noted that:

*“The subsidiary has been instrumental in the implementation of our transformation agenda and helping us regain our status in the industry. To tell you the truth we were losing grounds to these new generation competitors, some of them got to the UK before us and were taking big businesses away from us because customers were getting the impression that we were not innovative. We lost about 7% of our market share in a space of 5 years and indeed had some catching up to do” (HBS).*

By cooperating and relying on the complimentary capabilities that exist between the HQ and the subsidiary and frequently exchanging information, the NSMNE has been able to retain and attract customers by offering customers services through the subsidiary. The subsidiary is also able to assure big businesses that are reluctant to deal with it because of its size that it can deliver the services they need, by making them aware of the size of its parent and its leading place in the Nigerian financial services industry. An interviewee noted that:

*“Our parent is a big company which gives us access to big companies that would normally not want to do business with us because of our size” (UK4).*

Figure 2 illustrates the complimentary elements that the UK subsidiary and the HQ of the NSMNE share. The figure shows the advantages that the HQ has by operating from the UK. These advantages mainly stem from the confidence and enhanced reputation that the UK institutional environment affords the NSMNE. Despite the size of the subsidiary, it offers the NSMNE a unique advantage that compliments some of the disadvantages of operating from a less developed country.



**Figure 2 Complimentary relationships between the HQ and UK subsidiary**

In sum, the HQ does not rely on using formal MCSs to set performance targets for the subsidiary, but relies on informal processes that encourage the free flow of information, flexibility and adaptive decision-making. Harzing and Noorderhaven (2006) describe this process as “control by socialization and networks” (p.198) which involves building solidarity across the organisation. Adler and Kwon (2002, p.29) described solidarity as a benefit of social capital that is associated

with strong social norms and beliefs, which encourages compliance with rules and reduces the need for formal controls. Through this form of controlling and coordination, the HQ can share benefits in other forms to boost the overall performance of the NSMNE. An interviewee pointed out that *“In NSMNE we look at the larger picture; that is what we have been trained to do. You look at what will be beneficial to the organisation at large (BOM1).*

Birkinshaw et al. (2000) argued that multinational enterprises may be more concerned about worldwide profitability than the specific performance of a subsidiary, thereby focusing on the bigger picture of how that could be achieved. By focusing on the larger picture, the NSMNE is able to explore opportunities cooperatively by exploiting the organisational social capital that exist between the HQ and subsidiary, rather than placing a specific emphasis on subsidiary profitability, which often motivates the use of formal MCSs. Relying on the social capital generated from cooperative relationships between individuals and groups not only helps to improve overall MNE performance, but is also useful in resolving differences among the various actors that are involved in cooperative functions (Masquefa 2008).

### ***The challenges of social capital reliance***

Tan and Mahoney (2006) as well as Yaping (2003) argued that, having expatriates from the HQ in charge of key positions at the subsidiary may be an appropriate way to exercise control and integrate the goals of the HQ and subsidiary. However, the NSMNE presents an interesting case, where none of the traditional recommendations for dealing with integration and control by management and organisational scholars have been applied. On the contrary, the UK subsidiary of the NSMNE can use its discretion to make decisions that support the overall corporate objectives of the NSMNE. Rather than send expatriates to the subsidiary to head key positions to enable the HQ have control of the subsidiary operation, NSMNE has adopted a policy of using locals who have the expertise and understanding of the UK institutional environment to manage the subsidiary's operation. This makes the subsidiary autonomous of the HQ. Hence, rather than send expatriates to manage the subsidiary operation, staff members have been sourced from the UK. Interviewee (UK1) noted that *“We employ experienced staff members who have worked in other foreign MNEs in the UK. Sometimes, staff members from the HQ are sent for secondment duties to gain international experience from the subsidiary. You have to remember that those of them at the Plc (HQ) may have a lot of domestic experience, but the UK is the first international subsidiary of the NSMNE”*.

This has implication, not only for research but for practice and policy in relation to the use of local or expatriate staff to manage the operation of MNEs subsidiary. Yaping (2003) for instance, argued that local staffing of the subsidiary could be risky because of the problem of information asymmetry. That is, *“information available on-site may not be available to a parent company”* (p.728). This may be more problematic if the subsidiary enjoys greater autonomy that gives it accesses to information and specialised knowledge (Hölmstrom, 1979). While social capital has been suggested in this research as a means through which the HQ-subsiary relationship has been maintained, there are risks inherent in the social capital relationship that are based on trust, reciprocity and shared interest.

Tan and Mahoney (2006) found that reliance on the expertise of staff members at the subsidiary enables them to resist pressure for better performance from the HQ. For example, the HQ was in effect conceding that the subsidiary could not be made to perform better because it operates in a different institutional environment. Interviewee (HBS) explained that *“the peculiarity or what I*

*will call the features of that industry sometimes is a challenge. In the UK, the operating environment does not offer more than 12-13% on return on equity. And the group is saying that the subsidiaries should at least return 25%, so you discover that your aspiration locally may not be able to be met by the subsidiary as a result of the environment. So, you see that because of the peculiarity of different businesses, it is sometimes difficult to have the central aspirations that will commonly drive the subsidiary, as I said, because they don't have the same characteristics, different businesses in peculiar environments”.*

Adler and Kwon (2002) posit that, the reliance on social capital (trust and reciprocation) as a means of controlling subsidiary operations may reduce the incentive for entrepreneurial activities that could improve the performance of an enterprise. Social capital scholars argue that this constitutes a social capital risk (Leana and Van Buren, 1999, Adler and Kwon, 2002). That is, the HQ may be paying a price in return for the social capital-legitimacy and knowledge transfer it enjoys. Hansen (2002) for example, found that it took project teams that enjoyed bonding social capital among members longer to complete their task than others with weaker ties among members. This is because maintaining cordiality in the relationship may make it difficult to request better performance from underperforming team members. However, the HQ in this case exercises some level of control through the board of directors of the subsidiary that reviews the decisions made by the subsidiary management, to ensure that the subsidiary operates per its mandate and in the interests of the HQ.

### **Contributions and Future Research**

This paper examines how differences in the institutional environments of a multinational enterprise (MNE) shape the role of MCSs and social capital in the HQ-subsidary relationship of an emerging economy MNE. Contrary to suggestions in the accounting and international business literatures, the MCSs of the headquarters have not been imposed on the subsidiary in our case study of a Nigerian company with a UK subsidiary. We attribute this to the UK strong institutional environment where the subsidiary resides, which did not necessitate a transference of MCSs from a weak institutional context based HQ. Rather, the subsidiary is autonomous and allowed to advance business plans and engage in other activities within the mandate from the HQ in a way which adds value to the NSMNE. The autonomous status of the subsidiary is a deliberate effort of the HQ to present the subsidiary as devoid of the negatives associated with operating from the weak institutional context in Nigeria. It helps the HQ to present the subsidiary as a UK-based and regulated entity that embodies the values of the UK society. This is important because of the perception in the Nigerian institutional environment, that the UK is more developed, more organised and has a legal system which is free from interference, unlike the case with Nigeria. This research particularly contributes to the literature on MCSs by providing insights into how the institutional environments of the MNE may impact the way the HQ of an emerging MNE coordinates and integrates the subsidiary operation. It highlights the usefulness of the NIS in helping to make sense of the institutional environments in which enterprises operate.

It also contributes to the literature by highlighting the significance of relational factors on cross-border integration and the control of business operations in a situation where MCSs are not imposed. Through the lens of social capital theory, the study sheds light on the importance of social relational factors in shaping the cross-border relationships of an MNE. Organisational social capital was particularly found to constitute an important element of the HQ-subsidary relationship

at NSMNE, helping in the integration and coordination of the multinational operations. However, where social capital becomes the main mechanism of coordination and integration of HQ-subsubsidiary operations, the focus may have to be, as in this case, on the need to achieve group goals, rather than specifically designated target goals for the subsidiary. The implication of this is that it may limit the potential of the subsidiary to explore its environment and search for opportunities. These are important insights into the relationship between developed country based subsidiaries and their LDC based HQs.

However, while the social capital theory has been useful in understanding controls and coordination in MNEs, further research might benefit from the exploration of specific ties and structures of the relationships. In this way, an understanding of how the position occupied by actors in a MNE's network, impact on the generation or hindrance of social capital will be insightful for future studies. Also, further research could be conducted to investigate how social capital is implicated in situations of informal control. There is also the need for research aimed at understanding the strategic approach that MNEs from LDCs are adopting in their internationalisation efforts, and how MCSs are implicated or adapted to the strategy that such MNE may choose. Also, the claims that cultural distance may play a part in the use of MCSs for coordination and control of subsidiaries operations could be investigated further. For example, this could be done with two subsidiaries within the West African sub-region and the UK, using multinationals from Africa that operate in both regions. An English-speaking country like Ghana, which shares similarities (colonial history and some cultural practices) with Nigeria, may be a suitable case study. Where language barriers could be overcome, a Francophone country within the region may also be used to aid comparison as Francophone countries share different colonial histories with the English-speaking countries of Africa.

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