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# Investigating Relationship between Control Mechanisms, Trust and Channel Outcome in Franchise System\*

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## Abstract

**Purpose** - The overarching aim of this study is to empirically test the effect of ex-post control mechanisms on multi-dimensional trust and channel performance in franchise systems. Although the franchise system is a vertical marketing channel based on trust between the franchisor and the franchisees, issues related to franchisee's opportunistic behavior have persisted and thus requires research into the effective control system of franchise headquarters.

**Research design, data, and methodology** - In this study, data was collected from 150 franchises to identify the effect of two types of franchising headquarters' control system on the multi-dimensional trust and franchise channel outcome between franchisor and franchisee. To test the hypotheses intended to achieve this aim, structural equations modeling technique is utilized.

**Results** - The results of this research reveal that among the two formal control systems studied (output and process control), output control positively and significantly affects multidimensional trust. Additionally, among the three dimensions of trust employed in this study, only expertise has a positive and significant effect on contract compliance. Equally, only expertise and integrity have a negative and significant effect on opportunistic behavior.

**Conclusions** - The study provides managerial and theoretical insights into understanding ex-post control mechanisms, trust, compliance and opportunistic behaviors in franchise systems.

**Keywords:** Control Mechanism, Multi-dimensional Trust, Compliance, Opportunistic Behavior

**JEL Classifications:** L81, M30, M31.

## 1. Introduction

The predominant aim of establishing strategic alliances is to create value that may prove to be a daunting task for a single firm (Cao & Yan, 2018; Ozdemir, Kandemir, & Eng, 2017; Chiambarretto & Fernandez, 2016). Nonetheless, it takes effective governance to realize value creation in any

form of organizational system. Creating value in any form of strategic alliances or network systems involving joint productions of service may prove to be challenging. An archetypal format of alliance systems is franchising (specifically retail franchising) in which franchisor managers offer support to franchisees across the chain for effective service delivery and good behavioral dispositions aimed at enhancing the business fortunes of the parent brand (Nyadzayo, Matanda, & Ewing, 2015; Yakimova, Owens, & Sydow, 2019). Without a concerted effort between franchisees and franchisor, the franchise network system will struggle to thrive and may eventually collapse. This solidifies the need for effective governance.

Evidence within the franchising scholarship reveals that effective governance encompasses both formal and informal controls designed to complement each other to engender franchisee compliance with the standards and guidelines of the franchisor (Dickey, Harrison, McKnight, & George, 2008; Herz, Hutzinger, Seferagic, & Windsperger, 2016; Yakimova et al., 2019). Among these two main forms of control, extant research has argued that formal controls mostly lead toward

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effective and successful outcomes. Specifically, formal controls seek to curtail franchisee tendencies toward behavioral dispositions that are inconsistent with franchisor standards (Zhang, Lawrence, & Anderson, 2015). This notwithstanding, prior research highlights the fact that such governance systems operate within the framework and ambit of franchisee trust towards the franchisor (Nyadzayo et al., 2015; King, Grace, & Weaven, 2013). This is in keeping with alliance and network governance research which advocates for the strategic adoption of formal control (Wang, Dou, & Zhou, 2012). Due to the nature of formal controls (outcome and behavioral), we contend that an effective association of formal controls and trust will lead toward beneficial exchange relationships.

Despite the burgeoning and blossoming state of alliance and network research, there seems to be a paucity of research that deciphers the nuances of how formal controls enhance trust in franchise systems. Specifically, how process and output controls influence dimensions of franchisee trust remains silent in the current franchise literature. There seems also to be dearth of studies that investigate how trust within the franchise system (specifically franchisee trust) influence behavioral outcomes such as contract continuity and opportunism. Furthermore, most of the existing researches have been done in western and European contexts (Makhija & Ganesh, 1997; Lou & Tan, 2003). From the South Korean context just a few exist. Consequently, this paper sets out to progress knowledge by offering an extended understanding of the effect of ex post control mechanisms on dimensions of trust and how the latter affects contract continuity and opportunism in franchise systems. Through this paper, we make a humble contribution from a South Korean context to the ongoing discussion on effective governance mechanisms in alliances and networks.

## 2. Theoretical Background and Literature Review

### 2.1. Agency Theory

The agency theory is conceptualized as a normative microeconomics/accounting approach for achieving optimal and profit-maximizing forms of control (Eisenhardt, 1985; Bergen, Dutta, & Walker, 1992; Baiman, 1982). The theory incorporates the principal, the agent, environmental uncertainty and the achieved results (Stathakopoulos, 1996) in its elucidation. In typical franchise systems, agency relationships are formed when one firm (herein called the principal) depends on a second firm (herein called the agent) to carry out an action on behalf of the principal. The theory asserts that, problems related to control in principal-agent relationships emerge as a result of disparities in information, goals and risk preferences of the related

parties (Baiman, 1982). The theory is thus, premised on the design of control systems with a motive of realigning the incentives of both principal and agent to ensure that similar outcomes are desired by both parties (incentive compatibility). Control in this theory can be grounded on behavior or outcome. Accordingly, the theory is focused on governance mechanisms that are used by principals to gain control over the actions of agents. Two major governance mechanisms that are evident in the agency theory are the explicit contracts and monitoring (Bergen et al., 1992). Though explicit contracts represent an ex-ante mechanism of management control (Anderson & Dekker, 2005), which is crucial for the commencement of any form of agency relationship, evidence within the current literature suggests that it is not necessarily complete and hazards may still remain even in the presence of mutually agreeable contracts (Anderson & Dekker, 2005).

Consequently, ex-post monitoring has been argued to be essential to the principals in gathering more comprehensive information on the actions and outcomes of agents, especially in the alignment of goals (Eisenhardt, 1989; Jensen & Meckling, 1976). The behavioral (process) monitoring/control approach of the franchisor incorporates regulating franchisee actions or behavior that has the tendency of producing certain outcomes (Todd, Crook, & Lachowetz, 2013; Heide, Wathne, & Rokkan, 2007; Yi, 2018). On the other hand, the output monitoring/control approach of the franchisor takes the form of metering the visible consequences of franchisee actions (Heide et al., 2007). This usually takes the form of franchisee's overall sales volume, sales growth and market penetration. For the purpose of this paper, we limit ourselves to the ex-post control mechanism because that is what actually monitors that real behavior of franchisees and agents after entering into the contract and argue that an effective ex-post formal control (output and process) will engender more trust from the franchisees and will subsequently lead to desired behavioral outcomes. Consequently, in consonance with Heide et al. (2007) we represent monitoring with control (mechanism). The agency theory is therefore relevant and accordingly adopted to provide theoretical basis for this study.

### 2.2. Control Mechanism

Control mechanisms have been conceptualized as key instruments used to monitor the activities and behaviors of members in any formal organization (Koza & Dant, 2007). Drawing from Dekker (2004) and Eisenhardt (1985), control of relationships in and between firms can generally be delineated into outcome, behavior and social control mechanisms. To this end, Bradach (1997) avers that plural firm-franchise systems that take the form of parallel existence of company-owned and franchise units require a blend of these types of controls. Accordingly, Lusch and

**Table 1:** Previous Research on Agency Theory

Author	Title	Summary
Jensen and Meckling (1976)	Theory of the firm: Managerial behavior, agency costs and ownership structure	<ul style="list-style-type: none"> <li>Agency costs are as real as any other costs.</li> <li>The level of agency costs depends, among other things, on statutory and common law and human ingenuity in devising contracts.</li> </ul>
Baiman (1982)	Agency research in managerial accounting: A second look.	<ul style="list-style-type: none"> <li>The paper emphasizes the connection between the principal-agent literature, the transaction cost economics literature and the Rochester literature based on the work of Jensen and Meekling (1976)</li> </ul>
Eisenhardt (1989)	Agency theory: An assessment and review	<ul style="list-style-type: none"> <li>Agency theory offers unique insight into information systems, outcome uncertainty, incentives, and risk.</li> </ul>
Bergen et al. (1992)	Agency relationships in marketing: A review of the implications and applications of agency and related theories	<ul style="list-style-type: none"> <li>Agency theory is likely to prove most useful for examining situations characterized by factors unique to the theory-factors that make contracting with and controlling the performance of agents especially difficult.</li> </ul>
Stathakopoulos (1996)	Sales force control: A synthesis of three theories	<ul style="list-style-type: none"> <li>A comprehensive model of salesforce control systems is developed. Three alternative theories (i.e., organization theory, agency theory, and TCA theory) contribute to the design of optimal control systems</li> </ul>
Anderson and Dekker (2005)	Management control for market transactions: The relation between transaction characteristics, incomplete contract design and subsequent performance	<ul style="list-style-type: none"> <li>Transaction costs are found to be positively related to contract extensiveness.</li> <li>Different transaction characteristics are associated with different control dimensions.</li> </ul>
Heide et al. (2007)	Interfirm monitoring, social contracts, and relationship outcomes	<p>The authors propose that the actual effect of monitoring depends on:</p> <ul style="list-style-type: none"> <li>The form of monitoring used (output versus behavior)</li> <li>The context in which monitoring takes place.</li> </ul>
Todd et al. (2013)	Agency theory explanations of self-serving sales forecast inaccuracies	<ul style="list-style-type: none"> <li>The paper espouses how sales compensations systems can inadvertently cause excessive inventory expenses as a result of self-serving product forecasts by salespeople</li> </ul>

Jaworksi (1991) observe that a combination of control mechanisms is relevant and typical for the retail settings. As intimated earlier, from an agency point of view, the monitoring efforts are aimed at averting and deterring franchisees from behaving opportunistically. In achieving this, the franchisor induces the franchisees to comply with stated clauses and statutes that are included in the franchise contracts (Pizanti & Lerner, 2003; Garg, Rasheed, & Priem, 2005). For the purpose of this research, we limit ourselves to only formal (outcome and process) control mechanisms as these have been argued to give effective outcomes on both behavior and performance.

Evidence within the extant literature has also suggested that trust is a key outcome of control mechanisms (Davie & Prince, 2005). Trust has been operationalized as an important dimension that engineers positive outcomes and enhances the confidence level in any relationship involving two parties. For that reason, we include trust as a key outcome of control mechanisms in franchise systems. Next, we discuss the specific control mechanisms.

### 2.2.1. Process Control

Process control is mostly considered as being cast in the mold of behavioral control. To this end, Wang et al. (2012) and Anderson and Oliver (1987) operationalize process control systems as addressing the process of selling as opposed to the outcomes. In a typical process control system, and specifically situating it within the franchise

context, franchisees may be evaluated and compensated based on any other factor that are not in themselves measures of accomplishment, but may trigger sales performance. In classic control systems, product knowledge, personableness, closing ability, presentation quality, number of active accounts, services performed, calls made, days at work and amount of correspondence are common rubrics (Kang & Jindal, 2015; Jackson, Keith, & Schlacter, 1983; Anderson & Oliver, 1987). In this system, agents are rated by principals based on these variables, which are subsequently weighed and fused into a composite evaluation based upon which decisions on salary and promotion are made. It has been argued that there could be drawbacks to this control approach. For instance there could be complexity and subjectivity of evaluation. The part on subjectivity raises concerns to the effect that subjective ratings of agents (franchisees) by principal(franchisor) may induce bias, halo effects and ignorance; a scenario that increases trepidations about lack of credibility in the evaluation system (Cocanougher & Ivancevich, 1978; Behrman & Perreault, 1982; Jackson et al., 1983).

Despite these drawbacks of process control, the extant literature suggests some profound advantages, which far outweigh the former. The overarching advantage of process control systems is the control they afford the principal. In such a system, the principal (franchisor) imposes his/her ideas of what the agent (franchisee) should be and to achieve desired outcomes. Additionally, in a process control system, franchisor can direct franchisees to perform certain

behaviors as part of the strategy of the company without necessarily convincing the franchisee about the validity of the strategy. In effect, process controls ensure that franchise systems are able to achieve strategies involving developmental work and certain behaviors that are consistent with the strategy of the company. Furthermore, process controls enable the franchisor to eliminate certain inequalities that may emerge in using other control measures. Accordingly, Churchill, Ford, Hartey, and Walker (1985) emphasize that though process controls may engender perceptions of inequity, subjectivity is crucial to the adjustment of performance evaluations.

### 2.2.2. Output Control

Historical evidence suggests that salesforce, managers and the performance appraisal systems adopted by principals have sought to emphasize outcomes rather than behaviors (Mooi & Frambach, 2012), especially in the determination of compensation. A key factor is availability of simple and seemingly equitable measure of sales volume. Some indices used in accessing output control include but not limited to, sales unit volume, gross margin, net margin, and sales costs. (Wang et al., 2012; Behrman & Perreault, 1982). Some arguments have been raised within the extant literature against output control. For instance the inherent lack of direction in such a system may fuel behaviors that could harm the business in the long run. More so, output controls mostly focus the agent (franchisee) on activities with immediate payoffs which are detrimental to the long-term results.

Despite these drawbacks of output controls, some advantages abound. For instance, the fact of agents spending considerable time directly interacting with final customers makes supervision difficult, accompanied by the difficulty to predict success. It is also extremely difficult to profile successful agents and to specify universal rules of thumb with respect to what makes one agent more effective than the other (Weitz, 1981). These and many other bottlenecks have impelled principals to allow their agents to use their own methods (Anderson & Oliver, 1987). Hence, instead of actively directing the agents, they give a varied group of agents, free rein and rather hold them to account for the results. The output control system is the type that has the least resistance. The implication is that it provides a compelling level of individual motivation since non-achievers end up receiving no compensation. This solidifies the long-held position that output controls are meant to maintain motivation. To this end (Wang et al., 2012) notes that Output controls also reflect the extent to which the principal emphasize bottom-line results in personal communications.

### 2.3. Multi-dimensional Trust

The strategic relevance and importance of trust in interpersonal dyads has been reported in the extant

literature (Helm & Tedeschi, 1973). Trust and its strategic role in social business exchanges has been a common interest of researchers in several academic realms (see for instance, Clarkin & Alzola, 2005; Morgan & Hunt, 1994). Trust is regarded as a key prerequisite and a central pivot for successful relationship marketing (Morgan & Hunt, 1994). Hence, from both a connotative and evaluative perspective, trust has been conceptualized as a willingness to depend on an exchange partner in whom one possesses confidence (Moorman, Zaltman, & Deshpande, 1992). It also refers to expectations possessed by one partner that the other is dependable and can be relied upon to deliver on its promise (Sirdeshmukh, Singh, & Sabol, 2002). Embedded within trust are the elements of belief and intent; a behavioral intention to remain in a relationship trustingly (Kim, Jin, & Swinney, 2009; Rousseau, Sitkin, Burt, & Camerer, 1998). The extant literature has acknowledged some dimensions of trust. For instance Mayer, Davis, and Schoorman (1995) identify ability (competence), benevolence, and integrity as key elements of trust. While the Mayer model is widely cited in management and organizational behavior literature for its explanatory power (Carlson, 2019). Others like Kim et al. (2009) operationalize trust from competence-based, benevolence-based and integrity-based trust perspectives. These dimensions have been applied in both consumer and industrial research. Accordingly, competence has been operationalized as the ability to realize promises, which emanates when the organization holds sufficient expertise, knowledge, skills, leadership and other features in related domains (Xie & Peng, 2009). Further, benevolence has been defined as a sincere concern for other's interest and motivation to do good for them while integrity has been theorized as the adherence to a set of sound principles (Xie & Peng, 2009).

Based on previous studies, this paper adopts expertise, benevolence and integrity as key dimensions of trust. We operationalize expertise as a group of skills, competencies and characteristics that affords a party (the franchisor) the ability to have influence within the franchise system domain. This conceptualization lends credence to extant literature (Cook & Wall, 1980; Sitkin & Roth, 1993; Griffin, 1967) which has emphasized similar positions. Further, we operationalize benevolence as the extent to which the franchisor is believed to want to do good to the franchisee aside from the profit motive. This operationalization is consistent with Ishak, Wei, and Romle (2016) who hold similar conviction. Finally we conceptualize integrity as the franchisee's perception that the franchisor adheres to a set of philosophies and *modus operandi* that the franchisee finds acceptable. This position is consistent with Dickey et al. (2008) who made a similar assertion.

### 2.4. Contract Compliance

The extant literature highlights compliance as a key

outcome of motivation, commitment and cognitive processes that jointly drive decisions of one party to execute what the other party desires. From a behavioral school of thought, franchisee compliance refers to conformance to both contractual obligations and relational expectations that are resultant from working norms and embedded in the franchise agreement. Compliance could also be viewed as a continuum where cooperation and opportunism can be found at both ends on the scale (Brill, 1994). According to Elango and Fried (1997), franchisee compliance has become a vital franchisor performance indicator and goal and is deemed highly indispensable for investing in future planning and management, thereby easing the franchisor's entrepreneurial ambition for growth. As a consequence, the franchisor seeks to ensure franchisee compliance to the franchise policy through effective incentive and control systems. To this end, Fenwick and Strombom (1998) opine that franchisees that do not act in compliance with recommended franchise policies end up performing below average profitability. Compliance enables franchisor to strengthen their own legitimacy in satisfying end user needs effectively. The level of influence that the franchisor possesses over the franchisee affects the effectiveness of the franchise. Therefore franchisors have a duty of directly or indirectly influencing the compliance of franchisees with the franchise policies.

## 2.5. Opportunistic Behavior

The viability of franchising as a management approach has been questioned by researchers. For instance Michael (2000, 2002) notes that franchise organizations deliver poorer service and product quality, are less successful marketing strategists and engage in less advertisement compared to a their wholly company owned competitors (Hwang & Suh, 2017). The theoretical implication of this is that franchisees have more incentives to engage in opportunistic behaviors. Accordingly to Brickley, Linck, and Coles (1999) note that some franchisees take advantage of the positive effects of others' investments while minimizing investments of their own. Though franchisor puts in efforts to monitor and control franchisee behavioral dispositions, opportunistic behaviors continue to be a threat to performance and competitiveness of the franchise organizations (Michael, 2002). Williamson (1998) operationalizes opportunism as "self-interest seeking with guile". It can be manifested in different forms, including, but not limited to, withholding facts, exaggerating one's difficulties, distorting and disguising the truth, and even outright lying (Kang & Jindal, 2015). Due to the delicate nature of business relationships, opportunistic behaviors (like those stated above), could generate significant long-term negative consequences (Mooi & Frambach, 2012; Niesten & Heide, 2000).

## 3. Hypothesis Development and Research Model

### 3.1. Process Control and Multi-dimensional Trust

Also referred to as behavior control by some scholars (Wang et al., 2012), process control refers to rules and regulations, as well as standard operating procedures which stipulate the nature and manner in which partners in a franchisee system need to accomplish their assigned tasks. Process controls are adopted to monitor whether the actual behaviors of franchisees tally with their pre-specified behaviors (Dekker, 2004). The extant literature has reported that process controls are associated with positive consequences such sales skills, motivation, job satisfaction, trust, performance, among others (Baldauf, Cravens, & Piercy, 2001b, Challagalla & Shervani, 1996; Piercy, Cravens, & Lane, 2001; Attuahene-Gima & Li, 2002). In keeping with this, scholars like Anderson and Oliver (1987) have argued that process control is associated with higher intrinsic motivation which enables salespeople to learn better ways of doing things, reinforce appropriate behaviors, and gain procedural knowledge which are critical prerequisites in achieving organizational goals. Likewise, the nature of process control leads to enhancing procedural knowledge of franchisees which equips them with the ability to learn better approaches and improve their competence. This advance into enhanced capability and competence as far as their performance and behavior are concerned. Most importantly, process controls are designed with an underlying purpose of the distinct influence on the behavior of the partner (Adler & Borys, 1996). Similarly, process controls are designed to give franchisees regular feedback, flexibility and feedback (Nyadzayo et al., 2015; King et al., 2013). Consequently, this is regarded as a central element which predicts how controls operate within franchise networks and will influence franchisees trust.

Due to its nature of being a system characterized by mutual interdependence and asymmetrical control, the effectiveness of any franchise system is heavily contingent upon substantial manifestations of trust between the franchisor and franchisee. For this reason, the franchisor counts on the franchisee to perform at expected levels and within the ambit of tightly defined guidelines, while the franchisee also depends on the franchisor to both manage (training and process design) and promotional support (brand equity). Consequently, we argue that the control mechanism (process control) rolled out by the franchisor will affect and influence the franchisee's trust in the former, upon which subsequent behaviors (on the part of the franchisee) may emerge. Different dimensions of trust have been proffered in the extant literature (for instance credibility, ability, competence, integrity, expertise, among others) (Davies & Prince, 2005; Mayer et al., 1995).

For the purpose of this paper, we limit trust to expertise, integrity and benevolence. As preconditions for franchisees'

trust, evidence of franchisor expertise, integrity and benevolence are likely to produce vital clues with respect to the health of the franchise system as a whole and its contributory relationships. For this reason, we argue that the process control approach of the franchisor can serve as a signal of expertise. The nature of process control demand high levels of skills and expertise from the franchisor, especially since it involves both control of both routine actions as well as portions that empower the franchisee and build on their capabilities. Hence expertise is viewed as a group of skills, competencies and characteristics and affords a party (the franchisor) the edge to have influence within the franchise system domain (Cook & Wall, 1980; Sitkin & Roth, 1993; Griffin, 1967; Cho, 2017). Based on the foregoing discussions, we argue that the franchisor's process control will positively influence on the franchisee's trust in the expertise of the franchisor.

Benevolence is conceptualized as the extent to which the franchisee believes that franchisor has intentions and motives to do good to the franchisee aside from the profit motive (Ishak, Wei, & Romle, 2016). Benevolence implies that the franchisor has some specific attachment to the franchisee. It stands to reason that through their process controls franchisees may perceive that the franchisor wants to help them (achieve their targets and shape their behavior) and may regard this action as benevolence on the part of the franchisor. Benevolence as a trust dimension is thus the perception of a positive orientation of the franchisor toward the franchisee. To this end Clarkin and Alzola (2005) describes benevolence as the extent that one partner in an exchange system believes that its counterpart has motives and intentions that are beneficial to the other when new conditions arise. For this reason, we argue that the franchisor's process control will engender a positive influence on the franchisees' trust in the benevolence of the franchisor.

Consistent with the foregoing, integrity has been operationalized as the franchisee's perception that the franchisor adheres to a set of principles that the franchisee finds acceptable. Two key features in integrity as a dimension of trust are; adherence to and acceptability of principles. Other issues such as consistency of the franchisor's past actions, credible communications about the franchisor from other parties and the degree to which that franchisor's actions are consistent with his or her words all influence the degree to which the franchisor is considered to have integrity. Ultimately, the manner of the franchisor's process control will send impressions and signals of integrity to the franchisee. As a result, we argue that the nature of process control (in which both the activity and capability of the franchisees) are monitored and controlled will send positive perceptions of integrity about the franchisor and engender a positive influence on the franchisee's trust in the integrity of the franchisor. From the preceding discussions, it stands to reason that process control when effectively

pursued in the franchise system will have positive effects on multi-dimensional trust and hence we advance the following set of hypotheses:

- H1:** Franchisor's process control will have a positive effect on franchisee's multi-dimensional trust.
- H1a:** Franchisor's process control will have a positive effect on the franchisee's trust in the franchisor's expertise.
- H1b:** Franchisor's process control will have a positive effect on the franchisee's trust in the franchisor's integrity.
- H1c:** Franchisor's process control will have a positive effect on the franchisee's trust in the franchisor's benevolence.

### 3.2. Output Control and Multi-dimensional Trust

In typical franchise systems, output control mechanisms specify results that are to be attained by the franchise system and its units. Evidence from Dekker (2004) suggests that in an output control system, rewards and incentives are dependent on task performance and goal achievement. Output control mechanisms do not specify how specific tasks may be executed but which performance goals need to be realized (Koza & Dant, 2007; Lusch & Jaworski, 1991).

Though some extant literature has questioned the outcomes of output control (Stathakopoulos, 1996; Murphy, 2004; Schwepker & Good, 2005), we argue that output control leads to engineering trust among franchisees. Correspondingly, due to the fact that franchisees under output control are inherently motivated to perform and achieve outcomes without apparently unwarranted intrusions, we maintain that franchisees develop trust in franchisor. This assertion lends credence to Wang and Netemeyer (2004) who intimate that franchisees under output controls achieve their goals and develop more trust in the system. Accordingly, Plouffe, Hulland, and Wachner (2009) as well as Roman and Iacobucci (2009) emphasize that output controls grants franchisor the ability to create perceptions of trust among the franchisees when effectively pursued. We argue, based on the foregoing and previous discussions that output control mechanisms when effectively pursued in the franchise system will have positive effects on multi-dimensional trust and hence we submit the following set of hypotheses:

- H2:** The Franchisor's output control will have a positive and significant effect on multidimensional trust.
- H2a:** The Franchisor's output control will have a positive and significant effect on the franchisee's trust in the franchisor's expertise.
- H2b:** The Franchisor's output control will have a positive and significant effect on the franchisee's trust in the franchisor's integrity.

**H2c:** The Franchisor's output control will have a positive and significant effect on the franchisee's trust in the franchisor's benevolence.

### 3.3. Multi-dimensional Trust and Contract Compliance

As discussed previously, trust represents the franchisee's confidence in accepting calculated levels of risk with the franchisor (Coleman, 1990), enabling the franchisees to cope with the vulnerability in relationship with their franchisor. One major outcome of franchisee trust as revealed in the extant literature is compliance, which is operationalized as an outcome of motivation, commitment, and cognitive processes that mutually stimulate decisions of one party to pursue what the other party desires. Behaviorally, franchisee compliance represents conformance to both relational expectations and contractual obligations that are originated from tacit working norms in the franchise contractual agreement. Compliance on the part of franchisees in any franchise system is regarded as an important franchisor performance objective and is viewed as veritable for investing in future management and planning (Payan & McFarland, 2005). The franchisor therefore aims consistently at achieving franchisee compliance to franchise policy through an effective incentive and control system. Compliance enables the franchisor to strengthen its own legitimacy in meeting end user needs and wants as expected. Though extant literature has studied the relevance of compliance in franchise system and how it is achieved, majority of these studies have dwelt on how incentives, controls, transaction analysis, influence strategies, social power as well as literal communications influence compliance (Fenwick & Strombom, 1998). With regards to how trust in the franchise system (specifically franchisee trust) influences compliance, there seems to be paucity. We therefore approach franchisee compliance to a franchisee from a trust (multidimensional) orientation. Therefore we propose the following set of hypothesis:

- H3:** Franchisee's multi-dimensional trust will have a positive and significant effect on the franchisee's contract compliance.
- H3a:** Franchisee's trust in franchisor's expertise will have a positive and significant effect on franchisee's contract compliance.
- H3b:** Franchisee's trust in franchisor's integrity will have a positive and significant effect on franchisee's contract compliance
- H3c:** Franchisee's trust in franchisor's benevolence will have a positive and significant effect on franchisee's contract compliance

### 3.4. Multi-dimensional Trust and Opportunistic Behaviors

Akin to many contractual relationships that involve

delegation, franchising relationships bring in their trail, several problems for franchisors (Combs, Michael, & Castrogiovanni, 2004). Majority of these issues arise because franchisees may engage in certain behaviors that are deemed opportunistic. Behaviors that are classified as opportunistic include, but not limited to, harming a franchisor by leaking proprietary information and intelligence about the franchise, failing to pay royalties, and free riding on other outlets (Kidwell, Nygaard, & Silkoset, 2007; Akremi, Mignonac, & Perrigot, 2011). By positioning franchisees as residual claimants, franchisees are energized to exploit efforts that enhances their own investments (Kaufman, 1994). While this does not completely erase opportunistic behavior, it reduces it substantially (Combs et al., 2004).

One of the major reasons and motives for formal control mechanism is to obviate and discourage opportunistic behavior. Yet, extant research have consistently revealed that formal controls applied by franchisor generally do little in eliminating opportunistic behavior (Shane, 2001; Kidwell et al., 2007; Dant & Nasr, 1998).

In response to this, we argue that beyond formal controls, trust within the franchisor and franchisees will have a better impact in ameliorating any predispositions towards opportunistic behavior. We maintain that since trust represents the franchisee's confidence in accepting calculated levels of risk with the franchisor (Coleman, 1990), it will enable the franchisees to cope with the vulnerabilities in their relationship with the franchisor. Hence, consistent with previous discussions on trust, we surmise that franchisee's trust in the expertise, competence and benevolence of franchisor will reduce their motives and intentions of engaging in opportunistic behaviors. Consequently, we suggest that when high levels of franchisor expertise, integrity and benevolence are substantial, significant value will be anticipated from the franchisor relationship and norms, leading to reduced franchisee opportunistic behavior. Based on this, we proffer the following set of hypothesis:

- H4:** Franchisee's multidimensional trust will have a negative effect on franchisee's opportunistic behavior.
- H4a:** Franchisee's trust in their franchisor's expertise will have a negative effect on franchisee's opportunistic behavior.
- H4b:** Franchisee's trust in their franchisor's integrity will have a negative effect on franchisee's opportunistic behavior.
- H4c:** Franchisee's trust in their franchisor's benevolence will have a negative effect on franchisee's opportunistic behavior.

### 3.5. Research Model

Based on the hypotheses so far derived, the authors presented research model as belows:

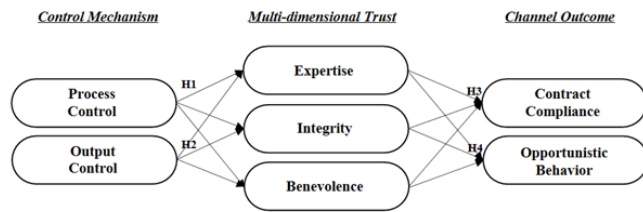


Figure 1: Research Model

## 4. Methodology and Research Design

### 4.1. Operational Definition and Measurements

A quantitative research approach utilizing structured questionnaires was adopted for this study. This was meant to enable the calculations of actual statistical measures of theorized hypothesis on empirical data (Hair, Ringle, & Sarstedt, 2011). The survey questionnaire was made up of two sections. The first section had questions bordering on the constructs of interest in this research (process control, output control, expertise, integrity, benevolence, contract compliance and opportunistic behavior). The statements measuring the constructs were measured on a seven-point likert scale affixed with “1= strongly disagree” to “7= strongly agree”. With respect to the measures, the items for process control were adapted from literature (Wang et al., 2012). The items for output control were adapted from (Wang et al., 2012), while items for expertise were adapted from (Blomqvist, 1997; Doney & Cannon, 1997; Kharouf, Lund, & Sekhon, 2014). Integrity items were adapted from (Blomqvist, 1997; Doney & Cannon, 1997; Kharouf et al., 2014), while items for benevolence were adapted from (Blomqvist, 1997; Doney & Cannon, 1997; Kharouf et al., 2014). The items for contract compliance were adapted from (Dickey et al., 2008) while items of opportunistic behavior were adapted from (Kang & Jindal, 2015).

The second section of the questionnaire centered on the demographic information of the firms (types of franchise

sectors, gender of respondents, as well as period of franchise operations with current franchisor). All the scale items were purified using scale generation and purification processes and techniques proffered by scholars (King et al., 2012; DeVellis, 1991; Flynn & Percy, 2001); specifically through exploratory and confirmatory factor analysis. In order to evaluate the various hypotheses earlier stated in this study, the structural equation modeling (SEM) approach was employed. The SEM is a preferred modeling method because it grants researchers the ability to control measurement error, provides information on the degree of fit of the tested variables and is also able to test multiple relationships (Byrne, 2013).

### 4.2. Samples and Data Collection

Data was obtained from food franchisee firms selected from across South Korea. Purposive sampling was adopted in selecting them. We subsequently contacted the franchise firms through the e-mails, phone numbers and social media accounts stated on their profiles to establish agreements to partake in this study. Prior to the administration of the questionnaire, an adequate assessment of the psychometric properties of the scale items was carried out by testing for face and content validity using some industry experts, as well as marketing professors (Bagozzi & Yi, 1988). For the purposes of minimizing concerns about common method bias (Podsakoff, MacKenzie, & Podsakoff, 2012), information provided by these franchisees came from two categories of personnel in each firm. Particularly, the managers completed the section on the firm profiles/characteristics while the marketing/sales officers completed the predictor and outcome variables. Out of the 170 franchise firms that were contacted, 154 responses were returned from which four (4) of the questionnaires had anomalies and had to be discarded. Consequently, we made use of 150 fully filled and valid questionnaires which were adequate for the intended analysis. The final usable data therefore represented a response rate of 88.2%.

Table 2: Descriptive Statistics of Respondents

Classification		N	%	Classification		N	%	
Types of Franchise Sectors	General Korean Food	6	4.0	Period of Franchise Operation with Current Franchisor	Less than 1 year	15	10.0	
	Meat-related Food	13	8.7		1~2 years	23	15.3	
	Japanese/Chinese	3	2.0		2~3 years	29	19.3	
	HOF	2	1.3		3~5 years	34	22.7	
	Food/Kimbab	22	14.7		5~7 years	21	14.0	
	Pizza/Hamburger	15	10.0		7~10 years	14	9.3	
	Chicken	41	27.3		above 10 years	14	9.3	
	Bakery	17	11.3		Age	20's	9	6.0
	Coffee & Ice Cream	31	20.7			30's	22	14.7
Gender	Male	68	45.3	40's		54	36.0	
	Female	82	54.7	above 50's		65	43.3	



The profile of the sampled franchise firms is presented in Table 2. The results from the distribution of the firms in the franchise sector shows that 4.0% of the firms operate in general Korean food, 8.7% deal in meat-related food, and 2.0% are into Japanese/Chinese food. Franchisees dealing in HOF made up 1.3%, Food/Kimbab (14.7%), Pizza/Hamburger (10.0%), Chicken (27.3%), Bakery (11.3%), as well as coffee and ice cream (20.7%). In terms of the period of franchise operation with current franchisor, 9.3% have been operating with current franchisor for over 10 years while another 9.3% have been operating with current franchisors for a period of 7-10 years. 14.3% have been with the current franchisor for a period of 5-7 years, 22.7% for a period of 3-5 years, 19.3% for a period of 2-3 years and 15.3% for a period of 1-2 years.

#### 4.3. Reliability and Validity Analysis of Variables

The reliability of the measurement items was assessed by examining the loading and the internal consistencies on their corresponding constructs (Fornell & Larcker, 1981). Results indicated standard estimates that ranged from 0.585 to 0.96 with internal consistency (Cronbach's Alpha) values also ranging from 0.766 to 0.925 (see Table 3). Confirmatory Factor Analysis (CFA) was also employed to test the

measurement model. Hair et al. (2011) underscores that most model-fit indices should attain the acceptable standards in order to be eligible for model fitness. As can be gleaned from Table 3, all CFA indicators exceeded the recommended values, indicating adequate fit to the data collected. The six-component CFA fitted the data well, with all indices satisfying their respective benchmarks. Drawing on Anderson and Gerbing (1988), Normed Chi-Square ( $X^2/df$ ) value was 1.435; CFI=0.948; NFI=0.851; RMR=0.026, GFI=0.868, TLI=0.936, and IFI= 0.950. With factor loadings significant at 1 percent, for the sample, convergent validity of the measures was supported (Bagozzi & Yi, 1988). Also embedded in Table 4 is the average variance extracted (AVE) which ranged from 0.538 to 0.806. Discriminant validity was established by comparing shared AVE values between pairs of constructs with their squared phi correlations. In all cases AVE values were greater than the shared squared phi correlations associated with each pair of constructs. This suggests discriminant validity, which is an indication that the constructs are distinct from one another as emphasized by Fornell and Larcker (1981). Table 4 presents the descriptive statistics and the correlation matrix. The correlation coefficients ranged from 0.031 to 0.630. The correlations were significant at both the 0.01 and 0.05 levels of significance.

**Table 3:** Results of Reliability and Validity

Items	Construct	st. estimate	S.E.	C.R.	AVE	CR	Cronbach's a
Process control1	process control	0.811	-	-	0.543	0.887	0.775
Process control2		0.682	0.127	7.583			
Process control3		0.841	0.184	7.512			
Process control4		0.585	0.13	6.648			
Expertise1	expertise	0.76	-	-	0.75	0.914	0.843
Expertise2		0.96	0.141	8.633			
Integrity1	integrity	0.744	-	-	0.579	0.878	0.799
Integrity2		0.811	0.128	8.764			
Integrity3		0.724	0.117	8.059			
Benevolence1	benevolence	0.709	-	-	0.604	0.888	0.807
Benevolence2		0.743	0.126	8.18			
Benevolence3		0.87	0.116	9.056			
Compliance1	contract compliance	0.851	-	-	0.553	0.862	0.766
Compliance2		0.618	0.129	6.788			
Compliance3		0.744	0.108	7.649			
Opportunism1	opportunistic behavior	0.878	-	-	0.806	0.969	0.925
Opportunism2		0.901	0.063	15.346			
Opportunism3		0.914	0.064	15.677			
Output control1	output control	0.682	-	-	0.538	0.888	0.805
Output control2		0.662	0.184	7.119			
Output control3		0.761	0.159	8.02			
Output control4		0.819	0.136	8.471			

Model fit:  $\chi^2=268.318$ ,  $df=187$ ,  $RMR=0.026$ ,  $GFI=0.868$ ,  $NFI=0.851$ ,  $IFI=0.950$ ,  $TLI=0.936$ ,  $CFI=0.948$

**Table 4:** Results of Correlation Analysis

Construct	Mean	st.d	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Process Control (1)	4.0483	.47566	1	.630	.238	.291	.151	.211	-.167
Output Control (2)	3.9817	.51087	.630	1	.304	.395	.309	.271	-.132
Expertise (3)	3.8900	.66269	.238	.304	1	.442	.547	.261	-.177
Integrity (4)	3.8911	.54683	.291	.395	.442	1	.568	.234	-.162
Benevolence (5)	3.8044	.45888	.151	.309	.547	.568	1	.289	-.031
Compliance (6)	4.0978	.39298	.211	.271	.261	.234	.289	1	-.209
Opportunism (7)	2.9467	.90823	-.167	-.132	-.177	-.162	-.031	-.209	1

\*\*p < 0.01; \*p < 0.05

**Table 5:** Results of Hypotheses Test

H	Path	st. estimate	S.E.	C.R.	P	Result
H1a(+)	process control → expertise	0.114	0.157	1.211	0.226	Not supported
H1b(+)	process control → integrity	0.124	0.139	1.27	0.204	Not supported
H1c(+)	process control → benevolence	-0.075	0.118	-0.792	0.428	Not supported
H2a(+)	output control → benevolence	0.368	0.107	3.581	***	Supported
H2b(+)	output control → integrity	0.404	0.126	3.829	***	Supported
H2c(+)	output control → expertise	0.296	0.138	2.99	0.003	Supported
H3a(+)	expertise → contract compliance	0.24	0.088	1.906	0.057	Supported
H3b(+)	integrity → contract compliance	0.096	0.125	0.626	0.531	Not supported
H3c(+)	benevolence → contract compliance	0.072	0.151	0.447	0.655	Not supported
H4a(-)	expertise → opportunistic behavior	-0.298	0.195	-2.44	0.015	Supported
H4b(-)	integrity → opportunistic behavior	-0.252	0.281	-1.672	0.095	Supported
H4c(-)	benevolence → opportunistic behavior	0.336	0.346	2.085	0.037	Not supported (reversed)

Model fit:  $\chi^2=375.606$ ,  $df=194$ ,  $RMR=0.053$ ,  $GFI=0.833$ ,  $NFI=0.792$ ,  $IFI=0.887$ ,  $TLI=0.863$ ,  $CFI=0.885$

#### 4.4. Model Fit and Hypothesis Test

The parameter estimates presented in Table 5 depict the final results which gives a better illumination to the findings of the study in consonance with the proposed hypotheses. The model-fit indices for the structural model gave enough evidence of a good model fit ( $\chi^2/df=1.936$ ,  $RMR=0.053$ ,  $GFI=0.833$ ;  $NFI=0.792$ ;  $IFI=0.887$ ,  $TLI=0.863$ ,  $CFI=0.885$ ). H1a states that franchisor's process control will positively and significantly influence franchisee's trust in the expertise of the franchisor. Our results revealed that there was positive but insignificant relationship between process control and expertise ( $\beta=0.114$ ,  $p>0.05$ ). H1b states that franchisor's process control will positively and significantly influence franchisee's trust in the integrity of the franchisor, which was a positive but insignificant effect of process control on integrity ( $\beta=0.124$ ,  $p>0.05$ ). H1c states that franchisor's process control will positively and significantly influence franchisee's trust in the benevolence of the franchisor. The result showed a negative and statistically insignificant relationship ( $\beta=0.11$ ,  $p>0.05$ ). H2a of the study (output control positively and significantly affects expertise) was positive and statistically significant ( $\beta=0.296$ ,  $p<0.05$ ). Similarly, H2b (output control positively and significantly affects integrity) was positive and significant ( $\beta=0.404$ ,  $p<0.05$ ). Furthermore, H2c that asserts that output control

positively and significantly influence benevolence was positive and statistically significant ( $\beta=0.368$ ,  $p<0.05$ ). Additionally, H3a (expertise has a positive and significant effect on contract compliance) was positive and statistically significant ( $\gamma=0.24$ ,  $p<0.05$ ). However, H3b (integrity has a positive and significant effect on contract compliance) was positive but insignificant ( $\gamma=0.09$ ,  $p>0.05$ ). Equally, H3c (benevolence has a positive and significant effect on contract compliance) was positive but insignificant ( $\gamma=0.072$ ,  $p>0.05$ ). Nonetheless, H4a that states that expertise has a negative and significant effect was negative and significant (supported) ( $\gamma=-0.298$ ,  $p<0.05$ ). H4b (integrity is negatively and significantly related to opportunistic behavior) was also negative and significant (supported) ( $\gamma=-0.252$ ,  $p<0.05$ ). Finally H4c was that franchisee's trust in the benevolence of the franchisor will have a negative and significant effect on opportunistic behavior. To this, the results showed a statistically significant but positive relationship.

## 5. General Discussion

### 5.1. Theoretical and Practical Implications

This paper highlights franchisees' trust towards franchisor as a consequence of ex-post formal control mechanisms and

how the former subsequently influences contract compliance and opportunistic behaviors. The study examined these relationships grounded on the Agency theory. Generally, the study found output control as the former control mechanism that is germane to multidimensional franchisee trust. This result is consistent with previous research (Koza & Dant, 2007; Lusch & Jaworski, 1991). Prior research has shown that in a typical output control system, franchisees enjoy high levels of job autonomy since they are only responsible for results and are less monitored for their routine activities (Dekker, 2004). Specifically, Plouffe, Hulland, & Wachner (2009) as well as Roman and Iacobucci (2009) surmise that output control grants franchisor the capability to generate perceptions of trust among the franchisees when successfully pursued. Thus in consonance with previous research, our study reinforces the position that franchisor's output control is a key antecedent to franchisee trust in the franchisor.

However, the results could not lend support for the positive relationship between process control and franchisee trust. Though this outcome is unexpected, it lends credence to some previous research. For instance, Hutlink and Atuahene-Gima (2000) underscore that process control is less effective in motivating agents which might affect their development of trust in the principal. Similarly, Deci, Koestner, and Ryan (1999) assert that process control limits autonomy and signals distrust in agents. Heide, Wathne, and Rokhan (2007) agrees with the foregoing by positing that process controls (which are aimed at regulating behaviors obstructively and decreasing autonomy) may engender reactance, lead to loss of trust and even opportunism. This study therefore from a franchise system perspective, reinforces the assertion that process controls may not necessary have positive influences on trust building in relational exchange systems.

Additionally, the findings reveal that among all the three dimensions of trust, only expertise had a positive and significant effect on contract compliance. Unlike many other studies, we introduced expertise as a key dimension of trust which is cast in the mold of the conventional ability/competence constructs. Past research has emphasized the indispensable role of trust in the expertise (which is conceptualized within the frame of ability and competence) in achieving compliance in franchise systems. For instance expertise has been conceptualized as a group of skills, competencies and characteristics that grant one party the ability to have influence (like creating trust) within a franchise system domain (Cook & Wall, 1980; Sitkin & Roth, 1993). Therefore our study reinforces the position that franchisee's trust in the franchisor's expertise will lead to contract compliance. Nonetheless, with respect to integrity and benevolence, there was positive but insignificant effects on compliance. This outcome may be attributable to the long held position that compliance represents relational expectations and contractual obligations specifically based on

incentives, controls, transaction analysis, social power, literal communication as well as influence strategies (Fenwick & Strombom, 1998; Hunt et al., 1987), but not necessarily on the integrity and benevolence of the franchisor. Consequently, franchisees' trust in the integrity and benevolence of the franchisor may not significantly influence their compliance and as such, governance by trust which is grounded on expertise will more effectively reduce non-compliant behavior, as well as strengthen the franchisor's brand equity and overall performance.

Our results further reveal that among the dimensions of trust, expertise and integrity, but not benevolence, jointly negatively affect opportunistic behavior. This outcome lends credence to Coleman (1990) and Kidwell et al. (2007) who posit that trust represents the franchisee's confidence in accepting calculated levels of risk with the franchisor and this will enable them to handle the liabilities in their relationship with franchisor. As a consequence, our research suggests that when high levels of franchisor expertise and integrity are substantial, franchisees will anticipate significant value from the relationship leading to reduced franchisee opportunistic behavior. The non-significant effect of benevolence on opportunistic behavior may be attributed to the fact that due to the characteristics of benevolence (a sincere concern for other's interest and motivation to do good for them (Xie & Peng, 2009)), some agents tend to rather exploit the situation and take advantage of that to perpetrate opportunistic behaviors.

Overall, this research progresses knowledge and provides empirical and practical insights into a question that has remained fundamentally unaddressed in the current franchise literature; What are the key effects of ex-post control mechanisms on multidimensional trust and channel performance in franchisee system. The study reveals that among the formal control mechanisms, output control (but not process control) significantly and strongly predicts multidimensional trust in franchise systems. Additionally, among the dimensions of trust, expertise is shown to exert the strongest effect on contract compliance in the franchise system. Finally, our results reveal that two dimensions of trust (expertise and integrity) are germane in significantly reducing opportunistic behavior in franchise systems.

## 5.2. Limitations and Future Research Directions

The current study has some limitations which prompt curious avenues for further and future research. First, the paper is limited to only the food franchise sector. Hence, our findings are only within the remit of this sector and managers as well as scholars should be cautious in universally generalizing it with other franchise formats and contexts. Secondly, the hypotheses generated in the research were tested using franchisee firms from a single country, is cross-sectional in nature and hence, may not connote static effects in other contexts. In addition, due to

the fact that organizations' strategic orientations and outcomes may be context specific, there are avenues for further research to validate and substantiate the construct relationship and findings from this study. The effects tested in this research are relationships and not causalities. Also, the concepts examined in this study are relevant across various economic contexts.

Consequently, these findings open up fresh debates on the phenomenon under study, especially the possible disparities that may exist between ex post control mechanisms and multi-dimensional trust and subsequently, multi-dimensional trust and channel outcomes. Furthermore, a research that adopts different variables under control mechanisms, trust and channel outcomes may reveal interesting insights.

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