

# Development Venation of the Theories Related to Research on "Company & Farmer" Organizational Issues

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## Abstract

At present, "company & farmer" is a common organizational form in the practice of agricultural scale management in China. Its development is of great significance to agricultural modernization. For the micro research of "company & farmer" organization, we need to define the nature and characteristics of this kind of organization to make it an observable object. Secondly, based on the specific objectives of rational choice between companies and farmers, explain the background conditions for the existence of such organizations. On this basis, we can analyze the contractual support and governance means of "company & farmers" organization, and put forward an efficient way of property right allocation. In addition, the new social division of labor formed by such organizations also deserves attention. The domestic and foreign theoretical achievements related to the above can be sorted out according to the organization type, organization generation, organization property right and contract, division of organizational elements and so on. Then, the relevant theories can be synthesized according to the venation from appearance to essence, from abstract to concrete, and from theoretical hypothesis to practical verification, so as to form the basis for further deepening the research of "company & farmers" organization.

## Keywords

"Company & farmer"; Organization; Relevant theory.

## 1. Introduction

The starting point of organizational research can be traced back to Max Weber's "ideal type" in 1920 [1]. Through the generalization of similar phenomena, Weber refined the main characteristics of bureaucratic organization: strict rules and regulations, power and hierarchy are related; The management personnel of the department level are specialization and professionalization, and the managers pursue the benefit maximization; Bureaucratic organization is based on rationality and legal authority. According to Weber's abstract classification, there is hierarchical relationship in the organization, which needs to take the setting of property right relationship as the background and prerequisite.

Of course, this authority and hierarchical relationship not only comes from property rights, but also the internal requirements of economic interests. As Knight (1921) put it, "confident and overly risky people take risks or insure the suspicious and timid people by ensuring that they have a certain income in exchange for ownership of actual results" [2]. Knight preliminarily explained the economic logic of the formation of organizational authority, and the ownership of actual resultshe referred to has taken the embryonic form of the concept of "residual rights" which Hart (1988) focused on later [3]. In Knight's research, Weber's abstract generalization of bureaucracy with rational basis has been concretized. The economic rationality of the bureaucracy is that the organization is a tool to allocate and control risks through the specialization of command functions under uncertain conditions. However, Knight did not

explain why this tool must be realized through bureaucratic organization rather than market organization.

Coase's pioneering research (1937) has promoted the cognition of the essence of organization, and the rational basis of organization's existence is more specific and logical. Coase put forward the concept of transaction cost for the first time, and distinguished two "ideal types" of market organization and bureaucratic organization under the neoclassical paradigm of rational choice. He believes that both the market and the enterprise (or hierarchy) are two different ways of organizing the division of labor, that is, two different ways of transaction. The reason for the forming of enterprise is that the transaction cost of the division of labor by enterprise organization is lower than that by market organization [4]. On the one hand, enterprises realize division of labor and cooperation with authority; On the other hand, enterprises replacing a series of short-term contracts with long-term employment contracts has the advantage of saving transaction costs.

In fact, these pioneering studies on organizations have extracted three key questions in subsequent research. first, what are the observable variables that distinguish different types of organizations? That is, the boundary problem of the organization (what); Second, why choose a certain type of economic organization? That is, the logical problem of organization selection (why); Third, how can the participants of economic organizations coordinate to achieve efficiency with comparative advantages? That is, how.

## 2. The Essence and Boundary of Organization: Clear or Fuzzy

In Coase's (1937) research, the market and enterprise organization are entirely different. He pointed out that markets and enterprises are two alternative means of allocating resources. In the market, resource allocation is automatically adjusted by the price mechanism; In enterprises, resource allocation is completed by authoritative organizations. Here, corresponding to the automatic adjustment and command mode, there are different property rights. Producers in enterprise organizations do not have the same freedom of action as in the market. It can be seen that the property right structure is a criterion to divide the organizational boundary.

Alchian and Demsetz (1972) disagreed with Coase's view that the essence of enterprise is team production [5]. In fact, regarding the enterprise as a team does not deviate from Coase's point of view, but further explains why there is authority. According to the logic of Alchian and Demsetz, the market organization is an "invisible team", and the market price mechanism can generate sufficient incentives. However, due to the free riding problem, the enterprise team organization needs to introduce incentive and supervision. The supervisor needs to be supervised until an authority appears. Therefore, the enterprise has the attribute of integration in property rights as a team.

The research of Cheung (1983) provides another method to identify organizations. He does not approve of using the nature of team production to explain the difference of organizations. He believes that people's laziness, deception or speculation are common, which depends on the selected contract method or the measurement and pricing of property in the transaction [6]. If the worker is rewarded for every small contribution, the worker will not be lazy, or at least his laziness will be reduced. The problem is that if we really take the labor achievements of workers as the transaction object, there will be high product information costs and labor measurement costs. Further, Cheung changed the statement that enterprise instead of market to "replace another form of contract with one form of contract". For organizational participants, property rights can be traded through a wide range of contractual arrangements, and the choice of contract is subject to transaction costs. Following Cheung 's research ideas, contract has become another criterion to distinguish different organizational types.

Organizations, including enterprises, are essentially the connection of a series of contractual relationships (Jensen & Meckling, 1976) [7]. Regarding the enterprise as a contractual organization different from the market helps to promote the micro research of the internal relations of the organization, but the boundary of the enterprise is no longer clear. Since the property right has never been fully defined (Barzel, 1982) [8], the transfer of factors usufruct also involves an incomplete contract. Therefore, from the perspective of property right definition and transaction, the enterprise as a factor contract does not have a completely defined boundary. In reality, pure factor contract does not exist, and commodity contract is similar. However, this is in line with the development of reality. Phenomena such as stakeholder governance, strategic alliance and enterprise network can be explained under the framework of property rights and transaction costs.

The dichotomy of commodity contract and factor contract is too abstract and simplified for the real world, while the property right theory of organization is different. Taking the incentive effect of property rights as the core issue, Grossman & Hart (1986), Hart & Moore (1990) focused their research on the transfer degree of property rights [9], mainly discussing how the allocation of residual control rights of various assets affects the result of transaction [10]. The views on the property rights of organizations seem to emphasize the incompleteness of commodity or factor contracts, and it is considered that there may be intermediate organizations. Logically speaking, since property rights cannot be completely defined in advance, the content of residual rights and the scope of their transactions may be diverse. Integration or market relationship is only one of the possible states of property right allocation, and there are a large number of quasi-integrative organizations (or quasi-market organizations). The study of property right relationship does not make the boundary of organization clear again, but attributes the essence of organization to property right transaction, so as to avoid the problem about organizational boundary. In other words, where residual control is defined, that is the boundary of the organization.

"Company & farmers" is a summary of a large number of phenomena in which companies lead farmers to develop in reality. As an "ideal type", it is not an enterprise, certainly not a simple market organization. The company has no complete authority, and farmers are not independent economic organizations. There is also no definite organizational boundary for the large-scale management organization of "company & farmers". However, from the perspective of formation and evolution, one corresponding organizational form is the integrated agricultural enterprises (including family farms), and the other organizational form is the return of farmers to the state of "working alone". Moreover, in reality, "company & farmer" mainly develops from the form of the market organization. Agricultural order between companies and farmers are long-term, which is different from short-term commodity contracts. Farmers do not produce under the supervision of the company, and there is no factor contractual relationship between the two sides. Therefore, from the perspective of contract type and property right relationship, we might as well treat "company & farmers" as a quasi-integrative organization.

### **3. Economic Logic of the Choice of Organization Mode: Production Cost and Transaction Cost**

Before Coase put forward the view that "the emergence of enterprises is to save transaction costs", enterprises were invisible "black boxes". In classical enterprise theory, the goal of maximizing enterprise profits is actually transformed into minimizing production costs. Under the paradigm of production function analysis, the concavity of constraint function in optimal programming is self-evident. Therefore, saving production cost is not only a necessary condition but also a sufficient condition for profit maximization. However, the existence of

transaction cost changes the constraints and the nature of its function. Saving production cost may not achieve the goal of the organization.

Although the organization has no clear boundaries, changes can always be observed. The choice of organization is also a dynamic change of organization boundary. If the economic rationality of an enterprise only lies in specialization and scale, as long as the investment does not exceed the scope of economies of scale, more owners of relevant assets will join the enterprise, and the boundary of the organization will be extended. According to this logic, the economic organization mode of the people's commune is that too much investment leads to diseconomy of scale. In fact, the problem of collective production organization mainly lies in supervision rather than technical reasons (Lin Yifu, 1990) [11]. Until now, it is still technically feasible to complete the supply of high-standard farmland, water conservancy and hydropower and other infrastructure with large-scale investment. Technical expertise and economies of scale are not the only reasons for organizational choice. As Cheung (1983) put it, "if every activity can be measured and priced, the benefits from specialization and collaboration can be realized without factor market".

It is not enough to emphasize the impact of transaction costs on organizational efficiency. As early as in *Capital*, Marx has pointed out that "cooperation not only improves individual productivity, but also creates a kind of productivity, which itself must be collective power" [12]. Coase's implicit assumption in the nature of enterprise is that the transaction changes from the market to the internal organization of the enterprise, and the division of labor and technology are unchanged. Therefore, saving transaction costs seems to be the only function of the enterprise. In fact, as a form of promoting division of labor, compared with self-sufficiency economy, enterprises may increase transaction costs, but as long as the increase of economic benefits of division of labor exceeds the increase of transaction costs, enterprises will appear (Yang Xiaokai, 1994) [13].

The choice of organizational modes such as enterprises and markets is not only considered by technology and production efficiency, but also constrained by transaction costs. Williamson (1987) believes that "the criterion of organizing business transactions is assumed to be a strict instrumental criterion for saving transaction costs, which can be basically divided into two parts: the saving of production expenditure and the saving of transaction costs" [14]. Therefore, the purpose of organizing economic activities is to minimize the sum of production costs and transaction costs. Williamson's view suggests that too much emphasis on transaction costs is also undesirable. The compromise way is to consider both specialization and the particularity of the transaction, which may be his intention to raise the issue of asset specificity. On the one hand, specialization and scale require specialized assets. Because the specialization of processes and products inevitably has special requirements on asset performance. On the other hand, special assets, including machinery, equipment and facilities, may be locked up when they are limited to the use in an organization. It was originally to improve efficiency. Because it lost the possibility of participating in other division of labor, it just limited the realization of efficiency. In Williamson's analysis, it is called the potential threat of opportunism, which is an important factor affecting transaction costs.

As rational people, companies or farmers choose the "company & farmers" quasi-integrative mode, which also follows the general logic of organizational choice. It can not only be easily sold and purchased, but also sell at a good price relative to the cost, which is convenient for further processing and production. As a result of the conclusion of contracts between companies and farmers, if the transaction is still difficult and the production efficiency is not improved, it is difficult to imagine the possibility of this organization in reality. The company drives the development of farmers to form a "company & farmers" organization. The "win-win" of comprehensive balance between transaction cost and production cost is the prerequisite and realistic goal of its existence and development.

#### 4. Organizational Contract and Governance: the Continuum from Market to Hierarchy

The contract embodying property right transaction relationship is an important means to achieve the organizational goal. For an organization, property right is the macro relationship framework, while contract is the micro tool of the organization. Any contract contains specific rights and obligations. These provisions reflect different governance mode, that is, the institutional matrix in which the transaction is negotiated (Williamson, 1979) [15].

Williamson followed the tradition of old institutionalism when studying organizational contract and governance. At the beginning of the 20th century, Commons (1934) first proposed to take transaction as the basic unit of analyzing economic organization. He believes that the purpose of establishing economic organizations is to coordinate the potential contradictions between the two sides of the transaction, so as to avoid actual or possible conflicts [16]. In addition, Commons divides transactions into three types: goods trading, management trading and quota trading. These three activity units include all in economics. Williamson put forward the concept of governance to investigate the contract selection under different transactions, so that transactions with different attributes can be matched in different ways of cost and efficiency. Therefore, the discussion of organizational boundary is more microscopic, and the general logic of economic organization is constructed by the study of transaction object attributes and the comparative analysis of transaction costs.

As Hayek (1945) said, "social and economic problems are mainly the problem of rapid adjustment under specific time, place and conditions" [17]. In the uncertain world, adaptability is the core issue of the organization, and governance is the means to enhance adaptability. Hayek believes that the price system is an effective means of information exchange and adjustment. At the same time, the price system is one of the structures that people inadvertently discover and begin to learn and apply before they understand it. Here, the word "structure" is synonymous with Williamson's governance. Therefore, the price system referred to by Hayek can also be understood as the governance means of market organization. In addition to the spontaneous market, there is also conscious, thoughtful and purposeful cooperation between people, which is realized through bureaucracy (Barnard, 1938) [18]. There are also adaptability problems within the hierarchy. The survival of the organization depends on maintaining the balance between various complex characteristics. When the environment changes, it requires the readjustment of the internal processes of the organization.

MacNeil (1974) divided contracts conducive to exchange into three types: classical contract, neoclassical contract and relational contract [19]. Classical contract corresponds to Hayek's spontaneous adaptability. It achieves its purpose through independent and decentralized decision-making and strengthening "reality", and supports the form of market organization. However, for long-term contracts executed under uncertain conditions, with full consideration of reality (including future needs), even if possible, the information cost is high. Long term and incomplete contracts need a specific adaptive mechanism. When facing greater unexpected interference, the transition from classical contracts to neoclassical contracts is conducive to the sustainability of transactions. The neoclassical contract does not need to accurately foresee and stipulate the relationship in reality, but leaves room in the content. Neoclassical contract is more flexible and adaptable because of its "framework". On the other hand, supporting flexibility requires a third-party arbitration institution trusted by both parties to resolve disputes. When the possible impact of accidental interference on both parties is more serious, due to the high execution cost and limited scope of use of arbitration, more flexible and adaptive arrangements need to be considered (Williamson, 1988) [20]. Relationship contracting runs through (transaction) and is completely (related to reality), which may or may not include the "initial agreement" (MacNeil, 1974). The relational contract for more special transactions

means that the neoclassical adjustment procedure is replaced by bilateral governance or unified governance.

The Enlightenment from the research on organizational contract and governance is that with the increase of transaction complexity, decentralization will give way to centralized decision-making, and deterministic provisions will give way to framework terms. Therefore, the scope of adaptation will expand from the present to the uncertain future, which is difficult to adjust and can be adjusted flexibly. At the same time, the way of adaptation and governance will shift from "Hayek's market" to "Barnard's hierarchy". In the continuous spectrum of contracts between the market and the bureaucracy, "company & farmer" obviously does not belong to the market contract relationship, and the market organization is difficult to adapt to the strong uncertainty of agricultural production due to its natural and biological attributes. This kind of organization is not a bureaucratic type, and there is no complete control relationship between companies and farmers. There may be neoclassical contractual relationships in its derivative forms. For example, under the mode of "company & cooperative & farmers", cooperatives may play an intermediary role, which does not change the contractual relationship between companies and farmers. The "company & farmer" organization relies on the contractual relationship between the market and the bureaucracy, as well as the corresponding governance methods to improve its adaptability in agricultural production and management activities.

## 5. Factors and Resources in Organizations: Knowledge, Information and Entrepreneurial Talent

The organizational research based on the property right theory and transaction cost analysis method has not completely left the neoclassical analysis paradigm. The in-depth understanding of the essence and Realization of the organization actually introduces more elements into the input-output relationship under the framework of rational choice. The specific manifestation of transaction complexity is that the factors of production affecting costs and benefits are more complex.

With the development of modern enterprise theory, in addition to the traditional elements such as land, labor and capital, new elements such as information, knowledge and talent began to be used in the analysis of organization and contract. In the early research, information has entered the vision of organizational problems. Coase (1937) initially defined the transaction cost as "the expenses and expenses in finding the transaction object, concluding the contract, executing the transaction, negotiating the transaction, supervising the transaction and so on". To a large extent, Coase refers to the need for necessary information to use the market price mechanism. If information can be obtained without cost, there is no difference in realizing transactions through the market or enterprises. In fact, information is not only a scarce resource, but also incomplete (Arrow, 1972) [21]. For the development of Coase's concept of transaction cost, Cheung (1983) emphasizes the information cost, including information about product quality and labor process. Barzel (1982) summarized the impact of information on transactions as assessment costs. The implicit conclusion of many studies is that if information is not an element of organization, the differences between different organizations will no longer exist.

In parallel with how to obtain knowledge, the problem is who is obtaining information and what information he wants to obtain. Information and knowledge are not completely irrelevant. Obtaining information as much as possible is the premise of making correct decisions. Any production process involves the problem of "how to do", and production is inseparable from decision-making. Production planning needs macro strategic decision-making, and the production process needs on-site decision-making. For specific problems, decision makers need to have special knowledge and ability. Consistent with Hayek's view, Jensen & Meckling (1999) believes that the knowledge owned by any single decision-maker or group of decision-

makers is only an insignificant subset of the knowledge set known by human beings [22]. When knowledge is valuable in decision-making, it is beneficial for these decisions to match the decision-making power with the available knowledge. However, Hayek's research does not mention the cost of knowledge conversion between subjects. Unless it is general knowledge, the knowledge of great significance to decision-making may not be mastered by the people with decision-making power. Therefore, the allocation of decision-making power has become an important issue of organizational efficiency.

Jensen & Meckling said that special knowledge is related to entrepreneurial talent, which is also the main defect of farmers' decentralized management. Marshall has pointed out that entrepreneurial talent is the "fourth element" in the Principles of Economics [23]. Entrepreneurial ability includes the management ability and innovation ability of operating enterprises. The relationship between this element and land, labor and capital is not mutual substitution, but mutual supplement. When producing the same number of products, we can use more capital and less labor, or more labor and less capital. However, the three elements of labor, land and capital must be reasonably organized in order to give full play to production efficiency. To some extent, entrepreneurial talent is the core competence of an organization (Foss,1993). Organizations with entrepreneurial talent have considerable competitive advantages [24].

The cooperation between companies and farmers in a quasi-integrative way reflects the indispensability of information, knowledge and entrepreneurial talent. Generally speaking, farmers are far from the market, but close to the field, while companies are the opposite. Companies and farmers. Communication between the two sides is an effective means to overcome their respective information disadvantages. Farmers have decision-making power, but generally do not have the knowledge of operation and management. The company has entrepreneurial talent, but does not have the right to operate the land. Farmers have production knowledge and know how to deal with it according to the site conditions in the process of crop growth. The company has experience in market situation and technology application. The emergence of "company & farmer" organization has built a platform for information exchange and a means of division of knowledge and talent.

## **6. Extended Application of Organization Theory: Realization form of Agricultural Large-scale Management**

Foreign discussions on organization and contract mainly focus on the field of industry and commerce, such as vertical integration, reciprocal trade, franchising and other topics, and rarely touch on agriculture. Since the 1980s, the analytical paradigm of new institutional economics has been gradually accepted by Chinese scholars. At the same time, the research on the application of its basic concepts, methods and ideas to China's agricultural development has also begun. Property right, organization and contract have gradually become the key words with high frequency in the research literature of agricultural economy at home and abroad. The existing research results abroad show that in about 100 years, there have been different focuses on the issue of organizational contract, such as essence and boundary, principal and agent, residual control and claim, contract law and governance. In contrast, in China's research on agricultural scale operation organizations in recent 20 years, various theoretical branches and research focuses have been carried out almost at the same time.

Agricultural organizations also have essential and boundary problems. Cooperative is a type of large-scale management organization that is more discussed. At present, most farmers' professional cooperatives grow and operate under the pattern of farmers' differentiation and departments and capital going to the countryside, so they have formed a special appearance. Too much emphasis on professional cooperation with single business often leads to universal

"elite capture" [25], which is not conducive to the realization of farmers' dominant position (Wen Tiejun, 2013). Moreover, professional cooperatives are not strictly productive organizations. The main purpose of establishing and developing professional cooperatives is to form collective behavior and meet the challenges of the market. However, the production of the members of the cooperative is still completely independent, and the cooperative may not have professional production efficiency. According to the empirical analysis of Huang Zuhui and other scholars (2011), the improvement of the entrepreneurial ability of the principals of cooperatives and the level of human capital of members have an important impact on the efficiency of cooperatives [26]. The overall efficiency level of farmers' professional cooperatives is low, and the problem of organizational efficiency is an important reason.

While the development of professional cooperatives is facing organizational problems, family farms with certain scale and management ability have attracted the attention of academic circles. As an economic organization, family farms are more suitable for production activities with low level of division of labor and low requirements for matching between production factors (Chen Jiping, 2013) [27]. In terms of production links, household production is more matched with the characteristics of agricultural division of labor, and has higher organizational efficiency in management. Moreover, family farms also have certain business advantages in procurement, sales and technology. However, to realize large-scale management in the way of family farm organization, we need to take the large-scale transfer of land as the premise. According to domestic and foreign experience, the moderate scale of family farms is about 10 times of the average household operation scale. According to this experience, the average operation scale of family farms in China will reach 26.7 hectares in 2030 (Su Xin et al., 2014) [28]. In China, facing the constraints of man land relationship, the expansion of family farms is limited. Small family farms do not have advantages in mechanization and standardization, and it will be difficult to cope with the competition of corporate farms (Zhou Duanming et al., 2014) [29]. With the advantages of both the efficiency of farmers' family organizations and large-scale management, we need to consider ways other than cooperatives and family farms.

"Company & farmer" realizes the combination of household production and corporate management. In China, "company & farmer" and agricultural marketization are born simultaneously. From the 1980s when CP Group extended its transnational business to China's agriculture to the "Wen's Group model" that began to rise in China in the 1990s, the radiation of companies to drive farmers' production has gradually become a common way to realize large-scale management. Specific property relations and contracting activities are the premise of realizing transaction and cooperation, and so are agricultural large-scale management organizations. For example, the formation of cooperatives is "common property rights", and the members are "mutually beneficial relations". Leading enterprises and family farms need to transfer land and employ certain labor force. The "company & farmer" is based on the product purchase and sales relationship and order contract. Due to the frequent breach of contracts by companies or farmers in the incentive market competition (Liu Fengqin, 2003) [30], "company & farmers" has been practiced in many places, but its organizational stability is not high (Liu Fengqin, Li Jinning, 2018) [31].

With the variety of agricultural products and the changing market environment, simple property rights and contractual relationships are difficult to deal with complex transactions. Simple purchase and sales orders and the loose relationship between companies and farmers are vulnerable to the impact of the market. As a practical and feasible large-scale management organization, "company & farmer" needs to go beyond the market interface of bilateral cooperation. This paper holds that the subsequent proposition of "commodity contract is better than factor contract" may be: how to form large-scale management of agriculture without introducing entrepreneurial talent through factor contract. In the new century, quasi-integrative organizations and "supermarket contracts" are not individual phenomena in



various fields (Liu Dong, 2005) [32], The interest community of companies and farmers is not only different from cooperatives, but also different from family farms or integrated agricultural enterprises (Liu Dong, Wang Yiting, 2014) [33]. Whether the supermarket contract of "company & farmer" is a special and particular contract type and the applicability of supermarket contract in the practice of agricultural large-scale management deserve further attention and research.

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