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It Takes Both Trust and Lack of Mistrust: The Workings of Cooperation and Relational Signaling in Contractual Relationships[1]

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1. Introduction

There has been so much talk about trust in the literature on economic transactions that the term has become blurred in its meaning and is often misleading. In order to clear the air in this conceptual jungle, Dasgupta (1988) has operationalized trust game-theoretically via a paradigmatic sequential game and Coleman has suggested to model placing trust as calculated risk in situations in which an actor has to act before he knows what his potential exchange partner is going to do. A person will place trust if and only if the expected gain from trusting is higher than the expected loss (see Coleman, 1990). In response, Williamson (1993) has suggested a moratorium on the term "trust" because he believes that in contracting it means nothing else than calculated risk whereas trust in the "deep" sense only occurs in some personal relationships. Have Dasgupta and Coleman helped to clarify what is "really" involved in placing trust or have they helped to diffuse the whole issue by preparing the insight that the very concept of trust adds nothing to the more precise concept of calculated risk?

Many others have doubted that trust can be reduced to "calculated risk" even if there is "an element of calculativeness" or "instrumentality" involved. Noninstrumental aspects of trust concern mainly relational issues, such as social embeddedness, liking, relational norms. "Instrumental models are inadequate to explain people's trust in others" say Tyler and Kramer (1996, p. 6)

Of course, relational issues may turn out to feed into calculativeness (for example, "social embeddedness" may create reputation effects)[2] and vice-versa (for example, trust relationships may be engineered).[3] But are there two kinds of trust? If so, how does each work? Do they have different preconditions? Are they dependent on each other? These and many other related questions cannot be answered at present with the given theories of trust.

2. Trust and Mistrust: Not Two Sides of a Coin

Mistrust. Let me begin with self-interest and calculativeness. Take a scenario used by Williamson as example. There are two periods. In the first period, orders are being placed. In the second period, the production occurs dependent on demand realization. The buyer may confirm or cancel the order in the second period. If the supplier has no loss when the order is canceled, there is no problem. If he has to make a specific asset investment in the first period in order to produce in the second, he loses a certain amount if the order is canceled. Clearly, in that case, the supplier would like compensation (i.e. a hostage) to be agreed upon beforehand or else he will not make the specific asset investment. This is a matter of the distribution of risks: the supplier does not want to carry it all. If the buyer flatly refuses to share the risk, the case is closed. If he is willing to post a hostage, by his very act he removes the necessity to invoke any issue of trust. If, however, the buyer refuses to post a hostage but instead promises not to cancel the order even if demand is low, then a potential issue of trust is involved: will he or will he not keep his promise. A closer look convinces us that the supplier has good reason to mistrust the buyer simply because keeping this promise is against the well-understood self-interest of the buyer. Anybody with some experience of how people act knows that when a promise is blatantly against well-understood self-interest, there is good reason to assume that the promise will not be kept. The risk is thus easily assigned. In such situations, mistrust is legitimate and not a sign of ill will or abnormal risk-aversion. It is the legitimacy of mistrust that creates **focal points** for the solution and makes remedies relationally neutral. In other words, the mistrusting party in such a situation can claim the necessity of remedies, pinpoint a menu of solutions and show good faith at the same time. Common understandings of how people feel, act, and react, given the habits and mores of this group, are enough for this legitimacy effect to occur. They create focal points (Schelling, 1960), and for that common experience rather than particular powers of farsightedness are necessary. This effect gives rise to an interesting phenomenon: when mistrust is legitimate, it is relationally neutral, i.e. it does not say anything specific about the person who mistrusts because any other reasonable person in his place would have reacted similarly. Legitimate mistrust will thus also not burden the relationship. Nor will it vanish due to relational developments. The need for credible commitments will thus not vanish even when there is a good relationship between the transacting parties.

Generally, any explicit or implicit promise that is blatantly against the self-interest of the promising party will be legitimately mistrusted. Solutions to legitimate mistrust problems are therefore **incentive alignments** (via credible commitments, be that on the basis of legal requirements or hostages, or through reputation effects, middlemen, delegation or other means) in which incentives are changed in such a way that breach would not be blatantly in the self-interest of the promisor. “Legitimate” mistrust refers to a situation in which reasonable observers would say that any other reasonable person put into this situation would also assign a low probability to the promise being kept, irrespective of the "true" intention of the promisor at the moment of making the promise. It does not take considerable farsighted powers to spot blatant misalignments of interest (i.e. to be legitimately mistrusting) and to chose remedies from a menu of instruments. There is accumulated experience in any industry; there are accumulated governance instruments in any industry; and people make use of these instruments as from a menu (see DiMaggio and Powell, 1991).[4] Williamson's insistence that only farsighted contracting could possibly detect misalignments of interest and the need for credible commitments is based on the mistaken idea that "myopic" is equivalent to "dumb" and "scatterbrained".

Trust. Now let me come to the "non-calculative" side of contracting and let me begin with an example. A supplier is faced with a sudden spell of high absenteeism and he is short of labor and in a rush because the product has to be shipped to his client. He could solve his time problem by skipping the rather laborious quality control. The quality control is not something the supplier and his client have put in the contract. There is thus no specific sanction in the contract for failing to conduct quality control. However, the spirit of the agreement implies that the price agreed upon is for a certain quality and so far things have been satisfactory for both parties. Clearly it would be against the suppliers longer-term interest to be unreliable with regard to quality control because the on-going relationship with the client would be strained if he were. But at this moment, it would be in the suppliers short-term interest to skip the control just this once and the client would have a difficult time proving that it had been skipped. The client trusts the supplier that quality control is performed.

How does this situation differ from the previous one? There is no legitimate mistrust in this situation. Longer-term and short-term incentives point in opposite directions and one cannot possibly speak of the supplier's blatant self-interest in not performing the quality control. Still, there is a short-term temptation to deviate from the agreement. The point is that the temptations to defect are random and that one cannot even come up with a reasonably exhaustive list in advance (let alone say something about the distribution of these events). Thus, it is not possible to assign risk to the various future temptations to defect. In this sense, there is radical uncertainty and it is this radical uncertainty that makes it impossible to reduce relational issues to the estimation of risk. In on-going relations, short-term incentives to cheat are highly situation specific. In one situation, time pressure might create a temporary incentive to compromise on quality control; in another situation, a new but demanding client may create an incentive to put running orders of old clients on the back burner; in yet another situation, the need for quick coordination prohibits the establishment of proper safeguards and thus creates temporary incentives for self-serving post hoc explications of highly implicit agreements. In such ongoing relationships there is no possibility to keep aligning the interests in order to neutralize temporary temptations, or to decide for every situation anew whether to trust or not to trust, or to have “stand in” partners just in case. **One party trusts the other if he believes that the partner’s short-term temptations to defect do not lead to reductions in the partner’s reliability.** The instruments necessary to achieve trust are different than those used to reduce mistrust. What is more, I will argue below that in order to start building trust, legitimate mistrust must already be strongly reduced.

3. How Trust Problems Are Dealt with in the Literature

In the literature we basically find three ways in which genuine trust problems (as opposed to problems of mistrust) are treated. There are severe problems with each one of them.

First, trust problems are taken to be a **subcategory of mistrust problems**. For example, for Williamson governance structures are mainly to be distinguished on the basis of what the anticipated problems would dictate **in order** to minimize the room left for **ex post** problems. Aspects related to the governance of the **ex post** problems that occurred despite **ex ante** measures received short shrift,[5] and there is no indication in Williamson’s work that he recognizes the difference between the two kinds of problems as an important difference.[6]

The problem with failing to distinguish mistrust problems and genuine trust problems is not just “information impactedness” (the term Williamson uses for people’s limited ability to look into the future) but also the way people are likely to deal with situational temptations. If one assumes farsightedness, differences between short-term and longer-term[7] interest of contracting parties are negligible. Problems of trust are then also negligible. Breach in a longer-term relation then only occurs if the longer-term interests are no longer served by the relation which turns the situation into one of legitimate mistrust. However, if one assumes a sizable portion of myopia among human beings, then this difference does become very prominent. There is overwhelming evidence for the fact that people are apt to let short-term aspects prevail over long-term aspects far beyond any degree that can be called rational in any meaningful way (see for example Loewenstein and Thaler, 1989; Loewenstein and Elster, 1992). Farsightedness is the more likely the more instrumental the goods, the larger the stake in some future event, and, more importantly, the more predictable and calculable the sequence of future events. This predictability, in turn, depends mostly on institutions and habits rather than on cognitive abilities. Despite lipservice to the importance of the “spirit” in which contracts are executed, Williamson holds on to farsightedness as the standard assumption. Why? He admits that not to do so is too costly to him in terms of the tools he would like to use. “But for farsightedness, transaction cost economics would be denied access to one of the most important ‘tricks’ in the economist’s bag, namely the assumption that economic actors have the ability to look ahead, discern problems and prospects, and factor these back into the organizational/contractual design.” (Williamson, 1993, p. 129). In such a context, problems of mistrust can be analyzed but problems of trust cannot. In addition, as discussed above, even though it is possible to analyze mistrust problem with farsightedness, it is not necessary to assume much farsightedness in order to deal with **ex ante** anticipation of problems due to misalignment of interests. To the contrary, it is important to know what a **savvy** contract partner has to know in any particular industry and why farsightedness as a disposition is not enough to have the relevant knowledge for being savvy. Thus, even though Williamson claims to follow Macneil's (1978) analysis of the changes of contracts to relational contracts, the very insistence on being able to use the "tricks in the economist's bag" keeps him (and not just him) from bringing in those tools that are necessary to analyze the contractual relationship as a human relationship. These tools must include theoretical recognition of the human proclivities (such as radical uncertainty and myopic opportunism) that give rise to specific governance structures that are meant to deal with them.

Second, in the literature, we also find the opinion that genuine trust problems should be treated as **problems of disposition**, i.e. as problems related to the selection of genuinely trustworthy business partners. There are honest people and there are dishonest people and the question is whether the latter have a chance to pose as honest people and whether the honest people can signal their type easily to their potential partner (see for example Frank, 1988; Liebrand et al., 1986). It is probably true that people have different preference strengths regarding honesty and other-regard, but there is little evidence that these differences in preference strengths generally outweigh the situational differences in temptation. There is even some evidence to the contrary (see for example Ligthart, 1995). In other words, given myopia, even smaller situational temptations can beat preferences for honesty and other-regard.[8]

A variant to the personality type view of trustworthiness and trusting is the assumption that people are able to commit themselves to a cooperative disposition and are able to effectively signal this commitment (see for example Gauthier, 1984). The objections against the personality type view also hold for this variant and there is even less empirical evidence for it.

A third way to deal with genuine trust problems is to assume **social bonding** (for example Tyler and Degoey, 1996; Lawler and Yoon, 1995). Here, some psychological mechanism (such as informal interaction, similarity in values, sharing important life events) creates a positive change in people's preferences concerning the welfare of others (through liking). As a consequence, the situational temptations must be very large in order to make people act against the interest of the partner. Because these relationships are symmetric, the partners become both more trustworthy and trusting. It is very likely that such a mechanism plays a role in many longer-term contractual relationships. However, the assumption of a stable preference change hides the dynamics of emotions of liking and the mechanisms that are necessary to maintain a stable positive emotion vis-a-vis the other. In addition, knowing you are liked also increases the expectation of regard for your specific needs and circumstances, lowering contract performance (Flache, 1996).

A community version of this conceptualization of trust is subject to the same objections. For example Sabel (1993) suggests that we focus on a shared sense of fate and community rather than on self-interest when dealing with trust. But then, no mechanism is specified how a shared sense of fate and community can be maintained in the face of conflicting interests and golden opportunities to breach.

There are problems with each one of these views on how trust works in longer-term contractual relations. It is also noteworthy that the two views which deal with genuine trust problems say nothing about the possible relation between problems of trust and mistrust.[9] Summarizing the work of many scholars on trust, Tyler and Kramer conclude that little is known about this relation between the two kinds of trust. "Future research might most profitably explore the **situational** dimensions that shape the importance of instrumental and noninstrumental concerns" (Tyler and Kramer, 1996, p. 12). The remainder of the paper is devoted to exactly this task. It takes off from a central intuition of the trust theories just discussed: people can be trusted if they don't think of doing something that violates trust. But as it stands this intuition cannot be integrated into a theory of action.

4. Framing

From the foregoing, it became clear that the way trust is conceived depends to a large extent on the theory of action that is being employed. The neoclassical theory in economics and game theory can explain quite well the workings of mistrust once the fiction of full information has been dropped. Here, considerable theoretical progress has been made by exploring hostages, reputation networks, middlemen, control effects, information effects, and effects of the shadows of the past and future.[10] If, within the neoclassical framework, genuine trust problems can at all be separated from mistrust problems, they are likely to be treated as dispositional problems (type selection). Motivational theories on preference formation, emotions and attachment as springs of action have led to the consideration of personal relationships regarding trust, but they cannot handle mistrust problems and cannot deal well with situational fluctuations in temptations to breach.

It is the **cognitive** turn in psychology which has brought new tools for the analysis of trust. Although this "turn" has started already in the 1950s, it has taken a long time to move from issues concerning categorization to issues concerning lack of information to issues concerning information overload. Especially Simon has been very adamant about the importance of focused attention for explaining human behavior (see Simon, 1997, pp. 368ff). Whereas issues of lack of information are particularly important for mistrust problems, issues of information overload are crucial for an adequate conception of the dynamics of trust. Individuals cannot possibly attend to everything. Attention must be selective, and what is being attended to is particularly important for determining the kind of action that is taken (see also Fazio, 1990). Different bits of knowledge are mobilized, different categories activated, with the result that the individual is more sensitive to some kind of information than to another, relies more or less on stereo-types, places more value on certain outcomes etc. For example, individuals' negotiating behavior is affected by instructions that tell them to be cooperative or to be competitive (see Carnevale and Lawler, 1986). Individuals can be **primed**, that is, certain stored knowledge, categories, or attitudes can selectively become more easily accessible thereby influencing a person's information processing (see Higgins and Brendl, 1995). At the same time, aspects not belonging to the selected construct are inhibited thus creating a double selective effect (see Bodenhousen and Macrae, 1998; Houghton and Tipper, 1996). Note that although these effects steer attention, they need not be conscious or work via prior intention. For example, a person in a situation in which others speak highly of the value of achievement can get "primed" to focus on achievement without being aware of it (see Bargh, 1997). Most important for influencing a person's cognitive activity and thereby the action that is based on such activity are goals (see Gollwitzer and Moskowitz, 1996). Recently, one prominent researcher in this field even claimed that "most cognitive activity is goal dependent" (Kruglanski, 1996). As we will see, the link to the workings of trust is very direct. Goals can be influenced by the situation but they cannot be conjured up at will. At any given moment you have them or you don't. One might try to change one's goals over time but that takes a great deal of effort, if it works at all. One also might try to avoid situations that mobilize goals one does not want to have mobilized (such as staying away from the sight of food if you want to lose weight). If my contract partner's goal is the preservation of a good business relationship **and** if his interests are not grossly misaligned with mine, he would reliably not pay much attention to short-term opportunities that would break our agreement. His information processing would automatically inhibit the consideration of alternative belonging to contrary goals and enhance the consideration of alternatives that are goal congruent. Assume to the contrary that the partner had no such relational goal but wanted to make me believe he had. He then would have to deal again and again with the temptation to breach even if such a breach is against his longer-term interest. Chances are, he would succumb to many of these temptations. Faking to have a goal takes much effort because goals are so influential on cognitive activity. In order to flesh out this argument, we have to go into some more detail about this cognitive extension of rational choice theory.

What we need is a model that links insights from cognitive psychology to a theory of rational action. For some years now, such a theory has been developed under the label of "framing"[11] (see Lindenberg, 1988, 1993). The basic idea is as follows. In human cognition, entities (goals, things, words, meanings, aspects, characteristics, relations etc) can be in the foreground or in the background. What is in the foreground (i.e. in the "the frame") is analyzed and attended to in more detail than what is in the background and, even more important, it is analyzed **in terms** of what is in the foreground. Therefore, it has a much higher impact on the choice of action. The frame can be of varying strength (or "salience") relative to the background. The decision making process regarding the choice of a course of action is sensitive to the salience of the frame. When it is very salient, the entities in the background don't influence the choice of action at all; the less salient the frame gets relative to the background, the more action will **also** be affected by entities in the background. The model has been successfully tested empirically in various studies (see for example Braspenning, 1992; Ligthart, 1995). It shares the focus on the selectivity of the information processing with concepts such as "mindset", "orientation", "frame of reference" but it puts more emphasis on the possible effects of the background goals and thereby on the precariousness of the frame in the face of competing goals.

The frame is determined by the "definition of the situation" which contains a goal that is more salient than all other possible goals in that situation. Take as example that Fred, CEO of company A, is in a meeting with his staff discussing cost cutting measures when a call is coming in from Ralph, the CEO of company B. Ralph needs help desperately. Fred realizes right away that it is an emergency and he defines the situation vis-a-vis his friend Ralph as "a friend in urgent need". In that case, goals related to the meeting, and, more importantly, goals related to "not losing valuable resources (such as money, time or effort)", will be pushed into background. **Money to Fred is at that moment worth much less than a moment ago** when he was in the meeting focused on cost cutting measures. What is in the foreground is the goal to help a friend in urgent need.

The friendship frame mobilizes appropriate chunks of knowledge, rules and criteria. For example, the legitimate amount of help (in terms of money, time and effort) for which Ralph can ask is roughly indicated by the strength of the friendship, the consequences for Ralph of not helping, etc. The opportunity costs for helping are not keenly perceived because they belong to goals in the background.

Technically, we can speak of a situationally variable marginal utility of goods. The strength of this situational effect of marginal utility depends on the relative weight of the focal goal (the frame) to the background goals. If Fred's company had just lost a million dollars before Ralph contacted him about his problem, then the goal "not to lose valuable resources", though in the background, would be stronger and weigh down more heavily the salience of "helping a friend in need". A lower salience of the friendship frame would translate itself into a lower probability that Fred would go all out to help Ralph. In the extreme, the background goal could become so strong that it displaces the focal goal.

There is also a dynamic aspect involved. A frame's salience is lowered by incompatible background goals and increased by compatible ones. For example, the salience of acting according to friendship norms may be strengthened by the wish to get social approval and to maintain a certain identity, both compatible with norm conformity. But the salience can be lowered by increasing cost of norm conformity. Helping depletes resources and increases the relative strength of the background goal "not to lose valuable resources". If the friend keeps coming back for more, then the background goal will become stronger and lower the salience of the frame "to help a friend in need" even if you are convinced that the friend's need is real. You may still help but you increasingly lower the amount (i.e. deviate more from the optimal amounts for friendship), and when you come into a situation where the salience of the frame approaches zero, i.e. when it gets close to a toss up whether you help or not, the frame is likely to switch to "watch your own finances". With the new frame, other alternatives come in with their own ordering, other knowledge chunks are being mobilized, and links to other kinds of situations come into view. You may regret not being able to see the friend as friend anymore when he turns up, to see him only as a drain on your finances. But, like all constraints, the frame itself cannot be chosen at will, only influenced over time, for example by trying to avoid situations which lower the salience of a particular frame.

4.1. Overarching frames

There are of course many goals people can pursue and there can be just as many frames. However, goals are generally hierarchically organized, which allows us to consider a few high-level goals each of which can become an overarching frame with many subgoals.

Gain. One such overarching frame is concerned with the resources (called gain frame). A gain frame is most typical of what people generally associate with rational choice. Gain as a goal is here defined in terms of increasing one's scarce resources, such as money, disposable time, marketable knowledge, marketable skills, decision power, social influence etc. Again, the kinds of knowledge chunks, beliefs, attention to situational aspects etc. that are being mobilized in a situation where gain is the frame are specific to the task, the more so the more salient the frame. If somebody is asked for help, then a person in a gain frame will not mobilize beliefs about the general obligation to help or about the legitimacy of asking for help, but rather, say, beliefs about the possibilities of making a profit and the legitimacy of making the best of the situation for yourself.

Loss is not the same as negative gain. The asymmetry between losses and gains in terms of utility (when both are subjectively medium or large) seems to be well established (see Kahneman, Knetsch and Thaler, 1991). Losses weigh heavier than gains. Gains are by and large less disruptive than losses and thus are less likely to be accompanied by a strong emotional response. The time horizon of a loss frame is short because the goal is strongly linked to emotions (see Loewenstein, 1996). It is the emotional strength of the loss frame and its short time horizon that make it so dangerous to a longer-term business relation.

The goal of a loss frame is to prevent or get rid of the feeling of loss. At times, gains are so firmly anticipated that not getting them feels like a loss, like a disruption after all expectations have already adapted to the increase in resources. This can particularly happen with so-called "golden opportunities" that suddenly arise and, if not taken advantage of right away, will vanish and leave the impression of loss, of a missed opportunity. In can easily be imagined, how such “golden opportunities” brought in by third parties can act like random shocks in an ongoing contractual relationship.

Normative frame. Here, the goal is “to act appropriately”, to “do the right thing”. In our friendship example, a friend asking for help is likely to trigger an overarching normative frame with the subgoal “to help a friend in need”. Given the friendship norms, helping a friend in need is the appropriate thing to do and there is an appropriate range for the amount of help that the friend can legitimately ask. Within that range, the cost of helping is not sharply calculated because it belongs to a goal in the background (say, the goal “to watch one’s scarce resources”). Ligthart (1995) has demonstrated this influence of norms on frames experimentally. The frame also activates relevant knowledge chunks, criteria for judging the success of ones plan of action etc. The important point to make here is that the cost of conformity and the benefits of non-conformity are pushed into the background. There, they still have an effect. However, the effect is much smaller than when they are in the foreground (gain frame). Experimental evidence demonstrates the effects of gain and normative frames on negotiations. For example, De Dreu and Boles (1998) found that individuals with a “social value orientation” (comparable to a normative frame) chose significantly more frequently “appropriateness” as their guiding goal for negotiation whereas individuals with a competitive value orientation (comparable to a gain frame) chose significantly more often “effectiveness” as their guiding goal for negotiation.

The relative strength of the three frames. Generally, the strength (i.e. salience) of a frame increases with two kinds of variables: (“hot”) emotional and (“cool”) instrumental relevance to self. For salience, “hot” goals are stronger than “cool” ones, ceteris paribus. The **apriori** ranking of the three frames in terms of strength vis-à-vis each other is thus: loss frame first, then gain frame, then normative frame. The loss frame is tied more directly to emotions and short-term effects than the other two. Increasing one’s own resources (gain frame) is more directly instrumentally relevant to self than conformity to norms for the sake of appropriateness. In order not to be displaced by a loss or a gain frame, a normative frame must be stabilized via congruent “background” goals which, in turn, are directly, emotionally and/or instrumentally relevant for self. For example, the background of a normative frame can be the valued membership of a group and/or an emotional tie to a certain identity (say, a “self-respecting business man”). I will return to the issue of frame stabilization below.

Rationality. Readers who are familiar with Weber types of action may surmise that there is a certain affinity between these types of action and the overarching frames. Indeed there is. However, there is a very large difference. For Weber, instrumental (i.e. means-end) rationality was only linked to one type of action. This is quite different in the framing approach. Notice that rationality is compatible with each one of the three frames. While this is most obvious for the gain frame, it holds equally for the loss and the normative frame. Even junkies badly in need of a fix are capable of rational planning of actions (such as steeling car radios for money, making the right contacts etc). What makes them appear less rational in common sense analysis is a normative component frequently attached to rationality: it should be long-term in orientation and it should not be linked to emotions. Yet such a normative component has little to do with the logic of means/end relationships per se. There is no intrinsic reason to consider neglecting short-term interests to be more rational than to neglect long-term interests. Socially, it is of course often nicer if people stick to long-term interests in case there is conflict with short-term interests.

People in normative frames are also acting rationally to pursue their goal of acting appropriately. They do not just follow rules blindly. Rules define what is appropriate in a general way but all the particulars need to be filled in. If Fred is to help his friend, he has to use his wits to do it well.

5. The Dynamics of Trust

What is the relation of framing to the dynamics of trust? Considering the three overarching frames, it becomes clear that trust and mistrust have to do with the way these frames affect each other. **A normative frame**[12] **largely suspends opportunistic behavior**. This is crucial for the placement of trust. In a longer-term business relation, I trust my business partner if I have reason to believe that with regard to our agreements, he is in a normative frame and that this frame is quite stable in situations in which possible background goals might lower its salience and displace it. A normative frame has two potential enemies: first, the goal to increase one's scarce resources (gain); second, the goal to avoid feeling losses.

If we turn to the first goal (gain), we can see what the relationship is between trust and reducing mistrust. Blatant self-interest in economic contexts can be identified with gain. When gain is highly salient, it will displace a normative frame no matter how good the intentions are. **Legitimate mistrust** is the perceived likelihood that a potential or actual transaction partner's interests are not aligned with one's own interests and that the partner's actions are (and will be) driven by a salient gain frame such that relational and normative considerations are pushed into the background. The partner will be **strategically opportunistic** (i.e. willing to lie, cheat and generally harm the other) because restraints on that opportunism would come from goals that are so far pushed into the background that they will not affect the partner's actions. The salience of the gain frame has to be lowered first lest it keeps a normative frame from guiding the action with regard to the relationship. Thus, unless interests are aligned there is no possibility for the establishment of a business relationship in which a normative frame plays any important role. A normative frame for the ongoing business relationship must be "flanked" by interest aligning arrangements if it is supposed to have any stability at all. Removing cause for legitimate mistrust is thus a necessary condition for the establishment of trust. However, it is not a sufficient condition.

Once strategic opportunism has been removed, there are still the random shocks of situational temptations. They consist of sudden potential losses and golden opportunities, both of which are likely to trigger a loss frame. In that case, the partner will be **myopically opportunistic**, responding to short-term temptations possibly against his longer-term interests. Myopic opportunism is especially likely where a normative frame (and thus trust) is especially needed: in situations in which monitoring contract performance in detail is costly. Trust will only be established if strategic **and** myopic opportunism are being checked. We have seen that much attention has been given in the literature to ways in which interests can be aligned, especially through credible commitments, in order to reduce strategic opportunism. How is myopic opportunism handled in the daily routines of longer-term contractual relationships?

5.1. CHECKING MYOPIC OPPORTUNISM

People are interested in the stability of their partner's normative frame, but interestingly, they are also interested in the stability of their own normative frame and this is mainly due to the effect of **loss** on framing. If a person experiences a loss, say due to uncooperative behavior of another, then the fact that losses quickly produce strong emotional reactions makes it likely that whatever frame a person is in, it will be replaced by a frame in which eradication of the feeling of loss is the focal goal. If nothing can be done to restore the loss, then "getting even" would be one way, although not a productive one, to balance the loss. For example, Uzzi (1997, p. 59), in investigating interfirm networks in the apparel industry, found that "if the strong assumptions of trust and cooperation are exploited in embedded ties, vendettas and endless feuds can arise." A loss frame can be very destructive of both partners' resources. Uzzi reports a CEO as saying "If you screw a guy like that [a close tie] he'll stay in business just long enough to get even" (ibid.). Partners would like to avoid bringing another person into a loss frame when they have to confront the consequences. Thus they are interested in not "slipping" into uncooperative behavior via myopic opportunism.[13] **They are interested in their own frame stability**. This offers the possibility that the stability of normative frames is maintained by joint efforts rather than by controlling efforts of one partner over another. The possibly destructive consequences due to vindictive reactions to loss change the trust game considerably because they create a stake in not **appearing** to be untrustworthy and, since goals have such a strong impact on behavior, that is most easily achieved by **being** trustworthy. Yet, trustworthiness is not something one can achieve easily without others. For this reason, we have to consider the influence of groups.

Groups. It is an established insight in sociology that normative frames can best be stabilized in groups,[14] especially through rites and rituals and a common purpose. The rites and rituals work directly on the salience of the frame by increasing the value of the focal goal, decreasing the value of conflicting background goals, increasing confidence in the efficacy of the joint effort, and making members alert to possible dangers. Quite typically, the worthiness of the group goal is enhanced by its relation to the realization of a still higher goal (i.e. the group as unit being part of a larger group). The group's ability to achieve the common purpose is brought into relief by its relative superiority to other groups. The insignificance of internal divisions (i.e. the importance of not letting background goals become unduly important) is stressed by a collective definition of the dangers for cooperation, especially those stemming from certain other groups.

The upshot is that the stabilization of normative frames is very likely not just done by the contracting dyad but by one or more larger groups of people who share the common purpose of frame stabilization. These groups can be voluntary association of the industry; they can be lobbying organizations, country clubs, charities, and religious organizations. The larger the random shocks of situational temptations, the more likely that such groups play a crucial role in frame stabilization for longer-term business relationships. Such random shocks are likely to differ by industry. Weber (1978, p. 1206) has pointed to this group mechanism in American business, but because of the overriding attention given to mistrust problems, there has been little contemporary research into these group processes yet. In any case, it is the contention of this paper that genuine trust problems in economic transactions cannot be studied adequately unless these group processes are brought into relief.

Not just rites and rituals but also joint **conventions** are products produced by such groups. A crucial question is: when has the other been myopically opportunistic? Take for example rules dealing with the identification of sources of disturbance. What disturbances can come up in the contractual fulfillment in a particular industry? Who is to blame for such disturbances? For example, if the production costs suddenly skyrocket and put pressure on price agreements, what conventional understandings are there to prevent both myopic opportunism and the misplaced suspicion of myopic opportunism? Similarly, there are conventions about quality and quality control, about sources of negative externalities, about the measurement of damages. It is knowledge of these conventions which makes arbitration in conflicts so much more important than courts, and Williamson, who does not identify any of these group processes, is none the less right when he mentions arbitration as a means for "harmonious adaptations and preserving the continuity of exchange relations" (Williamson, 1985, p. 178).

5.2. Relational signals

What norms are being followed when a contract partner is in a normative frame? Of course, there can be many substantively different norms that have to do with the specific industry but the claim of this paper is that with regard to relational concerns (i.e. with regard to solidary behavior), norms pertain to behavior in five typical situations that ask for sacrifice for the relation. The generality of these norms lies in the generality of the five situations for any cooperative project. What can greatly differ is the amount of sacrifice that can be legitimately claimed in any of these situations and the specific behavior that signals conformity to the norm. Let me first turn to the five solidarity situations. Let Ego and Alter be the business partners. The behavior described is the behavior expected.

> *Common good situation.* Ego and Alter both belong to a group that produces a common good. Ego will contribute to the common good even if he could freeride (the minimal amount of contribution in terms of money, effort, time etc. expected for solidary behavior varies).[15]
>
> *Sharing situation.* If there are joint divisible benefits and costs and if Ego is the one who can divide them, he will not seek to maximize what he gets from the benefit and minimize what he gets from the costs but take his "fair share" of both (what the "fair share" is varies).
>
> *Need situation.* Ego will help Alter in times of need (what constitutes need and how much help is minimally expected for solidary behavior varies).
>
> *Breach temptation.* Ego will refrain from hurting Alter even at a cost to himself (the minimal amount of cost expected for solidary behavior varies).
>
> *Mishap situation.* Acts can be intendedly solidary but factually turn out to go against the expectation of solidary behavior. In that case, Ego will show that he meant to act differently, that he feels sorry that it turned out that way, and he will make amends if the mishap has caused damage to others. Also if Ego knows in advance that he will not be able to keep to the agreement, he will warn others in advance, so that they can mitigate the damage.

People in a normative frame want to act "appropriately", they want to do the right thing. Thus they want to follow the norms that are appropriate in this situations and act according to these norms. In this way they will always come to roughly the same expectations in each of the five solidarity situations. However, a normative frame is precarious because it is subject to the barrage of competing frames. People know that they cannot take for granted that the partner will stay in a normative frame. If "golden opportunities" come along, the partner's frame might change to a gain frame. For this reason, partners will monitor each other's frames. Behavior in these five situations is important in itself for any joint project. However it is equally important for the **relational signals** it gives off. As long as these signals are all positive, the normative frame is stable and the partner is trustworthy (see also Wielers, 1993). This allows the partners to monitor other contractual behavior via these relational signals and thus economize on monitoring costs. If the signals are “o.k.”, one does not have to keep checking the quality, does not have to keep counting the quantities etc. Conventions thus focus first and foremost on the functioning of relational signals, prominently including the “right” level of sacrifice in each of the five solidarity situations. When relational signals don’t function properly, trust cannot develop or be maintained, no matter what the written contracts look like.

Observe that since behavior in these five situations signals the stability of the normative frame (and thus the trust-worthiness) of the partner, there can be no substitution between these situations. Defection is any one of the five situations points to the lack of a normative frame, and seemingly cooperative behavior in one or more of the other fours situations will then be interpreted as strategic cooperation, ready to turn into defection whenever a temptation to do so comes up. A partner thus cannot make up for having given in to a breach temptation by helping in need because the help will be interpreted as coming from a gain frame, as being an attempt to appear as if a normative frame still reigned. There must of course be enough opportunity to observe behavior in these five situations. For this very reason alone, trust takes time to build and for this reason alone, one would expect the shadow of the past of an active business relation to have a strong impact on trust, more so than the prospect of a future business relationship. Findings by Blumberg (1998) confirm this asymmetry between past and future in interfirm contracting (see also Gulati, 1995).

5.3. THE COMPATIBILITY OF DOING BUSINESS WITH SOLIDARY BEHAVIOR

It is often observed that doing business with close friends and relatives is bad. The reasons are obvious. The norms of solidary behavior for these relationships are such that they make the only legitimate ground for inequality. If I start a restaurant with my brother and I invest more than he does, strong solidarity norms will put pressure on me to ignore the difference in investment and divide profits equally. Such norms also put a larger premium on the group than on the individual. For example, sacrifices should be judged by standards relating to the entire group rather than to individual welfare. If normative frames in business relations mobilize these kinds of norms, they act like a high tax (because of equality) and are stifling for the individual (because of the preponderance of the group). However, these norms are also counter-productive with regard to trust, especially if the input of the partners is different. Since **equality** is so important, results for the individual are not dependent on his input as long as the input is not determined by nonsolidary behavior. This is where the difficulty arises: “if I simply cannot work as hard as you, I cannot contribute as much as you, I cannot keep as easily to the agreements as you do, and that is not my fault.” Moral hazard problems are a common phenomenon in strongly solidarity groups with nonhomogeneous inputs (skills, capital etc). Solidarity without equity is subject to such exploitation hazards and thus not well suited to guide business relations.

What is needed in business relations is a weak form of solidary behavior in which the distributional norm is equity, not equality; in which the well-being of the individual and not the group is the paramount point of reference; and in which the sacrifice legtimiately expected for the sake of the relationship is never so high that it drains profits (see Lindenberg, 1988; Ligthart, 1995). Weak solidarity should not be confused with "weak ties" in Granovetter's sense. Weak forms of solidarity are not to be equated with intransitive ties in open networks. Because of the importance of groups for the stabilization of normative frames, weak solidarity flourishes best when there are generally (i.e. transitive) "friendly" (not "close") relations among the various interacting dyads involved in related business transactions. Confirmation of this point was recently produced in a study of friendship in organizations which showed – to the surprise of the researcher who was weaned on Granovetter's distinction between weak and strong ties – that friendly relations are transitive whereas close friendship relations that develop here and there on top of these friendly relations are not transitive (Van de Bunt, 1999). Studies of trust should thus also include attention to the conditions of weak solidarity and the dangers of degeneration into strong solidarity which is stifling for business relationships. In the study by Uzzi (1997) already cited, a beginning has been made to look at these dangers. In a recent article on the rules of the game in industrial cooperation, Brusco (1999) comes to very similar conclusions.

5.4. Some empirical points

Relational signals. In a recent study of the better dress sector of the apparel industry in New York, Uzzi (1997) made a distinction between "arm's-length ties" (market relationships) and "embedded ties" (close or special relationships). The apparel industry contains simultaneously market and embedded relations, the former being a majority, the latter being the relations of special importance. Individuals (contractors, manufacturers, production managers etc) would behave blatantly with self-interest in the market and cooperatively in the embedded relationships. This clearly speaks against the stable preference theories of trust and his detailed findings point clearly in the direction of relational signals in these five telltale situations.

The embedded relations developed over a longer time and typically showed solidary behavior in the five situations. The profitability for each was seen as a *common good*. "We are all in the same boat" Uzzi reports a contractor as saying. Uzzi found that extra effort was voluntarily given and reciprocated, there was joint problem solving, much communication and a very quick understanding of what adjustments had to be taken.

Signaling in *sharing situations* was also part of the routine interaction. Uzzi found a belief among partners of embedded ties that the other would not act in self-interest at another's expense; this showed up in concrete action such as resource pooling among partners and, when transactions had to be done fast, post hoc pricing. As one CEO put it “we do first and fix price after” or another CEO would say “the contractors know that they will not lose.” Dyer (1997) reports from Japan, that more than 75% of the suppliers of large firms interviewed indicated that if an inequity occurred in the present transaction, it would be ‘remembered’ and corrected in the future.

Help in *need situations* was taken for granted: “If there was a problem you knew you’d work it out and they’d help you” said a manufacturer of 30 years experience. A production manager even reports creating work for the contracting partners when there is a lull in the market. “We will put a dress into work to keep the contractor going. We’ll then store the dress in the warehouse.” By contrast, in arm’s length relationships the other would “push the price down when the contractor tells his production problems.” Restraint vis-a-vis *breach temptations* was very evident in Uzzi’s study. He reports that there is nondefection where defection clearly would serve the self-interest of a business partner. But then, there is also a watchful eye. Too frequently need situations are under suspicion of being covert breaches, putting the partner on the alert. Clear breaches are not forgiven. “If he switches to a new contractor then I won’t work with that manufacturer again.” This is in contrast to *mishap situations*. A manufacturer expressed it thus: “When you deal with a guy you don’t have a close relationship with, it can be a big problem. Things go wrong and there’s no telling what will happen. With my guys [his key contractors], if something goes wrong, I know we’ll be able to work it out.” One partner also warns the other about expected problems so the other can adjust in time. A production manager explains: “I tell them [key contractors] that in two weeks I won’t have much work. You better start to find other work.”

Contract clauses. If one throws mistrust and trust problem into the same hopper, as transaction cost economics does, then one would expect substitution effects between mistrust reducing and trust building measures. For example, social network effects (social embedding) should then reduce the number of clauses in a contract that deal with interest alignment. If, however, mistrust-reducing measures are necessary in order for trust to materialize, no such substitution effect across the mistrust/trust line is expected. To the contrary, mistrust-reducing measures are complements rather than substitutes for trust increasing measures. Blumberg (1997) has studied contracts regarding interfirm R&D cooperation in order to test the substitution hypothesis implied by transaction costs economics. Much to his surprise, he found virtually no relation between social embeddedness of partners and mistrust reducing measures in these contracts.

Governance structure in organizations. From the previous points, it follows that the specific ways in which mistrust is reduced and trust is built depend on what interests need aligning and on what rules and actions signal relational interest in a particular industry or a particular culture. For organization studies, this is important because it implies that there is no reason to assume that the Japanese model is

the example for reducing mistrust and building trust in organizations; nor are the standard governance solutions in transaction cost economics immune from this dependence of signals on rules and culture. For example, life-long employment ceases to be the ultimate relational signal when hiring for projects has been socially accepted and legally flanked so as to reduce blatant legitimate mistrust. In a similar vein, internal labor markets may not be necessary for motivating employees to train others and to be trained (with a concomitant wage sacrifice). Both active and passive training may become part of a project-based organization of work in such a way that the **functional legitimation** of training enters into the relational signals (see Lindenberg, 1993). What is claimed here is that whatever circumstance and culture, stable employment relations involving positions with considerable damage potential will always be accompanied by mistrust reducing measures and positive relational signals in place.

In a recent study, comparing Japanese and American companies, Mühlau (2000) showed that, when relations are important, governance structures function mainly by clear relational signals from employers to employees. This holds for wages, for promotions, and generally for governance by fair rules. When relations are not deemed important enough by the employer that relational expectations would be kept, employers take extra steps to prevent the development of relational expectations on the side of the employees. Informal rules also are subject to relational signaling. Wittek (1999) found that informal control strategies in organizations can best be explained by how control affects relational signals. He corroborates empirically that smooth functioning of an organization is incompatible with ambiguous relational signals even when interests have been aligned.

6. Conclusion

In the literature we find basically two traditions in theorizing about trust. One is the tradition within micro-economics and game theory that takes trust as calculated risk. The other is the psychological tradition that takes trustworthiness and trusting as based on a presumed other-regard without calculativeness. Both conceptions are wanting. The calculated risk approach is useful for the analysis of situations in which potential business partners do not come to an agreement because they legitimately mistrust each other. Mistrust is legitimate if foreseeable and blatant self-interest runs against keeping to the agreements. The solution to legitimate mistrust problems is interest alignment through credible commitments, such as hostages, through reputation effects, middlemen, and other means. Once legitimate mistrust problems have been removed, contracts can and in all likelihood will be entered. These aspects have been studied quite well by economists and rational choice sociologists. Strategic opportunism can be checked by interest alignment.

Were it not for longer-run contractual relationships, this concentration on mistrust problems would be sufficient. However, most interesting contractual situations for which mistrust problems arise are also potentially longer-term contractual arrangements. During such longer-term relations many occasions arise in which there are unforeseeable temptations to cheat or deviate in some way from the contractual agreements. Giving in to these temptations may even be against one's own longer-term interest, and still it happens time and again that people fall prey to such temptations when "golden opportunities" arise or when difficulties render cutting corners temporarily attractive. An approach that only considers farsighted contracting (as for example transaction cost economics) these problems of "myopic opportunism" cannot even describe let alone analyze.

I submit that myopic opportunism creates genuine trust (as opposed to mistrust) problems. The central question is: How and under what conditions can people be relatively confident that the other will not give in to myopic opportunism? And what do people do in various circumstances in order to achieve this confidence? Existing theories on trust (relating to [honesty-]dispositions and the positive effects of liking) cannot handle this question adequately even though their central intuition seems to be right: people can be trusted if they don't think of doing something that violates trust.

Indeed, if people do not perceive the opportunities to breach, they will not breach. The cognitive turn in psychology has produced tools for the analysis of such phenomena of selective attention. A theory of framing links these insights from psychology to a theory of rational choice. This theory will not be summarized here. Suffice it to say that it argues that people in a stable normative frame will disregard the opportunity costs of keeping to the rules and act intelligently to realize what is appropriate in the light of these rules. People in stable normative frames can be trusted not to do anything that would break the agreement. However, the crucial question then is; how can such frames remain stable against the random shocks of situational temptations?

In a nutshell, the answer is that first of all legitimate mistrust must be eliminated. Interest alignment is thus a necessary but not a sufficient condition for trust to arise in the daily routines of working through a contractual relation. In addition, the normative frame must be stabilized by group processes (common rites and rituals and common conventions). This suggests that trust in complex contractual relations cannot be studied in dyads but must be studied in industries, including voluntary associations (social clubs, churches, sports clubs, lobbying groups etc) in which members of this industry meet in the context of informal groups.

Because the stability of the normative frame is precarious, it is rational for partners to focus their monitoring on signals of this stability rather than on the details of the contract performance. As long as the frame is stable, contractual performance will be as good as it gets. It is suggested that the monitoring of frame stability takes place by looking at relational signals in five situations in which the partner must show some sacrifice if the frame is stable. Together, actions in these five situations make up solidary behavior (i.e. relationship-preserving behavior). Deviations in any one of these five situations signals problems with the stability of the cooperative frame. For this reason the day-to-day interaction between business partners will be governed by the exchange of relational signals. The conventions that are necessary to interpret the signals are in all likelihood the work of a group and not of a contracting dyad, and they can change over time with changing circumstances of what is "usual," how severe the risks are for individuals etc. (think for example of an increase in project employment or a massive change in the private or public social insurance).

The direction for future research suggested by this paper is to look at processes of interest alignment as a precondition for building trust in longer-term contractual relationships and to start analyzing group processes and relational signals for the maintenance of frames which, in turn, create trustworthiness and trusting. Explicit analyses of what makes a person "savvy" in a particular industry or contracting context should replace the standard assumption of a dispositional farsightedness of individuals. The approach suggested here also argues against seeing life-time employment, internal labor markets or any other governance instrument as "ideal" without having analyzed the question what interests need to be aligned and what signals are consensually taken as positive relational signals in a particular industry.

Notes

1 I thank Anna Grandori and two anonymous reviewers for valuable suggestions.

2 See Raub and Weesie (1990).

3 See Casson (1991).

4 DiMaggio and Power, however, fail to identify the choice from the menu of governance instruments as a remedy against legitimate mistrust. Rather, they see the choice only as a means to legitimate one's own organizational form.

5 The two aspects most often mentioned are (1) the restriction of **ex post** adjustments to those where the hazards of opportunism are least, and (2) the importance of the "spirit" in which adaptations are effected (Williamson, 1979, p. 248; 1985, p. 76). At times, he also mentions arbitration and reciprocal exposure of specialized assets (Williamson, 1985, p. 178) but they receive no explicit treatment in relation to the mechanisms of **ex post** adjustments.

6 Within neoclassical theory and game theory, it is difficult to even recognize the distinction between mistrust and trust problems. The main reason for this, it seems to me, lies in the fact that in order to focus not just on mistrust but also on genuine trust problems, one has to go against two related central assumptions in both neoclassical theory and in game theory: farsightedness and rational discounting. First, for economists trained in neoclassical theory it is very difficult to let go of the assumption that basically all important things can be anticipated, that this ability is even part of the implicit definition of rationality. Second, for economists trained in neoclassical theory, it is also difficult to accept that the way in which people discount future events cannot generally be called rational.

7 When I use "longer-term" relation I mean by it a relationship which lasts at least long enough for situational random shocks to occur and to tempt a person away from the agreement. This is the case in all relationships that extend beyond a spot exchange. Of course, the problem becomes more serious the more extended the relationship is and the more intelligent effort is needed for the tasks agreed upon. The higher the intelligent effort needed for the execution of the tasks, the more exclusive the concentration must be.

8 The co-called "low cost" view of moral principles (see Kirchgässner, 1992) would also lead to this conclusion. However, as will be seen later, I argue that this view fails to specify the workings of moral principles.

[9] A paper by Sitkin and Roth (1993) goes some of the way of making a distinction between the two. But the theoretical link between the two is not worked out.

[10] See Buskens (1999); Gal (1997); Klein (1997); Landa (1994); Raub and Weesie (1990); Snijders (1996).

[11] Because the term "attention" is highly ambiguous (see Pashler, 1998) I avoid it and speak instead of "framing". But notice that the term "framing" as used here differs from many other uses of this term. The framing theory used here is a stochastic theory of choice in which the choice probabilities depend on the relative strength of the frame. I will not go into any technical exposition here.

[12] I will deal with the content of norms in section 5.2.

[13] This point as been worked out in some more detail in Lindenberg (1994).

[14] See for example work done on intergroup relations (Sherif, 1996; Turner and Giles, 1981); on "collective identity" in the social movement literature (for example Pizzorno, 1978; Melucci, 1989); and on "purposing" in organizations (see Veill, 1986).

[15] A prisoners' dilemma could be seen as either a common good situation or as a breach temptation, depending on the particular interpretation given to the story.

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