

Trust as Intellectual Capital in Pursuing Flexibility in Business Contracting

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This paper looks contracting from an intellectual capital perspective, and specifically from the trust point of view. The paper discusses the role of trust as intangible asset in flexible contracting. The paper looks both trust and contracting from relational and processual perspectives meaning a collaborative activity between partners and partnering organizations in contracting processes. The purpose of the paper is to increase understanding of the role and nature of trust as intangible resource for contract management in pursuing flexibility thinking in contracts. Trust is seen as a leadership skill³ which leaders may use in influencing contract management specifically when negotiating flexible contracts. The proactive law approach provides potential in approaches, theories, and applications to discuss and integrate the organization behavior and leadership perspectives with contracting. It is commonly the management at different levels that is involved in contracting processes in organizations. Contracting involves behavioral skills such as communication for trust building. Trust is a relational asset forming a foundation for collaborative efforts between contracting parties. Therefore, examining the role, antecedents, and consequences of trust as a powerful element in business contracting is well grounded. The paper aims to broaden the scope of discussion about new approaches and practices needed and emerging in the changing field of contracting. Moreover, the purpose is to discuss flexibility in contracting in the view of how trust may facilitate and advance flexibility. Originality of the paper is based on the two main points: examining the role of trust in contracting as a relational, intellectual capital, and bringing a scarcely studied processual view into discussion about trust development and flexibility in contract management. The paper advocates the idea of seeking a balance between trust and contracts, i.e., control vs. freedom and flexibility.

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1. Introduction

The study looks business contracting from organizational and managerial research perspectives, more specifically, from the trust point of view. We discuss the nature of trust and business contracting and how trust in flexible contracting comes into scene. The paper pursues initiating opportunities of examining the topic as multidisciplinary and international issue, and in research collaboration within the network that exists and/or may be further developed. A new direction, unexplored so far, is to broaden the scope into empirical research on real life operations and changing contexts in which trust and contracting are embedded currently. Therefore, innovative and creative views and ways of studying the relationship between trust and flexible contracting are needed to increase scientific knowledge of the topic. The paper advocates the idea of pursuing a balance between trust and contracts, i.e., control vs. freedom and flexibility, in other words, decreasing a tension, that may exist between a ‘controlling role’ of contracts, and a flexible, relationally ‘balancing role’ of trust.

The paper focuses on contractual relations which have raised more attention in ever more complex business relationships networks within and between organizations. Trust is brought into discussion as influential force for co-operation and co-creation in contracting, and for a more effective collaborative atmosphere within organizations and beyond. Despite of the contract practices that may have a starting point in suspicions (distrust) there is also space and freedom for the parties to decide how to draft contracts in the practices of contracting. In this process managerial leadership plays a role and trust building forms a useful skill. First, the article provides a literature review of trust and the nature of trust in the contracting context; second, a discussion is made from the contracting point of view, and third, ideas are presented of the integration of these two perspectives in the view of balance and flexibility.

2. Concept of trust

Interpersonal trust is reciprocal in nature, and thus *relational* deriving from repeated interactions over time between trustor and trustee. Information available to the trustor from *within the relationship itself* forms the basis of trust between parties. Reliability and

dependability in previous interactions with the trustor give rise to positive expectations about the trustee's intentions.

2.1 Trust as intellectual, intangible capital

Trust has become an essential intangible asset in organizations and leadership. Trust promotes social order and cooperation. It is a resource that creates vitality and enables innovativeness for organizations.⁴ Trust is embedded in the known theoretical classification of intellectual capital as human, structural and relational capital⁵. Trust building is seen as human intellectual skill in leadership.⁶ It is seen as intangible asset within structural capital; and as relational in customer interaction and inter-organizational relationships.⁷ Trust is a key element in cooperation and communication in organizations contributing to knowledge sharing in different types of relationships between actors.⁸

Contracting processes are generally consisted of a number of human beings from multiple and different constituencies, backgrounds and cultures. In these contexts, differing manners likely exist and ways of communication and professional jargons as well as amenity and willingness to trust differ; moreover, perceptions and understanding of the meaning and even the role of trust in organizational contracting contexts vary. It is worth noticing that, in networks, intra-organizational processes such as managerial leadership could support the development of atmosphere, communication, openness and mutual understanding,⁹ e.g., willingness to compromise in the negotiations of different exchanges and transactions

⁴ Savolainen, T. Lopez-Fresno, P. (2013) Trust as Intangible Asset - Enabling Intellectual Capital Development by Leadership for Vitality and Innovativeness. *The Electronic Journal of Knowledge Management* 11, (3), 244-255.

⁵ Edvinsson, Leif and Malone, Michael (1997) *Intellectual Capital: Realising Your Company's True Value by Finding its Hidden Roots*. New York, NY: Harper Collins.

⁶ Savolainen, Taina (2011) Luottamusjohtajuus inhimillisen pääoman uudistamisessa. (Leadership by trust in Renewing intellectual capital) In Puusa, A. and H. Reijonen (eds.): *Aineeton pääoma organisaation voimavarana*, UNIPress, 117-141.

⁷ Edvinsson & Malone, 1997; Nahapiet, J. Ghoshal, S. (1998) Social capital, intellectual capital, and the organizational advantage. *Academy of Management Review* 23, (2), 242-265; Savolainen, 2011.

⁸ Savolainen et al., 2014; Ikonen, Mirjami and Savolainen, Taina (2011) Renewing Human Intellectual Capital by Building Trust in Intra-organizational Relationships. In *Proceedings of the European Conference on Management, Leadership and Governance, Sophie-Antipolis, France*

⁹ Savolainen, T. (2010) Role of trust in managing customer focus: Multilevel theoretical and empirical issues. In *Proceedings of the 5th EIASM Workshop on Trust within and between organizations, Madrid, Spain*.

requiring contract making. Negotiated agreements provide the basis for business, government and inter-organizational and -national relations.¹⁰

These questions show the complexity of the area of contract management from the social, cultural and organizational point of view. Power relations make trust more complex and fragile in relationships. Moreover, cultural differences appear; they are manifested in varying degrees of power distance, uncertainty tolerance, and collectivism.¹¹ Therefore, our aim is to stretch beyond a mere excellent contracting suggesting that there are issues that matter in successful contract management from which the proactive law approach could benefit.

Trust is approached mainly as a relational concept and has been defined and categorized in numerous ways. The study takes a closer look at the concept of trust in business contracting context. While many definitions exist the concept remains without a generally accepted definition.¹² The *relational definition* of trust, applicable to the perspective of this study, is developed by Mayer et al.: “The willingness of a party to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor, irrespective of the ability to monitor/control that other party.”¹³

This definition of trust by Mayer et al. is applicable to relationships in an organizational context, i.e., in a relationship between a trustor and a trustee who is perceived to act and react with volition toward the trustor. Making oneself vulnerable is taking risk and implies that there is something of importance to be lost. Trust is not taking risk per se, but rather it is a willingness to take risk.¹⁴

Trust is defined above from a relational perspective which thus links it with relational contracting. Trust is paradoxical phenomenon in the modern society that is characterized by increasing uncertainty, complexity and risk. Broadly defining trust in exchange relationships,

¹⁰ E.g. structural, affective and contractual factors have been studied by Mislin et al., 2011.

¹¹ Hofstede, Gert. (1997) *Cultures and Organizations: Software of the Mind*. McGraw-Hill USA; cf. Trompenaars, Fons and Hamden-Turner, Charles. (1997) *Riding the Waves of Culture: Understanding Cultural Diversity in Business*. London: Nicholas Brealey Publishing Ltd.

¹² McEvily, B. Perrone, V. Zaheer, A. (2003) Trust as an organizing principle. *Organization Science* 14, (1), 92-103; p. 101.

¹³ Mayer, R. Davis, J. Schoorman, D. (1995) An integrative model of organizational trust. *Academy of Management Review* 20, (3), 709-734.p. 712.

¹⁴ Mayer, R. Davis, J. Schoorman, D. (1995) An integrative model of organizational trust. *Academy of Management Review* 20, (3), 709-734; p. 712.

and also related to contractual relations in intra- and inter-organizational relationships, the following definition by Hosmer is applicable: “The reliance by one person, group, or firm upon a voluntarily accepted duty on the part of another person, group, or firm to recognize and protect the rights and interests of all others engaged in a joint endeavor or economic exchange.”¹⁵

Trust-based relationships refer to the situation where, instead of the intent to pursue and gain merely personal benefits, willingness to collaborate and compromise exist between parties. Paradoxically, trust involves uncertainty, complexity and risk in the current business environment.¹⁶ Contract making is often multipart decision making effort within dyads or on a group level. While risk taking is at the core of trust,¹⁷ trust forms a source of security. Therefore, it seems clear that the more a person trusts another’s future actions, the more securely and with more confidence the said person will take part in the activities of the object of trust.¹⁸ Here trust is seen as a mechanism that enables organizational actors, such as managers, to create open organizational culture which, in turn, affects the sharing of information and knowledge. Information sharing facilitates problem solving and adaptation. Contracting actors (parties) are willing to share private information with one another including short and long-term plans and goals. As a result mutual trust develops and increases and willingness to collaborate, consequently.¹⁹ Thus, trust reduces uncertainty and vulnerability in the relationships between inter- and intra-organizational actors.²⁰ In other words, a tendency to making contracts by lawyers for avoiding conflicts or disputes in courts represents a kind of mistrust- or distrust-based approach to contracting. A trust-based approach instead favors compromising and lowering risk preventively in the negotiation process of contracts.

¹⁵ Hosmer, L.T. (1995) Trust: The connecting link between organizational theory and philosophical ethics. *Academy of Management Review* 20, (3), p. 381.

¹⁶ Bachmann, Reinhard (2000) Conclusion: Trust – Conceptual Aspects of a Complex Phenomonon. In Lane, C. and R. Bachmann (eds.): *Trust Within and Between Organizations*. Oxford: Oxford University Press.

¹⁷ Mayer et al. (1995).

¹⁸ Das, T. Teng, P. (1998) Between trust and control: developing confidence in partner cooperation in alliances. *Academy of Management Review* 23, (3), 491-512.
1998, p. 494.

¹⁹ Poppo, L. Zenger, T. (2002) Do Formal Contracts and Relational Governance Function as Substitutes or Complements? *Strategic Management Journal* 23, 707-725.

²⁰ Möllering, G. Bachmann, R. Lee, S. (2004) Understanding organizational trust – foundations, constellations, and issues of operationalisation. *Journal of Managerial Psychology* 19, (6), 556-570.

When companies use contracts as means of cooperation and communication in business it may produce a competitive advantage for businesses. Contracts provide also means of control and change. Contracts play a proactive role, in other words, to prevent disputes and to achieve business goals in turbulent organizational changes. The proactive approach would benefit businesses for contracting practices and business competitiveness, accordingly.

2.2 Trust in contracting

Pertaining to contracting, a traditionally held view is that contracts in general refer to lack of trust or distrust. Recently, scholars have pointed out that the relationship between trust and contracts depend on when, why and how contracts are used. Weibel et al.²¹, Möllering²² and Klein Woolthuis et al.²³ suggest that trust and contract can be both complementary and substitutive.²⁴ As contracts tend to be more or less incomplete trust is needed as an asset and skill to pursue collaboration and balance emerging or existing conflicts or disputes. Trust may play the role of moderator and facilitate flexibility for achieving the expected outcome, for instance, trust may enhance communication and sharing information.²⁵ Trust is therefore involved as an essential part of contractual arrangements, i.e., a process and relations.

Organizational leadership and culture have an influence on the success of contracting processes. Different types of contracts need different form of trust.²⁶ Higher level of trust makes decision making more efficient by simplifying the processes of seeking and interpreting information.²⁷ According to Barry and Oliver,²⁸ the heading “post-negotiation

²¹ Weibel, A. Madhok, A. Mellewigt, T. (2007) Trust and formal contracts in interorganizational relationships - substitutes and complements. *Managerial and Decision Economics* 28, (8), 833-47.

²² Möllering, Guido (2006) Trust: Reason, Routine, Reflexivity. Oxford: Elsevier. p. 66.

²³ Klein Woolthuis, K., Hillebrand, B. Nooteboom, B. (2005) Trust, Contract and Relationship Development. *Organization Studies* 26, (6), 813–840.

²⁴ On complementarity see also, e.g., Poppo & Zenger (2002).

²⁵ Vlaar, Paul (2013) Trust and contracts: together forever, never apart? In Bachmann, R. and A. Zaheer (eds.): *Handbook of Advances in Trust Research*. Edward Elgar, 29-54.

²⁶ Malhotra, D. Murnighan, J.K. (2002) The effects of contracts on interpersonal trust. *Administrative Science Quarterly* 47, (3), 534-559; see also Möllering, Guido (2006) Trust: Reason, Routine, Reflexivity. Oxford: Elsevier.

²⁷ McEvily, B. Perrone, V. Zaheer, A. (2003) Trust as an organizing principle. *Organization Science* 14, (1), 92-103; p. 93.

²⁸ Barry, B. Oliver, R. (1996) Affect in Dyadic Negotiation: A Model and Propositions. *Organizational Behavior and Human Decision Processes* 67, (2), 127-143.

affect” includes the concept of trust. Mislin et al.²⁹ found out that trust is built by the talks consisting of the negotiation process. Therefore, in sustaining competitiveness through excellent contracting trust-based relationships enable negotiations which may result in prosperous outcomes. Processes of trust are quite scarcely studied so far, in other words, how trust develops, is built and re-built. An important issue is the process by which trust evolves.³⁰

Therefore, a literature review of trust and contracting in empirical settings as well as conceptual studies could shed more light into the role trust plays in contracting and into the emerging issue of flexibility, more specifically. To mention a few studies in prior research, e.g. Lane and Bachmann³¹ have described contract law as an important institutional framework for trust-based interaction. Möllering³² depicts that assurance and orientation gained from the existence of sanctions promotes trust. Not only dyadic relationships but also industrial, organizational and network level relations are examined in the literature. For example, legal regulation has an effect on the development of trust in the workplace.³³ Contractual trust can develop into organizational trust.³⁴ As Chenhall and Langfield-Smith³⁵ have stated, interpersonal trust rarely arises spontaneously in business organizations but trust is fostered through formal contracts. These researchers have also produced empirical evidence on the mechanistic control inhibiting the development of trust. The literature review leads to specific expectations on peculiar mechanisms needed for flexible contracting.³⁶ Trust is posed as a prerequisite for knowledge sharing in addition to traditional modes of

²⁹ Mislin et al. (2011) Mislin, A. Camoagna, R. Bottom, W. (2011) After the deal: Talk, trust and the implementation of negotiated agreements. *Organizational Behavior and Human Decision Processes*, 115, 55-68.

³⁰ Mayer et al. (1995); Savolainen, Taina and Ikonen, Mirjami (2015) Emergence of trust development process - a qualitative study in the team context. In S. Jagd and L. Fuglsang (eds.) *Studying Trust as Process within and between Organizations*.

³¹ Lane, C. Bachmann, R. (1996) The social constitution of trust: Supplier relations in Britain and Germany. *Organization Studies* 17, 365-395.

³² Möllering, Guido (2006) *Trust: Reason, Routine, Reflexivity*. Oxford: Elsevier.

³³ Streeck, Wolfgang (1992) *Social Institutions and Economic Performance: Studies of Industrial Relations in Advanced Capitalistic Countries*. London: Sage.

³⁴ Chenhall, R. H. Langfield-Smith, K. (2003) Performance Measurement and Reward Systems, Trust, and Strategic Change. *Journal of Management Accounting Research*, 15, (1), 117-143.

³⁵ Ibid.

³⁶ E.g. Jeffries, F.L. Reed, R. (2000) Trust and adaptation in relational contracting. *Academy of Management Review* 25, (4), 873-882.

governance such as formal control mechanisms. Moreover, understanding the roles and dynamics of contracts and trust is crucial for inter-organizational collaboration.³⁷

We suggest a *processual approach* as an alternative for the traditional approach. In a process view, trust in contracting is seen as a process, where exchange or negotiation between two parties is occurring during the whole process of relationships between parties. Both parties have expectations related to their current and future needs and values. Trust is embedded in a series of episodes, in which information is exchanged in order to determine how to proceed in contracting. The process of interpersonal, dyadic trust development appears more complex and uneven than the prior research has suggested.³⁸ Trust development in contracting may also easily turn into lack of trust or distrust instead of a positive development cycle of trust.³⁹

2.3 Role of trust after the deal

The literature on negotiation has not adequately captured the dynamics in negotiation.⁴⁰ Reciprocity in negotiations increases the understanding of how actors (parties) behave. Trust is also highly dynamic and contextual in nature. Regarding both trust and negotiation as dynamic phenomena leads to yet unexplored process perspective. Trust in contracting is seen as paradoxical in nature, as the coexistence of trust and distrust may produce turns and shifts within relationships between people involved. Rebuilding trust depends on the extent and motives of trust breach: In contracting, misunderstandings may unintentionally occur, and from the perspective of trust development, misunderstandings should be settled down as early as possible. In the process of contracting, a clear articulation of the periods of considering and rethinking is important in order to avoid misunderstanding and trust diminishing.

³⁷ Blomqvist, K. Hurmelinna, P. Seppänen, R. (2005) Playing the collaboration game right - balancing trust and contracting. *Technovation* 25, 497-504.

³⁸ Ikonen, Mirjami (2013) *Trust Development and Dynamics at Dyadic Level. A Narrative Approach to Studying Processes of Interpersonal Trust in Leader-Follower Relationships*. Joensuu: University of Eastern Finland, Business School. (Diss.); Savolainen, Taina and Ikonen, Mirjami (2015) Emergence of trust development process - a qualitative study in the team context. In S. Jagd and L. Fuglsang (eds.) *Studying Trust as Process within and between Organizations (submitted manuscript, forthcoming)*.

³⁹ Cf. Ikonen, M. (2013).

⁴⁰ Gelfand, M.J. Smith Major, V. Raver, J.L. Nishii, L.H. (2006) Negotiating relationally: The dynamics of the relational self in negotiations. *Academy of Management Review* 31, (2), 427-451; p. 428.

Recently, the need for trust in negotiation is discussed by Lewicki and Polin.⁴¹ In the current paper, negotiation is also defined as a process, *negotiating*, as a part of a larger process of contracting which includes all the organizing and coordinating activities within and between organizations, e.g. making sense of one's partner and the environment.⁴²

3. Leadership role in contract management

The discussion in the paper aims to advocate *the idea of seeking a balance between trust and contracting (a tension between control and freedom and/or flexibility)*. Leadership plays a role in this and, thus, the perspective of managerial leadership is brought into discussion. Moreover, the nature of trust needs to be discussed in the context of contracting. Leaders act in daily processes of organizations and use the means of influencing people by building trust and other managerial skills. Leadership is defined in essence as exerting influence on a group of people or an individual for achieving common goals in interaction with people.⁴³

The management is commonly involved in contracting processes in organizations at different levels and forms. Following the definition of influencing and interaction, contracting behavior involves interactive and influential leadership activity. Leaders key task in general is to communicate, advocate, and achieve common goals through people to achieve expected and mutually satisfying results between individuals, parties, and within groups. For this trust forms a foundation for willingness to mutual collaboration. Interaction and time with open communication are the key building blocks for functioning relationships.⁴⁴

Showing of trustworthiness, i.e., competence, benevolence and integrity, become more important for leaders. Communication and negotiation skills are essential for collaborative

⁴¹ Lewicki, Roy and Polin, B. (2013) The role of trust in negotiation processes. In R. Bachmann and Zaheer, A. (eds.): *Handbook of Advances in Trust Research*. Edward Elgar, 29-54.

⁴² Vlaar, Paul (2013) Trust and contracts: together forever, never apart? In Bachmann, R. and A. Zaheer (eds.): *Handbook of Advances in Trust Research*. Edward Elgar, 29-54.

⁴³ Cf. Yukl, Gary (2010) *Leadership in Organizations*. 10th ed. Prentice Hall.; Northouse, Peter (2004) *Leadership. Theory and practice*. 3rd ed. Thousand Oaks, CA: Sage Publications, Inc.

⁴⁴ Savolainen, Taina (2008) Leadership and trust as influential forces for contract management. In *Publications in Law/21*. University of Joensuu: University Printing House, 119-129.

and trustful working atmosphere and collaborative activity.⁴⁵ Leaders have impact on the openness of culture, and atmosphere that encourages free flow of ideas, knowledge and their sharing. Leadership and organizational culture characterized by freedom and openness also best foster and support collaborative inter-organizational relationships needed for productive contracting.

3.1 Relational view into leadership, trust and contracting

In general, the relationship as such involves relational processes or relatedness. Thus, a relationship exists where there is an element of interdependence and some type of interaction⁴⁶. Leaders are responsible both in vertical and horizontal relationships in intra- and inter-organizational relationships. As Bachmann⁴⁷ notes, trust does not occur spontaneously and automatically but is deliberately created and shaped, which justifies studying how trust develops and searching for a better understanding of effective trust-building as a process.⁴⁸

Pertaining to leadership perspective, there are two theoretical frameworks to studying trust development in contracting relationships, namely Leader-Member Exchange Theory (in intra-organizational leader-follower relationships) and the Agent Theory (dyadic contractual vertical relationships). Leader-Member Exchange Theory (LMX) describes a leadership role and behavior in internal organizational relationships. It can be applied in this study, as the perspective of contractual relationships is in focus and dyadic and group level activity comes into question.⁴⁹ The LMX-theory looks mainly a dyadic level⁵⁰, as stated above with the

⁴⁵ Savolainen, T. Lopez-Fresno, P. Ikonen, M. (2014) Trust-Communication Dyad in Inter-Personal Work Relationships - Dynamics of Trust Deterioration and Breach. *The Electronic Journal of Knowledge Management*.

⁴⁶ Atkinson, Sally. (2004) Senior management relationships and trust: an exploratory study. *Journal of Managerial Psychology* 19, (6), 571-587.

⁴⁷ Bachmann, R. (2011) At the crossroads: Future directions in trust research. *Journal of Trust Research* 1, (2), 203-213.

⁴⁸ Savolainen, T. Lopez-Fresno, P. Ikonen, M. (2014) Trust-Communication Dyad in Inter-Personal Work Relationships - Dynamics of Trust Deterioration and Breach. *The Electronic Journal of Knowledge Management*.

⁴⁹ Brower, H.H., Schoorman, F.D. Tan, H.H. (2000) A Model of Relational Leadership: The Integration of Trust and Leader-Member Exchange. *Leadership Quarterly* 11, (2), 227-250.

definition of trust. Trust makes cooperation desirable; and leadership support enables individuals to convert that desire into action in work relationships which may also be multipart. Both trust and leadership are necessary, but in combination they create conditions for integrating the disparate thinking and actions of dispersed people which commonly characterizes contracting circumstances.

In the most advanced stage of development reaching a partnership/company stage, specific (and dyadic) relationships extend to groups and networks – called as ‘Team-Making Competence Network’⁵¹. This is what applies well to contracting contexts. Network relationships have been examined from the interaction/ network perspective for a couple of decades (called as B2B and IMP - Industrial purchasing and marketing). The approach comprises three dimensions: technical, social and economic. Trust and contracts are seen as linked in the IMP approach since they are even defined as mutually exclusive. If high level of trust exists, official rules and contracts are not perceived necessary.⁵²

Contract is intangible resource referring to *intellectual property* that is co-created with contracting parties. Successful projects and outcomes are delivered and achieved in environments where high levels of trust exists among the collaborators, and in which they may openly share their problems, concerns, and opinions without suspicions and fear of punishments. This makes trust and contracting support each other and business competitiveness, eventually. Trust and trust building form intangible asset and skill, utilizable at organizational, group and individual levels as antecedent and foundation for contractual relations and needed in exchange arrangements when contracts are made and implemented.

As advantages of trust are many, cost effectiveness may be realized as one of the most important gains from the competitiveness point of you; making deals and realizing them become less risky and complex if parties trust each other. Moreover, conflicts can be solved more constructively in relational, often face to-face, interaction. In conflict situations, acceptance is achieved to decisions even unpleasant if the motives and good intentions of a

⁵⁰ Graen, G.B. Uhl-Bien, M. (1995) Relationship-based approach to leadership: Development of leader-member exchange (LMX) theory of leadership over 25 years: Applying a multi-level multi-domain perspective. *Leadership Quarterly*, 219-247.

⁵¹ Ibid.

⁵² Huemer, L. (2004) Activating trust: the redefinition of roles and relationships in an international construction project. *International Marketing Review* 21, (2), 187-201.

party or authority can be trusted. Rebuilding of trust occurring, e.g., as a consequence of malpractices is an important issue of business contracting management in inter-organizational relations and networks. Yet, the issue has been scarcely discussed and examined so far.

3.2. *Control, trust and flexibility*

According to agent theory contracting partners usually have different expectations of the advantages of contracting and the theory suggests developing control mechanisms to manage the processes. The current paper focuses on the tension between control and flexibility. Contracts are relational governance arrangements in economic exchange based on collaborative actions within and between organizations. Inter-organizational exchanges are typically repeated exchanges that are embedded in social relationships. Governance is value-based and agreed-on process occurring in social relationships. Through the social processes, relational governance play a role in mitigating the exchange hazards targeted by formal contracts.⁵³ As contracts can be seen as a form for collaboration, trust functions as both foundational and complementary mechanism.⁵⁴ In reality, contracts tend to be incomplete and trust is needed for initiating and developing collaboration and achieving the expected outcome. Thus, trust becomes a necessary part of a contracting process. At least in the situations where a contract cannot be defined explicitly, the expectations of the actions of the other party are communicated, clarified and expressed through trust.⁵⁵

3.3 *Balancing trust and control*

This paper suggests that the appropriate solution in tensions between control and trust may be reached through combining and balancing the two. Control alone can be very expensive, but so can mere trusting. Control plays commonly a role if the level of trust is low. Trust, in turn, is related to and, in fact, viewed as a part of control but also a substitute for hierarchical

⁵³ Poppo, L. Zenger, T. (2002) Do Formal Contracts and Relational Governance Function as Substitutes or Complements? *Strategic Management Journal* 23, 707-725.

⁵⁴ Cf. Bradach, J. and Eccles, R (1989) Price, authority and trust: from ideal types to plural forms. *Annual Review of Sociology* 15, 97-118.

⁵⁵ Dasgupta, Partha (1988) Trust as a Commodity. In Gambetta, D. (ed.): *Trust: Making and Breaking Cooperative Relations*. Department of Sociology, University of Oxford, 49-72

control.⁵⁶ If one trusts another, there is less need to control the other's behavior and activities. When suspicions decrease or do not arise, flexibility may increase. Thus, the appropriate result might be reached through balancing trust and control. This may have implications to the entire process of business contracting, more specifically to flexibility that facilitates adaptation to unforeseeable issues and events.⁵⁷

4. Conclusions

Erosion of trust in society and business life is evident due to major changes at multiple levels. In contracting, on the other hand, flexibility is needed, as tight regulations and complex contracts increase bureaucracy. In the global scale, increasing flexibility in contractual relations, virtualization of organizational forms and more complex intra- and inter-organizational relationships (including diversity and e-relationships) have made networks less easy to manage for exchange arrangements.⁵⁸ Thus, challenges and contradictions exist and solutions will be needed.

In conclusion, the discussion imply that, in contracting processes trust and trust building form and influential intangible asset and skill for more effective contract management where leadership skills need to be developed. In business contracting, trust building and showing trustworthiness cannot be overestimated in the current business environments making strong requests of cooperative abilities in intra- and inter-organizational practices. Trust has become one of the key resources in collaborative exchange relationships within and between organizations. It, thus, deserves to be studied and understood as competitive asset and advantage in organizations and networks.⁵⁹

This paper highlights the importance of raising the level of awareness of the role trust, trust building and leadership skills play in the processes of contracting in organizations and

⁵⁶ Costa, A.C. Bijlsma-Frankema, K. (2007) Trust and Control Interrelations. New perspectives on the Trust-Control Nexus. *Group & Organization Management* 32, 392-406.

⁵⁷ Poppo, L. and Zenger, T. (2002).

⁵⁸ E.g. Creed, W.E. Miles, R.E. (1996) Trust in organizations, a conceptual framework. In R. Kramer and T. Tyler (eds.): *Trust in Organizations: Frontiers of Theory and Research*. SAGE, 16-39.

⁵⁹ Savolainen, Taina (2011) Luottamusjohtajuus inhimillisen pääoman uudistamisessa. (Leadership by trust in Renewing intellectual capital) In Puusa, A. and H. Reijonen (eds.): *Aineeton pääoma organisaation voimavarana*, UNIPress, 117-141.

networks. The discussion is crystallized in the suggestion of a balancing view to ease tensions between trust and control for pursuing flexibility in the processes of business contracting. Therefore, the main point for further research is concluded in the aim to discover empirically how trust develops and is built and re-built, and how it facilitates and makes balance between trust and control for flexibility in business contracting. The view of process studies in trust was also brought into discussion of flexible business contracting. As scarcely discussed and examined so far the process perspective would deserve more attention in further empirical research.

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