

TRUST AND DISTRUST IN TEMPORARY CLIENT-CONTRACTOR RELATIONS

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ABSTRACT

Adversarial inter-organisational relations have since long been considered a major problem in the construction industry. In Sweden, however, clients have been hesitant to abandon traditional procurement practices, and there are still only a few examples of explicit partnering projects. The aim of this paper is to identify mechanisms that influence the development of trust and co-operation in client-contractor relations in construction. 15 clients were interviewed to capture current attitudes to closer co-operation with contractors. It was found that although co-operative contractual arrangements were employed, clients did not express strong trust in contractors. It is argued that an emphasis on rational reasoning and economic incentives leads to the adoption of highly specified contracts and close control. Two other aspects were found to reinforce this tendency by hampering the development of relational trust. First, traditional, highly specified construction contracts as well as procurement practices give rise to attitudes and behaviour that contradict common-sense perceptions of how a trustworthy person acts. Contractors adopt a critical, intolerant attitude to the client and the consultants, and clients become suspicious of contractors. Openness and consistency are discouraged. Second, competitive tendering in unique projects combined with high variations in demand cause problems in arriving at a common perception of a fair price. Either party is likely to feel badly treated, which induces both opportunism and fear of retaliation. It is concluded that to foster stable trust relations, formal interest alignment that justifies rationally based trust is needed. Such incentive contracts also prevent perceptions of unfairness and communicates co-operative intentions.

However, to maintain contractor commitment and enable creative co-operation, more carefully elaborated communication strategies are important.

BACKGROUND

Adversarial inter-organisational relations have since long been considered a major problem in the construction industry, and the recent general interest in partnering and collaborative buyer-supplier relations has brought new interest to the subject. The aim of this paper is to increase the understanding of why co-operative client-contractor relations in construction seem to be so fragile. Rational models, such as transaction cost economics, as well as descriptive psychological and sociological models are considered. To investigate current client attitudes and practice, interviews were carried out with 15 clients. First, the construction context and contracts are described.

CONSTRUCTION CONTRACTS

Most buildings are custom-made to meet the needs of a specific client. However, as the same systems and components frequently recur in different projects, the standardisation in the construction industry is industry-based rather than company-based. Also organisational roles and terms of exchange are standardised (Kadefors 1995). The roles of the main participants – the client, the architect, the different consulting engineers, the main contractor and the sub-contractors – are much the same between projects and in Swedish construction a few, standard forms of contract dominate. In the traditional general contract, the client appoints consultants to specify the building design. Main contractors are then invited to tender, either openly or after pre-qualification. Often, a fixed price is set for the contract and it is normal to appoint the lowest bidder. In another standard contract, the design-build contract, the specifications are less detailed and ideally described in terms of performance requirements. Here, the contractor appoints the design team and is responsible for the performance of the completed building. In Swedish design-build contracts specifications tend to be quite detailed.

During the construction phase, which generally lasts more than a year, there are often many specification changes. As every building is unique, the drawings and specifications in the

contract documents always contain errors and omissions that have to be corrected. Furthermore, changes in user needs, market demand or governmental regulations modify client preferences and lead to changes in requirements. Other causes of changes are weather and soil conditions and the supply of material and labour. Therefore, a central part of the contract pertains to how changes are handled. Standard contractual agreements stipulate that when a client chooses to change the requirements, or when errors or omissions in the specifications are found, the appointed contractor has the right to carry out the “extra” work that follows. The pricing of this work is based on contractor cost and is not subject to competition. Thus, specification defects and client changes entail extra costs for the client and opportunities to improve profits for the contractor. This causes problems for the relations. The client fears that the contractor will scrutinise the contractual documents for errors and ambiguities that may lead to claims, exploit their monopolist position by excessive pricing of extra work, or save money by shirking on quality. Clients often employ site engineers to inspect site work, and all contractor claims and suggestions are critically examined to detect signs of opportunism.

However, because of the uncertainty the client and the contractor have to interact frequently during the contract period for communication and joint problem solving, and this limits the degree of conflict possible. Also, the client is strongly dependent on the good will of the contractor both to deliver work of good workmanship, and to handle unforeseen circumstances in a co-operative way. Consequently, the scope for emotions and social norms to influence the terms of exchange is often considerable.

CRITICISM OF TRADITIONAL CONTRACTS

For many years, contractors have tried to persuade clients to employ design-build contracts more frequently and also to make design-build contracts less specified so that the contractors may participate in the initial phases of a project. Contractors argue that their knowledge of construction technology and the current market prices of alternative building materials may bring significant value to the process. They complain that it is dissatisfying to always be suspected and not being allowed to contribute their knowledge. Also,

traditional contracts procured by competitive tendering make it difficult for contractors to make a profit.

Many clients share the view that closer co-operation with the contractor would be advantageous. They look for a better integration of design and construction, less conflict and more flexibility. Still, many clients are suspicious of contractors and are reluctant to abandon general contracts and their control of the design. There is a tendency that clients view co-operation as something that primarily benefits the contractors.

INTERVIEW METHODOLOGY

The interviews were carried out as a part of a masters thesis in collaboration with Skanska, the construction company, who was interested in their clients' attitudes towards early procurement of a design-build contractor (Gerle and Nyberg, 2000). The interviews were semi-structured and the questions were related to trust and co-operation in client-contractor relations in general. The interviews were taped and transcribed.

The interviewees were selected because they represented major clients and, in some cases, because they had used co-operative arrangements. Skanska did not directly influence the choice of interviewees. Of the 15 clients interviewed, 8 represented purely commercial developers and property owners. These companies mainly own office buildings and shopping facilities. The other 7 clients were connected to a specific industrial or public core business.

INTERVIEW RESULTS

A couple of clients reported that they were satisfied with traditional general contracts and never considered using other forms. Another couple used traditional general contracts, but said that they would like to try more collaborative forms but felt that this was too risky. Most clients preferred specified design-build contracts. The main reasons were that project execution tended to be smoother with less fuss about minor issues, and the contractor's single point performance responsibility. Also, the client function's superiors and customers sometimes required to know the price before they decided to start a project or sign a deal.

Concerning the value of bringing in contractor competence in the design, there were different opinions. Some clients considered this valuable, but others said that their experience was that contractors did not contribute much when they were invited to participate. Early contractor involvement was not very common. If it was difficult to specify the requirements at an early stage, clients could bring in the contractor early and then use cost-plus contracts in combination with some kind of profit-sharing arrangements. However, this method would be chosen only when there was insufficient time to use more specified contracts.

Almost all clients, both public and private, emphasised the importance of competition. The general view was that without competition, the contractor would not make an effort and the client would not obtain a good price. Some clients had long-term relations with contractors for smaller projects, but made sure to check prices now and then. For larger projects, there was almost always a competitive bidding procedure. In cost-plus contracts, clients could make contractors compete on their profit margin and administration costs. For many clients, the difficulties of achieving competition before the product is defined was the major obstacle to early contractor procurement. Profit-sharing arrangements were preferred, although fixed price contracts seemed to be most common. The clients also emphasised the importance of finding the right contractor staff, but the contractor companies were considered to be very similar. Instead, the view was that good people could be found within most of the reasonably big contractor companies. Several clients said that they liked to have good relations with a number of contractors, who then would be competing with each other on price.

Thus, traditional general contracts was not the dominating contract form. However, despite the variety of procurement routes used, the clients did not express strong confidence in contractors. They were perceived as being focused on reducing costs at the expense of quality and clients maintained that the traditional general contracts tended to shape the contractor's behaviour, culture and competence. Collaborative forms were used mainly to avoid conflicts and fuss about extra payments or when more specified contracts could not be used. Clients were interested in closer co-operation with contractors, but did not think

that contractors were ready to assume increased responsibility and participate more in initial phases of a project. A main criticism of contractors was that they lacked in respect and responsiveness towards user and client needs.

In the following sections, major bases for trust and the relationships between trust and control are described. This framework is then used to analyse the specific situation of client-contractor relations in construction.

BASES AND TYPES OF TRUST

Rosseau, Sitkin, Burt and Camerer (1998) identify the following forms of trust in recent trust literature:

Deterrence-based trust is based on costly sanctions for breach of trust. Detailed contracts, monitoring and sanctions can foster co-operation, which may in turn foster trust. However, such measures may also be seen as substituting for rather than building trust.

Calculus-based trust is used to describe a wider rational choice perspective on trust. Trust is viewed as a product of the incentive structure shaping the interests of a person, and a perceiver's knowledge of these interests (Kramer 1999).

Relational trust arises in repeated interactions. Throughout the interaction the parties obtain direct, personal experience and information that form the basis for relational trust. As this kind of trust is based on emotions, it is also referred to as affective (McAllister, 1995).

Institution-based trust refers to the role of institutions in shaping the conditions for trust. Important institutions are, for example, legal systems and other societal norms pertaining to conflict management and co-operation. Institutional factors also determine the importance of reputation.

Perceptions of fairness are considered fundamental to trust and co-operation. People tend to express strong emotional reactions to perceived injustice and are often prepared to punish

perceived harmdoers even at their own expense (Bies 1987). Elangovan and Shapiro (1998) suggest that perceptions of unfairness may induce betrayal. Ring and Van de Ven (1994) maintain that co-operation is not possible without perceptions of equity and that this can be more important than relation outcomes.

Another way of approaching trust building is to focus on the behaviour and attitudes of the individuals involved. What qualities in an exchange partner are likely to inspire trust? Based on a review of trust literature, Mayer, Davis and Schoorman (1998) suggested that, apart from the trustor's propensity to trust, the most important antecedents of trust were the trustee's perceived *ability*, *benevolence* and *integrity*. Benevolence encompasses factors such as loyalty, receptivity and caring, while integrity includes consistency, fairness, reliability, openness and value congruence. All three qualities are considered to be required for trust to arise.

TRUST AND CONTROL

Different bases of trust are not necessarily complementary. There is a complex and ambiguous relation between trust and control. From a rational perspective detailed contractual specifications, close monitoring and sanctions for non-conformance should reduce feelings of vulnerability and, thus, facilitate and increase trust. However, both trust and distrust strategies tend to be reciprocated by the kind of behaviour they anticipate. Some formal mechanisms of control and performance appraisal tend to elicit shirking and work-to-rule behaviour (Sitkin and Stickel 1996; Elangovan and Shapiro 1998). The message communicated to a contract partner or an employee by close monitoring is that he or she is not trusted and that self-interested behaviour is expected. Thus, distrust manifested in close control risks to induce opportunistic strategies that, in turn, justify distrust. Furthermore, control strategies affect the person controlling. Once suspicion has been raised about another person's motives or competence, the perceiver tends to apply a more active and mindful mode of thinking (Fein 1994). As a consequence, it is more likely that bad performance will be detected. Also, a suspicious person may be too focused on monitoring the other party to engage in the spontaneous interaction and information sharing that is considered to be a main benefit of trust-based relations (Kramer, 1999). Thus,

several mechanisms contribute to distrust becoming a self-fulfilling prophecy (Kramer 1999).

However, trust as well may be self-fulfilling. Shown trust communicates that co-operation is expected and people tend to reciprocate with a behaviour that justifies trust. Das and Teng (1998) note that taking some initial risk allows the trustee to demonstrate his or her trustworthiness. Also, making non-recoverable investments signals commitment and trust, leading to escalating trust. Another mechanism reinforcing trust is that the trusting party subconsciously makes extra efforts to ensure that the trusted party succeeds, in the end justifying the original decision to trust (Hayashi, 2001).

Still, arms-length relations still dominate in many sectors, not only construction. Many strategic alliances fail because the confidence in partner co-operation is low (Das and Teng 1998). For some reason, control/conflict strategies based on deterrence are perceived as less risky than trust/co-operation strategies. It has been found that people generally tend to overemphasise the importance of extrinsic, economic incentives and underestimate the role of intrinsic motivation, based on for example social recognition and meaningful work (Miller and Ratner 1998; Nelson 1999). Also, social and organisational norms are important in shaping trust behaviour and departing from the dominant paradigm carries personal risks (Kramer, Brewer and Hanna 1996). The main question behind decisions to choose co-operative arrangements may therefore not be whether it is *rational*, but whether it is *appropriate* (Miller and Ratner 1998).

Das and Teng (1998) emphasise the role of communication in building confidence in partner co-operation. Clear and explicit goals are often considered critical for control. However, explicit goals are often difficult to formulate at the initial stages of an alliance, and there is often some goal incongruence. Das and Teng (1998) therefore point at the importance of the goal-setting process as social control mechanism in itself. Through this process, the partners may gain a better understanding of each other's preferences and situation and collective norms and values can develop.

TRUST IN CONSTRUCTION

Choice of contract and rational analysis

Why are highly specified contracts, close control and distrust common in construction? A framework that has gained much attention by construction management researchers is Williamson's (e.g. 1979) transaction cost theory, which stipulates that transaction costs arise because of the need to specify, monitor and enforce contracts when the parties' interests diverge. Transaction cost analysis of project relations in construction generally shows that the temporariness, interdependence and uncertainty of construction relations open up for opportunistic contractor strategies (Eccles 1981; Reve and Levitt 1984; Stinchcombe 1985; Winch 1989). According to transaction cost analysis the client-contractor relations are often found to entail too high transaction costs to permit market exchange at all. Thus, calculative reasoning induces clients to employ detailed specifications and close monitoring of contractor performance.

The clients interviewed often referred to the economic interests of the contractor, when justifying their distrust. A typical statement was:

After the contract is signed, we have opposed interests. It is very clear. The client wants to pay as little as possible, and the contractor wants to get paid as much as possible.

Another opinion was that as the liability period for construction projects lasts only two years, contractors have no reason to consider life cycle costs and can therefore not be trusted. The clients also considered the influence of the contractor's internal reward system and career paths on the behaviour of the contractor's employees:

I have the feeling that contractor employees are still rewarded based on how much money they bring back. As long as the site managers make money, the company doesn't care what methods they use or if the client is satisfied.

Thus, rational analyses seemed to play an important role in the interviewed clients' assessment of the situation. Consequently, changing contractual incentives to increase goal alignment was viewed as the key to co-operation by many clients.

The contract-behaviour dimension

The implication of the above discussion is that calculus-based trust is often low in construction. Another potential source of trust is interpersonal interaction during the relation, which may result in relational trust. Many clients reported that trust may be built successively in a project, if the contractor was perceived as trustworthy. However, there was also considerable dissatisfaction with the behaviour of contractors. One aspect mentioned was the contractor's claims for "extra" payments when the specifications were changed. Up to the point when the contract is signed, the contractor may be very co-operative in accommodating for changes without increasing prices. However, this may change as soon as the contract is signed:

As a client it is hard to understand that although you have a very good discussion in the beginning, suddenly, when the contract is signed, all changes cost money.

To the client, this sudden change in contractor attitude is easily interpreted as a lack of benevolence and consistency. Another aspect that is problematic is that contractors are entitled to extra payments when there are errors and omissions in the contract documents.

In practice, clients expect the contractor to oversee with minor issues:

All contractors know that the documents are not perfect, but some contractors think that they are clever ... as a client you find it very irritating.

Such claims imply criticism towards the client and the consultants, who are responsible for preparing the drawings and specifications. Therefore, contractors may be perceived as taking advantage of the client's mistakes, which is clearly not benevolent:

Everybody makes mistakes, the contractor makes mistakes and the client makes mistakes. What is most important to avoid distrust is that neither of the parties take advantage of the other's mistakes. If you don't, trust is strengthened, and if you do, distrust will arise. It doesn't matter if you have the right to do it.

Another aspect that affects perceived trustworthiness is that each contractor's chances of being awarded the contract increase if they do not disclose problems they find in the tendering documents while preparing their bid. Instead the contractor may anticipate that change orders leading to additional payments will result from the errors, and reduce their bid correspondingly. After the contract is signed, the contractor may claim both for the work and for disturbances and re-planning of construction work.

In sum, the rules of interaction set by the contracts give rise to behaviours that contradict the rules for developing relational trust. Contractors risk being perceived as disrespectful, non-responsive, deceitful and intolerant, while clients tend to adopt a suspicious attitude. The contracts encourage both parties to criticise and blame each other, rather than to listen, assume responsibility and show respect. Also, sharp differences in how contractors behave before and after a deal is signed contradict preferences for predictability and consistency underlie perceptions of trustworthiness.

To build a co-operative relationship in this kind of contractual relation, contractors probably need to be sensitive in deciding when to, for example, charge extra. A contractor who follows the formal rules too closely is not likely to be perceived as trustworthy. For the clients there are also pitfalls. Several of the clients interviewed maintained that it is important as a client to be aware that these are the rules of the game, and that it would be wrong to blame the contractors for behaving as prescribed by rules that clients themselves have set. However, most of the clients interviewed expressed strong feelings towards claims, which suggests that this aspect of the relation is difficult to handle without damaging relations.

In construction, the uniqueness and complexity assures that there will always be mistakes and oversights that may serve to justify distrust. Also, co-operative intentions are often difficult to discern from opportunistic ones, which means that co-operative behaviour may be punished by mistake. It is hard to prove that the overall outcome would have been better with a more trusting approach, especially as there is a risk for hidden problems of quality that may not show until many years later. Thus, the distrust inherent in the traditional roles is more likely to be confirmed than contradicted.

Perceptions of fairness

Perceptions of fairness are fundamental to co-operation (Ring and Van de Ven 1994). However, fairness pose considerable problems in the construction context. In studies of economic exchange, Kahneman, Knetsch and Thaler (1986) found that the parties' outcomes in buyer-seller relationships were coded as gains or losses in relation to a

reference transaction. A fair transaction implied that the buyer was entitled to the reference price and the seller to the reference profit. The seller was allowed to raise prices to protect the reference profit if, for example, wholesale prices increased, but it was perceived as unfair to raise prices to exploit increased market power. Notably, auctions were found to be perceived as unfair, except for objects of investment such as property and antiques. This means that market prices are often perceived as unfair.

This has important implications for construction contracts. Projects are unique and most often, prices are set by competitive tendering. Construction markets are characterised by strong variations in supply and demand, and prices vary considerably. In this situation, the client is likely to perceive the price in a recession as a reference price while to contractors, contracts procured in a recession are under-priced and unfair. When demand increases and prices go up, the clients' view is that contractors unfairly exploit their market power. Thus, competitive tendering combined with high variations in demand makes it hard to arrive at common perceptions of equity. A contractor procured in a recession may use this to justify more self-interested behaviour. Also, a client will also be more suspicious if the contractor is pressed, because opportunistic strategies are then expected.

CONCLUSIONS

This paper has focused on factors affecting trust and distrust in Swedish client-contractor relations. Rational theories, based on calculations of the trustee's incentives to honour trust, tend to justify a distrusting client strategy with detailed contracts and close monitoring of contractor performance. Two aspects that reinforce this tendency because they hamper the development of relational trust were identified:

- Traditional, highly specified construction contracts as well as procurement practices give rise to attitudes and behaviour that contradict common-sense perceptions of how a trustworthy person acts. Contractors adopt a critical, intolerant attitude to the client and the consultants, and clients become suspicious of contractors. Also, openness and consistency are discouraged.
- Equity is often considered to be a basic requirement for co-operative relations. However, competitive tendering on unique projects combined with high variations in

demand cause problems in arriving at a common perception of a fair price. Either party is likely to feel badly treated, which induces both opportunism and fear of retaliation. Distrust and control risk to be counter-productive and induce opportunism. Therefore, it is likely that more trusting strategies would enhance performance and that the risks of such strategies are over-estimated. However, there is an important social aspect. Client representatives are monitored by their principals and colleagues, and personal risk avoidance may keep them from using other procurement options than the established ones. That contractors need detailed specifications and that competition is crucial for contractor performance seemed to be a strong belief among clients, and to depart from this norm would probably entail criticism. Also, if rational assessments predict distrust, suspicion is latent in the relationship and trust based on interaction will be fragile. To make relations more stable, formal interests therefore have to be shaped so that calculus-based trust may be justified to some degree. In construction, the most common way of doing this is incentive contracts and open books. Such contracts may also breed trust in themselves, because they are seen as co-operative. Furthermore, the openness as well as the gainshare/painshare aspect may reduce perceptions of unfairness. However, other measures apart from the formal contracts are required to ensure constructive co-operation and increase contractor motivation and commitment. Obtrusive forms of control such as detailed specifications and monitoring should be avoided. Instead, clients need to engage strategically in project communication to build trust, listen to contractor opinions and ensure constructive conflict likely to improve performance. A process where goals are set jointly can be as important for project control as the goals themselves.

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