European Management Journal 33 (2015) 431–437

Contents lists available at ScienceDirect

European Management Journal

journal homepage: www.elsevier.com/locate/emj

The development, escalation and collapse of system trust: From the financial crisis to society at large

Frens Kroeger

Centre for Trust, Peace and Social Relations, Coventry University, United Kingdom

ARTICLE INFO

Article history:
Received 2 March 2015
Received in revised form
18 July 2015
Accepted 18 August 2015
Available online 28 September 2015

Keywords:
System trust
Trust in expert systems
Confidence
Trust and modernity
Trust crises
Financial crises

ABSTRACT

This theoretical outline sketches the development, escalation and collapse of trust in expert systems, using the recent financial crisis as an example, but aiming at the description of broader underlying mechanisms. After reviewing the literature on the genesis of system trust, it identifies spirals of system trust that escalate both "vertically" (actors placing too much trust in the system) and "horizontally" (wider and wider circles of actors placing trust in the system). Both the apparent stability and the potential for collapse inherent in these spirals results from the fact that system trust is typically more distant, and consequently lacks some of the safeguards present in interpersonal trust. Ironically, thus, attempts to eliminate the influence of trust by introducing impersonal rule systems may increase rather than reduce the risk posed to systemic stability.

1. Introduction

Over the past two decades, trust has evolved into a central concern in much of organization theory. This is not least because trust has become problematic across a wide range of societal sectors. Media coverage and public debate about the loss of trust in systems as different as food production and regulation, the activities and control of intelligence agencies, or "yet another once-trusted British institution: the police" (The Guardian, 2013a,b,c, 2014a,b) chime with ever-new academic findings of declining trust in government, business, health systems and regulatory regimes (Armstrong, 2012; Edelman Trust Barometer, 2013, 2015; Stevenson & Wolfers, 2011; Walls, Pidgeon, Weyman, & Horlick-Jones, 2004). Possibly the most glaring of these systemic trust failures was implicated in the emergence of the 2008 financial crisis (Bachmann & Hanappi-Egger, 2014; Gillespie & Hurley, 2013).

However, conceptual underpinnings for major trust failures of this kind have been slow to develop (Gillespie, Hurley, Dietz, & Bachmann, 2012; Möllering, 2013). More generally, the trust in economic and social systems has remained strongly underresearched.

The present paper contributes to addressing this important gap. In the form of a theoretical outline, it explores the question how trust in expert systems can escalate and collapse. Although it focuses on these dynamics in the context of the financial system, it is interested not in a historical account of the recent crisis (for this refer, e.g., Shiller, 2008; Reinhart & Rogoff, 2008), but in the more generalizable mechanisms involved in the escalation and collapse of such trust.

Why keep the model this general? First, note that the present paper represents no more than a brief (and accordingly, rough) outline, seeing that first conceptual steps are still wanting before empirical research can build on and examine the validity of the sequence hypothesized here. Second, it is hoped that the usefulness of this analysis will not be restricted to the financial sector, but may be instructive in regard to other sectors and functional spheres of society. Whether they are eventually found to exhibit highly similar or vastly different dynamics, the observations presented here can serve to establish a "null hypothesis" against which to chart the processes and principles of other expert systems.

I will return to both of these points in the concluding section. Before that, the following sections will define central terms (Section 2.1) and briefly review the literature on the development of system trust (2.2); and then chart the different steps of the sequence put forward in regard to system trust: development towards predominance (Section 3.1), expansion (3.2), escalation (3.3), and stability as well as potential collapse (3.4).

E-mail addresses: frens.kroeger@coventry.ac.uk, fk247@cam.ac.uk.

http://dx.doi.org/10.1016/j.emj.2015.08.001
0263-2373/

Within this sequence I will discuss, and identify as fallacious, two assumptions or "illusions" regarding the role of trust. The first is the idea that trust does not matter any more in a given sphere such as the financial system. The second, that the respective system is unquestionably stable because this is widely taken for granted. We could call the first the illusion of "the end of trust", and the second the illusion of stability. A common theme between them is an inherent underestimation of, and a consequent lack of attention to, trust and its significance to the system.

2. Interpersonal and system trust

2.1. Definitions

First, the central concepts of interpersonal and system trust require brief definition. Particularly for the sake of communicability and connectivity to other research on trust, this contribution adopts the definition of trust put forward by Mayer, Davis, and Schoorman (1995) and since adopted by trust researchers across a wide variety of disciplines (see Schoorman, Mayer, & Davis, 2007). Mayer and colleagues define (interpersonal) trust as

> "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 or control that other party" (1995: 712).

While the argument presented would be compatible with a wide variety of slightly differing definitions of trust, note in particular the central elements of voluntary vulnerability (Bigley & Pearce, 1998), relating to the future behaviour of others, which is fundamentally unpredictable due to their freedom of decision (Luhmann, 1979).

These elements can apply both to individual trustees and to social or institutional systems (what Giddens (1990) called "expert systems"). Even though here, too, trust needs to relate to the human behaviour which instantiates and reproduces the respective system, it ultimately refers to the systemic principles which guide that behaviour (also see Sydow, 1998; Bachmann, 1998). (To elaborate on one of Giddens's examples (1990: 28), even though passengers never meet the engineers who construct, service and monitor the planes which they fly in, they have reasons to trust that the respective expert systems generate predictability and safety.)

Thus, just as in Luhmann's classical definition, in system trust the trustor "basically assumes that a system is functioning and places his trust in that function, not in people" (1979: 50).

2.2. The genesis of system trust

While interpersonal trust building has been studied in considerable depth (for an overview, see Lewicki, Tomlinson, & Gillespie, 2006), the genesis of system trust has remained strongly underresearched. Luhmann (1979), using the example of the monetary system and building on Simmel (1990), merely alluded to repeated confirmatory experiences in using money, referring chiefly to the fact that serious disappointments or breakdowns need to be *absent* in daily use. System trust relies on a high level of taken-forgrantedness (Luhmann, 1988).

The comparatively few relevant contributions since can be grouped into two distinct categories. The majority of contributions examines (1) the facilitation of system trust through mechanisms which increase systemic predictability; these mechanisms, in turn, can be grouped into (a) social norms; (b) the punishment of malfeasance; and (c) the promotion of relevant communication. A second, separate theoretical strand is composed of (2) conceptions of a "scaling up" of trust from the interpersonal to the institutional and systemic levels.

A number of authors have focused on the supportive capability of *social norms* in making the behaviour of systems and their representatives more predictable to the outsider (see for instance Braithwaite & Levi, 1998: chap. 2–3). Of particular importance here are norms relating to the fairness of social and economic exchanges, reciprocity, and mutuality (Cook, Levi, & Hardin, 2009: chap. 1–4). Wicks, Moriarty, and Harris (2014) add that normatively controlled power equilibria are helpful in preserving fairness and therefore making the trusted entity more trustworthy.

This ties into increased predictability through *punishment of malfeasance* and the discouragement of untrustworthy behaviours. Especially Hardin (2002) has argued that institutional design has to encapsulate the self-interest of the officials administrating the larger systems. Legal and compliance mechanisms can be institutionalized as trust safeguards (Wicks et al., 2014; also see Sztompka, 1999). This includes specialized agencies for monitoring and sanctioning breaches of trust, such as regulators (Pixley, 2004).

A number of contributions discuss the structured *promotion of communication* about trust-relevant issues. Some actors, such as credit-rating organizations and financial news organizations (Pixley, 2004), specialize in the evaluation and dissemination of trust-relevant information. Other communication, while less formalized, can be equally consequential. Braithwaite (1998) discusses "communities of dialogue", i.e., institutionalized debate about relevant systems in political and administrative circles. These and similar debates can be facilitated by "network brokers" who keep communication between relevant parties going (Barr, Ensminger, & Johnson, 2009; McEvily & Zaheer, 2004). Finally, Papakostas (2012) discusses a variety of mechanisms which institutionalize "structured skepticism", particularly in the form of rules enforced by independent and impartial bureaucracies.

In comparison, research has only begun to investigate the "*scaling up*" *of trust across levels*, i.e., its translation from the interpersonal to the institutional and to the system level (Farrell, 2009; Kroeger, 2012). One of the most promising concepts in this field is the "facework" of individuals who represent the trustworthiness of institutions and expert systems (Giddens, 1990; Kroeger, forthcoming), drawing attention to dynamics of generalization from the interpersonal to the systemic level. Equally, it is worth studying how individuals can build helpful institutions (Lyon & Porter, 2010). Calls for studying meso-level phenomena related to system trust (e.g., Cook et al., 2009: chap. 5–7) are a logical consequence of these developments.

The present contribution will suggest an additional mechanism that can lead to the rise, but also to the fall of system trust, based on its reflexive nature and the resulting group dynamics.

Note that in all of the above renditions, system trust is significantly more *distant* than interpersonal trust (also see Harris, Moriarty, & Wicks, 2014: chapters 3–4). The trustor's experiences clearly lack the immediacy of interpersonal trust building (Khodyakov, 2007), where the object of trust is easier to observe, and often responds directly to the trustor's actions, signalling (un) trustworthiness in a much more immediate and continuous fashion.

3. System trust: growth, escalation, collapse

3.1. From interpersonal to system trust

Giddens (1990) connects interpersonal and system trust in the context of a broad historical or "evolutionary" progression. His well-known argument about the development towards (late) modernity shows how virtually all sectors of contemporary