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Research Paper

Trust and formal contracts: complements or substitutes? A study of tourism collaboration in Poland[☆]Katarzyna Czernek^{a,*}, Wojciech Czakon^c, Paweł Marszałek^b^a Management Theory Department, University of Economics in Katowice, 1 Maja 50, 40-287 Katowice, Poland^b Department of Money and Banking, Poznań University of Economics and Business, Al. Niepodległości 10, 61-875 Poznań, Poland^c Faculty of Management and Social Communication, Jagiellonian University, Łojasiewicza 4, 30-348 Kraków, Poland

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ABSTRACT

The aim of the paper is to explore whether trust and formal contracts should be treated only as substitutes, or – a less popular approach in the literature – as complementary bases for dyadic and network cooperation in the tourism sector. Sixteen in-depth interviews were conducted with tourist entrepreneurs running their businesses in different parts of Poland. Nine different circumstances were identified in which cooperation was based either on trust or formal contracts, or on both. The results suggest that these two bases of cooperation do not have to be treated as substitutes, as each of them has different functions and different origins. Moreover, written agreements are not a result of a lack of trust in a partner, but they do sometimes stem from other factors (e.g. accounting requirements in a company).

1. Introduction

Nowadays, cooperation in the tourism sector is one of the most important conditions of competitiveness and a firm's survival. To establish and develop cooperation, actors sign formal contracts or rely on trust, manifested by oral agreements (Klein Woolthuis, Hillebrand, & Nootboom, 2005; Gulati & Nickerson, 2008; Poppo & Zenger, 2002; Puranam & Vanneste, 2009). Usually, formal contracts and trust are perceived in the literature as substitutes. Some authors even claim that formal contracts hinder trust building. However, other scholars take the opposite stance. For instance Poppo and Zenger (2002) claim that governance mechanisms can complement each other, and can thus be perceived as complementary bases of cooperation. In Poppo and Zenger (2002) work, trust is analyzed as a part of so-called relational governance, together with relational norms such as: flexibility, information sharing and commitment. Using data on outsourcing relationships in information services, Poppo and Zenger (2002) empirically established that relational governance and formal contracts operate as complements, not substitutes.

In tourism literature, trust is relatively rarely analyzed regarding entrepreneurs. Authors focus mainly on local community trust towards local authorities or institutions (Nunkoo & Ramkissoon, 2011a, 2011b; Nunkoo, 2015; Nunkoo, Ramkissoon, & Gursoy, 2012) and on client trust towards providers (Akamavi, Mohamed, Pellmann, & Xu, 2015;

Fam, Foscht, & Collins, 2004; Han & Hyun, 2015; Sparks & Browning, 2011; Wan, Law, Hung, & Guillet, 2014). Moreover, there is a lack of research where researchers try to assess if, and in which situations, these two different bases of cooperation are treated by tourist entrepreneurs as substitutes or as complementary. A notable exception is a study where Beritelli (2011) analyzes two possible approaches to tourism cooperation, i.e. a formal approach based on formal contracts and written rules, and informal ones, based on social relations and trust. He wondered which of the two allows for the establishment of cooperation in tourist destinations. His research showed that interpersonal relations based on trust dominated over institutional solutions. Moreover, he claimed that in tourism destinations, the variables that he used, connected to information and communication, were not linked with the formal community, but rather with informal relations between partners. On that basis, Beritelli (2011) claimed that in tourist destinations, actors cooperate despite formal, professional and political bonds, and tend to use mutual trust and understanding stimulated by effective and frequent communication. In his research, these two approaches – formal relations leading to formal contracts and social relations based on trust – were treated as substitutes, the latter proving to be crucial and sufficient for the establishment of cooperation in a tourist destination. However, the author stressed that it may be useful to first choose people for cooperation, and later the institutions which

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they represent. This shows that both sources of contact – formal and informal – can be useful at different stages of cooperation. This allows them to be thought of as complementary. However, neither [Beritelli \(2011\)](#), nor other authors showed in which situations, when it comes to establishing cooperation in tourism destinations, oral agreements based on trust and formal contracts can be treated as substitutes or complementary to each other. This paper will contribute towards filling this gap.

The aim of the paper is to ascertain whether trust and formal contracts should be treated only as substitutes, or – a less popular approach in the literature – as complementary bases of dyadic and network cooperation in the tourism sector. Sixteen in-depth interviews were conducted with tourist entrepreneurs running their activity in different parts of Poland. They were asked about factors that determine how they establish cooperation with tourist enterprises – whether they base this cooperation on trust (oral agreements) or formal contracts. The results suggest that trust and formal contracts were often treated as complementary to each other, not necessarily as substitutes. This finding agrees with the stance that both forms can supplement each other and that writing a formal agreement does not necessarily have to negatively influence relations between partners, especially trust.

This paper consists of six parts. The first part is the introduction. In the second the theoretical background is presented. Mentioned here the advantages and disadvantages of using trust and formal contracts. This allows us to present the arguments of authors treating trust and formal contracts as complementary. In the third part, the research methodology is outlined, and in the fourth, the research results are presented. The research results are presented in the fifth part. The last part presents the conclusion.

2. Literature review

2.1. Trust and formal contracts in the literature

Trust, as an important factor in cooperation between two or more partners (dyads or networks), is more and more often analyzed in general management ([Fulmer & Gelfand, 2012](#); [Granovetter, 1985](#); [Gulati & Nickerson, 2008](#); [Gulati, 1995](#); [Hoffmann, Neumann, & Speckbacher, 2010](#); [Palay, 1984](#); [Uzzi, 1997](#)) and tourism literature ([de Araujo & Bramwell, 2002](#); [Bramwell & Lane, 1999](#); [Czernek, 2013](#); [Grangsjö, 2006](#); [Jamal & Getz, 1999](#); [Kale & Singh, 2009](#); [Nunkoo & Gursoy, 2016](#); [Nunkoo & Ramkissoon, 2011a](#); [Roberts & Simpson, 2000](#); [Selin & Chavez, 1995](#); [Wang & Krakover, 2008](#); [Wang, 2008](#); [Zemła, 2014](#)). Trust has become even more important in micro- and macro-economic analyses due to the assumption of the forward-looking behavior of agents and the increasing role (on both micro and macro levels) of expectations and commitments in economic activity ([Goodfriend & King, 1997](#); [Morgan & Hunt, 1994](#); [Sargent, 1996](#); [Woodford, 1999](#)).

Trust can be understood as a ‘psychological state comprising the intention to accept vulnerability based upon positive expectations of the intentions or behavior of another’ ([Rousseau, Sitkin, Burt, & Camerer, 1998](#), p. 395). On the other hand, formal contracts represent promises or obligations to perform particular actions in the future ([Macneil, 1977](#)). They are concluded in writing and they specify all the duties that all sides have to discharge.

In general, the literature perceives trust and formal contracts as substitutes: using one reduces the necessity of using the other ([Dyer & Chu, 2003](#); [Dyer & Singh, 1998](#); [Granovetter, 1985](#); [Larson, 1992](#); [Ring & Van de Ven, 2006](#); [Uzzi, 1997](#); [Puranam & Vanneste, 2009](#); [Strätling, Wijbenga, & Dietz, 2012](#)). Trust reduces transaction costs by ‘replacing contracts with handshakes’ ([Adler, 2001](#)). Some authors even claim that formal contracts can call into question the existence of trust and hamper its development ([Bernheim & Whinston, 1998](#); [Fehr & Gächter, 2000](#); [Macaulay, 1963](#)). [Macaulay \(1963, p. 22\)](#) claims that trust brings trust and companies discourage the use of an elaborate contract because it ‘indicates a lack of trust and blunts the

demands of friendship, turning a cooperative venture into an antagonistic horse-trade’. He claims that using only formal contracts can generate opportunistic behavior when there is no possibility to specify all agreement details in the contract, which a partner can use in the future. [Domhoff \(1971\)](#) and [Useem \(1979\)](#) further claim that taking partners to court and threatening partners with lawyers hampers relations. They claim that solving conflicts in this way is very rare. When trust exists, formal contracts between partners are at best an unnecessary expense, and in the worst case they can bring the opposite effects to those planned. Similar conclusions were formulated by other authors, for example, [Fehr and Gächter \(2000\)](#); [Bernheim and Whinston \(1998\)](#) and [Ghoshal and Moran \(1996\)](#).

Treating trust and formal contracts as substitutes is a result of the advantages and disadvantages of both of these cooperation governance mechanisms. Scholars stress many different advantages of trust ([Alvarez, Barney, & Bosse, 2003](#); [Palay, 1984](#); [Zaheer, McEvily, & Perrone, 1998](#)). For example, according to [Granovetter \(1985\)](#), close relationships and trust towards a partner make his activities more predictable and allow fears accompanying relations between unfamiliar people to be allayed. According to [Granovetter](#), trust can be an even more important source of honesty than general morality or institutions, including formal agreements. These, according to [Granovetter](#), are substitutes of trust rather than its elements. Moreover, according to [Granovetter \(1985\)](#), trust allows us to obtain information from known, reputed partners. Such information is more complex and valuable than information from unfamiliar sources and people we do not trust. In other words, trust allows for the reduction of transaction costs ([Williamson, 1985, 1991](#)) connected to finding a partner and developing cooperation ([Bromiley & Harris, 2006](#); [Dyer & Chu, 2003](#); [Dyer & Singh, 1998](#); [Dyer, 1997](#); [Granovetter, 1985](#); [Gulati, 1995](#)). Trust is especially needed when there is an increase in the risk of opportunistic behavior stemming from high specificity of resources, problems with monitoring partners, and market uncertainty. When trust exists, even in such situations, partners decide to behave properly because they know that in the long term, the costs of investment in such cooperation will be returned ([Poppo & Zenger, 2002](#)). Moreover, the expectation of long-term cooperation reduces the need to monitor a partner in the short term ([Poppo & Zenger, 2002](#)). In tourism literature, such advantages of trust are stressed, among others, by [Czernek and Czakon \(2016\)](#), [Czakon and Czernek \(2016\)](#); [Timothy \(1998\)](#); [Caffyn \(2000\)](#); [Roberts and Simpson \(2000\)](#). For example, [Ingram and Roberts \(2000\)](#), who analyzed hotels in Sydney, claimed that friendship and trust between the managers of the hotels positively influenced their behavior and helped them to fight against price attacks.

Trust also has some disadvantages. First of all, it often involves considerable costs in terms of time and resource allocation ([Larson, 1992](#)). Secondly, it can hinder innovative development as it may restrict companies from gaining new information and new opportunities ([Gargiulo & Benassi, 2000](#); [Uzzi, 1997](#)). Thirdly, it makes partners more vulnerable to opportunistic behavior by the other party, and the subsequent negative consequences. Some disadvantages of trust in the tourism sector are stressed by [Caffyn \(2000\)](#); [Czernek \(2017\)](#); [Czernek and Czakon \(2016\)](#). [Parker \(2000\)](#) also stressed the negative consequences of trust, claiming that too low a level of formality in a partnership structure (ad hoc meetings, the lack of formalized task division and responsibility), and too close relationships between partners can lead to lower performance. Some negative aspects of trust in the tourism sector were also stressed by [Jack and Anderson \(2002\)](#) in research into the effects of strong ties on the entrepreneurial process.

Also, formal contracts have many advantages and disadvantages. Regarding the positive side of formal contracts, firstly, specified, clear rules and expectations in cooperation provide partners with a point of reference in their agreement. This makes it easier for them to cooperate and fulfil a partner's expectations, and to be sure that their own activities are in line with the agreement ([Heide, 1994](#)). Secondly, formal, specified contracts allow an individualized approach to a client and provide the opportunity to adjust an offer to his or her needs

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