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Control vs. Trust
Mastering a different management approach

By John Hagel and John Seely Brown

Control vs. Trust

Business confronts intensifying competition and growing uncertainty. Such conditions naturally favor the control mindset: managers batten down the hatches, bring all resources required for business success under their direct control, and rely on no one else. Micro-manage all activities. Keep everything by the book and don't tolerate any exceptions. Squeeze the maximum out of every resource and every person.

But there's a problem: Businesses aren't self-sufficient. If anything, they are becoming increasingly interdependent. Lean supply chains require significant collaboration between suppliers and customers. Adding value around products and services often demands greater collaboration between vendors and a complex array of channel partners. The quest for more operating cost efficiency traditionally leads to business process outsourcing. Getting costs out of products calls for more collaboration between a company's product design staff, component suppliers and outsourced manufacturers.

Not only is collaboration increasing, so is the need for flexibility. We just don't know any more where markets are headed. Customers are increasingly ready and able to move to the best offer. Competitors are entering markets from unexpected directions — both in terms of geography and industry. Technology innovation continues to deliver radically new capabilities. We thought for a while that business cycles with their wrenching shifts in demand patterns were a thing of the past. As if all that weren't bad enough, then we had September 11 and the growing prospect of disruptive terrorist attacks.

The control mindset cannot cope with this. Control requires the ability to dictate all activities. Control seeks to preserve stability and predictability. The forces at work in business today will make control-based management approaches less and less effective. Even information technology that was once the ally of, and shaped by, the control mindset is moving along a different path. New IT architectures — in particular, distributed service architectures shaped by Web services technology — are creating much more flexible platforms for business activities.

Managers need to return to basic principles to discover a different approach to management — one that can fully exploit the economic potential of collaboration and flexibility. Ultimately, managers want to be assured of two things: that parties will deliver end products as promised and that parties will not abuse privileged access to corporate resources and relationships to the detriment of the corporate owner. Control is one, increasingly less effective, way of assuring these two things. Trust offers a different management approach designed to assure the same thing.

Trust focuses on establishing shared expectations regarding end products, rather than specifying in detail the actions that must be performed to deliver the end products. Trust-based management then concentrates on designing appropriate incentive structures and reducing barriers to motivate appropriate action. It rests upon the recognition that performance generally falls short of expectation for one of two reasons — either the parties lack the "will" (i.e., they are not sufficiently motivated) or they lack the "skill" (i.e., they don't have the capability to act). Of course, there is a third reason that performance falls short — unanticipated events like terrorist attacks, earthquakes, or accidents can wreak havoc on the best of intentions and capabilities. As we will discuss, trust-based management approaches can also help to insulate businesses from these unanticipated events better than more conventional control-based approaches.

By focusing on end products, rather than the detailed activities required to deliver the end products, the trust-based approach creates the basis for a very different management model. Rather than supporting tightly coupled business activities, trust-based approaches encourage much more loosely coupled business activities. Participants can be added and removed much more easily. More specialization can occur because loosely coupled relationships can accommodate more participants. Rapid innovation can occur in all areas of business activity because the loose coupling allows participants to change the way they operate without disrupting the operations of others.

This article explores the key elements of a trust-based management approach. It will make the case that trust is a much more versatile and powerful way than control to deliver business results in an increasingly interdependent and uncertain world. But it will also suggest that trust approaches require management to develop a very different set of skills. Since trust approaches can only be implemented gradually, management has an opportunity to learn and acquire these skills along the way. The key at the outset is to shift from a control mindset to a trust mindset and to understand the kinds of skills that will be required to succeed in moving to a very different management approach.

The components of truust

Trust-based management does not start with the assumption that all parties can or should be trusted. Quite the opposite. This approach begins with the assumption that trust must be actively built and maintained. This becomes one of the key challenges for management.

What is required to build and maintain trust? Four broad elements must be addressed:

- Expectations must be shared by all parties
- All parties must be sufficiently motivated to deliver against expectations
- All parties must have the requisite capabilities to deliver against expectations
- Notification mechanisms must be in place to provide early warning of any potential shortfalls in performance or abuse of privileged access

Shared expectations — creating shared understanding

Trust ultimately depends upon a clear understanding of expectations regarding end products. Under a control approach, managers can intervene at any moment to clarify their expectations. In contrast, trust approaches require reasonable investment at the outset to ensure that expectations are appropriately set so that the various parties can proceed on their own initiative. Of course, over time, as the various parties get to know each other and understand the expectations of all involved, less effort is required to ensure that this element is in place.

In the early stages of building trust relationships, managers need to ensure that all parties understand each other well enough to be able to establish shared expectations regarding end products. If one manager says that the product needs to be "blue," do the other parties understand how tight the color specification really is? If it is tight, do they understand precisely what shade of blue must be delivered? Too often, trust is eroded because the various parties attach different meanings to specifications of end products.

In setting shared expectations, managers need to resist the temptation to over-specify the end products or to specify actions required to create the end products. One of the greatest strengths of a trust approach is that it creates flexibility for the various parties to innovate to come up with more efficient and effective ways to create the end product. Over-specification reduces degrees of freedom and thereby limits flexibility.

This is particularly counter-productive when the specifications start to intrude upon the activities required to deliver the end product. For example, it may be tempting for a manager to specify that a supplier must produce the color blue by sourcing a dye from a particular supplier and using the dye in a prescribed procedure. This usually suggests that the control approach is creeping back in. Managers need to continually check themselves to ensure that the end-product specifications are the minimal ones needed to support the business objectives.

Incentive structures — creating the will to perform

The best way to ensure that parties will perform as expected is to create the right incentive structure to motivate appropriate behaviors. This is challenging enough within a single organization. It becomes even more challenging as the parties involved span multiple enterprises. Designing the right incentive structures requires a deep understanding of the economic drivers and aspirations of each of the participants. Given the great diversity of participants, it is rarely possible to implement a uniform incentive structure. Incentives need to be tailored to meet the unique needs of each category of participant.

The will to perform can be shaped by both positive incentives (rewards) and negative incentives (penalties). Rewards generally provide a more powerful and enduring form of motivation, although penalties certainly play a useful role in motivating behavior, especially on the margin when unanticipated events make execution more challenging than expected.

Managers often assume that rewards must involve near-term cash benefits. Certainly, these are an important component of reward systems. Ultimately, of course, all forms of rewards for businesses must somehow be translated into cash flows, whether near-term or long-term. Having said this, most managers tend to over-emphasize cash benefits in designing reward systems and under-emphasize two other forms of rewards.

Structured appropriately, knowledge-based rewards can generate a powerful increasing-returns dynamic.

One of the problems with near-term cash benefits is that they tend to create friction in relationships. In most business contexts, the near-term cash pool available for distribution among participants is relatively fixed. If one party receives more cash benefits, then others must do with less. A zero-sum game is established.

Two other rewards avoid this outcome by creating much more of a win/win relationship. First, any business relationship generates information as a by product. The information may be about the activities performed — for example, performance data that can be very helpful in benchmarking activities and identifying gaps in performance. Alternatively, the information may be about customers — for example, information about purchase patterns can be enormously valuable in structuring future marketing and sales programs and redesigning products to make them even more appealing. Often, managers spend so much time focused on allocating near-term cash benefits, that they neglect to assess what kind of information might be generated and who has rights to access this information. Yet, this information has significant economic value and can shape long-term business performance. Providing access to this information on an ongoing basis can often represent a powerful reward to motivate action.

Another reward even more frequently ignored involves the opportunity to accelerate knowledge building. We are all familiar with the pronouncements that we are moving into a knowledge economy where knowledge is the key competitive access. Yet, when we structure reward systems, we rarely focus explicitly on the important opportunity to accelerate knowledge building. This can in fact be the most powerful reward of all, since greater knowledge — whether in the form of better understanding how to design products, how to produce and deliver products, or how to build stronger relationships with customers — creates significant option value for the enterprise. Enterprises can use this knowledge not only to cut cost but also to drive new forms of revenue growth.

Rather than simply deciding how to allocate a fixed set of cash benefits, participants in business relationships can now focus on how to generate even more economic value through enhanced knowledge. Structured appropriately, knowledge-based rewards can generate a powerful increasing-returns dynamic. In reward systems driven by cash benefits, new participants often create a proportional dilution of economic rewards for everyone else. In knowledge-based reward systems in contrast, new participants can often create proportionately more economic value for the other participants by creating even more knowledge-building opportunities.

Knowledge-based reward systems also tend to foster longer-term relationships. If participants believe they can gain significant new knowledge over time in a business relationship, they are much more inclined to take a long-term view of the relationship. Their focus shifts from the individual transaction, where they may even be prepared to endure an economic loss in return for the ability to participate in longer-term knowledge-building opportunities.

Rewards are the primary driver of business activity, but penalties can also play an important role in building trust. In trust-based approaches, business participants tend to be much more loosely coupled, bound together by broad expectations about end products. With the right rewards in place, participants can be more confident that these expectations will be met. Recall, though, that the other expectation is that participants will not abuse privileged access to resources or relationships. If the rewards are sufficiently powerful in the long term (as in knowledge-based rewards), this in itself can act as a significant deterrent to abuse. When coupled with appropriate economic penalties that overwhelm any potential economic gain from abuse, participants can gain more reassurance that their trust will not be misplaced.

Organizational capability — ensuring the skill to perform

Incentive structures are a critical foundation for trust-based management approaches. Given the right incentives, participants will be strongly motivated to build and strengthen whatever capability is required to deliver against expectations. Having said that, managers must also focus on assessing in a rigorous and objective manner the relative capabilities of the various parties to deliver. This is key to the process of setting realistic expectations at the outset. If the gap between required capability and actual capability is too great, no amount of reward can bridge that gap, especially in the near term.

Capability audits and performance histories can provide valuable evidence of capability and, just as importantly, highlight gaps in capability. In implementing trust-based management approaches, executives may often decide to address capability gaps by adding more specialized participants that can complement the original participants. Control-based approaches tend to resist adding more participants to a business relationship because of the significant management complexity overhead. By adopting a more loosely coupled approach focused on end products, trust-based approaches can more readily accommodate additional participants.

The challenge of unanticipated events

Of course, even with the most compelling will and extraordinary skill, unanticipated events can, and frequently do, disrupt business activities. In some cases, these may be acts of nature, as in the case of hurricanes or earthquakes. In other cases, these may be malicious acts of terrorists, hackers, or common criminals. Surely, trust-based approaches are vulnerable to such disruptions.

Everyone is vulnerable to such disruptions at some level. The key question is a relative one: Are trust-based approaches more or less vulnerable than control-based approaches? In this context, trust-based approaches have some significant advantages relative to control-based approaches — they are likely to reduce vulnerability, while never fully eliminating it.

Because of the loose coupling fostered by trust-based approaches among business participants, the impact of unanticipated events can be more effectively contained and recovery can generally occur faster than for more hard-wired business activities. In loosely coupled relationships, the impact of an attack on one participant is often dampened for other participants. In part, this is simply because of the design of the relationship. Rather than tightly linked activities where a disruption in one activity ripples inexorably through all the other activities, the activities in loosely coupled relationships occur much more independently of each other, connected only by end products delivered by one participant to the next.

This loosely coupled design thus facilitates a number of measures that can reduce vulnerability to unanticipated event. For example, participants in loosely coupled relationships can be much more geographically dispersed. Since managers do not need to be micro-managing activities, participants can be far removed. For this reason, unless the unanticipated event is truly global in scope, geographically dispersed operations can absorb the impact much more readily.

Similarly, loosely coupled relationships can accommodate far more participants than tightly coupled relationships. As a result, managers can work with multiple participants having similar capabilities. If one participant is hit, other participants can be brought in to fill the gap. Redundancy becomes a key measure to reduce vulnerability.

Because more participants can be accommodated, managers can draw on much more specialized capabilities. These specialized capabilities can be useful both in the anticipation and in the recovery from potentially damaging events. This is especially true in the case of malicious acts. Control-based managers must build their own security capabilities internally to reduce dependence on others. Inevitably, except perhaps for the largest enterprises, these security capabilities lack the scale necessary to be world-class. In trust-based approaches, managers can draw upon specialized security firms that have deep expertise and very broad experience in anticipating and responding to potential security issues. This capability is far more likely to offer greater protection against security breaches.

Finally, companies in loosely coupled relationships can protect themselves against potentially damaging events by resorting to safety nets in the form of performance bonds and insurance policies. Of course, these options are also available to companies that operate with a much more control-based approach. Nevertheless, greater security capability could be mobilized and the potential damage has the potential to be more readily contained in loosely coupled relationships.

One key to containing the potential damage from unanticipated events is a robust event notification system that can quickly get the word out to all affected participants regarding potential jeopardy in key performance milestones across the relationship. These event notification systems need to be selective — they need to discriminate between events that have the potential to disrupt the activities of other participants versus simply causing additional challenges for the affected participant. Otherwise, the control-based approach begins to creep in and management rapidly becomes overwhelmed with information overload, losing the ability to differentiate between events requiring intervention and minor perturbations in business as usual. Achieving the right selectivity requires a deep understanding of the activities involved and their economic impact.

Changes in management capabilities

Moving from a control-based approach to a trust-based approach requires a significant set of capabilities for managers. It begins with a shift in mind-set: if management does not buy into the assumptions that lead to the belief that a trust based approach is both necessary and feasible, management will not attach importance to the capabilities required to successfully implement the trust based approach. Four broad capabilities must be developed in order for managers to successfully make the transition to this new management approach.

Relationship management

Executives must become much more adept at structuring and managing relationships that extend across enterprises. The track record today for partnerships and alliances in general is dismal — more than two-thirds of all such relationships fail to generate economic value. The trust-based relationships discussed above are much more firmly grounded in the core business processes of the enterprise than most partnerships and alliances. At one level, they offer the potential for more economic value creation. But, if mismanaged, they can also create the potential for significant value destruction. Understanding the economics of each participant and tailoring the appropriate incentive structures to mobilize necessary resources becomes critical to creating economic value. Few managers today have a detailed understanding of the economics of other enterprises or much experience in structuring incentive systems across enterprises.

Persuasion skills

Most managers have reasonable persuasion skills and experience within their own enterprise. However, most heavily rely on command and control mechanisms to reinforce their persuasion efforts. These mechanisms are far less readily available in trust-based approaches. Persuasion becomes central to achieving impact. Once again, the challenge magnifies as the scope of persuasion expands across multiple enterprises, each driven by different management cultures and styles. Often, the manager must wrestle with how to build shared meaning as a prerequisite to persuasion.

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Strategist and entrepreneur

Building trust-based relationships requires the ability to move comfortably between very long-term strategic issues and very near-term operational and organizational issues. Not many operational managers are comfortable as strategists. They are often even less comfortable as entrepreneurs, especially if they have spent their entire career in large, slow-growth enterprises. Yet, in building trust-based relationships across multiple enterprises, these managers must now think much more as the owner of an independent business unit than as the administrator of a cost center within a large enterprise.

Knowledge brokers

If knowledge building is the key to creating compelling and long-term incentive structures, managers must become much more skilled in understanding how knowledge can be built, not just across functional boundaries, but also across enterprise boundaries. Creating the conditions for knowledge building to occur requires a specialized skill set. Developing and implementing the measurement systems to determine whether progress is being made and expectations met on this critical dimension is even more challenging.

Building trust incrementally

Trust does not emerge quickly. Ideally, it is built upon a foundation of lengthy shared experience where all parties develop more confidence in the will and skill of the others. In a rapidly changing business world, managers often do not have the luxury of that lengthy shared experience — they must find ways to accelerate the building of trust while honoring the inherent lead times involved.

The shift from control to trust should be approached pragmatically and with caution — it most certainly will not be a rapid cutover. Nevertheless, there are ways to accelerate the building of trust. The most powerful technique involves a sequence of carefully constructed value exchanges that are designed to build capability and confidence in a very different way of doing business. In each round of value exchange, one participant offers something of value to another participant in exchange for something of value in return.

The trajectory of these value exchanges can evolve along two different dimensions. In one dimension, the early rounds focus on activities of relatively limited value in order to manage the risk that the other party might not perform as expected. Over time, the value of the activities involved increases as more experience accumulates, indicating that the participants can trust each other.

Businesses might not have the luxury of starting with low-value activities. They might need to start with high-value activities. In this case, the second dimension of movement in building trust can be from high specification of activities to much lower specification of activities and more focus on appropriate specification of end products. If the activity is of very high value to the enterprise, the managers may begin with a more traditional control-based approach. They may only gradually reduce the focus on tight specification of activities as the other participants provide evidence of their ability to perform as activity specifications are slowly eliminated.

In either case, the objective is the same. Through a sequence of carefully structured interactions, managers must strive to migrate toward a set of relationships involving high-value activities but with very low specification of the activities themselves. By structuring a rapid sequence of interactions, managers can build both the capabilities and the confidence required to manage effectively in this new environment, without exposing the enterprise to unnecessary risk.

Trust-based approaches offer significant promise to create economic value in markets characterized by intensifying competition and growing uncertainty. Properly applied, these approaches enable managers to achieve much higher levels of collaboration and flexibility than would ever be possible with more control-based approach. Far from increasing vulnerability to unanticipated events, trust-based approaches can, if applied property, actually reduce vulnerability. These approaches, however, require a far different set of capabilities than most managers today possess. Because of the lengthy lead-times required to build these capabilities, managers are advised to begin now in moving to these trust-based approaches. Fortunately, the process for implementing these new approaches provides ample opportunity to build the capabilities without exposing the enterprise to undue risk.

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