# Acting Cooperatively While Being Revolutionary : An Insider-Outsider Cybermediary Theory

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## Abstract

*In this paper we present an alternative perspective of a financial services cybermediary. Drawing on the institutional entrepreneurship literature and identity theory, we develop a theoretical model for cybermediaries that aim to become core players in the emerging on-line financial services field. In this model an alternating emphasis on either an insider perspective and interorganizational linkages, or an outsider perspective and revolutionary interpersonal interaction, enables cybermediaries to evolve from a legitimate peripheral position to a core directing position in the emerging on-line financial services field. Both feed-back and feed-forward learning processes hereby help to ensure the pivotal role of cybermediaries by locking in the identities of the main institutional constituents to their advantage.*

## 1. Introduction

The convergence of information and communication technology in the form of Internet-standards is leading out to the creation of new e-commerce organizational fields [6, 56]. By organizational field we mean "those organizations that, in the aggregate, constitute a recognized area of institutional life : key suppliers, resource and product consumers, regulatory agencies, and other organizations that produce similar services or products." [17]. Many early e-commerce analysts predicted the demise of intermediary retail channels during the construction of these new organizational fields [30]. Drawing on transaction cost economics [13, 55], analysts predicted that standardized information and communication technology would offer the prospect of greater efficiency and nearly frictionless supply and demand relations. After all, one of the most important functions of intermediaries (or middlemen) is to provide matching services for buyers and suppliers [56].

In this light, intermediaries can only subsist when intermediated exchange provides greater gains from trade than direct exchanges between consumers and suppliers [48]. Therefore, predictions that brick-and-mortar companies would start selling their products and services directly to Internet customers, resulting in massive "disintermediation", proliferated [51]. However, disintermediation – or the pushing out of middlemen by other firms that don't appeal to intermediaries anymore – has only happened in a limited fashion [12]. On the contrary, new intermediation opportunities are arising in the Internet marketspace for a new kind of intermediaries : cybermediaries [41].

Many scholars are trying to grasp the nature of new intermediation opportunities on the Internet [11, 12, 30, 37, 41, 56]. Apart from looking at these intermediation opportunities however, additional theory building endeavours should also address the question why e-commerce organizational fields are still in their infancy. Up to now, most companies have failed to achieve a significant lock-in [46] of a profitable customer base using Internet-technology. In this paper we contend that the puberal state of financial services cybermediaries [19] is a major reason for this failure. This sounds paradoxical, since financial services are so-called intermediary or second utility services, which are only useful as a complement to first-utility products like books, food, shoes…

At first sight, banks thus should be the first victim of disintermediation in e-commerce organizational fields. However, banks have traditionally served as third party enablers of first utility business services. The third party legitimacy of banks has always been an important factor for the viability of business-to-consumer and business-to-business relationships [20]. It co-determined whether customers, government, the media and even competitors would sufficiently trust a company to even consider initiating transactions with it [1]. Therefore, the virtualization of physical money into its digital counterpart and the comprehensive diffusion of on-line financial services is likely to trigger the adoption rate of business-to-business and business-to-consumer routines over the Internet considerably [10].

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## 2. The identification of cybermediaries : a theoretical agenda

Generally speaking, the role of cybermediaries can be dichotomized into performing the function of matchmaker versus performing the function of expert or specialist [55]. However, we contend that financial services cybermediaries can perform an even more important function : playing a pivotal role in the development of institutions that provide legitimacy (as the basis of transactional integrity, quality and reliability) in new organizational fields [37]. How should entrepreneurial cybermediaries go about in building these institutions? In this paper we address this question by outlining how successful institutional entrepreneurship is inextricably bound up with the framing of organizational identities. We define identities as "shared social meanings that persons attribute to themselves in a role" [7 : p. 242]. Identities are socially produced by actors who locate themselves in social categories and self-reflexively interact with others in terms of these frames [44]. Our focus hereby transcends the transaction cost economics view [13, 55] in the sense that it views organizations and industries as social communities of individual actors instead of mere economic institutions of organizational transactions.

We assert that the strategy of a cybermediary should first of all consist of acquiring legitimacy in the eyes of its institutional constituents, such as the media, government, customers and financial services companies (its competitors). To this end, a cybermediary should build an organizational identity reflecting integrity and cooperative spirit in relation to its constituents (and thus also its competitors). In this view, cybermediaries should thus first become legitimate insiders. Once this is achieved, we posit that a cybermediary's success is built on its ability to induce its competitors (and other constituents) to renew themselves and revolutionize their institutionalized identity. Paradoxically, cybermediaries then should also be outsiders, in order to be able to revolutionize the perspectives of their traditional competitors. In this manner, cybermediaries' central role in triggering processes of renewal helps them induce a collective legitimation effort of the emerging on-line financial services field to their advantage.

## 3. Organizational fields as legitimate orders

In organization theory the view of organizations and organizational fields as social communities, instead of just economic institutions, is rapidly gaining ground [45]. In this view, organizations and organizational fields do not emerge automatically, but rather are constructed by entrepreneurs whose actions and behaviours are both facilitated and constrained by the structure and resources available in the social community in which they are embedded [27]. As contended by Weber [53 : p. 124] "social action may be oriented by the actors to a belief (Vorstellung) in the existence of a 'legitimate order'". Building new organizational forms and a new industrial structure like an e-commerce financial services field thus involves delineating the new boundaries of a legitimate order of activities, starting from the legitmate order of the traditional financial services boundaries.

To establish these boundaries, managers build a network of interorganizational relations in which they exchange information [23, 27]. Whenever managers perceive that mutual problems can be resolved collectively, they reciprocally evolve to institutionalize simplified cognitive models or frames about these problems [36]. By participating in the negotiation of these frames, boundary spanning entrepreneurs are able to influence the legitimate order of an emerging organizational field to their advantage. Framing in this context is regarded as providing the ordering of activities and meanings that individuals need to make sense of the enactment of their daily routines [25 : p. 87].

## 4. Perspectives of incumbents and new entrants

Banks have for most part of their history been unquestioned fiduciary parties, which led out to the delimitation of legitimate spheres of organizational activity being predominantly based on taken-for-granted social norms [18, 50]. Legitimacy in this view has got more to do with *organizational identity* than with demonstrations of organizational competencies. Incumbent banks are structurally legitimate, in the sense that their structures and procedures often serve as easily monitored proxies for less visible targets of evaluation such as strategies, goals, outcomes [35, 50].

Big banks' status as "too big to fail", and in some cases weak incentives to be aggressive, resulted in the largest banking organizations in the industry exerting a unique influence on competition [38]. Banks, as they grew larger, have literally become more of their environment [8]. The snag attached to this is that banks increasingly narrowed their focus on their own enactments of the environment [54], causing a spiral of growing consensus on a restricted set of beliefs. New entrants on the other hand, in general perceive their organization as an open system, since they are not sufficiently embedded in existing social networks to control environmental selection processes [8, 54]. Figures 1a and 1b illustrate the different perspectives of

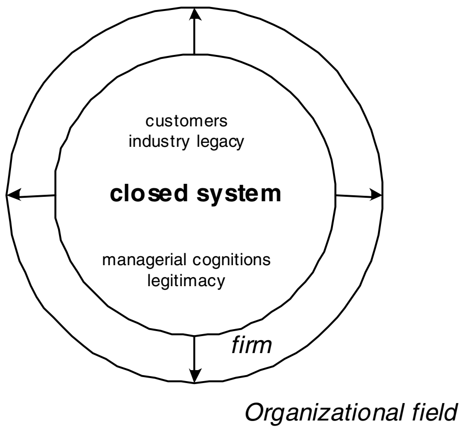


**Figure 1a. Perspective of incumbents**

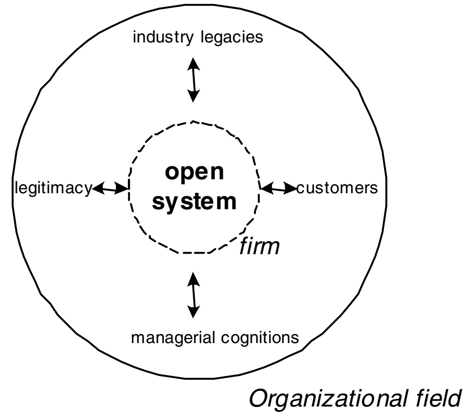


**Figure 1b. Perspective of new entrants**

incumbents and new entrants of the boundaries of the emerging on-line financial services field.

New entrants try to embed themselves in an organizational field by building a brokerage network, wherein flexible information access is prevalent. In order to anticipate the selective processes that delineate the boundaries of the emerging on-line financial services field, new entrant managers try to span these boundaries by creating resource interdependencies across several industry legacies, customer types and legitimacy bases. For instance Egg (www.egg.com), the UK-based Internet banking division of Prudential Banking, tries to overcome the inherent second-utility nature of financial services, by establishing interdependencies with suppliers of first-utility products as wines, books, food and drink, CD's, … An other example is provided by Security First Network Bank, which leveraged the banking industry expertise of Cardinal Bancshares and the technical expertise of SecureWare, to not only sell Internet-only financial services, but also develop secure customer interface software for incumbent banks [10].

As noted by Campbell [8] and Weick [54], adaptive evolution focused on processual change works best when the evolving social organization is a small part of the total environment. Hence, to anticipate environmental turbulence and the need for changing resource dependencies, new entrants build flexible organizational processes, which allows maximal strategic flexibility [52]. For instance Dublin-based First-e (www.first-e.com), backed up by a consortium of venture capitalists and technology firms, leverages the ICT and security skills of Enba to develop Internet-only financial services, contracts out its clearing operations to Royal bank of Scotland PLC, and outsources its on-line brokerage trades to the investment bank Dresdner Kleinwort Benson, is an example of such a brand new entrant. This enables First-e to keep abreast of unforeseen developments in the emerging on-line financial services field.

## 5. The organizational identity of new entrants

To easily cope with environmental turbulence, flexible organizational processes should go together with the formulation of a flexible organizational identity. A basic assumption in this paper is that the statement of an organizational identity is a strategic act. An adequate statement of such an organizational identity should satisfy the following criteria : claimed central character, claimed distinctiveness and temporal continuity [4]. This means respectively that the essence of the organization should be clearly pointed out, the organization should be clearly distinguished from others, and continuity over time should be demonstrated. As mentioned above, it is important for new entrants to portray themselves in a flexible way, and not to self-classify themselves too precisely. Albert and Whetten [4 : 268) enumerated several reasons for this line of argument : "ambiguous classification may prevent the organization from being typecast and thereby rendered more predictable than desired…an overly precise or micro-classification might quickly become outdated [and] the formulation of identity [is not expected] to be honed to great precision [anyway]".

Let us illustrate this with the case of First-e. First-e, which is now active in the UK, Spain, Germany and France, claims to be the first Internet bank to balance the global nature of Internet-technology and the local demands of customers, on a European scale (see website www.first-e.com). The essence in this claim is that First-e is the first true Internet bank. "The point about the Internet is that it is global. For banks the Internet should thus be a way of seamlessly crossing borders" claims the Economist [19]. First-e wants to capitalize on this essential characteristic of the Internet to become the world's first global Internet banking group. What is more, the self-classification of being a bank is typical of the image of continuity First-e wants to give itself. However, to prevent being looked upon as just "another bank" [40 : 2831], First-e prefers to distinghuish itself from traditional disintermediation claims, by calling itself a "re-intermediator" [40 : p. 2832]. This way, First-e wants to ensure its institutional constituents that it plans to revolutionize the on-line financial services field, by treating customers not just like an "account number", but as "a relationship" [40 : p. 2833). Or as first-e Chief Executive Azalbert said : "we can do what an established bank does without the cost and the hassle…What is more, we pass the cost-saving benefits of the Internet on to our customers." [21]. First-e thus claims to be able to set a new trend in the financial services organizational field. However, First-e is not overly precise in the constitution of its identity. Using the code-words Internet, bank and personalization, First-e manages to be credible and appealing without being too concrete about its plans.

## 6. The renewal of identities in an organizational field

It is generally acknowledged that new entrants are the main driving force of technological revolutions and the subsequent disbanding and renewal of organizational fields [42, 43]. In the past, the emphasis was mainly on competitive relationships between new entrants and incumbents, predominantly in a context of economic transactions. These studies assume individual actors adopt a largely exogenous perspective of organization-environment relations. However, theories of cooperation, stressing the endogenous nature of social interactions, are gaining ground in organization science [47].

The prevalence of cooperation among interacting entrepreneurs as the basis for the renewal of social communities and organizational identities is increasingly being recognized. Scott [44] for instance indicates the importance of social identity theory, when emphasizing that individuals play an active part in creating goals, identities and solidarities that provide meaning and generate ongoing social commitments in organizational fields. The identity interaction model [34] corroborates this contention by stating that individual identity is formed and maintained through interaction with others. Entrepreneurial individuals hereby use existing rules and social resources to frame identities in the organizational field to their advantage [7].

Organizational identities are formed in a process of ordered interorganizational comparisons and reflections upon them over time [3]. Cooperative learning between organizations hereby is a principal means of achieving the strategic renewal of organizational identities [14]. Cooperative learning starts at the interpersonal level and gradually gets embedded at the organizational and field level. Learning basically involves the cognitive process of destroying and creating identities [32]. This corresponds to a double feedback loop, consisting of, on the one hand, cognitive feed-forward processes, and, on the other hand, behavioural feed-back processes [14].

Feed-forward processes allow the unlearning of old identities and – simultaneously – the learning of new identities at the interpersonal level. Cooperative entrepreneurs frame identity constructions at the interpersonal level and rely on feed-forward mechanisms to embed these identity constructions into cognitive frames at the (inter)organizational and field level. Concurrently, feedback processes enable these frames to flow back from the field level to the (inter)organizational level to gradually become institutionalized as taken-for-granted frames at the individual level, thus affecting people's behaviours and consequent actions. After a few cycles in the feedback-loop, negotiations and decisions about systems, structures, strategies, and procedures get locked-in the new taken-for-granted frames [28].

## 7. Managing legitimacy : the insider-outsider paradox

How can new entrant cybermediaries become successful institutional entrepreneurs in an emerging on-line financial services field? According to Hybels [29 : p. 241; italics added] "the institutionalization of a feature of society derives from a legitimation process that occurs over time, and the legitimation process itself derives largely from institutions other than that being legitimated." Two aspects of the statement are important here : the time aspect, and the notion that existing institutions (for instance incumbent firms) provide support in the legimation process of new institutions, although this could mean cannibalizing their own legitimacy.

The general interest of new entrants is best served by revolutionary change. For new entrants use disruptive change to redefine dominant perspectives in the organizational field to their advantage. However, upon embarking on a new line of activity, particularly one with few precedents in the social order, new entrants have to face the daunting task of winning legitimacy. Therefore, new entrants first have to justify to peer or superordinate organizations their right to exist [33] as legitimate insiders in the organizational field, before demonstrating their technological superiority. Early entrants, as institutional entrepreneurs, must devote a substantial amount of energy to legitimation processes in the new on-line field, in the sense that they need to motivate cooperation of other actors by providing them with common meanings and identities [22]. The process of legitimation is thus looked upon as fundamentally that of "mobilizing collective support" [59 : p. 39] in the creation of frames and identities.

In order to mobilize revolutionary support, new entrants need to create a sense of being outsiders that exist independent of particular incumbents [4]. Paradoxically, new entrants thus on the one hand need to be insiders in the existing financial services organizational field to be able to participate in legitimation processes. On the other hand, new entrants also need to be outsiders to be able to influence legitimation processes in the emerging on-line financial services field to their advantage.

To achieve this, new entrants should follow a double track of integrating new activities under the umbrella of preexisting taken-for-granteds [58] and simultaneously disentangling new activities from certain preexisting regimes, to avoid new activities being perceived as marginal or illegitimate [50]. This can be attained by focusing on identity, learning and legitimate membership processes, which entail each other [32].

In order to influence learning processes in the emerging on-line financial services field, new entrants should focus on identification processes. Learning through identifying is more powerful than attempts to teach individuals via incentives or propaganda [31]. Role models – as prototypes in identification processes – are hereby very influential factors. By on the one hand categorizing their actions as new – emphasizing the outsider perspective, and on the other hand accuentating their self-perceived similarity with the group – emphasizing the insider perspective, cybermediaries can become de facto prototypic members of an emerging on-line field. This corresponds to the idea that identities in organizational fields are the result of the integration of two questions : "who do we think we are" and "who do they think we are?" [26]. Members of the organizational field are prompted by the feed-back from outsiders concerning the impression they make to assess the similarities between the inside and the outside view.

Obviously we're confronted with a paradox here : how can cybermediaries emphasize both an insider and an outsider identity? To resolve this paradox, we clarify the different levels of analysis of the observed phenomenon [39], as depicted in figure 2. Legitmation processes are instantiated at the organizational field level by institutional constituents through feed-back processes. Therefore, to be able to influence these legitimation processes, cybermediaries need to have an insider identity at the field level. However, in order to influence these legitimation processes to their advantage, cybermediaries need to negotiate revolutionary feed-forward processes at the interpersonal level. They can do this by influencing interpersonal interactions using their outside perspective. In this way, the organizational identity at the interorganizational level mediates between the interpersonal and the organizational field level; it reflects both insider and outsider identity features.

As mentioned above, new entrants' influence as a role model on learning processes in existing organizational fields relies on legitimate participation [32]. Therefore, in a first stage, new entrant cybermediaries need to establish interorganizational linkages to legitimate insiders (like incumbent banks), in order to obtain peripheral legitimacy in the traditional financial services field. Legitimate insiders in general could be [29] the state (f.i. contracts, regulation, legislation), the public (f.i. lobbying instances), the financial community and the media. The example of First-e is a good illustration of the above. First-e piggybacks on the banking licence of French Banque d'Escompte, to acquire sufficient inside legitimacy [40]. However, to make an impact and to be portrayed as an outsider also, First-e rolled out a major ad campaign, encompassing TV, radio, print and outdoor activity, a few months after its start-up, stressing the revolutionary nature) of its plans [60]. The same dynamic is visible in the strategies of incumbent firms like Prudential Banking. Prudential banking established its outside venture and new Internet brand Egg (www.egg.com), to prevent its Internet-activities to be perceived as marginal and achieve a sense of operating outside the traditional financial services field. At the same time, Egg can take advantage of the inside credibility of its mother company to acquire sufficient legitimacy as a start-up.

In the second place, and equally important, new allegiant institutions should be created which provide legitimacy to participants in the new organizatonal field. To be a pivotal player in the legitimation of the emerging on-line financial services field, cybermediaries should be perceived as legitimating institutions themselves. How can this be achieved? According to [29 : p. 243] "one actor's perception of the legitimacy of another is most strongly influenced by the behaviour of a third actor that appears independent." Weber [53 : p. 126] stressed that there are two principal ways to become an institution in a legitimate order (like an organizational field) : (1) appealing to purely disinterested motives and (2) acting out of self-interest, but then only "through expectations of ulterior consequences". The example of Dublin-based Egg provides a good example of the above principles.

players provide essential cooperation (for instance by giving information about the existing product

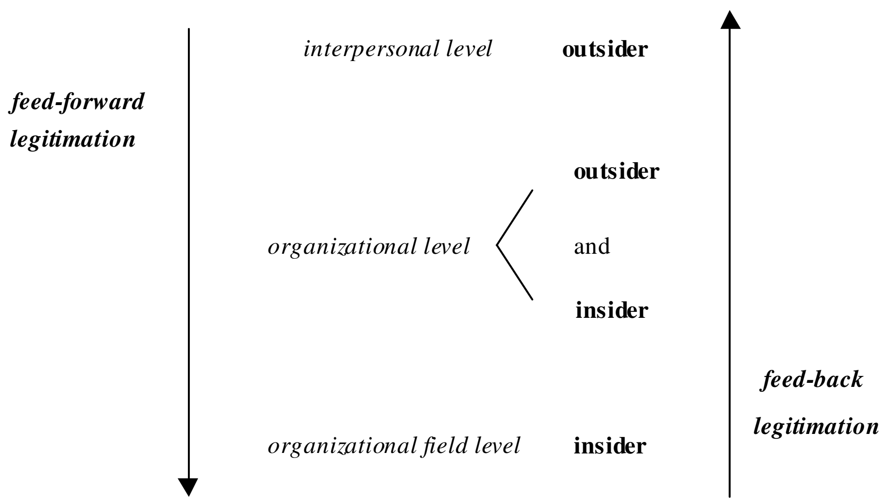


**Figure 2 : insider-outsider legitimation processes**

Egg initiated a virtual community for its customers (www.eggfreezone.com), in which independent media sources provide "objective" information about the financial services world. Moreover, to improve the credibility of this information, customers are encouraged to post all their griefs and complaints on a publicly available webpage, resulting in so-called "institutional gossip" [37]. Preexisting legitimating entities should also be convinced to lend support in building new institutions. Egg therefore launched a web-based personal investment supermarket in which incumbents as Prudential and Legal & General offer their products.

Dutch cybermediary Independer (www.independer.nl) provides another illustration of an institutional entrepreneurship endeavour. As the name "Independer" signals, the aim of this new cybermediary is to broker between the needs of customers and financial services suppliers by taking a third party position. The two founders of Independer are former employees of the Dutch bank ABN-Amro, who intuitively developed the idea that offering Dutch customers price transparency of the intricate offerings of incumbent banks would be very feasible on the Internet. The founders of Independer thus enact existing financial services by offering comparisons and price transparency to its customers. The founders of Independer hereby use interpersonal linkages established in their prior job to make some incumbent

offerings). What is more, Independer uses the role model of Dutch celebrities to ensure that its revenue streams are perceived as transparent, and to reflect its third party nature. These Dutch celebrities – which have no linkages to the traditional financial services field – supervise the redistribution of revenue surpluses to customers (in the form of loyalty programs). Finally, Independer uses independent media sources to create a sense of objectivity about the information provision on its website. So, on the one hand Independer'services concern existing, legitimate products, and on the other hand Independer is trying to confirm its third party or outside identity to differentiate itself from existing commercial players.

## 8. A lock-in model and three propositions

New entrant managers should act as brokers between incumbent managers that are open to innovations, and e-commerce players outside the financial services field that offer complementary first-utility services. These brokerage activities with a small core of incumbents play a crucial role in helping new entrants to catalyze cooperation of non-cooperating incumbents [24]. Incumbent managers are likely to mimic each others' behaviour [23]. In this way, a self-reinforcing legitimation dynamic is set in place in the emerging on-line financial services field. As asserted by complexity theory and affirmed by cognitive theorists as Weick [54: p. 157; italic added], "minor disturbances, when

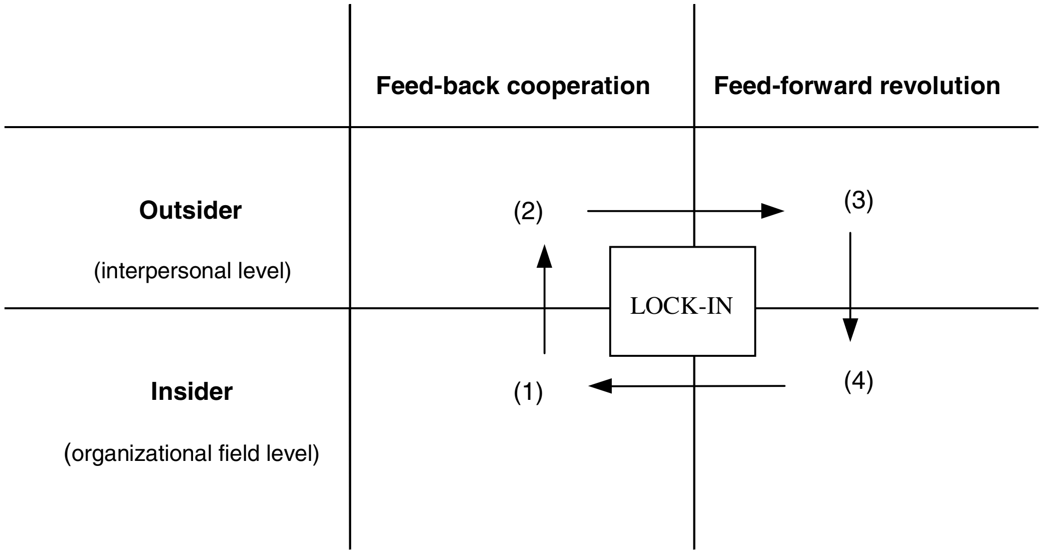


**Figure 3 : lock-in of identification processes**

they are embedded in a deviation-amplifying loop, can grow into major happenings with major consequences." Small initial conditions may lead to an uncontrollable – or locked-in – sequence of significant outcomes, and trigger legitimation externalities. As a consequence of this self-reinforcing dynamic, incumbents are likely to engage faster in unlearning or cannibalization processes of their structural – traditional – legitimacy. What is more, in this way new entrants will find it easier to influence legitimation processes in the emerging on-line field to their advantage. New entrant managers thus can gradually evolve from a peripheral legitimate position in the traditional financial services industry to become a core player – a legitimating third party – in the emerging on-line financial services field.

To achieve this, new entrants will have to master the driving forces of lock-in and positive network externalities. The principles of lock-in and network externalities are primarily based on complementarities of products and services [46]. Shapiro and Varian's [46] theory of lock-in and positive network externalities primarily focuses on the way sellers' and buyers' behaviours get institutionalized in a feed-back loop driven by transaction cost economics. They outline an aggregate macro-theory and mainly disregard feed-forward processes at the interpersonal level. Consequently, in this paper, we propose that cognitive feed-forward mechanisms – enabling negative network externalities – ushered in by individuals should complement behavioural feed-back mechanisms. In this manner, we hope to contribute to a lock-in theory that is sufficiently dynamic to be viable during the crucial institution building phase of an e-commerce field. The double feed-back loop underlying this complemented lock-in theory is depicted in figure 3.

Let us briefly clarify the four different steps of the loop. To acquire the identity of a legitimate insider in the financial services field, a new entrant needs to establish cooperative linkages (at the interorganizational level) with incumbent players (1). Once this is achieved, new entrant entrepreneurs can start influencing the framing of the identities of cooperating incumbent players through interpersonal interactions (2). As outsiders, new entrants introduce revolutionary perspectives at the interpersonal level (3) and rely on feed-forward processes to embed them at the organizational and field level (4). Feed-back processes flowing from the field level (1) to the organizational level then in turn influence the identification processes at the interpersonal level (2), et cetera...

After many cycles of this double feed-back loop, cybermediaries' lock-in of institutional constituents' views and identities can become significant. However, this implies being able to manage the tension between being an insider and being an outsider throughout the whole process of institution building. This is a very difficult task, as illustrated by the example of Security First Network Bank (www.sfnb.com), the US-based Internet bank. SFNB was set up in 1995 by Cardinal Bancshares and SecureWare, but taken over by the incumbent Royal Bank Financial Group in 1998 [10]. SFNB's immediate success with its secure software made it hesitate in which direction to proceed : either be an Internet-bank providing Internet-only financial services, or be a software company selling off its software packages to incumbent players. SFNB's modest successes as an Internet bank and its later takeover by the Royal Bank Financial Group, in this repect can be attributed to its lack of focus on remaining an outsider, and its premature profit-seeking toward incumbent insiders [10].

Summarizing the above theoretical outline, we can now suggest following propositions :

**<u>Proposition 1 :</u> The viability of a cybermediary depends on its strategic combination of "insider" and "outsider" features of organizational identity**

**<u>Proposition 2 :</u> The viability of a cybermediary depends on its strategic combination of cooperative interorganizational linkages and revolutionary interpersonal interactions**

**<u>Proposition 3 :</u> A viable cybermediary strategy is based on strategically brokering first- and second utility services using the strategies outlined in propositions 1 and 2.**

## 9. Conclusion

Institutional entrepreneurship is not about being very innovative, but about making new perspectives acceptable to incumbent constituents. Paradoxically, being revolutionary thus means being able to cooperate. In other words, institutional entrepreneurship involves "the ability to relate to the situation of the 'others'" [22 : p. 398]. A cybermediary that wants to be a successful outsider thus needs to be able to relate to inside perspectives of incumbent players. However, this can only be accomplished by being an insider itself. The message we're trying to convey in this paper is that an on-line financial services organizational field can not be built up from scratch, but requires institutional constituents (the media, customers, incumbent firms, the state) from the originating organizational fields (in this case, principally the financial services field) to allocate their resources to new ventures. Of course, new institutions need to be built in a new organizational field. However, the making of new institutions requires combining existing institutional patterns in a credible fashion, so as to motivate the cooperation of other actors in the framing of common meanings and identities. By clarifying the levels of analysis of the insider-outsider paradox, we hope to have contributed to understandings of how cybermediaries can be successful institutional entrepreneurs. Our aim hereby not only is to contribute to the success of these cybermediaries, but also to shed some light on how new e-commerce organizational fields can be established as a means of economic development at a societal level.

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