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Ethical decision making: on balancing right and wrong

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Chapter One

Ethical Decision Making: An Introduction

Lying is often profitable. Daily life provides ample opportunities to gain financially by behaving unethically. When filing an insurance claim or describing a product they are trying to sell, people have an information advantage over their interaction partners. While these people know how damaged the goods really are or the true state of the product they attempt to sell, their counterparts hold no such information. Even generally decent and honest people may be tempted to use such private information and over-estimate the value of damaged goods for the insurance claim, or refrain from mentioning hidden defects in products they are trying to sell. Possessing private information can be ethically challenging.

However, not every opportunity to profit leads us to lie. Moreover, even if we end up not being totally honest, we usually lie modestly. When we file an insurance claim detailing which items were placed in the suitcase that we recently lost during a trip abroad, we may exaggerate the value of the rather old digital camera that was in the suitcase by describing it as brand new. We might be rather reluctant however, to add to the insurance claim items that were not in the suitcase in the first place. Similarly, when describing the car we are trying to sell we may hide the information about the car's problematic engine but avoid holding back information about the defected air-conditioning system as well. We might use our private information about the content of the suitcase or the condition of the car to boost our profit to some extent but avoid lying too much. But how attractive is it to be in situations that allow us to possess private information and lie for profit? Do we seek such situations or in contrast, avoid them even at a personal cost? And why do we use our private information modestly rather than benefit ourselves even more? That is, why does exaggerating our insurance claim by inflating the value of the camera feels ethically legitimate while requesting compensation for a necklace that was not in the suitcase feels ethically wrong? Why does not mentioning the engine problem in the car we attempt to sell feels right while not mentioning all known defects feels wrong? Simply put, what determines how much we lie?

There are many reasons not to lie too much. Such major lies are more likely to be detected by others (Gino & Bazerman, 2009), may be harder to redress, and may carry costly punishment when detected. Indeed, most law enforcement policies are based on the classical economic approach to crime and punishment (Becker, 1968) suggesting that the extent to which people would lie depends on their cost-benefit analysis of the situation. According to this approach, when considering whether to lie or not, people compare the profit that would be generated by the lie with the costs attached to the

likelihood to get caught times the magnitude of subsequent punishment. Interestingly, however, and in contrast to this idea, most of us are also able to report instances in which we “could get away with it,” yet decided to be (relatively) honest – we choose a more ethical course of action and gave up potential profit that could have been generated by lying. Such introspection is at odds with the idea that unethical behavior is purely the product of external considerations such as being caught or punished. It is, however, quite in line with psychological research showing that when making judgments and decisions, people are also driven by ethical considerations and sentiments (e.g., Haidt, 2007; Bowles, 2008). In the current dissertation, I focus on situations in which people hold private information about the value of the goods they possess and may lie about this information to boost their financial profit. I maintain that even under conditions of complete anonymity, when the information is completely private and the likelihood to get caught is eliminated, people sometimes act honestly, and sometimes lie and deceive, that they sometimes act ethically, and sometimes bend the rules to serve their immediate self-interest.

But why is it that people ‘lie just a bit’ even in situations in which their likelihood to get caught is practically zero? And why would people knowing that they would not be punished, opt for minor lies when bigger ones may generate even more personal profit? Recent work addressing the psychology of lying explained people’s tendency to refrain from lying by focusing on people’s desire to hold a positive self image (Baumeister 1998; Bem, 1972). People generally seek to affirm the self through promotion, enhancement, and protection of their self view, and they do so through a variety of cognitive and behavioral tactics and strategies (Baumeister, 1998; Sedikides & Strube, 1997). One such strategy involves the tendency to internally attribute one’s positive characteristics, features, and behaviors and externally attribute one’s negative characteristics, features, and behaviors. Mazar, Amir and Ariely (2008) proposed that one important positive aspect that people seek to maintain is their self image as honest individuals. To do so, when confronted with tempting and ethicality challenging situations, people will lie for profit but only to the extent that they would not endanger their self view as honest people. This leads them to lie but in modest ways (Fischbacher & Heusi, 2008; Mazar, et al. 2008; Gino, Ayal & Ariely, 2009; Gino, Norton & Ariely, 2010).

Here I adopt this idea that in deciding whether to lie or not people balance these two desires - serving their self interest and maintaining an honest self view. This dissertation studies the way that otherwise honest people maneuver their way in an ethically challenging world and try to understand the factors that influence the delicate

balance between gaining money and being honest. The studies conducted here aim to advance our understanding on how people balance right and wrong when they consider lying to institutions at large (e.g., insurance companies, tax authorities, or as experimental participants to the researcher) or to other people in their surroundings (e.g., their negotiation partners). Furthermore, these studies explore to what extent they are attracted or alternatively averse of situations allowing them to possess such private information which they could use to dishonestly profit at the expense of others. I propose that when challenged with an ethical decision people's likelihood to lie is determined by balancing their desire to be honest on the one hand, and serving their self-interest on the other. People navigate between the materialistic (e.g., money) and psychological (e.g., increased status if not caught) benefits the lie provides with its materialistic (e.g. punishment) and psychological (e.g. inability to see oneself as an honest) costs.

Society's bill for our minor lies

Why study minor lies? Should we care about what makes some people shape up their insurance claims? Is it interesting to figure out why someone 'forgets' to mention the barely functioning air-conditioning system when attempting to sell his car? Summing up the cost to society from people's 'minor lies' provides a clear answer – yes, minor lies matter. Examples are ample, in the United Kingdom 25 billion British pounds annually disappear by people underpaying their taxes (Levi, 2010) and similarly, 17% of the taxable income in Belgium remains undeclared (Stack & Kposowa, 2006). Piracy in the software industry is pervasive with 35% of global software estimated to be pirated, translating to 40 billion US dollars per year (Miyazaki, Rodriguez & Langendefter, 2009). Moreover, in the US 600 billion dollars are estimated to vanish due to employee theft and fraud (Mazar, et al., 2008). 'Borrowing' a pen from work is rather costly after all.

One industry that suffers greatly from people's minor lies is the insurance industry. In the United States, 10% of all insurance claims are estimated to be dishonest and pile up to nearly 24 billion US dollars annually (Accenture report, 2003; see Mazar, et al. 2008). People attempt to benefit themselves at the expense of insurance companies in ways ranging from exaggerating their otherwise legitimate claims (also known as buildup) to planned or outright fraud by filing claims about events that never occurred (Crocker & Morgan, 1998). The latter type of fraud is often referred to as hard fraud and is a criminal behavior that, if detected, is often followed by legal prosecution. The former type however, is referred to as soft fraud and falls into what Tennyson

(2008) called the “gray area of abuse or unethical behavior” (p. 1183). For example, hard to diagnose injuries, such as lower back pain or spinal disorders, are one main source of buildup employees tend to use when claiming health insurance compensations for work related injuries (Crocker & Morgan, 1998), and such buildup of medical claims forms the majority of dishonest insurance fraud in the American governmental health care programs (Hyman, 2002). More broadly, Tennyson suggested that “most analysts believe that the costs and prevalence of opportunistic soft fraud – particularly buildup – vastly overweigh those of more systematic, planned, or criminal claims frauds. This suggests that consumer ethics, attitudes, and psychology are an important element in the insurance fraud equation” (Tennyson, 2008; p. 1195). It is these ethical attitudes and psychological factors influencing people’s likelihood to use minor lies that this dissertation explores.

Ethical decision making: Balancing right and wrong

Past research on the psychology of ethical behavior focused on identifying individuals who are more likely to lie based on some features of their personality (e.g., Hegarty & Sims, 1978; Hing, Bobocel, Zanna & McBride, 2007; Trevino & Youngblood, 1990) and advanced lie detecting techniques and technologies (for a review see Ekman, 2009). In contrast, work in the business and organizational ethics disciplines often adopted a more prescriptive approach detailing how ethical people should behave (e.g., Ferrell, Fraedrich & Ferrell, 2008). Recent social psychological work however, focused on a more descriptive approach, suggesting that lying is not a behavior performed by only a selected few ‘bad apples’ but rather by people from all walks of life. This descriptive behavioral ethics approach focuses on identifying situations which influence people’s likelihood to behave unethically (De Cremer, 2009). This is the approach adopted in the current dissertation. As detailed in the examples above, I believe that not mentioning the air-conditioning problem in the car one is trying to sell, or describing an old digital camera as brand new when filing an insurance claim, are not behaviors restricted only to some rotten apples in society. Unfortunately perhaps, most of us may succumb to such temptations sometime, abusing our private information to dishonestly benefit ourselves at the expense of others.

A growing literature in psychology focuses on studying situational factors influencing people’s likelihood to dishonestly benefit themselves on the expense of institutions at large (e.g., tax authorities, employer’s budget). In this line of studies participants commonly hold private information, about their levels of performance in various tasks for example, and receive pay according to their reported performance

levels. Since only participants know how well they performed, they can lie and benefit financially. Comparing their reported performance levels to the performance level of participants who are evaluated objectively (by the experimenter) provides a measure for lying. Schweitzer, Ordóñez and Douma (2004) for example, presented students with random letter strings from which they had to create as many existing English words as they could. After completing this task participants were given dictionaries and were asked to grade their own work. Attaining a predefined goal (creating 9 existing words) meant receiving a monetary reward. Participants who were close to attaining their goal were most likely to use their private information concerning how many words they actually found, and lied more than others who were not as close to reaching their goal.

In another study involving private information about own performance, students were seated in a classroom with fellow students and had to solve twenty numerical questions (Gino, Ayal & Ariely, 2009). Students learned that they would be paid 50 cents for each correctly solved question and that they would grade their own work. Gino and her colleagues had a confederate set a dishonest social norm by standing up a short time after the test began declaring that he has correctly solved all items. Since the confederate was extremely quick in making this declaration, it was clear that he was lying. As the experimenter paid this confederate the full 10 dollars, students realized that they could get away with lying. Indeed, seeing the confederate's behavior led student to report higher level of performance compared to a control group that were graded objectively. Interestingly, when the confederate was wearing a t-shirt of a competing school, lying levels dropped as students wished to avoid the negative norm established by the out group member. Using yet another method to provide private information to people and assess their lying levels, other work found that people were more likely to dishonestly use pre-marked answers on an answering sheet the more mentally depleted they were (Mead, Baumeister, Gino, Schweitzer & Ariely, 2009), and furthermore when people adopted a viewpoint that denies personal responsibility to their actions (i.e., read a text promoting the belief in determinism over free will) they were more likely to lie by using an answer that was revealed to them by the computer which they were instructed to ignore (Vohs & Schooler, 2007). All in all, these different lines of research demonstrate that when possessing private information about own levels of performance, people lie to benefit themselves. People report finding more correct words than they really did, say that they solved more numerical questions than was really the case, or use the answers that they were supposed to ignore, all to make a profit.

Batson and colleagues (Batson, Kobryniewicz, Dinnerstein, Kampf, & Wilson, 1997; Batson, Thompson, Seufferling, Whitney, & Strongman, 1999) used yet another interesting method to assess lying by allowing people to privately toss a coin in order to determine if they or another person would get to perform an undesirable task. They found that people were more likely to win such coin toss than would be predicted by chance. This further demonstrates that holding private information about whether one correctly predicted the outcome of the coin toss, leads people to lie in order to avoid undesirable consequences. Recently, Green and Paxon (2009) found that in similar settings, when people had to provide information about whether they predicted correctly the outcome of a coin toss in order to gain financially, an increased activation in the dorsolateral prefrontal cortex (DLPFC), a brain area involved with complex cognitive behaviors and (social) decision making, was associated with higher levels of dishonesty. It seems that at least to some extent unethical considerations regarding private information we possess are localized to specific brain areas. Together, findings from various tasks that provide people with private information indicate that people use such information to dishonestly boost their profit. Importantly, this tendency is amplified under some situational conditions more than others, indicating that people balance the extent to which they lie.

A recent study in economics employed a simple method to further our understanding into the amount of lying people perform under complete anonymity conditions. Fischbacher and Heusi (2008) gave people the opportunity to roll a die, report the outcome and gain money according to these reports. As rolls were completely private, people could lie about the outcome of their rolls in order to gain more money. Fischbacher and Heusi concluded that some participants in their sample were lying as the distribution of reported outcomes differed from the distribution of an honest die roll. Across different experimental conditions, including manipulations of the profit generated by the lie, the number of times participants participated in the study, and the level of privacy in receiving pay for the task (i.e., by the experimenter vs. paying oneself from an envelop), a similar pattern of results appeared as in the psychological research reported above - people lied, but restricted their amount of lying. Notwithstanding this accumulated evidence from both psychological and economical research, demonstrating the modest levels of lying in various private information tasks and procedures, the theoretical questions addressed in this dissertation remain open. We know very little about the extent to which people would allow themselves to lie, when would people feel that they have crossed the ethical line

and that their lies became too big, and would they prefer to avoid being in such tempting situations to begin with.

Just as private information allows one to lie about his or her performance to benefit the self on the expenses of organizations at large, people in social settings use their private information to deceive their interaction partners in order to benefit themselves. For example, Steinel and De Dreu (2004) asked participants to send information about a joint payoff scheme to their counterparts who had to choose which of several payoff options they would like to implement. As only information providers knew the true values appearing in the scheme, they could deceive their counterparts about the actual state of affairs and trick them into choosing an option that was beneficial for the information provider, but not the decision maker. Compared to people who were motivated to act in a prosocial way, those who were motivated to act selfishly used the private information they possessed and sent deceitful messages to their counterparts. Similarly, Pillutla and Murnighan (1995) found that in order to get their offers accepted people use their information advantage in a strategic way. In asymmetric information settings, people who had an information advantage over their counterparts made offers that seemed fair (and were thus likely to be accepted) but were actually self-benefiting. Van Dijk, De Cremer and Handgraaf (2004) further found that selfish people were more likely than prosocial people to use such strategic deception when proposing offers to their counterparts. Work by Boles, Corson and Murnighan (2000) further found that people were more likely to use their information advantage when their counterparts were unaware of their negotiation alternatives (i.e., what would have happened in case they rejected the offers that were proposed to them). These pieces of evidence converge to demonstrate that also in interdependent situations of information asymmetries, when one party knows more about the value of the goods than the other party, people are often tempted to use their information advantage to benefit themselves at the expense of their counterparts.

Work in economics further demonstrates this tendency to use private information in a self benefiting manner, while restricting the amount of lying in some situations more than others. Gneezy (2005) found that people holding private information would deceive their counterpart based not only on the impact the lie had on their own outcome but also on their counterpart's outcome. He found that the larger the consequences were for the counterpart, the less people deceived this person. Furthermore, when people made a promise to their counterpart about the private information they held, they were less likely to lie as a function of the strength of the promise they made (Lundquist, Ellingsen, Gribbe & Johannesson, 2009). Similarly,

recent evidence from a TV game show indicated that people who volunteered to discuss their private information were less likely to lie about it compared to people who were asked to provide this information by the host of the show (Belot, Bhaskar & van de Ven, 2010). Finally, recent neuroeconomic work found that lying by breaking a promise (in an economic 'trust' game with monetary consequences) was associated with activation in the DLPFC, anterior cingulate cortex (ACC) and the amygdale, gaining further support to the idea that lying considerations, whether on the expense of institutions at large or people we interact with, are localized to specific brain areas (Baumgartner, Fischbacher, Feierabend, Lutz & Fehr, 2009).

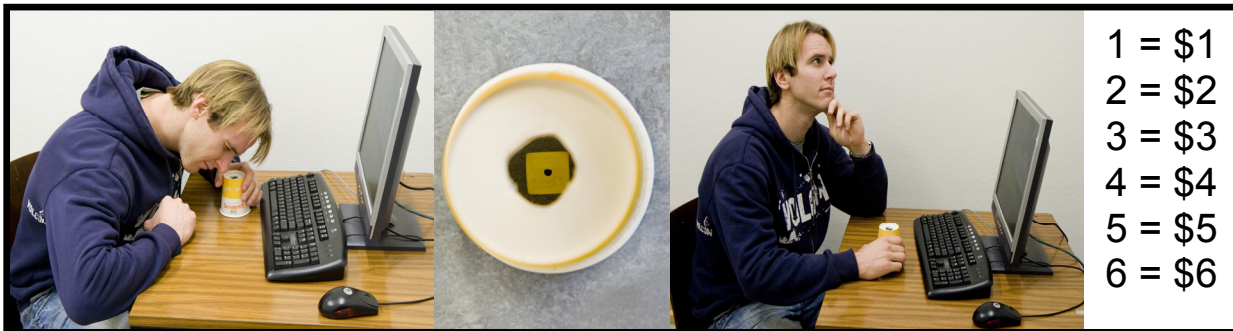
Taken together, evidence from psychological and economic research demonstrates that people abuse information asymmetries to dishonestly benefit themselves. Indeed, Oliver Williamson (1975) proposed that when knowledge asymmetry is coupled with opportunism our organizations (and economic markets) face moral hazards. This notion clarifies the potential temptation that is embedded in possessing private information. Yet, the basic questions of interest here remains open – what makes one lie for some amount but avoid lying for a larger amount? Where do people draw the line distinguishing right from wrong? How attractive do people find the possibility of being in situations in which they may possess private information allowing them to lie for financial gain? The three empirical chapters included in this dissertation attempt to provide insight addressing these questions. In all the experiments reported here people had private information that allowed them to lie (to the organization at large or to another person) in order to benefit themselves. The results described here provide evidence that people suffer a psychological cost from the mere act of lying as well as from lying too much (Chapter Two), that people find value in justifications allowing them to lie for profit while feeling honest (Chapter Three), and finally that people shy away from engaging in negotiation with another person when the situations allows them to use their private information to deceive their counterparts in order to benefit themselves (Chapter Four).

Overview of empirical chapters

The first two empirical chapters of the dissertation focus on situations in which one may dishonestly use the private information one possess and benefit on the expense of the institution at large. These chapters tested the proposition that people lie to gain financially, but only when such gains compensate the psychological cost of the lie. To address this issue we asked people to report the outcome of a private die roll and gain money as a function of their reports. As the die was placed under a paper cup with only

a small hole in the top allowing participants to see the outcome, they could lie and gain money, see Figure 1.1. That is, as in Fischbacher and Heusi's study (2008), people had private information about their actual roll which they could abuse to dishonestly report a higher value.

Figure 1.1. Die under cup task



In Chapter Two (Shalvi, Handgraaf & De Dreu, 2011a) we found that people's ethical maneuvering leads them to lie only when they may use what we termed middle-of-the-road lies allowing them to boost profit while avoiding lying a lot or lying very little. We interpreted this as evidence that people suffer a cost from lying as the lie must generate sufficient monetary compensation before people opt for such unethical course of action. Result of experiment 2.1 revealed that people avoided both major lies (i.e., over-reporting the highest possible outcome) and minor lies (yielding little material gain), but did over-report intermediate outcomes when this implied a substantial increase compared to an exit option. Furthermore, in this chapter we found that people who lie tend to justify their behavior deeming it a morally appropriate way to gain money. In discussing these findings we propose that organizations allowing freedom of choice while narrowing the available ways to unethically boost personal profit should see an increase in ethical behavior among their employees.

Building on the finding that people who lie seem to need a justification for doing so, in Chapter Three (Shalvi, Dana, Handgraaf & De Dreu, 2011) we manipulated the availability of justifications to those people who were invited to roll the die. The main prediction tested in this chapter was that people derive value from self-justifications as these allow them to lie for money while still feeling honest. As in Chapter Two, we asked participants to report the outcome of a private die roll and gain money according to their reports. Results of Experiment 3.1 suggested that the degree of lying depends on the extent to which lies can be justified. Specifically, when people were allowed to roll the die three times to ensure its legitimacy, but only the first roll was supposed to "count," and found evidence that the highest outcome of the three rolls was reported.

Eliminating the ability to observe more than one roll reduces lying. Results of three additional experiments (3.2, 3.3 and 3.4) suggested that observing desired counterfactuals, in the form of additional rolls not to be used to determine pay, attenuated the degree to which people perceived a lie as unethical. This modification in ethical perceptions mediated participants' likelihood to lie. A justified lie feels less unethical to use.

In Chapter Four (Shalvi, Handgraaf & De Dreu, 2011b), we move forward to study whether people maneuver towards or away from interdependent situations allowing them to use their information advantage to deceive another person in order to benefit themselves. To study this question we employed an asymmetric information ultimatum bargaining game with an exit option. The ultimatum bargaining game is an economic situation in which two people take decisions influencing their monetary outcomes. One person is assigned to be the proposer who offers a division of a commodity (e.g., money) to another person, a responder, who can accept or reject the proposed division. If the responder accepts, the commodity is divided as proposed but if the responder rejects, neither party receives anything (Güth, Schmittberger & Schwarze, 1982). Whereas classical economic theory (Camerer & Fehr, 2006) predicts proposers to offer the least amount possible and responders to accept anything greater than zero, this is not what typically is observed. In fact, across a large number of studies people tend to propose distributions that approximate fairness (i.e., a 50/50 split of the resource) and people tend to reject distributions that substantially deviate from fairness (e.g., Handgraaf, Van Dijk, Wilke & Vermunt, 2003; Handgraaf, Van Dijk & De Cremer, 2003; Oosterbeek, Sloof & van de Kuilen, 2004).

In the studies described in the current dissertation, we used an asymmetric information version of the game (Kagel, Kim & Moser, 1996). While the proposer always had information about the value of the goods to be split (chips to be converted to money) the responder had no such information. Temptation was manipulated by varying the value of the chips for the responder to be equal vs. lower than their value to the proposer. When the chips were worth the same amount to both proposer and responder, an offer that seemed fair (e.g. splitting the chips 50%-50%) was actually fair (e.g. equal money split if the offer is accepted). However, when the chips were worth more to the proposer, an offer that seemed fair (e.g. splitting the chips 50%-50%), was actually not (if accepted, the proposer would get twice as much money compared to the responder). Thus, in this latter game but not in the former one, proposers could use their private information about the value of the chips to deceive their responders by making an offer that appeared fair while it was actually not. We tested whether and

why people would avoid (or alternatively approach) situations that might tempt them to deceive another person.

The results described in Chapter Four suggest that temptation pushes people away from negotiating with others as people seek to avoid taking responsibility for their counterpart's outcome. Interestingly, those who actively decided to negotiate behaved more generously than others who are forced into a similar (tempting) setting. In three experiments (4.1, 4.2, and 4.3) we found evidence that reduced desire to be responsible for the other person's outcome serve as a situation selection mechanism, assisting people to avoid tempting social situations. Results revealed that people tend to avoid situations in which they can promote their self-interest by privately and anonymously cheating another person into a disadvantageous position. Experiment 4.2 revealed this tendency to be stronger (weaker) when the partner was described as cooperative (competitive). Experiment 4.3 showed that decreased willingness to be responsible for another's outcomes leads people to avoid tempting situations rather than to approach situations allowing them to be generous. We conclude that when navigating through social space, people avoid situations in which they may be tempted to use their private information to benefit themselves on another person's expense.

Finally, Chapter Five integrates the obtained results into a model of justified ethicality. In this concluding chapter I propose that the likelihood that one will behave unethically depends on the availability of justifications and one's subsequent modification in perceiving a given behavior to be (un)ethical. I discuss the theoretical contribution of this model and how it communicates with existing theories of ethical decision making. In addition, I address the usefulness of the model from a practical point of view and propose avenues for future research. Finally, it is worthy to note that the three empirical chapters (Two to Four) have been written as separate manuscripts and may thus be read independently. This resulted in some theoretical (but not empirical) overlap between these chapters.