

GREEDY LOSS PREVENTION: insurance and warranties

Abstract

In three studies, we show that loss aversion is essential to greed, in addition to acquisitive behavior. This drives them towards paying for insurances and warranties to avoid future financial or product loss. Furthermore, when they experience a history of no-losses, it limits their purchase likelihood of insurances.

Economic greed

Greed is omnipresent in our current society and highly relevant to economics. For instance, the media and public opinion attributed the financial crisis to the greediness of bankers and stockbrokers, who risked clients' money to ensure greater turnover to satisfy their greed (Papatheodorou, Rosselló, and Xiao 2010). Greed has also been related to corporate fraud (Smith 2003) resulting in the downfall of international corporations (Wells 2011). On a smaller scale individual greed is shown to be associated with higher debts (Lunt and Livingstone 1991).

Scientific research has caught up with this renewed focus on greed in society, making it a central concept in economical research. Greed is often invoked to explain non-cooperative behavior in economic games (Stanley and Tran 1998), resource exploitation (Ludwig, Hilborn, and Walters 1993) and is considered intrinsic to a materialistic lifestyle (Belk 1985). In this paper, based on previous work (Krekels, Pandelaere, and Weijters 2013; Seuntjens, Zeelenberg, Breugelmans, and van de Ven 2013; Wang and Murnighan 2011) we will focus on dispositional greed, defined as a personality trait that entails an insatiable, self-centered desire for more, whether of monetary or nonmonetary items.

Dual vision on greed

When people think about the concept of greed as defined above, they typically focus on acquisitive behavior (Wachtel 2003), classifying greed as a type of wanting more behavior. Though we endorse this wanting more perspective of greed, an important aspect is missing from prior conceptualizations. More specifically, avoiding losses might be another important characteristic of greedy people. Preventing that one loses certain items could be an essential part of attaining as much as possible.

Regulatory focus (Higgins 1997) nicely fits this dual vision on greed as a motivational principle. Regulatory focus theory elicits two different motivations, one focused on approaching positive or desired outcomes and one on avoiding negative or undesired outcomes. Where a promotion focus is concerned with attaining gains, advancement and accomplishment, a prevention focus is concerned with avoiding losses, safety and protection. This coincides with a twofold motivation within greed: greedy promotion is oriented towards attaining as much as possible of desired objects, whereas greedy prevention is oriented

towards not losing what one has already attained. We posit both to be essential in a greedy motivation.

This dual vision on greed is often indirectly incorporated in research, where the same uncooperative behavior might be explained by preventing losses in pay-offs, labeled fear, or increasing pay-offs, labeled greed (Rapoport and Eshed-Levy 1989). We believe that both these labels are an essential part of dispositional greed. Thus, using a newly developed dispositional greed scale (Krekels et al. 2013), we first examined whether a greedy motivation can be driven by a prevention focus as well as a promotion focus. An initial study (N = 184, 91 men, M age = 30.9, SD = 11.8) indeed indicates a positive correlation between dispositional greed (table 1) and both a promotion and prevention focus (Grant and Higgins 2003) ($r = .25$ and $.26$, $p < .001$).

Insurance policies and warranties

Although a theoretical understanding of the dual promotion and prevention motivation in dispositional greed are relevant and useful, in this paper we will mainly focus on the effects of a prevention motivation on everyday consumer behavior. The reasons for this focus are twofold. First, the effects of a promotion orientation seem more straightforward, as they align with a lay definition of greed as wanting more behavior. Second, though greed has mainly been conceptualized as a societal problem with excesses in big international businesses, we believe that small scale effects of a greedy disposition have a bigger effect on everyday life. More specifically, as a prevention orientation is mainly focused on safety and protection (Higgins 1997, 1998), in this paper we will examine the effect of a greedy disposition and its inherent prevention orientation on the purchase of insurance policies and warranties.

Under a prevention focus, people are more sensitive to losses and thus use avoidance strategies whenever possible to avoid negative outcomes. One industry that is primarily associated with protective mechanisms against possible losses and negative outcomes is that of insurance companies and warranties. By definition the purpose of insurance companies is to protect people from suffering potential negative outcomes of certain events. They can be regarded as vaccines in the non-biological environment: both are pre-emptive strategies against negative outcomes which do not prevent situations from happening but from having any resulting effects. Indeed, insurances and vaccines are often used in regulatory focus research (e.g. Kluger et al. 2004; Wiener, Gentry, and Miller 1986).

Similarly, extended service contract warranties can protect customers from losses. As product quality is not directly observable by customers and there exists a potential but undeterminable risk of product failure, buying a warranty diminishes the financial risk of a purchase (Shimp and Bearden 1982) through diminishing the effects of damages and assuring that the product will perform to expectations (Loveland 2010). Indeed, both warranties and insurances can be purchased as a means to minimize the effects of a problem should it occur. Thus, we expect dispositional greedy people to be more likely to purchase warranties and insurances to avoid losses, as it corresponds to their preventive motive (Lieberman et al. 1999) and does not contrast their promotion motive.

In four studies we show that preventing losses is not only an essential part of a greedy disposition, but indicate that this motivation effects consumer decision making with respect to buying and paying for insurances and warranties. This contributes not only to a theoretical understanding of greed, but also to its relevance for consumer behavior research.

Study 1: Loss aversion

As both prevention and promotion correlated equally strong in the aforementioned pre-test, we study loss aversion to examine the impact of one compared to the other. If the promotion orientation is stronger than the prevention orientation in greedy people, we expect low scores for loss aversion. However, if the promotion orientation would be weaker, we expect higher scores.

To test which of both motivations is stronger, we employed the method of Tom, Fox, Trepel, and Poldrack (2007), where respondents indicate their willingness to participate in a coin toss gamble with an equal 50%-50% chance of winning (10 - 45€, increments of 5€) or losing (5 - 25€, increments of 2.5€). These amounts were chosen as previous studies indicated people are roughly twice as sensitive to losses as they are to gains (Tversky and Kahneman 1992). Important to note here is that this test examines the effect of prevention versus promotion orientation, not that of loss aversion versus gain preference. 152 Students (102 men, M age = 21.1, SD = 2.7) participated in 66 randomized trials. These trials were divided in three tasks, interspersed with unrelated tasks to avoid answering fatigue and random answering. After another unrelated tasks they answered several psychological measures, amongst which the Dispositional Greed Scale (Krekels et al. 2013).

Linear regression showed that dispositional greed predicted respondents' loss aversion (table 2). Greedy people (+1SD) exhibit an average loss aversion ratio of 5.62 (SD = .59), indicating them to need on average more than 5 times the amount of gain versus loss to participate in the coin toss gamble. For non-greedy people (-1SD) this ratio is 3.82 (SD = .59). This shows that greedy people are not only oriented towards gaining more, but are also focused on preventing losses, and when balancing both, loss prevention is the more powerful motivation.

Insert table 1 about here

Study 2: insurances and warranties

The second study wanted to test the effect of greedy people's prevention orientation on real life behavior, more specifically on their preferences for buying insurances and warranties. As stated previously, buying an insurance or extended warranty is a way to cope with the possibility of losing or damaging the product and thereby diminishing the investment made. Indeed, risk aversion and prevention have often been cited as the cornerstone for the decision to invest in an insurance policy or extended warranty (Loveland 2010). In essence, all potential customers will experience some degree of concern that a product will not function up to expectations. However, to purchase an extended warranty or insurance, the concern of product failure must be sufficiently high (Shimp and Bearden 1982). We propose that, as greed has been shown to be linked with a prevention promotion and loss aversion, the more greedy a customer, the more he or she will be inclined to buy a product insurance or extended warranty contract.

108 MTurk participants (55 men, M age = 38.1, SD = 11.6) answered an online survey about product purchases, insurances and warranties. They saw three scenario's and afterwards

answered the Dispositional Greed Scale. The scenarios were chosen to represent both products and experiences, to be relevant for both warranties and insurances and to include different measurement of tendency to buy. The first scenario stated that the respondent was buying a smartphone, and the seller indicate that besides the limited basic warranty, they could buy three types of additional insurance plans. Insurance A cost 3\$ a month for 1-year basic damages insurance, Insurance B cost 6\$ a month for 1-year extended damage, loss and theft insurance, and Insurance C cost 8\$ a month for 2-year extended damage, los and theft insurance. Respondents indicated whether they wanted to buy any of these insurances or none.

The second scenario described them buying a second hand car with an expired warranty, but the dealer offered a 500\$ 2-year warranty. Respondents indicated their purchase likelihood and attitude towards the extended warranty. The last scenario described a ski trip, which offered a ski guarantee allowing them to rebook their trip to a different date or location if ski conditions were poor. Respondents indicated their willingness to pay to include the guarantee, or indicated the price drop needed to exclude the guarantee. We predicted greed to have positive significant effects on the choice of insurance, the purchase likelihood and the attitude towards the warranty in the first two scenario's. However, we did not expect an effect on the WTP measures in the third scenario, as we predicted there to be a conflict between their prevention motivation, that would direct them towards the ski guarantee, and their promotion motivation, that would direct them towards paying as little as possible.

Linear regression showed that there was indeed no relation between respondents' dispositional greed and their log-transformed WTP for the inclusion ($B = .183$, $t(52) = 1.339$, $p = .19$) or exclusion ($B = -.163$, $t(51) = -1.179$, $p = .24$) of the ski guarantee. Further analysis revealed greed to be indeed related to respondents' choice of insurance, the purchase likelihood and the attitude towards the warranty, but these relations were not linear but quadratic following a U-shape (table 2). The more greedy the responder, the more inclined they were to buy the more extensive insurance, the higher their purchase likelihood and their attitude towards the warranty. However, really non-greedy people had the same tendencies. Further analysis revealed this quadratic function to not be explained by either income or age. It is not entirely clear what explains non-greedy people's tendency to buy insurances or warranties.

Insert table 2 about here

Study 3: insurance after losing vs winning

The third study wanted to test whether we could eliminate greedy people's loss prevention. One possibility for lessening people's prevention orientation is the history of success versus losses. Previous research (Higgins et al. 2001) has shown that recent experiences with loss or success can indeed change people's current motivation. If greedy people are more aware of the possibility of losing certain items or money, could this be lessened by a history of non-losses? In other words, when greedy people experience that they do not loose for a while, will they become less focused on preventing losses?

To test this, a lab experiment was set up with 101 undergraduate students (53 men, M age = 20.3, SD = 1.9). They were instructed in a gamble game: they would have to predict whether a flipped coin would land on heads or tails. Respondents were told it was a normal coin, with a 50% chance to land on heads and a 50% chance to land on tails, making it a random gamble where they had no control over the outcomes. Respondents started with a certain amount of points, equal to the amount of coin flip and guess trials, and were instructed to keep as many points as possible. If their prediction was false; for instance they predicted heads but the coin landed on tails, they would lose a point, called a penalty. If their prediction was correct, nothing would happen. The point retaining was set up to prevent people's promotion orientation from influencing the experiment. Thus, people could only lose points, not gain them.

Before starting the final game, respondents entered a test-game. In this game, they would guess five times whether a coin would fall on heads or tails. They started with five points, and were instructed to keep as many points as possible. However, respondents were unaware of the fact that they had been divided into two conditions, and that the test trials were not random. Half the participants were participating in the loss-trials. In these trials, the first two coin tosses were programmed to show the opposite of what the responder had guessed, the third trial was programmed to be correct, and the fourth and last trial were programmed to be incorrect again. Thus, respondents in the loss condition made four wrong guesses, and ended with one out of a possible five points. Respondents in the non-loss condition experienced the exact opposite: first two correct guesses, then an incorrect guess, and finally two more correct guesses, ending with 4 out of 5 points.

After these test trials, giving them an experience of loss or non-loss, respondents were told they would play the real game with 20 trials. The person scoring the highest point at the end would win movie tickets. This incentive was chosen to be relevant for participants and to ensure that they were involved in the game. Furthermore, if they wanted, they could buy a type of insurance against making too many incorrect guesses. There were 4 types of insurances, eliminating 3, 6, 9 or 12 wrong guesses. If respondents bought any of these insurances, at the end of the game they would be given back the maximum amount of points they lost corresponding to the insurance they bought. To buy these insurances, they would have to do a boring task (crossing every letter 'e' in a paper regarding a subject they could not understand) for a certain amount of time: 2.5 minutes for three incorrect guesses, 5 minutes for 6 incorrect guesses, 7.5 minutes for 9 incorrect guesses and 10 minutes for 12 incorrect guesses. After these instructions, respondents indicated whether they wanted to buy insurance and the amount of wrong guesses they thought they were going to make. In an unrelated task, respondents also filled out the Dispositional Greed Scale.

We expected people in the loss condition to believe that they would make more mistakes, and therefore to be more inclined to buy a more extended insurance than people in the no-loss condition. Furthermore, we expected a quadratic relation between greed and the expectancy to make mistakes, and therefore to buy a more extended insurance. Finally, we expected to find an interaction between the condition and respondents' greed score, so that their greed score would have less of an impact in the no-loss condition than in the loss-condition.

A moderated mediation analysis partially confirmed our hypotheses. More specifically, both the condition ($B = -.54$, $t(97) = -1.932$, $p = .06$) and quadratic dispositional greed ($B = .02$, $t(97) = 1.973$, $p = .05$) were related to people's predicted amount of mistakes. However, there was no interaction between both variables. Thus, greedy people indeed predicted to make fewer mistakes in the no-loss condition, but the effect of dispositional greed was not

alleviated. Both dispositional greed and the condition only had main effects on the amount of mistakes predicted. This prediction was indeed further related to the amount of insurance people wanted to buy ($B = .25$, $t(98) = 2.01$, $p > .05$) (figure 1).

Insert figure 1 about here

Conclusion

In three studies we show that loss prevention has a big impact for greedy people in consumer decision making, especially towards insurances and warranties. A prevention focus is an essential part of dispositional greed, and has an even larger impact than the promotion focus, resulting in bigger loss aversion. Furthermore, when greedy people buy products, they are more inclined to buy an extended service contract and are more inclined to buy a more extensive insurance. However, they are not willing to pay more for it, as it probably contrasts with their promotion focus. Finally, when they are confronted with a history of non-loss, the effect of their willingness to prevent losses is lessened but not eliminated.

More research is needed to explain what happens with non-greedy people. Why is it that, when non-greedy approach the endpoints of the scale, they are also more prone to buy insurances and warranties? This cannot be explained by a prevention focus, as there is a simple linear relation between dispositional greed and prevention. Possibly an explanation lies in the fact that they also score lower on materialism. Perhaps their very low greediness and materialism is linked to a type of anti-consumerism. If so, their inclination to buy insurances is a not a way to prevent losses when they occur, but an approach to prolong the lifetime of a product. Thereby they would have to buy and thus consume less products, corresponding to their lifestyle and values. Further research is needed to test this one possible explanation and give more insight in low-greedy people's values and lifestyles, linked with their consumption patterns.

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TABLE 1

Study 1: Effect of Dispositional Greed on Loss Aversion

	Beta	SE	t	p
Constant	.18	.09	2.14	.034
Dispositional Greed	.19	.02	2.35	.020
F (df)	5.53 (1, 151)			
R ²	.035			

TABLE 2

Study 2: Effect of Dispositional Greed on ...

Type of insurance	Beta	SE	t	p
Constant	3.23	.81	3.98	.000
Dispositional Greed	-.97	.46	-1.82	.071
Dispositional Greed ²	.95	.06	1.79	.076
F (df)	1.66 (2, 102)			
R ²	.013			

Purchase likelihood	Beta	SE	t	p
Constant	7.51	1.45	5.17	.000
Dispositional Greed	-1.22	.82	-2.34	.021
Dispositional Greed ²	1.26	.11	2.42	.017
F (df)	2.95 (2, 105)			
R ²	.035			

Attitude towards the warranty	Beta	SE	t	p
Constant	4.91	.80	6.14	.000
Dispositional Greed	-1.06	.46	-2.06	.042
Dispositional Greed ²	1.20	.06	2.33	.022
F (df)	3.51 (2, 105)			
R ²	.045			

FIGURE 1

Study 3: Effect of Dispositional Greed and Loss History on Predicted Errors and Purchase Likelihood

