OVERCONFIDENCE AND ETHICAL DECISION MAKING

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ABSTRACT

Many factors can influence a person's decision making behavior in ethical choice situations. Some of those factors are reviewed and identified to position the reader for the contribution of this paper – arguing for the significant role that overconfidence plays in decision making tasks resulting in unethical choices of action. Propositions are developed and provided as suggests for future empirical work.

INTRODUCTION

How and why people make ethical and unethical decisions continue to be challenging questions. Day after day in the business news there are reports of unethical and illegal behaviors by a seemingly un-endless stream of executives and money managers who were clearly doing wrong. Some observers are wondering if the wrong-doing is becoming more prevalent and wondering how we might improve ethical behavior. Others suggest that there is "nothing new under the sun, especially in the world's oldest profession – separating people from their money" [16].

The majority of people want to behave ethically and want to see others do likewise. Thus, they are interested in obtaining better understanding of how and why individuals behave unethically. Such understanding could help those who are concerned with reducing the amount of unethical behavior. This research works towards the broader goal of enhancing our understanding of the various influences on unethical behavior. The specific purpose is to integrate theoretical and empirical findings in business ethics decision-making research with findings in confidence and overconfidence in decision-making and to identify hypothesized linkages between overconfidence and unethical behavior.

BUSINESS ETHICS, OVERCONFIDENCE AND ETHICAL DECISION MAKING

Business Ethics

The field of business ethics is commonly divided into two broad branches, normative ethics and empirical/descriptive ethics [30]. Normative ethics is addressed primarily by moral philosophy and theology and is concerned with ideas about how people ought to act. Descriptive and empirical ethics is addressed by business scholars including social and behavioral scientists. Underlying this domain of research is a concern with how people ought to act. However, the most direct concerns of these scholars are questions about how people actually engage in ethical decision making. In addition to trying to understand how people engage in ethics-related decision making, these researchers also focus on questions associated with explaining why people choose certain actions, and, at times, on predicting when people will behavior certain ways.

Normative business ethics research has primarily focused on four major divisions [12]. The first is a *societal* level group concerned with questions of the relationships among the chief institutions of society. This is important because it addresses questions concerning the nature of the corporation and the roles corporations ought to have. The second is a *stakeholder* level group concerned with questions revolving around the relationships between the firm and those primarily external groups affected by and which can affect the company. The third is an *internal policy* perspective in which researchers are concerned with what ought to be the relationship between the organization as an entity and the employees. The fourth is concerned with a set of questions revolving around the moral life of employees and what their relationships ought to look like with other employees.

A great deal of research in the empirical and descriptive domain of business ethics can also be characterized as focusing on issues relating to societal concerns, stakeholder concerns, internal policy concerns, and employee concerns. However, much of the research grows out of an organizing perspective in which understanding individual ethical decision-making processes takes center stage. This empirical and descriptive domain of business ethics scholarship relies on methods derived from theoretical (theory development and/or theory-driven), observational, experimental, and, in other ways (such as surveys of managers' opinions concerning business practices as more or less ethical), empirical traditions.

Scholarly models of individual ethical decision making have received a great amount of attention as both the foundation of a growing body of empirical business ethics research and as source of behavioral prescriptions for improving ethical behavior in organizations [37]. Many of the models of ethical decision making behavior rely on the four-stage ethical decision making process conceptualized by Rest [34] [35]. He suggests a model in which individuals must first recognize there is a moral issue at hand. Upon doing so, a person will make an ethical judgment and will establish moral intent. The final stage is action, or engaging in the ethical behavior. Jones expanded the model with the inclusion of a "moral intensity" element in the decision-making process [19].

Scholars have identified many variables that contribute to, or influence, ethical decision making in organizations [19] [30] [47]. When trying to model the ethical decision making process, most researchers have included two big categories of antecedents to ethical behavior. The first is the individual. This category includes all the traits, characteristics, cognitive abilities, thinking patterns, and other dimensions of particular individuals that contribute to their decision-making. Individual differences in values, morals, and other beliefs can greatly influence the outcome of their decisions. Differences in moral awareness, moral judgment, and moral intent, will lead to differences in ethical behavior. The second big category of influences on ethical behavior is the situation, or extra-individual influences on ethical decision-making process. The situation in a particular organization may influence the decisions people make within that organization. The type of language used, the metaphors employed, the reward and punishment systems, the ethical climate, the ethical leadership of top management, and related situational factors can and do influence individuals' decision making processes [47]. Many other situational-type factors have also been examined. For example, Christensen has argued the importance of law in ethical decision making, particularly in reference to the recognition of potential moral issues in given decision-making contexts [7]. One often-cited model of ethical decision making focuses on the interaction between an individual's cognition and the characteristics of the situation [46]. Since this time, many scholars have empirically tested components of the models and have also added or otherwise modified the models. For this paper, the major thrust is on individuals' overconfidence and how that may influence their decision making in ethical contexts in organizations. As such, it is primarily within the individual influences, particularly as it relates to the four steps outlined by Rest, that implications are discusses. However, there are also some indirect implications for the role overconfidence may play in ethical decision making that arise from situational factors. In particular, the question of how situational factors may make overconfidence more or less likely can have importance for ethical decision making.

Confidence and Overconfidence in Decision Making

Most assuredly, confidence is a desirable characteristic of organizational decision makers. From a dispositional viewpoint, those who are more confident (have more belief in themselves) can be described as being more decisive, more firm, more resolute, and less doubtful [44]. Confidence appears to be moderately related to cognitive abilities [43] [44] and somewhat related to the personality factor of "openness to new experiences" [32]. Confidence is one of only three major factors (the other two being skill and desire) contributing to an individual's performance in the workplace [42]. The beneficial traits of active hope, self-efficacy, optimism, and resiliency share a common confidence core [42]. As such, confidence contributes to increased job satisfaction and increased workplace subjective well-being [42].

Confidence is also important for its role as a metacognitive function. Metacognitive functions deal with one's awareness of one's learning and knowing/not knowing. As such, many scholars see confidence judgments as particularly worthy of study when concerned with decision making processes. The "metacognitive ability to appraise the relevance of one's own beliefs about the available evidence (and one's own performance) is an important factor in effective decision-making" [44, p.963]. In fact, it is suggested that when we cannot be sure that a belief is true, good thinking will help us to come to some judgment about how confident to be in that belief and that "appropriate confidence is, in most cases, a more realistic goal than certainty" [3, p. 70]. So, while having confidence in one's judgments has many positive and beneficial consequences, so does having an appropriate level of confidence given the available information and context. Furthermore, while there are problems associated with both under-confidence and overconfidence, a first look at some high-profile wrong-doers suggests that overconfidence is more directly associated with unethical behavior.

For the past thirty years scholars have been examining and reporting on the overconfidence phenomenon. There are competing hypotheses concerning the existence, extent, causes, and consequences of overconfidence. First, some ecological theorists suggest that overconfidence reports are due to methodological issues and that people are adapted to their environments such that they really do not make biased judgments [13] [20]. It follows that those who don't believe the existence of overconfidence believe that there is no "extent" of overconfidence. Most scholars, however, believe that the very large number of studies showing overconfidence indicates that something more than methodological issues is underlying them. Many believe that the evidence suggests the extent and consequences of overconfidence are quite substantial.

In a study of over 2000 managers, when asked to give answers in terms of a range for which they believed would include the right answer 90% of the time (90% confidence intervals around an answer) less than 1% of the managers were not overconfident [39]! These authors make the important point that not knowing about some industry question, or any other question for that matter, should not excuse one from poor performance on a confidence interval question. Rather, those who know more about the question should have narrower confidence intervals and those who know less should provide larger confidence intervals. They suggest that the extent of this type of overconfidence is great and that this metacognitive error is worthy of trying to correct in the workplace.

Not without controversy, overconfidence has most often been explained as a human information processing challenge [2]. Several have suggested causation associated with anchoring and adjusting heuristics [10]. Others have suggested causation associated with cognitive optimism [8], motivational issues [26], and illusion of knowledge [15], and a variety of other cognitive biases [21] [14] [45]. There has been a great amount of scholarly work examining overconfidence in decision-making. The methods of studying overconfidence and even the conceptualizations of overconfidence have varied. There appear to be three main forms of overconfidence, including over-placement (Lake Wobegon form), over-precision, and over-estimation [24] [28]. Over-placement is a judgment against comparison others in which individuals tend to assess themselves (or their teams, their groups, their families, etc.) as better than others. Over-precision is the finding that individuals, when asked to put confidence intervals on responses requiring a numerical answer, predictably indicate confidence intervals that are too small [41]. Finally, over-estimation can be over estimating one's actual abilities, performance, levels of control, or chances of success [28]. Some research examining self-enhancement treats over-placement and over-estimation as examples of one concept, i.e., self-enhancement, resulting from the same underlying causes [23]. Since people have imperfect information about their own performances and abilities people's estimates of these are regressive [28]. Furthermore, since people have even less information about the performance and abilities of others, their estimates of them are even more regressive.

Overconfidence has been provided as a cause, reason, or explanation for many problems including excess entry into industries [6], the cause of war [17] [18], financial failure of entrepreneurs and stock market bubbles [25] [31], labor strikes [29], failed acquisitions [9], lack of sufficient use of decision aids [40], and many others. While information processing issues are often identified in business ethics models, none of the models specifically identify "overconfidence" as one of the biases. Overconfidence is brought up in a few articles on business ethics but it is always a small mention of only one or two paragraphs. Yet understanding if and how overconfidence influences ethical decision-making processes can inform us in how to reduce our susceptibility to the effects. Many Enron-era scandal figures expressed surprise that anyone would question the morality, let alone legality, of their various activities [33]. Their confidence in themselves led to confidence in their ethical correctness. Mintzberg has explained that MBA graduates, who sat in classrooms for a couple of years, really don't learn much about the practice of management [27]. This may contribute to the overconfidence of many managers.

Overconfidence and Unethical Decision Making

Rest examines the large amount of research that has been done on the four component theory of moral reasoning and finds that it has been very useful for studying individual ethical decision making [35]. The four components model distinguishes among moral awareness, moral judgment, moral motivation, and action. Each is briefly explained below and associated with propositions.

Moral awareness is considered the first stage in ethical decision making. This involves an interpretive process wherein a person recognizes that an issue exists [47]. It is believed that there are individual differences in how "ethically sensitive" different people will be but that training and experience can help increase one's ethical sensitivity [47]. Others have focused on issue characteristics and their influence on moral awareness. For example, Jones suggests that the magnitude of consequences, concentration of effect, probability of effect, temporal immediacy, social consensus, and proximity will combine to create a particular "moral intensity" to the issue at hand [19]. The greater the moral intensity of an issue or particular context for a decision, the greater the chance that people will be become morally aware of the issue(s).

Overconfidence may negatively influence moral awareness in a couple of ways. The first is in the ceasing to search for, or to ask questions regarding, additional attributes of decision tasks (such as ethical issues to address). If one decides on something that one is going to do and is very much confident in that decision, there will be no need to continue to think about the decision or its consequences. This could preclude becoming aware of potential ethical characteristics involved in the course of action. Thus, may affect our search for additional characteristics about a decision task and thereby keep us from ever even considering that there may be a moral issue involved. Overconfidence may also influence moral awareness by influencing the cognitive judgment that there is an ethical component to the decision. One may make a decision and then ask "are there any conflicts of interest I need to consider here?" and come up with a "no" response more often if one first started out overly confident in that decision. This is distinct from actually bypassing, or overlooking, the consideration that there might be ethical elements involved in the decision and, instead, operates on the judgment that is made when there is a consideration. Thus, even if we consider whether or not there are some sort of ethical considerations to be aware of, for example, conflicts of interest, overconfidence may make us more likely to search out information that favors our confidently held prior conclusions as we engage in confirmatory search processing. We are more likely to rely on reasons supporting our decision than those pieces of information that contradict our decisions. Also, it may be that overconfidence is one of the larger underlying causes of so many individual executives' failure to recognize the ethical issues involved in many decisions associated with several of the big business ethics scandals of the past decade.

Proposition 1a: When people are overconfident in a particular decision, they will be less likely to become aware of moral issues.

Proposition 1b: When people are overconfident in a particular decision, they will be less likely to judge that there are ethical concerns within the decision task.

Rest's moral judgment is primarily based on Rest's theoretical ideas about cognitive moral development [22] [47]. When a person is aware of a moral issue, that person will begin to make a judgment. People's ethical reasoning can be at a pre-conventional stage in which punishment and reward are the primary indicators of right and wrong. While there is not a lot of "reasoning" per se going on at this level, an overconfident person who is reasoning at this level might be likely to judge at an overly confident level that reward will follow the behavior.

Proposition 2a: When managers are reasoning at the preconventional level, overconfidence will lead them to believe that there is going to be reward attached to the unethical behavior to a greater extent than which reward would actually be associated with the behavior.

The second in three possible stages of ethical reasoning, people can ethically reason at a conventional level. At a conventional level people's conceptions of right and wrong are externally oriented such that they rely on expectations of others to ascertain what is right and wrong. Here, overconfidence could cloud their view of what other's expectations are with respect to the decisions they are making.

Propostion 2b: When people are reasoning at conventional levels, overconfidence will make them more likely to believe that others think is acceptable to decide as they do on issues of ethical concern.

The third stage of moral reasoning for relatively more advanced and is called "principled" reasoning. It is not clear how overconfidence might influence ethical decisions if the person is reasoning at this "principled" level. Most managers are at the conventional level of moral reasoning,

Moral motivation (ethical intention) and behavior generally are said to stem from awareness and judgment of ethical issues. However, moral behavior does not always follow from explicit moral reasoning processes [4] [5] [38]. Moral motivation is the "degree of commitment to taking the moral course of action, valuing moral values over other values, and taking personal responsibility for moral outcomes" [36, p.101]. Confidence and commitment level can be easily construed as being somewhat related constructs. When people are committed to a particular course of action, generally they are confident that that is the course of action they ought to be taking.

Proposition 3: When managers are overly confident in their abilities to make ethical judgments, they will be overly committed to their choices involving ethical issues (both poor choices and good choices of action).

CONCLUSION

Much of the scholarly research on business ethics has focused on ethical behavior and the antecedent variables that influence decisions towards or away from ethical directions. We also see a great deal of work on the influence of contextual variables such as the organization's culture, codes of conduct, sanctioning mechanisms, training, and others. Overconfidence, while not addressed in the business ethics literature, may be a rather important part in explaining how it is that good leaders sometimes end up engaging in unethical behaviors, often without a good deal, or any, forethought about the ethical issues or the consequences of the behaviors. There has been very little attention to overconfidence in the business ethics literature. This paper intends to identify overconfidence as a potentially significant contributor to unethical behavior in the work place.

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