TO ACCEPT OR REJECT A CUSTOMER'S BUSINESS? THE INTERACTION OF CUSTOMER QUANTITATIVE MERIT, CUSTOMER REPUTATION AND THE DECISION-MAKER'S NEED FOR DISCRETION

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in partial fulfillment of the requirements for
The Degree of
DOCTOR OF PHILOSOPHY
May, 2006

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May, 2006

TO ACCEPT OR REJECT A CUSTOMER'S BUSINESS?

THE INTERACTION OF CUSTOMER QUANTITATIVE

MERIT, CUSTOMER REPUTATION AND THE

DECISION-MAKER'S NEED

FOR DISCRETION

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PREFACE

This dissertation employs two research methods – in-depth interviews and an experiment – to explore seller decisions to accept or reject business from a customer. In-depth interviews were conducted to identify the quantitative and subjective factors that influence customer selection decisions in retail bank lending. Among the factors identified to influence loan officer decisions to approve or decline a loan are customer quantitative merit, customer reputation, and the decision maker's need for discretion. These factors are proposed to comprise a three-way interaction that explains the acceptance or rejection of a customer's business (i.e., customer selection likelihood). The three-way interaction hypothesis is tested using an experimental scenario in a commercial lending context. The experimental scenario was administered to commercial loan officers. A valid and reliable scale for the need for discretion was also developed based on the literature and the results from the interviews. To the author's knowledge, the present study is the first to investigate at the individual decision-making level, factors influencing whether to accept or reject a customer's business. The results are discussed in terms of their generality to other marketing settings in which the seller decides whether to sell to a customer.

ACKNOWLEDGMENTS

Words cannot express my sincere appreciation to my friend and mentor, Dr. John Mowen, for inspiring me to ask interesting questions and to relish the journey in pursuing their answers. My heartfelt gratitude also extends to Dr. Tom Brown and Dr. Karen Flaherty-Pappas for encouraging me to realize my potential as a researcher and a teacher. I also thank Dr. David Carter for his assistance throughout the dissertation process. I wish to thank all the faculty members and doctoral students in the marketing department at the Spears School of Business at Oklahoma State University for contributing so much to my educational and professional development.

I wish to pay special tribute to my wife, Tara, whose devotion and love has allowed me to persevere throughout graduate school, and to follow my Savior Jesus Christ. I will always cherish the memories of wrestling, laughing, and playing with my two boys after long days at school. For this, I thank my children, Tanner and Karsten, for bringing so much perspective and meaning to my existence and providing a happiness that only children can bring. I also thank my good parents, John and JoAnn, for their unconditional love and support. I am grateful to supportive friends who have become very much a part of our home and have given us joyous memories. Finally, I thank my Heavenly Father for entrusting me with rich blessings as well as providing me an eternal perspective.

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LIST OF SYMBOLS

α	Cronbach's alpha – a measure of internal consistency reliability
(r)	item is reversed scored during the data coding process.

NOMENCLATURE

ANCOVA	Analysis of Covariance
ANOVA	Analysis of Variance
AVE	Average Variance Extracted
CC	Consumer Compliance Examination
CE	Customer Equity
CFA	Confirmatory Factor Analysis
CLV	Customer Lifetime Value
CPM	Customer Portfolio Management
CR	Composite Reliability
d.f.	Degrees of Freedom
EFA	Exploratory Factor Analysis
FDIC	Federal Deposit Insurance Corporation
FICO	Fair Isaac Corporation
NFD	The Need for Discretion
SS	Safety and Soundness Examination
SEM	Structural Equation Modeling
3M	3M Model of Motivation and Personality

CHAPTER I

INTRODUCTION

How to reduce the likelihood of acquiring an unprofitable customer is an important issue for marketing managers. Just as it is vital for firms to identify their best customers and to find new profitable customers, it is equally important to pinpoint bad customers and to avoid attracting future customers that will be liabilities on a firm's balance sheet (Cao and Gruca 2005; Ittner and Larcker 1998; Venkatesan and Kumar 2004). Acquiring the wrong customers is a predicament referred to as adverse selection (Cao and Gruca 2005). Once thought to be constrained to the marketing of loans and insurance, adverse selection is an issue that all companies confront (Reichheld and Schefter 2000; Reichheld 1996).

Adverse selection outcomes can occur with new customers or with existing customers when cross-selling products (Cao and Gruca 2005). To reduce its occurrence, firms employ a screening process to "weed out" bad customers. For example in banking, screening processes to evaluate customer loan requests vary in the information utilized and the use of human discretion. First, banks might evaluate customer loan requests using credit scoring systems that leave little if any discretion to human judgment. Alternatively, banks might employ a judgmental credit scoring system that combines an evaluation of the customer's quantitative information (e.g., credit score) with the loan officer's decision-making discretion. The present research adopts a judgmental credit

scoring system to explore individual decision-making processes in screening customers and making customer selection decisions.

Previous research exploring the individual's role in customer selection found that salespeople who took a systematic approach to qualify and acquire customers performed better than their counterparts (Szymanski and Churchill 1990). Acquiring the "right" customers leads to increased firm performance (Leigh and Tanner 2004; Reinartz, Krafft, and Hoyer 2004). Taken together, these findings indicate that individual employees who exhibit job behaviors focused on proactively managing customer relationships can contribute to the overall valuation of the firm (Gupta, Lehmann, and Stuart 2004). More commonly, discussion of measures to exercise caution in selecting customers has been reserved for markets of risk products, or when the purchase of the product imposes more risks on the seller than on the buyer (Cao and Gruca 2005). Recent application of modern portfolio theory suggests that firms should manage their customer portfolio as they do an investment portfolio, assessing the risks of current and prospective customers before investing resources into these relationships (Ryals 2003). It is when the "relationship risks" borne by the seller exceed those of the buyer that the characteristics of buyer-seller exchange can be examined.

In the marketplace there are various exchange conditions between buyers and sellers (Houston and Gassenheimer 1987). Typically in market exchanges, both the buyer and the seller evaluate the exchange partner as well as the terms and conditions of the exchange. Based on these buyer-seller evaluation judgments, two perspectives of the market exchange emerge. The first perspective, referred to as a buyer-choice market exchange, occurs when the seller desires to make a sale and the risks of exchange are

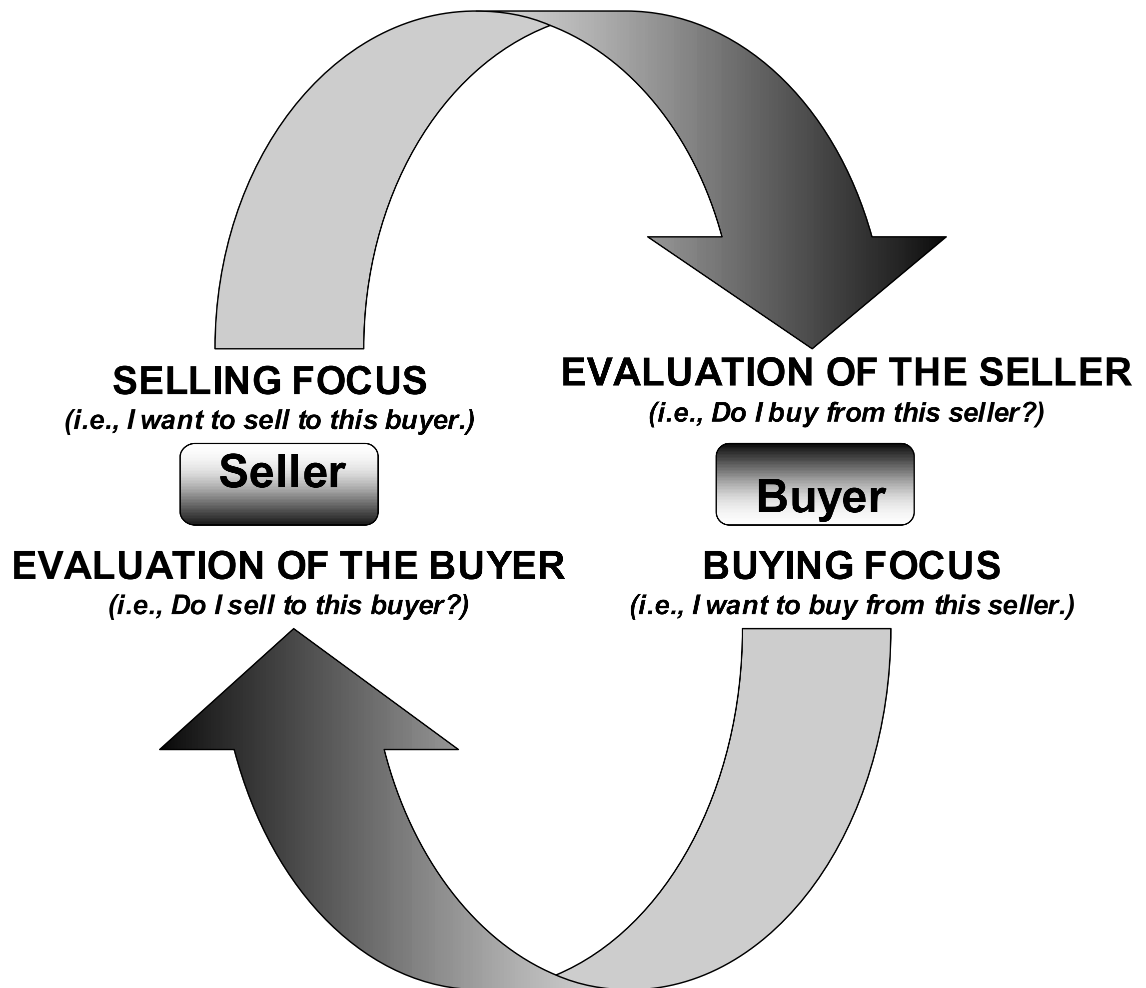
greater for the buyer than for the seller. When the conditions of the exchange are buyer-choice, the buyer must decide whether or not to complete the transaction with the seller based on an evaluation of the terms offered and other product alternative choices. This perspective of buyer-choice market exchanges has received the most attention in the marketing literature. A second perspective, however, can explain a number of other market exchanges. This perspective, referred to here as a seller-choice market exchange, occurs when the buyer desires to buy from a particular seller and the risks of exchange are greater for the seller than for the buyer. When the conditions of an exchange are "seller-choice," the seller evaluates the buyer and then decides whether to accept or reject the buyer's business.

Figure 1-1 illustrates these two different exchange perspectives. There are a number of examples of market exchanges where, because of the imposed risks on the seller, the seller decides whether the customer receives the product. For example, services such as banking, insurance, real estate, education, healthcare, and private clubs or fraternities all involve the seller forming an evaluation about the buyer and then deciding whether to accept business from the buyer and, if so, under what terms and conditions. The present research explores factors impacting such seller decisions.

While various literature streams acknowledge the importance of screening customers, previous work has not yet explored the individual and situational factors that influence specific seller decisions about whether to accept or reject business from a customer. For example, the industrial marketing and supply chain literature suggests criteria for evaluating suppliers and channel members. This literature, however, does not explore specific factors that influence individual decisions regarding selecting channel

Figure 1-1

Buyer-Seller Perspectives



partners (Wathne and Heide 2004). Also, recent research that has concentrated on measuring customer profitability (e.g., customer lifetime value) does account for the present and future value of the customer (Rust et al. 2004; Venkatesan and Kumar 2004) and implies that the selling firm should safeguard resource investments in its customer base by first determining the quantitative and subjective value of each customer. To the author's knowledge, work in this area has not investigated the factors that influence the decision-making process of determining the value of a specific customer and whether the business from the customer should be accepted or rejected. Furthermore, the personal selling and sales management literature suggests that salespeople with rigorous standards in qualifying customer prospects experience increased sales performance (Szymanski and Churchill 1990). At the conclusion of their work however, Szymanski and Churchill issued a call for future research into how different factors influence customer-selection decisions. This research represents a response to this call.

Research Questions and Design

This dissertation employs two methods – in-depth interviews and an experiment – to explore seller decisions to accept or reject business from a customer in addressing four research questions.

1. What quantitative and subjective factors influence customer selection decisions in the bank lending industry?

2. What influence do loan officers have on customer-selection judgments?

3. What are the joint effects of customer quantitative merit, customer reputation, and the decision-maker's need for discretion on customer selection likelihood?

4. What are the intervening effects of customer risk assessment, attitude toward the customer, and perceived value of the customer on customer selection likelihood?

A qualitative study (i.e., Study 1) was employed to answer the first two research questions. This study aimed at exploring the quantitative and subjective factors that influence customer selection decisions and the role of the loan officer in making these decisions. The context of the study was retail bank lending. The format consisted of sixteen in-depth interviews with bank executives and loan officers and five additional interviews with state and federal bank examiners and regulators. Based on the results of these interviews, the researcher developed the remaining two research questions.

Research questions three and four investigate the factors that influence individual decisions whether to accept or reject a customer's request for a product. Among the factors believed to influence seller decisions to accept or reject a customer's business are customer quantitative merit, customer reputation, and the decision-maker's need for discretion. These factors are proposed to comprise a three-way interaction that explains the acceptance or rejection of business from a new or existing customer (i.e., customer selection likelihood). The three-way interaction hypothesis is tested using an experimental case scenario design which involved embedding a fictitious customer portfolio in a survey. In addition, exploratory relationships are tested among three process variables believed to influence the decision. The experimental scenario was piloted with commercial loan officers and with MBA/undergraduate students and then administered to commercial loan officers across various types and sizes of banks in five U.S. states. A valid and reliable scale for need for discretion was also developed based on the literature and the results from the interviews.

Results and Contributions

The findings of in-depth interviews with bank executives, bank loan officers, and bank examiners revealed insights into factors that influence the customer selection decision process. First, individual bank loan officers have the greatest influence on customer selection decisions when the customer's request is for commercial lending products. This influence is most direct when the bank loan officer is deciding on a small commercial loan that falls within a prescribed lending limit or loan authority. Second, bank officers exhibit different behaviors when evaluating the information of prospective borrowers because of an individual's chronic need for discretion, or the propensity to seek autonomy from organizational norms when making decisions. Third, various types of information are used to evaluate and decide the outcome of a customer loan request. The types of information found to be most important when evaluating a small business loan request were information about the borrower's quantitative situation and information about the borrower's character or reputation. Finally, economic market conditions and the presence of federal and state regulations influence customer selection practices in banking. The findings from the interviews were critical in the design of the experimental model, including the measurement and manipulation of the model constructs. Based on a cue diagnosticity perspective, hypotheses were proposed and tested using an experimental case scenario design.

Based on a sample of 262 commercial loan officers, support was found for a three-way interaction of customer quantitative merit, customer reputation, and the decision-maker's need for discretion. The pattern of the interaction, however, did not follow the logic and argument of a cue diagnosticity perspective. The results, however,

do support the prediction that individuals with a high chronic need for discretion are influenced by customer reputation information, whereas individuals with a low need for discretion are not influenced by reputation, but instead by the borrower's credit score. Contrary to the hypothesis, these results were limited to situations in which the loan officer evaluated customers with a more favorable credit score. Exploratory analyses were also conducted and main effect relationships on customer selection likelihood were found for customer risk assessment, attitude toward the customer, and the perceived value of the customer.

Based on these results, this work contributes to the marketing literature in three ways. First, this research adopts a seller-choice process (versus a buyer-choice process) perspective to explore the factors influencing a decision whether to accept a customer's business request. Second, this research identifies and develops a scale for the individual's chronic need for discretion to explain behavioral tendencies in how customer information is evaluated and whether a customer's request is approved. Third, this research explores a model of the customer selection process that accounts for the effects of customer risk assessment, attitude toward the customer, and perceived value of the customer on customer selection likelihood.

Organization of the Dissertation

This dissertation contains six chapters. Chapter II provides a broad conceptual development discussion that describes the unique perspective of seller decisions in customer selection. Also included in this chapter is a review of the relevant literature,

including the sales and sales management, business-to-business marketing, supply chain management, customer profitability, and “firing” the customer literature.

Chapter III presents the qualitative in-depth interviews with bank executives, bank loan officers, and state/federal regulators. The results of these interviews are presented thematically around each of the study’s research questions.

Chapter IV describes the experimental study, introduces a proposed model of individual and situational factors believed to influence customer selection decisions. A conceptual framework is presented which describes the theoretical foundation for the model. Each of the model’s constructs are defined and the formal hypothesis is presented. The experimental methodology is outlined, including the scale development of the decision-maker’s need for discretion, the development and pilot testing of the scenario, the research design, and the analytical techniques used in testing the hypothesis. The results and findings from this study are discussed based on the study’s research questions.

Chapter V includes a general discussion of the results and the managerial and research implications. Research limitations and an agenda for future research conclude Chapter V.

CHAPTER II

CONCEPTUAL DEVELOPMENT

This chapter provides an overview of the nature of customer selection in marketplace exchanges and reviews the literature streams that are the foundation for the experimental study. This review is organized into three sections. First, a description of the different classes of marketplace exchanges is presented to describe the unique perspective of seller-choice decision processes. Second, examples of various contexts surrounding the class of exchanges involving seller decisions to accept or reject a customer's business are presented. Finally, the contributions of previous literature are discussed.

Marketplace Exchanges

There are various classes of exchange in the marketplace. Buyers and sellers evaluate and make decisions regarding with whom to transact business. Buyer and seller decisions regarding the terms and conditions of an exchange (i.e., whether to buy or to sell) reflect the need-satisfying purpose of exchange (Houston and Gassenheimer 1987). For example, buyers seek to obtain goods and services to satisfy their needs. Likewise, sellers choose to which buyers and sellers to provide their goods and services. Figure 2-1 depicts four marketplace situations involving buyer-seller exchange dyads. First, in one

class of exchange, buyers decide to which potential buyers they will refer or recommend goods and services. The figure refers to this class of exchange as Quadrant I (Should I refer this friend/associate?). Examples of buyers referring other buyers to satisfy their mutual needs of obtaining goods and services are buyer-hosted parties (e.g., Tupperware and Pampered Chef) and multi-level marketing schemes (e.g., Amway). In these examples, the buyers consider which friends to invite to a product party or which associates to introduce to a multi-level marketing program.

Second, arguably the most frequent class of exchange involves buyers choosing a seller to patronize. In Figure 2-1, this class of exchange is shown in Quadrant II (i.e., Which seller should I buy from?). Examples of Quadrant II exchanges span many consumer goods and services contexts (e.g., grocery stores, restaurants, airlines).

There are also seller-seller exchanges, in which, sellers decide from which seller/supplier to obtain needed materials and services in order to provide their products and services. Quadrant III in Figure 2-1 refers to this class of exchange (i.e., Which supplier should I use?). Examples of this class of exchange include the decision by Dell, the computer hardware company, to purchase microprocessors from Intel, or a hospital's decision to purchase materials from specific medical supply companies.

Because of the increasing awareness of the risks of adverse selection, attention focus has been directed to how sellers decide from which customers to accept business. This class of exchange is depicted in Figure 2-1 as Quadrant IV (i.e., Should I sell to this customer?). The present work focuses on this class of market exchange. Example contexts where the seller makes decisions regarding whether to sell to the customer include banking, real estate, insurance, healthcare, legal services, education, and private

clubs/affiliations. While commercial retail bank lending was chosen as the primary context for this type of exchange in this study, the following examples are taken from real estate, education, and consumer financial services. The next section elaborates on the contexts in which a seller makes a decision regarding whether to accept the buyer's exchange request.

Figure 2-1

Buyer-Seller Exchange Classes

Exchange Partner

Evaluator/ Decision Maker	**Buyer**	**Seller**
Buyer	**I.** **Should I refer this friend/associate?** Examples: • Pampered Chef • Tupperware • Amway	**II.** **Which seller should I buy from?** Examples • Consumer good products • Restaurants • Airlines
Seller	**IV.** **Should I sell to this customer?** Examples: • Bank lending • Real estate • Education • Insurance • Private clubs	**III.** **Which supplier should I use?** Examples: • Computer manufacturer • Automobile manufacturer • Hospital purchasing department

Sample Contexts

Real estate, consumer financial services, and education are contexts where the seller decides whether to extend an offer or opportunity to exchange with a buyer. In these and other contexts although the buyer may be the party that ultimately decides whether to accept the terms of the exchange the seller must first deem the buyer acceptable; only then will the seller extend an offer describing the terms and/or conditions of the exchange agreement.

In real estate the seller, both as a broker/agent and as the real-estate property owner, decides whether, and if so how, a buyer is serviced. Real estate agents/brokers may determine how time, effort, and promotional resources are allocated among their clientele. Such decisions are influenced by the perceived profitability of the customer based upon the customer's credit worthiness, purchase/sales price, and time urgency. The depth of relationship between an agent and a client may contribute to how time, effort, and financial resources are allocated. For example, an agent may be determined to service one customer more thoroughly than another because of personal or business relationship ties. Similar situation occurs when a property owner evaluates multiple buyers before selling a piece of property. Besides considering the offered purchase price, a seller may consider the buyer's credit worthiness, the buyer's intentions and interest in the property, the contract time frame, and the buyer's reputation.

Another context where buyers must meet certain qualifications is that of retail and wholesale consumer financial products. In these industries, a strong emphasis is placed on maintaining personalized information for each current and potential customer in order to screen and select customers (Wyner 2000). It is common practice for financial service

companies to extend offers to customer segments who meet demographic, behavioral, and psychographic criteria and who also are likely to respond and be approved to receive the offer (Cao and Gruca 2005). For example, a credit card offer may be targeted to customers who use credit frequently of credit usage behavior or who are believed to have a need for a new credit card (i.e., available share of wallet). Then, based on the customer's credit application, the customer is declined, or is granted specific interest rates, and annual fees and assigned to a specific level in a rewards programs. Because of recent developments in credit scoring technology and systems, these decisions are frequently made automatically and the role of individual employee discretion has diminished. In the area of insurance, however, the discretion of the agent plays an important role in qualifying new policies or re-pricing existing polices. A recent study reported that 92% of the largest personal automobile insurers in the U.S. use credit scores to qualify customers for automobile insurance; however, only 50% use insurance scores for both underwriting and pricing (Bray 2001). This study's findings suggest that while automobile and home insurers are increasingly using credit scores to assess the risk of each customer as a basis for selection customers, decision-makers also weigh other factors, including the applicant's driving history, previous claims, amount of outstanding debt, and length of time with the insurance company.

A third context where seller-choice exchange occurs is in education, where, at all levels, "buyers" (i.e., students and their families), may apply for admission into an educational institution or program. Admission decisions ultimately are based on a number of factors including for example, academic achievement, extra-curricular activities, relationship ties to the institution (e.g., alumni), and social standing in the

community. In fact, admission practices have been highly controversial. Recently the U.S. Supreme Court heard two cases involving the practice of weighing minority applicants more favorably in the undergraduate and law school admissions at the University of Michigan. Arguments both in support of and in opposition to admission practices that evaluate "soft" measures of the predicted success and contribution of the applicant in academic programs were presented (McFeatters 2003). President George W. Bush asked the federal government to file a friend-of-the court brief against the University of Michigan to iterate that giving preferential treatment to African American, Hispanic, and Native American applicants was unfair. Opponents of preferential treatment claimed that the preferential scoring system increased the odds of a minority applicant's being accepted at Michigan to be 234 times greater than for non-minority applicants with the same grades and test scores (McFeatters 2003). Parties in support of the University of Michigan argued that a point system for minorities is no different from the widespread practice of giving special consideration to the children of alumni, large donors, public officials, and faculty and staff, and to athletes from underrepresented parts of a state (McFeatters 2003). The U.S. Supreme Court ruled in favor of the use of minority class when evaluating law school applicants, but ruled against the same practice for undergraduate admissions (National Public Radio 2003).

In a formal statement regarding these cases, Justice Sandra Day O'Connor referred to admission practices which use "soft" variables such as the enthusiasm of an applicant's recommenders, the quality of an applicant's undergraduate institution, the quality of the applicant's essay, and the areas and difficulty of undergraduate course selection (Supreme Court of the United States 2003: 1-2). Similar to the use

of "soft" measures in evaluating applicants, the present work addresses the impact of "hard" and "soft" variables on customer selection decisions.

Literature Review

Customer screening and selection practices are critical to marketing practice. Various literature streams directly or indirectly recognize the importance of customer selection. For example, the personal selling and sales management literature refers to customer prospecting as the "lifeblood of selling" because of its importance in sustaining firm profitability (Futrell 2004). The business-to-business marketing literature also recognizes the importance of account and channel member selection and has proposed a systematic selection process for doing so (Sarkis and Talluri 2002; Gadde and Håkansson 2001). Also, recent emphasis on assessing the value or profitability of the customer demonstrates the importance of customer evaluation and selection (Ryals 2003). This importance is exemplified through marketing metrics such as customer equity (CE) and customer lifetime value (CLV). Often indirectly stated, these metrics place significant importance on customer selection in managing a customer portfolio. Customer portfolio management (CPM), which has adopted a perspective similar to earlier work in product or investment portfolio management (i.e., Boston Consulting Group), focuses on assessing the risk of each customer in order to increase the future value of the firm's customers (Ryals 2003). Another small but growing body of literature coinciding with research on customer profitability is what to do with customers that are not profitable (i.e., firing the customer) (Zeithaml and Bitner 2003). Each of these literature streams will now be reviewed.

Personal Selling and Sales Management

Prospecting is the first step in the traditional sales process (Futrell 2004). Most descriptions of the sales process propose that qualifying the lead or customer is the initial step in prospecting and lead management. Primarily serving as pedagogical frameworks, various descriptive models have been proposed to qualify and select customers (Futrell 2004; Jones, Stevens, and Chonko 2005). The most prevalent of these models is the M.A.D. model, which refers to a three-step qualification process of determining a prospect's money to buy, authority to buy, and desire to buy. In another pedagogical model, Ingram et al. (2006) propose that a qualified prospect is one that (1) can benefit from the sales offering, (2) has the financial wherewithal to make the purchase, (3) plays an important role in the purchase decision process, (4) is eligible to buy based on a fit within the selling strategy (i.e., fits the profile of the desired customer), (5) is reasonably accessible and willing to consider the sales offering, and finally (6) can be added to the customer base at an acceptable level of profitability to allow a mutually beneficial relationship between buyer and seller. Apart from these descriptive approaches, empirical work on customer selection models has surprisingly only recently been of interest to the marketing researcher.

One notable effort is the work of Szymanski and Churchill (1990), which took a "cognitive sales" perspective to better understand the factors influencing salesperson performance. This work focused on how salespeople use memory-triggered cues to classify and categorize potential customers. Szymanski and Churchill's work represents the first research to investigate the factors that influence client prospecting in a personal selling context. Szymanski and Churchill chose to explore the process of client

evaluation in the financial service industry because of this industry's reliance on prospect qualification and because of the disparity in selling performance across financial service sales agents. Based on prior consumer research in the area of memory (e.g., Alba and Hutchinson 1987), Szymanski and Churchill (1990) used a cue elicitation procedure to identify six independent variables or cue values (e.g., age range, number of children, degree of commitment to improve financial position, number of financial goals, income, and marital status). Each cue had a corresponding importance weight, and each respondent described these factors across categories of prospect type (e.g., general prospect, poor prospect, moderate prospect, good prospect, and ideal prospect). For their analysis, an objective measure of salesperson performance (e.g., average number of plans sold per quarter) was regressed on the cue values and cue weight across each prospect category type.

Szymanski and Churchill (1990) found that effective and ineffective salespeople differ in the importance weights they assign evaluation cues, as well as on the cutoff threshold values they establish for these cues. They found that, although the properties of the cues differ for good and poor performers, the quantity of cues do not. Their rationale for this finding was that all salespeople, regardless of their performance level, readily learn the basic steps of prospecting. These results show that good performers give less weight to the number of financial goals, age, and number of children in describing prospects. In terms of the cutoff points imposed on cues, they found that higher income standards, a higher number of goals, a narrower age range, and fewer children were the threshold trends related to salesperson success. Based on these findings, Szymanski and Churchill (1990) concluded that salespeople who apply stiffer standards in classifying

customers have higher sales performance. Furthermore, they proposed that future research look not only at the influence of cues on prospect classification, but also at how different factors influence customer selection decisions.

Business-to-Business Marketing

Exchange partner evaluation and selection are important concepts in business-to-business marketing management (Hutt and Speh 2001; Hutt, Johnston, and Ronchetto 1985). For example, research on account selection and management suggests that unless firms carefully identify key customer accounts, firms risk over-serving unprofitable accounts and wasting resources (Cespedes 1995). Therefore, the selling firm must determine how each new customer defines "value" prior to formally acquiring the customer. Then, the selling firm can decide if it can meet and leverage the "value" demands of the new customer while still meeting the demands of other customers (Cespedes 1995).

Related to account selection is work in the channels literature on the selection of channel members, especially supplier selection. According to Wathne and Heide (2004), the level of governance a firm has with its suppliers is facilitated in part by the extent to which the firm qualifies its suppliers. The governance provided through a formal qualification process protects the firm from opportunistic behavior by its partners (Stump and Heide 1996). Therefore, this research provides theoretical reasoning for evaluating and predicting systematically which prospective partners might cause governance issues for the firm.

An important contribution of the channels literature is the various evaluative criteria to aid in the selection of channel partners. Sarkis and Talluri (2002), taking a purchasing perspective, look at how the business "customer" selects a "supplier." Sarkis and Talluri suggest that the following factors should be considered when selecting a supplier: strategic performance factors (e.g., cost, quality, time, and flexibility), organizational factors (e.g., trust, management, culture), technological factors (e.g., compatibility, manufacturing, and design capability), and relationship factors (e.g., depth, communication openness, and reputation integrity). Gadde and Håkansson (2001) also include financial strength as an important factor in selecting a channel partner. Theoretically the work of Tarkis and Talluri, and Gadde and Håkansson is important to the present research because their work proposes a variety of "hard" (e.g., delivery speed) and "soft" (e.g., reputation) criteria.

In addition to helping a firm defend against opportunistic behavior, a systematic selection process provides an opportunity for the relationship partners to become socialized with one another's goals and values (Dwyer, Schurr and Oh 1987; Ouchi 1979; Wathne and Heide 2004). When relationship partners (manufacturer-customer) share similar goals and values, a relational bond is created that reduces the occurrence of relationship dissolution. Because it decreases the likelihood of opportunism and promotes on-going relationships, firms need to engage in systematic qualification of their customers or strategic partners.

The steep consequences of acquiring poor strategic partners have led Hutt and Speh (2001) to propose that the systematic evaluation of partners should be an ongoing process. This process enables the firm to replace poor performers with potentially better

ones (Hutt and Speh 2001). Hutt and Speh suggest that channel member selection should be formally included in the processes of channel management instead of being relegated to a channel design consideration. They recommend identifying prospects through discussions with company salespeople, and reviewing trade directories and publications and then qualifying prospects using firm and industry criteria including market coverage, product lines, personnel, growth, and financial standing.

Partner acquisition in industrial marketing also entails considering independent manufacturers' representatives as an important customer base (Silberman 1995). When regarded as "customers," independent reps can be valuable channel members and should be carefully selected and managed since they are contracted by several companies to represent what are often competing product offerings (Hutt and Speh 2001; Silberman 1995). It is imperative then for manufacturers to qualify and carefully select the best reps in their trade area to represent their products.

In summary, the business-to-business marketing literature, including research on supply chain management, recognizes the importance of customer/supplier acquisition. The primary contribution of this research stream the suggestion that a variety of "hard" and "soft" evaluative criteria combine to influence selection decisions.

Value of the Customer

A firm's relationships with its customers are one of its most important assets (Srivastava et al. 1998). Proactively managing customer profitability increases the profitability of the firm as a whole (Ittner and Larcker 1998). Because of the impact of managing customer relationships, it is no surprise that a significant emphasis has been

placed on developing marketing metrics to measure customer profitability (Rust et al. 2004). Among the metrics receiving the most attention are customer equity (CE) and customer lifetime value (CLV) (Rust et al. 2004; Venkatesan and Kumar 2004). Both CE and CLV support the notion that a firm should segment its customer portfolio and allocate expenditures for building and maintaining its most valuable customers. CE refers to the sum of the lifetime values of all the firm's current and future customers (Rust et al. 2004). CLV is the total financial contribution (e.g., revenues less costs) of a customer over the lifetime of that customer's relationship with the firm (Jones, Stevens, and Chonko 2005). Both CE and CLV are proposed as objective measures to help marketing professionals justify firm-dedicated marketing expenditures and to target the "right" customers.

However, despite being conceptualized as objective measures, CE and CLV both rely on subjective inputs in their calculation. For example, the measure of CLV includes three elements: duration of relationship, revenues, and costs (Ryals 2003). The duration of the customer's relationship with the firm is forecast by a key informant in the organization or is extrapolated from previous experience. Revenues are actual and anticipated sales of the customer. Because it is a challenge for firms to monitor the precise individual costs of servicing each of their customers, the actual costs of servicing the customer are difficult to pinpoint. However, customer service and sales automation systems have been effective in tracking one type of cost-- time spent handling and resolving customer requests and issues. Therefore, complicating the operationalization of CLV is the informant's qualitative evaluation of the customer's anticipated relationship duration and the customer's anticipated sales.

The idea of a firm segmenting its customer portfolio stems from the basic concept of portfolio analysis used in product and brand management (e.g., Boston Consulting Group Matrix). Ryals (2003) borrows the basic tenets of quantitative portfolio analysis (Sharpe 1964) to explore the application of modern portfolio theory (MPT) to customer portfolio management (CPM). Ryals (2003) demonstrates the application of MPT and the capital asset pricing model (CAPM) via a case methodology where a collaborative research project was undertaken with the customer management team of a leading insurance company. The inclusion of the MPT and the CAPM models into the active discussion surrounding customer and firm profitability is noteworthy because both MPT and CAPM suggest that CLV and CE may be inadequate measures of the true value of the customer because they do not account for the individual risk-level of the customer. Ryals (2003) provides examples of consumer mortgages/loans and credit card services as "real world" situations where both customer profitability and risk determines how customers are managed. Ryals (2003) proposed two strategic directions for incorporating customer risk management into the existing customer relationship management (CRM) paradigm. The first strategic choice is a risk reduction strategy, a "defensive strategy" aimed at preventing the loss of existing customer relationships (Johnson and Selnes 2004). The second strategic direction, risk-based pricing, is a more "offensive" strategy, where a risky customer may have to pay more than a less risky customer. Using financial services as the example, Ryals proposes the alternative strategy of refusing high risk customers in certain situation, but cautions that this should be an exception and not the rule.

Relating customer profitability to customer acquisition, Reinartz, Thomas, and Kumar (2005) proposed a process model to balance the costs of acquiring customers with the costs of retaining them. Their model proposes that resources be allocated strategically to customer acquisition and customer retention. They suggest that the likelihood of acquiring the customer is a function of firm actions (e.g., expenditures), customer actions (e.g., customer-initiated communication) and customer characteristics (e.g., industry type, annual revenue, and firm size). The duration of the relationship or the retention of the customer depends on the firm's investment in communicating with the customer. The work of Reinartz, Thomas, and Kumar is important to the present research because it takes a process-perspective in understanding the firm's acquisition of the customer.

This research stream aimed at assessing the value of customers is crucial to the present work because although specific factors have not been identified, this research stream suggests that a variety of factors influences the customer screening and selection process.

Firing the Customer

The present research focuses on exchanges in which the seller decides whether to accept business from a customer. Another situation in which the seller makes an important decision regarding how to manage a customer relationship occurs when a seller decides whether to "fire", or terminate a relationship with, an existing customer (Zeithaml and Bitner 2003). Dwyer, Schurr and Oh (1987) were the first to consider this concept in terms of what they called the "dissolution of the relationship." Relationship

dissolution refers to “the uncoupling of parties from highly evolved relationships” (Dwyer, Schurr, and Oh 1987, p. 23). Seller-initiated dissolution may result because the customer is no longer profitable, because the seller is dissatisfied with the customer, or because of involuntary switching beyond the control of the customer (e.g., service provider or customer relocate) (Hocutt 1999).

Firing the customer without generating negative publicity and word-of-mouth communication about the seller is a challenge. Zeithaml and Bitner (2003) suggest that one way of eliminating unprofitable customers from a customer portfolio is to increase the price or cost of the product or service offering. A more friendly approach to terminating a relationship with a customer is to help the customer find a new supplier or service provider that can better meet the customer’s needs. This strategy might be more effective in minimizing negative backlash. Another strategy is to consult with the customer to re-negotiate the customer’s expectations for the product and service, and if both parties are not satisfied, both the customer and seller may find an agreeable termination to the relationship (Zeithaml and Bitner 2003).

The perspective of seller-initiated termination of the relationship is valuable to the present research because it suggests that the seller must proactively evaluate a firm’s customers throughout the various stages of the relationship. Also this literature suggests alternative resolutions to managing “higher risk” or problem customers: through open-negotiating with the customer, risk-based pricing, and referring the customer elsewhere.

Conclusion

Based on this review of the literature, it is clear that customer selection practices are an important area of research. While each research stream contributes to this research, overall, customer selection is a neglected research area. For example, while the personal selling and sales management literature recognizes the value of qualifying the customer prospect (Szymanski and Churchill 1990), besides the work of Syzmanski and Churchill, the sales literature does not investigate the factors influencing the process of customer selection decisions. Similarly, the business-to-business and supply chain literature only provides examples of the selection criteria used by manufacturers and purchasing departments. In addition, this literature identifies relationship governance, the "fit" of the customer, and the socialization of relationship partners as theory rationale to argue for a systematic process for partner qualification and selection. However, it too fails to investigate factors influencing the customer selection decision.

Also reviewed was literature focused on the value or profitability of the customer. Implied in this literature is the need for the firm to manage its customer portfolio and assess the risks and the returns of the customer when deciding on which customers to invest in. The metrics proposed to measure customer profitability (e.g., CLV, CE) also suggest that the selling firm should make quantitative and subjective judgments regarding the value of each specific customer (i.e., CLV) and the overall customer base (i.e., CE). However, the factors that influence the quantitative and subjective screening and selection decision have not yet been explored.

Finally, the stream of literature directed at relationship dissolution or "firing" the customer suggests there are situations when sellers should terminate relationships with

their customers. Alternatives for firing the customer include modifying the terms and conditions of the customer's relationships. In sum, this literature provides another example of a seller decision in customer relationship man

CHAPTER III

QUALITATIVE STUDY

The primary aim of this dissertation is to identify the factors that influence the individual decision-making process in customer selection. Because no previous work has investigated these factors, a qualitative study was undertaken as a starting point. This chapter delineates the methodology of a qualitative study to answer the following research questions.

1. What quantitative and subjective factors influence customer selection decisions in the banking lending industry?
2. What influence do loan officers have on customer selection judgments?

The chapter begins with a brief discussion of the industry setting for this study--bank lending. After a brief explanation of what made this industry an attractive context for this study, the methodology and a discussion of the results of sixteen in-depth qualitative interviews are presented. The results from these qualitative interviews provide the basis for the experimental design in Study 2.

Industry Setting

The industry setting for this study is bank lending. The broad scope of bank lending allowed the researcher to seek information about customer selection in across banking products (e.g., retail consumer, wholesale consumer, retail commercial).

Banking was chosen as the context for this study for a number of reasons. First, banks are in a unique position to target and approve loans for customers who meet certain qualifying criteria. Second, for different consumer and commercial credit products, banks use different types of information to analyze the customer's financial strength, value, ability to repay. Cole et al. (2004) found that small banks tend to use more subjective data (i.e., "soft" information) to analyze business loans, while larger banks base their decisions more on quantitative financial data (i.e., "hard" information). The ability of small banks to use "soft" information enables them to survive doing small business lending because they can focus on relationship development and non-standardized loans better than can larger banks. DeYoung et al. (2004) described small banks as doing non-standardized loans (e.g., small business lending), whereas large banks that rely more exclusively on hard information are more fit to do standardized loan requests (e.g., credit card loans). The work of Carter and colleagues supported this notion that small banks do in fact perform better than larger banks in small business lending (Carter and McNulty 2005; Carter, McNulty, and Verbrugge 2004). The theoretical explanation that Carter and colleagues provided is that small banks are able to differentiate themselves because they are best suited to overcome the information asymmetry that exists when evaluating soft information. As a result, small banks are better able to meet the needs of their small business customers because they have access to better credit information and the organizational structure that allows for greater flexibility and discretion in meeting these customers' needs. Large banks, however, do business with larger firms, which typically interact in more impersonal ways, are less exclusive, and maintain shorter tenures with their banks (Carter and McNulty 2005).

The third factor in choosing bank lending as the context for this research is that banks traditionally have placed importance on the customer's relationship with the bank. Specifically, banks value relationships with customers and target the most valuable customer segments with their lending products. Fourth, changes in regulation and advancement in technology in banking have contributed to banks' taking a more aggressive strategy regarding segmenting customers and marketing their products. These changes in regulatory governance over the industry provide the opportunity to compare actual lending practices to the normative guidelines prescribed by policy makers and bank regulators. In summary, this industry provides a dynamic context to explore what variables influence discretionary customer selection decisions.

Methodology

Research Design and Sample

With an interview methodology, the range of perspectives to be examined is an important consideration. A sample with little variation will yield limited range of views, raising, concerns regarding the representativeness and generalizability of the data. Therefore, the researcher sampled informants from a wide spectrum of banks and from a variety of banking positions. Initially the sampling frame consisted of interviews with males in community banks and regional or super-regional banks located in a western U.S. state. This sampling frame was later expanded to include female participants. Initially, phone interviews were conducted with bank executives from eight banks in the western U.S. ranging in size from large regional banks to small community banks. At the completion of each of the bank executive interviews, the researcher requested permission,

to contact at least one loan officer. Some bank executives provided information for more than one loan officer. No preference was given for the type of loan officer (e.g., consumer/personal, residential mortgage, commercial). Interestingly, the loan officers in many of the smaller community banks who participated held an executive title/position (e.g., vice president) in addition to their loan officer responsibilities. The duration of each interview was approximately 40 minutes.

The ranges of the population of interview participants included the following characteristics. A complete listing of interview participant characteristics is found in Table 3-1.

1. Age – 29 to 66
2. Gender – male and female
3. Company Tenure – 1.5 years to 37 years
4. Industry Tenure – 5 years to 37 years

Table 3-1

Respondent Characteristics - Bank Executive and Loan Officer Interviews

Resp.	Bank Title/Position	Gender	Age	Company Tenure	Industry Tenure	Bank Description
1	President/CEO	M	64	37 years	37 years	Small, Rural Community Bank
2	Operations Manager	M	29	3 years	5 years	Large Regional Bank
3	President	M	47	14 years	23 years	Small, Suburban Community Bank
4	President	M	66	34 years	34 years	Midsize Community Bank
5	Vice President, Senior Loan Officer	M	57	32 years	32 years	Small, Rural Community Bank
6	Vice President, Branch Manager	M	58	9 years	32 years	Small, Rural Community Bank
7	Vice President, Commercial Loan Officer	M	34	13 years	13 years	Small, Suburban Community Bank
8	Vice President, Commercial Loan Officer	M	33	7 years	15 years	Midsize Community Bank
9	Consumer Loan Officer	M	47	11 years	29 years	Large Regional Bank
10	Senior Commercial Loan Officer	M	59	25 years	33 years	Midsize Community Bank
11	Commercial Loan Officer	M	45	4 years	20 years	Midsize Community Bank
12	Senior Commercial Underwriter	M	60	5 years	30 years	Large Regional Bank
13	Senior Vice President, Real Estate Lending	F	50	1.5 years	22 years	Small Community Bank
14	Vice President, Relationship Manager, Middle-Market Commercial	F	43	7 years	21 years	Large Super-Regional Bank
15	Vice President, Customer Contact	F	50	10 years	20 years	Midsize Community Bank
16	CEO	M	58	14 years	30 years	Small, Suburban Community Bank

Results

The following section describes thematically the results of the sixteen semi-structured interviews with bank executives and loan officers. The central themes of the interviews, included the evaluative criteria used in customer evaluation, the influence of

the economic environment on loan decisions, the role of the loan officer in loan decisions, and the impact of bank regulations on customer acquisition.

Evaluative Criteria

Informants mentioned a variety of loan criteria factors. Multiple informants referred to the "C's of credit" used in loan evaluation. A point of clarification regarding the term "credit": It became evident to the researcher that the universal jargon used for bank lending products is credit. Therefore, credit in this discussion should not be mistaken for the credit score reported by credit bureaus. Of the credit criteria used, a 66-year old president of a fast-growing, mid-size bank referred to capital, collateral, character, and capacity as the C's of credit evaluation.

> We look at the financial condition of the borrower, that is, or you can talk about the C's of credit you know, capital, collateral, character, capacity…. Those are the things we look at. What is the financial condition of the borrower? Is he strong or weak or what? What's the capacity that he has to pay this, the loan? We'll look at his credit report. Does his credit history tell us this should be a good credit? Goes to the character part of it. We look at the deal itself…. (#4, M – President)

Other informants included in their C's the customer's credit score, reported from the credit bureau, and other conditions referring to the economic or market conditions. Although many bank executives and loan officers described similar factors for evaluating customer loan requests, not all banks assess these factors the same way.

For example, at one of the banks, executive officers had differing perspectives on their bank's use of subjective information in evaluating loan requests. This bank's president/CEO described to what degree his bank uses subjective information in response to what information is used to evaluate loan customers.

> Not any more. We used to…if you had good experience with a guy over the years you could make a judgment; any more you can't do that. You have to pretty well stick to your criteria on how you're going to price it and if you are going to make it or not…. You have to justify, why you made the loan on your loan approval form, or why want to make the loan. It has to be more than "I like him," or that "he is a good guy," or "I know him." You know that those are not sufficient any more. (#1, M – President/CEO)

From the same bank, interestingly, a vice president/branch manager acknowledged how he sees the use of subjective factors in making loan judgments.

> There are [discretionary factors], you know. Possibly the borrower's family have been with ________[the bank] for 40 years. You know I think in a smaller bank like ours, this would come more into play. You know I made one this week; he is a CFO for a company that has seven figure deposits with us. Yeah, we are going to do all we can to keep this guy happy, 'cause he is our contact for that business relationship to the other entity.

Contradictory statements like these regarding loan criteria among bank executives in the same community bank present an important finding; that is, different perspectives do exist within and across banks in how they include subjective inputs when evaluating a customer's loan request. An operations manager of an on-line lending operation of a large regional bank provides further support for this internal contradiction regarding the subjective nature of evaluating customers.

> You would hope there isn't [a subjective component], but I think in reality there is…. Good bank customer, been with the bank for years, large deposit accounts, they know someone or have some friend at the bank— we'll maybe try a little harder on these loans to get them approved, compared to loans where there isn't as many emotional or political ties to the loan…. I will give you an example… Oregon, recent loan, 91-acres, wooded property… Typically you'd say, "Hey, it's going to be impossible to find comps for this property." But in this case, good bank customer, a couple hundred thousand in a deposit account, low interest paying account, good customer, never complains. We took this to the head of underwriting of the bank and said, "Is this possible?" They said they would be willing do it if we could find additional comps. So now

> we have an appraiser out hunting for additional comps on this property. (#2, M – Operations Manager)

From this dialogue it is clear that when banks evaluate loans for customers, the subjective judgment of bank officers influences the decision to give credit. The following sections illustrate this conclusion with informant responses focused on the two most subjective criteria: the character of the borrower, and the bank's relationship with the customer.

Character. Of all the criteria discussed by informants, character appears the most subjective. Informants said that evaluating the character of the borrower sometimes requires the subjective input of the loan officer and at other times the subjective inquiry of a bank loan committee. The highly subjective nature of evaluating the character of the customer is evident by the multiple ways character is assessed. One bank president explained that his bank uses the customer's track record of paying bills and the reported credit score as proxy measures of the borrower's character.

> Character is very important. I mean if someone comes in and their credit is terrible…. You know if their credit is not good, that's an indication of how they pay their bills, so probably we wouldn't even consider it. (#4, M – President)

A commercial underwriter with thirty years of industry experience described the objective and subjective evaluation of the customer's character and then stated his belief that the subjective outweighs the objective when evaluating the perceived risk of the customer.

> The two most objective measures come from historical records, credit bureaus, and you get a subjective side of that which comes from the officer's direct contact with the client. He knows how they interact in the marketplace. Are they civic-minded? Are they involved? Do they take care of their employees? What kind of

> business facilities do they maintain? You know you get someone who's pretty sloppy with their operation, it's going to carry over to how well they take care of their finances as well….
>
> Sometimes it's a real fine line between the subjective evaluation and objective evaluation. But it's often the case that the subjective will outweigh the objective; in other words, the numbers will tell you that someone might be able to pay a loan, but the subjective evaluation will say you don't want to take the risk. (#12, M – Commercial Loan Underwriter)

Prior experience with the customer appears to be the preferred measure of character, but in the absence of such prior history or experience, credit history may be a substitute measure of the customer's character.

> In the early days in this bank, even before I was here, it was a small bank; everyone knew everyone; it was all in ______[name of city]. And I remember a few of my first loan committees, "Well this is the son of Joe Blow…." That's getting talked about less and less, because now we've spread into two counties; we've got ten to eleven branches…. Some of our borrowers we are not familiar with on any long-term basis. I think credit worthiness, credit history, that kind of stuff, almost has to be a substitute for that [character] because who knows what the character of that individual is… so we do what we can to check that. If it is a repeat customer, I think it plays a big part in it, because we know the character, we had loans with the customer. That makes a giant difference. That definitely would be a mitigating factor even if everything else was average. (#8, M – VP/Commercial Loan Officer)

Another proxy of character is the reputation of the customer in the community and industry. Executives and loan officers in three banks described how they seek out the borrower's reputation.

> A lot of the people, actually most of the people we deal with, are people we have been dealing with for years. So we know them. We know their character, reputation in the industry. You can usually find that out. There is no real central… for example the credit bureaus do credit reporting, so that is a central way to get it; other than that, you have to go by reputation of the person in the community. That is, there is no central way of finding it. You get that by talking to people or if you have dealt with them, how they

> deal with you. If you have a new customer, about all you have to go off is the credit score, although we do occasionally have a loan come in, and the loan officer brings it in, and somebody says well you know I know this about that guy or gal and I think we need to be careful because here is something that happened with another deal I am acquainted with. (#4, M – President)

> Part of it is credit, but part of it is, have they've been in town long? Are they a person of their word? If they say they are going to do something, is it done? How do other people in town feel about them? Is it somebody you hear, don't do business with so and so; he'll take you every chance he gets. That's not the kind of customer you want. But we can't deny someone for that one thing, not a hearsay thing. But normally if that is the case there are several other problems too… other factors that are not good. (#13, F – VP/Real Estate Dept.)

> In a community like the size of _______, word can get around and so there would be some people that we just wouldn't get involved with even though there isn't anything tangible that you could point your figure to. (#14, F – VP/Relationship Manager)

In forming an evaluation of the customer, clearly no one factor is considered alone, but instead it is the "whole package," "whole picture," and "whole story" that "stacks together" to form a credit evaluation. If this is true then it is no surprise that bank executives have their own beliefs in how criteria are interrelated. For example, bank executives and loan officers referred to the relationship between the borrower's character and his or her capacity or ability to repay the loan.

> I've often said character has a real direct relationship to capacity; I mean, there are people that as long as they're able, they'll pay you. But if, even the best of people if they get, you know, in over their heads, or if some things go against them, or some things happen in life that their capacity is done away with, then they can't pay you no matter what their character is. So we have to take that kind of thing in consideration. (#4, M – President)

> We see clients that have the ability to pay loans but don't, and some that you wonder how they make it and they never miss a payment. (#12, M – Commercial Loan Underwriter)

> They might have money, but they don’t pay their bills; that kind of shows lack of character as far as I am concerned. You know they might not have the best cash flow, but they pay their bills on time. If they’re late, they call you, “I’m going to be three days late…” (#15 – F – VP/Customer Contact)

In summary, of the C’s of credit evaluation that banks use to select their customers, how they evaluate the customer’s character is the most subjective. Furthermore bank informants revealed that no one factor determines whether a customer gets a loan or not, or what the terms of the loan are; instead, they weigh all the factors in combination to justify a loan decline or loan approval decision. Often mentioned in the same breath as the character of the customer was whether the customer was a new or an existing customer of the bank. The next dominant theme to surface from these interviews was the significant emphasis placed on the customer’s relationship with the bank.

Customer Relationship. One of the recurring themes throughout the interviews was the emphasis on the bank’s relationship with the customer. Although many of the banks have not adopted a formal customer relationship management (CRM) system, all of the informants expressed their interest and described the concerted effort their bank makes to loan to existing customers. With some reluctance because of the potential of discriminating against new bank customers, one bank president/CEO admitted that his bank does consider the customer’s relationship in its loan decisions.

> We haven’t done too much of that, um what do they call it, C—M, yeah CRM, we have not done a lot of that [CRM]. You try to, you know, you have got a customer that you have experience with, that’s got good balances with you, hasn’t given you problems, those are positive things. You try to make allowances for those, but you have to be careful that you do not become discriminatory. (#1, M – President/CEO)

Evident from the interviews was the idea that not only do banks value the relationship with their loan customers, but also the customers themselves appear to safeguard their relationship ties to their bank. A bank president explained that even if customers are late in paying on other debts, if those customers keep current with the loans they have with his bank, the bank might have an increased interest in maintaining its relationship with them.

> Traditionally, experience with the lender carries a lot of weight. We have some customers that occasionally may be delinquent, but they choose to be delinquent with others and not us; that means a lot. If they are going to be delinquent, we're glad that they keep us current. (#3, M – President)

Most bank informants were very open about the importance of an established relationship with the customer when evaluating the credit of a customer. One 31-year-old bank vice president candidly revealed his bank's preference toward existing bank customers.

> If you've got an account here at the bank, you have got a lot better chance getting the loan then if you don't. A matter fact when I started here, the bank president would not loan to people who did not have an account with our bank. But you can't do that anymore. (#5, M – VP/Senior Loan Officer)

Relationship management becomes part of the bank's culture and as a result influences the responsibilities and effort of all bank employees, including loan officers and other customer contact employees. The community banks described this as an integral part of their bank's strategy. One community bank executive discussed generally how community banks differ from larger banks and how his bank uses the customer relationship to its competitive advantage.

> I think most community banks focus on that customer relationship. When a customer walks into a large regional bank, sometimes they

> don't get the warm fuzzy feeling that they might at a smaller institution. Also, most of the customers we know. We try to know a lot about them. We live in the community and are involved with them in community activities, or we are related or tied in with them some other way. It's that personalized service that we hope makes the difference, because there is a lot of banks out there, a lot of credit unions. What makes us different today, may not be what differentiates us tomorrow so it's a changing type of thing. But if relationships are maintained, then hopefully that will be the bond that keeps bringin'em back. (#3, M – President)

The trickle-down effect of a bank's relationship strategy does impact loan evaluation. Loan officer informants described how the bank's protocol for relationship management influences loan evaluation decisions differently for new customers.

> If he is a brand new borrower to the bank and brand new to the industry, we are going to heavily scrutinize the potential for him to succeed. In that case we might ask for things that are different. (#10, M – Senior Commercial Loan Officer)

Furthermore, the emphasis on the customer relationship has created added awareness of the contribution loan officers make to the overall success of the bank's relationship management strategy and has led banks and loan officers especially, to understand the distinction between transactional lending and relational lending. Relational lending is the desired practice for banks that have fully adopted a relationship management strategy. Two commercial loan officers described how their bank's emphasis on relational lending influences their loan decisions.

> They [the bank] like lending to relationships. They are not big into just transactional loans. Here is a guy that I found on the street; he's just looking for a half a million-dollar term loan on real estate, but he's got his relationship somewhere else. They're going to say, "Yeah you know if I feel like doing it great, but if we lose it no big deal." But if they [the customer] are willing to move their deposits here that goes a long way; if they're willing to have their banking relationship with us, we are going to value that. And if they have already been here for many years, we are really going to value that

> one, that's important… We just don't want to have a transactional-based portfolio. (#11, M – Commercial Loan Officer)
>
> Lending in this market is almost a loss-leader anymore, and so what is critical to us is to make it a relationship. We don't do transactional lending. We are looking at getting the treasury management, selling insurance, you know, all that stuff…. We want to sell 8 or 10 products to every client, so it is broad based understanding of all their financial needs. (#14, F – VP/Relationship Manager)

In response to a follow-up question regarding the use of formal CRM strategy, one commercial loan officer revealed his personal strategy and desire to make multiple loans to his customers instead of single transactional loans.

> Well, it's really great sometimes to hear the buzzwords from the big boys, but it all comes down to one thing, and one thing only, it's the personal relationship between the banker and his customer that's really going to make the difference…. I mean I want to deal with people for 20 years, and I have a lot of 20-year customers. That's what I am interested in. I don't want to do any one loan; I want to do a lifetime of loans. (#10, M – Senior Commercial Loan Officer)

However, various informants related how relational lending faces the challenge of convincing the loan committee to take a risk on existing customers. One loan officer described the resistance she and others in her bank branch find with their bank's loan committee.

> We're into taking a few more risks up here, but sometimes we're fighting tooth and nail to do it…. Some of the people may not look good on paper, but so many of us have been here in _______ [branch location] for years and know more about these people and previous things they've done…. Sometimes I think we are more willing to take risks on someone, because we do know them from other experiences…. Well just like loaning your best friend a hundred bucks; you're going to take more risks on someone you know a whole lot more about…. ________ [main bank location] is just looking at paper. (#13, F - VP/Real Estate Dept.)

Informant responses support the notion that a preeminent reason for adopting a relational lending strategy is to take advantage of the efficiencies of working with the existing customer base. One commercial loan officer that maintains a loan portfolio of thirty commercial customers with annual sales of $15 million to $500 million discussed the efficiencies resulting from working with existing customers.

> Existing clients are easier because you are already familiar with their management style. You're either comfortable with that or you're not already and you don't need to try to figure that out on a strange new company. So we probably put more time in figuring out the management and the management style, and the industry for new clients, whereas with existing clients you know, ideally we are close enough in touch with them that when there is a request it's not a big surprise. And we understand the business reason behind it and it's just that much easier to do. (#14, F – VP/Relationship Manager)

Although these informants indicate that relational lending is the accepted practice, not all types of lending involve the include customer relationship as a factor in the evaluation. A consumer loan officer described the process of evaluating a customer for a car loan as not changing for a new or existing customer.

> If a client comes in and says, "I've banked with you for 20 years. I want a car loan," I am still going to look at the same basic criteria for them than I do for anyone else. They still need to be credit worthy. (#9, M – Consumer Loan Officer)

It appears from this statement that the subjective value of the customer's prior relationship to the bank is not always a relevant factor, especially when considering consumer lending products. An explanation is that many banks have adopted a much more formal and centralized process for evaluating consumer loan requests. The consumer loan officer cited defines and evaluates credit worthiness from his counterparts in commercial lending. When asked about his loan evaluation process, this consumer

loan officer described a much more objective, automated process of credit scoring customers for the car loans and home equity products that he sells.

> My bank is centralized. Most of the consumer loan applications go to a consumer loan center where they are processed and either approved or declined. Then I have the option to take a second look at and decide if I want to override it, up to my lending limit…. We don't do a lot of exceptions. Usually if a loan center has made a decision, it's based on good sound criteria. I don't have to do a lot of loan overrides. (#9, M – Consumer Loan Officer)

Differences in the loan evaluation process exist not only between the different types of lending (e.g., consumer and commercial) but also between banks doing the same type of lending. To illustrate, a commercial loan officer and part-time college instructor described a conversation he had with a former student who was also a commercial loan officer at a large national bank.

> I had a student once that said, "Well at ________[my bank] we take the application and we fax it off to a center. Then when we get our decline notice back we notify the customer." I said, "What if you don't (get a decline)?" She said, "I have never done a loan, we've turned every one of them down." She had worked there for 2 years…. They didn't ask questions, they just scored it, and bam! (#11, M – Commercial Loan Officer)

In summary, the customer's relationship with the bank is an important factor in evaluating customer loan requests. Community banks were more likely to include previous relationship in their evaluative criteria, especially when evaluating commercial loan customers. Although most of the banks sampled have not adopted a formal CRM system, all of the banks to some degree value the relationship with their customers and espouse a strategy of focusing relational lending instead of transactional lending.

Economic Conditions

A second theme was the influence of the economic environment on the loan evaluation process. A commercial loan underwriter described the role of the marketplace in evaluating a customer's commercial loan request.

> Is this a business that fits in the market? Is it a business that is kind of going out of favor, people don't want the widget anymore? Or is it a new inventive type of thing, is it something on the leading edge and the company is just starting to develop it, the company has a lot of growth ahead of it, competition is favorable to it? You are not looking at somebody trying to start something that another business with greater capital could squeeze them out if they wanted to. (#12, M – Commercial Loan Underwriter)

A commercial loan officer with twenty years of industry experience, both in multi-state regional and community banking, described what he has seen as the impact of the economic climate on commercial lending decisions.

> Wherever I have been it, [the economy] has been important and a consideration. Like here at the bank—when I first got here the tech bubble hadn't burst yet; it was on its way. But things were still happening pretty strong in the construction area. Then things started to slow down and people started noticing some problems and you started hearing this message: "Hey, as we talk to the regulators, as we talk to the economists, they say things are going to slow down. When that happens people's cash flow tightens up. We need to make sure we understand where our customers are at and where they're going. We're not going to stretch as much. We're not going to go out on a limb as much. You know it was the same thing that I heard at ______[regional bank] and ______[regional bank]. "We need to be careful where we're at. We want to take advantage of opportunity but we want everyone to understand that the outlook is a little cloudy and uncertain right now, so let's be careful." (#11, M – Commercial Loan Officer)

From this statement it appears that banks adjust their criteria based on perceived economic opportunities and threats in the environment. The same commercial loan

officer cited above related the following metaphor he had heard from a colleague regarding how adverse changes in the economy “expose” poor lending practices.

> If the economy is shrinking a little bit and the tide’s going out, we’re going to find out who’s been swimming without their trunks on. You’ll get a little embarrassed and you can get in some trouble for skinny dippin’ where you are not supposed to. (#11, M – Commercial Loan Officer)

Another executive/loan officer related considering economic conditions when evaluating the loan request of a homebuilder.

> If I have a customer that has 3 spec houses out there and none of them have sold, and he wants to come in and do two more, I am going to look at that real closely. You’ve got three out there and if the economy is slowing down and things are not selling so well, then more than likely we are not going to make those…. When rates start climbing that might slow things down as well… customers are not going to want to buy those spec houses. (#13, F - VP/Real Estate Dept.)

These examples from informants suggest that the economic climate does in fact influence loan decisions. Also, the economic factors may originate from the local, state, and/or national levels. One commercial officer described his emphasis on responding to economic factors at the state level.

> Is it [the project] feasible given market conditions and within the general market we are dealing with here in ______[the state]? I generally do not look or gauge much on the national market. Nationally we might have a shortage of rental properties, but in this market we have a glut. (#10, M – Senior Commercial Loan Officer).

Once again banks vary in their responses to economic conditions. For example, informants described circumstances in which their bank either relaxes or tightens its loan criteria based on the economic environment. But altering the criteria may not be the only strategy. One informant from a super-regional bank described her bank’s generally

conservative policies and stated that her bank is less likely than its competitor to alter or adjust its loan evaluation process.

> We tend to underwrite fairly conservatively, but what that means is that we are always steady, and so in bad times we are lending pretty much the same way that we loaned money in good times. We are not swinging back and forth as our portfolio swings back and forth wildly. A lot of banks— you will see them adjusting their credit criteria very dramatically from one year to the next. And we don't tend to do that. We tend to be very stable and steady and our customers know what to expect from us. (#14, F – VP/Relationship Manager)

In summary, an important factor that influences banks' loan decisions is the economic conditions of the environment. Depending on the bank and the type of lending, a bank may exercise flexibility in how it responds to economic trends at the local, state, or national levels. Not all banks respond to economic conditions in the same way: some banks may be more conservative and less responsive to the environment, while some may be more risk-taking and more responsive to opportunities and threats in the environment.

Role of the Loan Officer

A third theme that emerged from these interviews was the importance of the individual officer in making loan decisions. In support of this idea, informants described situations where the loan office influences decisions both when the officer has an individual lending authority/limit, and also when he or she "sells" the loan to a loan committee or a supervising authority. A discussion of these two areas of influence follows.

Lending Authority/Limits. Twelve of the sixteen informants were directly involved in lending to customers to some degree. Of the twelve informants making loans, only one stated that he did not have a loan authority or lending limit. The lending

limits of the informants ranged from $25,000 to $250,000. In the cases where loan officers had a lending limit, informants described a process for approving loans up to their lending limit. Bank executive informants reported that lending limits are based primarily on the loan officer's tenure with the company and experience in the field. One bank president said that lending authority is based on loan officers' ability to evaluate a customer's loan request.

> …We recognize that some [loan officers] have a greater capacity for trust than others. I don't mean trust in the honesty-dishonesty, but trust in their skill to make good decisions. Their experience and their track record you know, they generally have higher loan limits than newer or younger or less experienced loan officers. (#4, M – President)

Interestingly, all of the banks that have lending limits reward loan officers with a salary, a title, and in some cases a bonus or incentive program based on portfolio growth, delinquency rates, and fee income generated from that portfolio. Two executives from a community bank described their strategy as being in a growth mode. They were also considering changes in the pay structure of their loan officers to include an incentive plan that would reward loan officers for the new loans they originate and close. One of these executives, the president/CEO, was reluctant to make this transition because he believed that an incentive-based pay structure might have a negative impact on his bank's culture and the quality of its loans.

> We probably are going to move to an incentive plan here in the near future. We have tried to avoid that because we think that it has the tendency for people to say "this is my loan, stay out of it." If I ask for your help, will you take a little of it and I will not get my little reward for it? We want people to feel free to work with each other on it, bouncin' the loan off of each other, work together without the idea that I get a dollar out of it and you don't get any. I just have seen so many of those that I am really leery about how that works. Sometimes it creates more problems. We even want the customer to

> know that they if they are comin' in that they have got the whole staff. But I am quite sure that has to change because the rest of the world doesn't seem to accept that philosophy. (#1, M – President/CEO)

Selling the Loan. The ability of the loan officer to prepare and present the case of the customer to either a bank loan committee, credit administrator, or another authorized bank officer was a requirement for loan officers across all of the banks sampled. One commercial loan officer stated his responsibility when taking the loan to committee.

> My job is to sell the loan, my job is to help the loan committee understand the quantifying numbers. This is why their profits are strong; this is why their days receivable are out of whack… to sell the story. (#11, M – Commercial Loan Officer).

The loan officer's preparation and knowledge of the file influences the judgment of those who approve the loan. One commercial loan officer who also reviews the responsibility to review loans as part of his bank's loan committee described the influence well-prepared loan officers have on loan decisions.

> They need to be prepared to answer questions first, and secondly, their presentation has to be of a nature where you want to ask questions. Sometimes it comes up and you listen to it and you go, there is not a prayer that I am going to approve that. You just know that everything they are saying is wrong. So you don't ask a question, there is no need. But in other cases you have curiosities, it might simply be, "I didn't know anybody was doing that." Or, "I didn't know anyone was in that particular geographic area." (#10, M – Senior Commercial Loan Officer)

However, although loan officers are expected to sell the loan, sometimes their unavoidable attachment challenges their ability to remain objective while trying to sell the loan to a committee or a credit administrator. One commercial underwriter described this challenge.

> Sometimes a loan officer gets so close to a credit that they convince themselves. The real test is if can you convince someone else that doesn't know the customer. (#12, M – Commercial Loan Underwriter)

Bank executives recognized this challenge this presents to their loan approval process. One bank president mentioned the consideration his bank has for loan officers representing their loan clients in loan committee.

> Obviously loan officers when they come to loan committee need to feel good about the loan. They need to feel strong about it. But they also don't want to influence, you know, they don't want to show their cards so to speak. They want the loan to able to stand on its own. So they make an effort to point out the positive aspects of a credit without perhaps expressing too much of their personal feeling about the loan. But in the end we want our loan officers to feel good about a credit they are presenting. Sometimes it's shot down and egos are bruised a little bit, but the process works. It's good. We like them to take ownerships for the credits they bring…. (#3, M-President).

Obviously not all loan officers are equally effective in selling loans to a committee or a credit administrator. One bank president described the influence a loan officer with a good track record has over officers with less experience.

> The track record of our loan officers is certainly a big part in his influence in the bank. We have some loan officers that have very large portfolios. They've developed good relationships with customers over many years and they are pretty astute in knowing what a good credit is and what the risks to the credit are. And when they come in to committee, if it is a larger loan that's over their limit, the committee may have more confidence in, say, in one loan officer over another, because of his experience, his track record, how he deals with the committee. (#4, M – President)

This bank president then compared the differences he sees in his loan officers to children in a family and their strengths and weaknesses to horses in a popular American film.

> It's a little bit like managing a family. Each of your children are different…that's one of the advantages that we have as a smaller institution is that we know our loan officers pretty well, all of our

> people. And we know what their strengths and weaknesses are and we know how much rope to give and how much to hold the reins a little tighter on some. I sometimes refer to the old Ben Hur movie where the old Arab had these two horses… the one was the race horse and the one was the steady one, and he put the steady on the inside and the race horse on the outside. This made a good team. That's really what we kind of try to do. (#4, M – President)

In summary, the role of the loan officer involves exercising influence in preparing and selling the loan. The track record of the loan officer appears to be a factor in the evaluation of customer loan files. These conclusions are based primarily on information related to the commercial lending process.

Regulators and Bank Examiners

The final theme that emerged from these interviews was the distinct and widespread perceptions of the role of federal and state regulators/bank examiners and how these perceptions influence loan decisions. Also related is how these perceptions varied according to the size of the bank. The discussion here centers on the different perspectives of bank regulation and how these perceptions influence the evaluation of customer loan requests. A more detailed description of the role of regulation and policy is reserved for a follow-up study involving interviews with informants from state and federal regulatory agencies.

One vice-president/senior loan officer revealed his bank's recent examination and described the outcome and the process his bank is using to become more compliant with examiners' requests.

> As you are aware, you have to be real careful with truth-in-lending and not discriminating and stuff like that. So what we do, and the bank examiners were here a short time ago, and said, "look you guys, you need to be more consistent in the way you price your

> loans too." Because they were seeing variances and I have done some analyses too, and they are right. We were seeing a variation between men, women, and different ethnicities as well. So, we now provide the loan officers with a rate sheet that runs off the credit report and debt-to-income ratio. And if the person meets those criteria, they are probably going to get the loan. (#5, VP/Senior Commercial Loan Officer)

Later in his interview he responded passionately to what he sees as a trend toward the decreasing use of discretionary factors when evaluating loan customers.

> That is diminishing, and diminishing, and diminishing, which I don't like. You hit a nerve with me. Bank examiners and your external auditors and the consumer groups, they're taking all the discretion away from you being a banker anymore. What the bank examiners would like us to become is just order-takers. You know, take the loan application, send it to some central office and if it meets their criterias then make the loan, and it comes back and send them on their way. I don't like that, but that is the way the industry is going. And I think they are trying to take any favoritism, discretion, whatever word you want to use for that, out of the hands of the lender and treat everyone just like robots…. (#5, VP/Senior Commercial Loan Officer)

He added that his community bank attempts to survive in a highly competitive marketplace and that regulations complicate how community banks attempt to differentiate themselves from the larger banks.

> The only way we can compete with the ________ [regional bank] and ________ [super-regional bank] is if we do value the customer and if we can have a banking relationship and when they come in we say, "How are you doing Heather? It is nice to see ya." If we don't provide that, if we don't let them know that we like them, and what they are doing, they can go to _____ or _____ and be treated like a number. That is the flustrating part of bank regulations. They are trying to put less and less value on your existing customer base 'cause you are discriminating against somebody that you don't know by showing a little favoritism to someone that you know and value and appreciate. It's a fine line and a tough act to really get done. (#5, VP/Senior Commercial Loan Officer)

These issues surrounding regulations were salient for many informants. Another VP/branch manager demonstrated this salience when evaluating two customers with the same credit score.

> What makes it hard is that you have to use your judgment a little bit. But the examiners come in and that makes their job hard, 'cause maybe you do a loan for this guy that has a 650, but turn down this guy that has a 650. (#6, M – VP/Branch Manager)

Another vice president/commercial loan officer described his awareness of regulators when considering discretionary or subjective factors.

> We really try to steer away from those [subjective factors]. That is primarily due to FDIC examiners. They like to see everything pretty objective and pretty cut-and-dried. We try to stay away from other factors that may influence us, just because we want to be fair to everyone that is applying for credit. (#7, VP/Commercial Loan Officer)

A loan officer at a community bank reminisced how regulators had influenced the lending exceptions at his previous employer, a fast-growing multi-state bank.

> You can't have 500 branches and each taking advantage of each of their local opportunities and running in their own direction, because [if] you got 500 people going in 500 directions, you end up saying we all need to come together and head in the same direction which means hey, we are credit scoring as far as the lending process goes. If we set a precedence here, we take one step out of policy here, then all of a sudden we have to do that, so when regulators come in and say how come you are doing this kind of lending in ______[city] and you're not in ______[city] or in ______[city], so the regulators come in and really enforce that you got to do things the same way. If you turn down this loan you've got to turn them all down that are like that. If you make this loan you have to make them all like that. (#11, M- Commercial Loan Officer)

Continuing in his reminiscences of this past experience and comparing it to his current employer, he related an example of how banks respond to regulation differently.

> I had one just a few months ago where it was a decline. He had a low credit score, had this, that, and the other. But because there is

> an opportunity to pick up some business down the road, it was a very low advance rate on the collateral, so we felt like we were safe and covered but we also spent 15-20 minutes discussing compliance issues. What's going to happen if the regulators come in and find out here is a white male person applying for a single credit? If this was a woman or a Hispanic, or if this was a non-profit organization would we make this loan? Yeah we would do it in a second because we are doing it now! So we need to make sure if they find we have declined loans like this, we are going to be criticized heavily for it. It [regulation] is taken in consideration, but where you have a portfolio that spans a fifty mile area from ________(city) to _______ market, it is a little bit easier to sort through stuff and say we are doing these kinds of loans, or we haven't done them in the past, whereas if you're a multi-state organization, it's really hard to say are we doing this or not in California, Washington, Idaho, Arizona, Nevada, so you just say we are not doing it and not doing it no matter what. (#11, M- Commercial Loan Officer)

As this example and others show, banks respond differently to the policies and legal pressures of regulations and frequent bank examinations. However, based on the example and opinion expressed of the commercial underwriter informant, one perception is that community banks in general feel less constrained and pressured by regulations because the regulatory focus is much greater for the larger regional banks since they pose a more significant economic threat in the case of failure. Therefore, community banks get away doing "good 'ole boy loans," or loans that are justified primarily on subjective factors.

> Even though community banks will have the same regulatory requirements, the regulators will often look at smaller community banks with a jaundiced or a blind eye, or however you want to put it, from the standpoint, not only do they recognize they service a certain segment of the community and given their size. Even if they went under they don't pose enough of a risk to the community as a whole that the financial welfare of the people would go bad. But you get into a larger one like ______, _______ or ________, then the regulators get real tight because they assume when you get that big if you start getting on the wild side, you can really impact the economy of a whole region by going south with your credit portfolio…. They [community banks] do what we call good 'ole boy

> loans. And that sometimes is a good thing, but in a bank the size of ______[our bank] you couldn't afford to do that because you are touching too many good 'ole boys. In a smaller community bank they can monitor their own credit portfolio, but they do have the tendency just simply because of the size and because they get clients where they know their clients, where "I knew their granddad. I knew the dad. I'm pretty sure what the kid's going to do… he was raised right." And they will make the loan. And with ______ [our bank] we might know the same customers and be willing to make the same loan, but the regulators hammer the wise out of us. (#12, M – Commercial Loan Underwriter)

In the process of conducting interviews, it was evident that regulation plays an important role in how loan decisions are made, but the process that bank examiners follow when reviewing a bank was not an issue until one informant, a CEO and founder of a small community bank, mentioned that examiners focus their attention on how well the bank stays within the specific policies drafted and approved internally. He also compared the policies of small banks to large banks, suggesting that banks of different sizes will operate within different set of guidelines.

> There are numerous policies that have to be employed by every lending institution. They have to be written policies and they have to be approved by the board of directors initially, and most of them approved annually on an on-going basis. Those policies are drafted to incorporate bank policy and any regulatory restrictions. And primarily what the regulators do when they come in and review our policies is, number one, that we are within any legal guidelines that may apply or regulatory guidelines, and two, that our policies are consistent with who we are. Obviously a smaller bank may do business somewhat different than a larger bank, and it's a product of size sometimes. But they [examiners] want to make sure that our policies are sound and that we are abiding by the policies (#16, M – CEO).

The CEO informant continued explaining the actual process of the examination and the emphasis of the examiners.

> All examinations are what they call risk-based, in other words they look where they feel the greatest risk is to the institution, that is

> primarily in loans. They look at our larger loans, almost all of our larger loans, and then they take a sampling of smaller loans. And they look at them to see if the story makes sense, if in their opinion they come to the same conclusion that the bank did when making the credit – that it's a sound credit, one that should be made. Occasionally you run into a situation where you may have a difference of opinion or something like that. But most of the time regulators, when that happens, you have a chance to sit-down and tell them the story or clarify some points that they may have. So, you know, [it] doesn't get really adversarial very often (#16, M – CEO).

In summary, bank regulations and those federal and state agencies that enforce them have an important stake in how banks evaluate the customer loan requests. This is demonstrated in the different responses from community banks and larger regional banks. The perceptions of many bank informants is that regulators insist that banks become more standardized in their loan evaluation process and that the enforcement of these policies may be more strict for larger banks than it is for community banks because of the more widespread economic impact and risk of the larger banks. The researcher cautions that these conclusions may be biased and single-sided, since these conclusions are based on the perspectives of bank executives and loan officers only. Therefore, in a follow-up study, additional interviews were conducted with state and federal bank examiners. The procedure and findings from this follow-up study provide greater depth and explanatory richness to the findings reported thus far.

Regulator/Examiner Interviews

As a means of further exploring the influence of federal and state regulations on customer selection in banking, follow-up interviews were conducted with five state and federal examiners/regulators. Two of the informants worked in a supervisory role at the

state level, one was the state supervisor of banks responsible for all aspects of banking in his state, and the other was the state supervisor of consumer credit and compliance. The other three informants were bank field examiners either employed by the Federal Deposit Insurance Corporation (FDIC), or the state or were self-employed independent contractors. Represented in the sample were examiners that had current or past experience with the two areas of examination – safety and soundness and compliance. Table 3-2 summarizes the characteristics of these informants.

Table 3-2

Respondent Characteristics - Federal and State Regulators/Examiners

Resp.	Position/Title	Gender	Age	Tenure (Examiner/Regulator)
1	State Supervisor of Banks	M	41	15 years
2	State Supervisor of Consumer Credit and Compliance	F	52	13 years
3	FDIC Senior Compliance Officer	M	46	18 years
4	State Examiner (Safety & Soundness/Compliance)	F	32	5.5 years
5	Federal Reserve Independent Contractor (Safety & Soundness)	F	38	16 years

The focus and process of the two types of bank examinations are very distinct from one another. Safety and soundness examinations focus on risks to the bank and to the FDIC system. These examinations are conducted more frequently, typically every twelve to eighteen months. Consumer compliance examinations evaluate a bank's

compliance with policy and regulations as it pertains to protecting consumer interests. These examinations occur less frequently, typically every two to three years.

A semi-structured telephone interview format was used. Open-ended questions were asked and the average duration of the interviews was 30 minutes. A presentation of the findings from these interviews follows.

Results

Regulators have a vested interest in a bank's customer selection process, especially as it pertains to practices posing threats to the FDIC, to the economy at large, and to protected consumer classes. Safety and soundness and consumer compliance examinations are the two types of examinations that banks undergo. Federal and state examiners cooperate to conduct these examinations concurrently. The results of interviews with five state and federal bank regulators/examiners regarding each type of examination are discussed separately, with a focus on the impact of these policies on customer selection decisions.

Safety & Soundness. Safety and soundness (SS) examinations are based on the CAMELS rating. Upon the completion of each SS exam, the bank is assessed a CAMELS rating score (1, the best – 5, the worst). The acronym CAMELS refers to SS guidelines: capital adequacy, asset quality, management, earnings, liquidity, and sensitivity to interest rate. Capital adequacy is concerned with whether the bank maintains enough capital on its balance sheets to offset its liabilities. Asset quality refers to the quality of loan collateral and how well bank assets hold loan value. Management refers to the management structure (i.e., senior executives and board of directors) in place

and what management is doing in terms of bank governance. Earnings is concerned with the profitability of the bank. Liquidity refers to the bank's setup regarding available cash. Sensitivity to interest addresses how a bank has structured its balance sheet to minimize risk with interest rate changes. These criteria reflect the focus of these examinations on minimizing risk for the bank, the economy, and the FDIC program. One informant described how the risk assessment and risk management philosophy of the Federal Reserve in a SS exam trickles down to reviewing loans.

> You want to make sure that in fact it is a collectable loan, because if it is not, then you are overstating capital. It is a one-by-one process. It is done by a sampling basis. But the crux of it really boils down to making sure that the loans on a bank's book are in fact collectable, because of if they're not, then there is going to have to be charged some capital and earnings. Then it, ultimately, gets back to the FDIC, whether or not there is some capital to cover the risks on the bank's balance sheet. Then if not, does this pose a threat? Is it potentially going to be a claim against the FDIC fund? (#5, F – Federal Reserve Contractor)

In evaluating the loan evaluation process in an SS examination, examiners use sampling procedures to review the criteria. SS examiners are interested mainly in quantitative criteria. As one informant described it, it "boils down" to the collectability of the loan as it pertains to the borrower's capacity to repay the loan.

> But it really boils down to the collectability, and that covers a variety of factors, like does the borrower have the wherewithal to repay the loan? Is it a viable business? Is it an individual that has earning's potential? (#5, F – Federal Reserve Contractor)

As one informant described the difference between SS and compliance issues, SS examinations are primarily "economy-driven," whereas compliance issues are related more to management controls. Because SS issues are economy driven, it is no surprise

that a state supervisor of banks discussed the influence of the environment on bank lending activity.

> We don't like to see a lot of speculation, but obviously right now we are in an increasing rate environment, so we would like to see banks take that into account…. We see a lot of competition of course, and with competition banks are taking a tighter margin for the loans. They are maybe not underwriting them as they should, because the bank down the street won't require certain information, and "so if we want this loan we can't require that information." (#1, M – State Supervisor of Banks)

Specific loan criteria were discussed relative to what examiners hope to see when they open approved loan files. One examiner noted the importance of the borrower's experience in his or her particular industry.

> I just can't emphasize how important it is when looking at credit risk and asset quality in each loan transaction, how important management is in commercial lending. I'm seeing that more and more all the time. If you make a loan to someone who doesn't have experience in that business, there is a high probability in default. It is really important in making a credit decision, very, very important. (#5, F – Federal Reserve Contractor)

The loan examination process zeros in on loans that make policy exceptions. Regulators like to see few exceptions; however, when exceptions are made, regulators zero in on whether exceptions follow the bank's prescribed policy. Two informants described their concern about loan exceptions.

> If there is a lot of policy exceptions to get a loan through and approved and the underwriting is somewhat less than adequate then that's where the concern would come from us. (#1, M – State Supervisor of Banks)

> If exceptions are made, how well are they justified and documented. For me a consistent application of policy is key. Then if deviations are made, it is important they are documented. (#5, F – Federal Reserve Contractor)

Exceptions are often made where strong quantitative factors substitute for other weaker quantitative factors. One informant referred to the decision-making process of making exceptions and gave examples of "sloppy" reasons for policy exceptions.

> It's a case-by-case situation. It's not just going through the process, we've violated this policy and some sloppy reason is given. Then that is not going to pass. It's going to be looked at. Was it a valid reason? Was it justified? You might see a situation where a bank makes a loan and the bank has a policy that they will only loan up to 70% of the value on a piece of real estate. That's their policy. Let's say they have a borrower that they just lent 75% to. A valid reason might be that the borrower has a strong liquidity position or they have an extremely impeccable track record, good credit, or all of the above. These are good reasons why we think it is good to take that added risk. But if you just say something like it's a beautiful building, that is pretty plain. There needs to be pretty good credit reasons that mitigate that risk, those are the reasons that you are willing to take that bet. Or, "I know that person, he is really good friend." That would not be a good reason. (#5, F – Federal Reserve Contractor)

In summary, SS examinations concentrate on assessing the risks associated with bank practices, especially the bank's lending practices. SS examinations focus primarily on reviewing the quantitative criteria used in loan evaluation, but other "soft" criteria do come into play. Policy exceptions are an area of concern that regulators key in on when reviewing a bank.

Consumer Compliance. Consumer compliance (CC) examinations are primarily concerned with reviewing a bank's activities regarding consumer protection regulations, including for example, the Equal Credit Opportunity Act (ECOA), Home Mortgage Disclosure Act (HMDA), Truth in Lending Act (TILA), Flood Disaster Protection Act, Real Estate Settlement Procedures Act (RESPA), and Fair Housing Act (FHA), and privacy of consumer financial information. This list is only a sample of the consumer

protection regulations associated with banking. One informant joked about the increasing emphasis on consumer protection in banking.

> We have all these new compliance regs, but when they make a new one they never take an old one out, so it grows and grows. So there is a lot of compliance regulations that they have to follow and it's a burden, you know; it's a lot of work, but they have to do it. We recognize that and so do they. (#2, F – State Supervisor of Consumer Credit and Compliance)

Because CC involves so many regulations, examiners conduct a risk assessment of the different areas of bank operation prior to going into the bank. To do so, they review information they have requested from the bank, especially a bank's policies regarding consumer compliance and a bank's track record as reflected by prior CC examinations. Once the examiner has a sense of the risk areas a particular bank, he or she pull sample files. For example, an informant described the process that he follows to sample HMDA loans.

> We always look at HMDA loans, which are mortgage loans, no matter what the percentage a bank makes a business in them…. We take the whole Excel spread of rates and borrower, and maybe the first time we'll pull out female borrowers. What I will typically do is bold female borrowers down the line, then do a sort on rates to see for instance as a snapshot to see if those rates go down on the bottom with the highest rate. That's a red flag, naturally. What we would like to see is disbursements throughout. That's on the first simple snap-shot…. We in fact look to see that loans that were made had either as good or worse criteria than for those that were denied. So in other words if someone that was a female was denied for a FICO of let's say 650, their Fair Isaac score, and they [loan officers] say they didn't have enough income. Then let's say we pull a loan and it was to a male and it shows that they have a 650 FICO and basically the same thing, but they made the loan. Then there is an issue that we need to follow up with management to say why was this person made a loan and not the other person? (#3, M – FDIC Senior Compliance Officer)

As with SS examinations, informants described the importance of board and management oversight. One compliance officer referred to the importance of bank management in CC as a "top-down approach," where the policies, philosophies, and practices of senior management and the board of directors are heavily scrutinized for CC issues. Another examiner noted the importance of a formalized bank compliance program in determining the extent to which sample files are evaluated.

> We don't go in and do transaction testing on all of them. We look to see what compliance program the bank has in place. We look at their program and then determine if there is any areas we need to do transaction testing on, or if the program that they have in place is sufficient for them to identify errors on their own without us coming in and doing transaction testing. (#4, F - State Examiner)

Another interesting finding was that informant responses affirmed what bank executive and loan officer informants described as different regulatory processes for different types and sizes of banks. As an example, one informant described such differences.

> [The examination process] is based on the bank's everything! The bank's size, its market, its history, its focus, its marketing, the products, who it's target marketing and so on, it just depends. We work with banks in the biggest cities and the smallest towns. Obviously in the way we look at banks in the smaller towns is going to be much different than the larger in the way they operate is much different. There's much more risk on fair lending and so-called compliance consumer risk in the larger banks because they don't know their population a lot of times so there is. They have to assume that there is potentially fair lending [issues]. There is a wide range of ethnic groups in their assessment area, so they have to be very cognizant that they have to be fair any time someone of an ethnic group or protected class is borrowing or wanting credit. So there are much more factors in larger markets. It's basically assessing the risk regardless, but it tends to be less risk in a smaller bank because of the volumes you are dealing with [in larger banks]…. (#3, M – FDIC Senior Compliance Officer)

Civil penalties that can be levied on banks because of compliance related issues can be astronomical. Two of the informants described specific examples of compliance failures that resulted in banks being disciplined.

> I've heard horror stories… a system where a bank would use a scoring system and for the loan officer's neighbor they'd override the rate and for the Hispanic borrower they'd override it and raise it. (#2, F – State Supervisor of Consumer Credit and Compliance)

> A concern nowadays is to get into the factual, empirical data as opposed to the old days where you'd handshake loan…. And we have seen that, I've just seen it recently. You wouldn't believe the terribly lousy loans, safety and soundness, and underwriting, because they (bank/loan officers) felt or get in these positions where they can't turn these people down because they know them and they are a small community. It's really a spiral they knew they were in. If they would've stuck to the rate sheets and credit score they wouldn't be in the trouble that they are. (#3, M – FDIC Senior Compliance Officer)

The most surprising finding in this follow-up study was the lack of compliance issues associated with commercial or business lending. Informants all agreed that there are many fewer compliance-related regulations for commercial lending. The state supervisor of compliance revealed that she often receives inquiries regarding compliance issues in commercial cases, but deflects those complaints because they are not "consumer" issues.

> Like I said, they're called consumer protection regulations for a reason— because they protect consumers…. I have this discussion every day with somebody who has a business account and wants me to go after the bank because they do not like how their business account is being handled and I just tell them, "You know what? You are not a consumer; consumer protection laws do not apply. If you don't like what you got from the bank and if you have a contractual agreement, see if they are violating it. And if they are then sue'em! If they're not and you have agreed to it, you've got a contract. You don't like it, go somewhere else." I am very… I don't mean to sound too harsh or hard-nosed, but consumer

> protection regulations do not apply. (#2, F – State Supervisor of Consumer Credit and Compliance)

A compliance officer revealed that he analyzes commercial bank products less because commercial loans are not covered under consumer compliance. Later in his interview, he explained why less emphasis is given to compliance in commercial banking.

> To be honest with you, commercial loans, for our purposes, are not… there's not that many issues with them as far as consumer compliance because they're not consumer loans, so it really mitigates our analysis on commercial products….
>
> In essence, the world has decided that the commercial borrower should be savvy by and large…. They ought to know more of the financial aspects. It's [compliance regulations] really protecting the smaller guys. Now that's not to say fair lending is, when you think about fair lending and what that really means, that's the only real criteria that overrides everything. So if they are being treated fairly then they don't need… let's say for a commercial property they don't need a RESPA and all the other consumer-related documents…. The lowest common denominator is a first-time homebuyer; that is why you have all these documents… whereas in commercial, these people know the market, they don't need disclosures, they [the government] are not as worried about the individual being dooped in what they are doing. (#3, M – FDIC Senior Compliance Officer)

To summarize, CC examinations are focused on protecting consumer interests, with "consumer" is defined as "noncommercial customers." Also customer acquisition decisions in practice should be consistent with the policy and regulation controls of management and board oversight.

General Discussion

The interviews with sixteen bank executives/loan officers and the five follow-up interviews with federal and state regulators/examiners revealed interesting and important

insights into customer selection decisions. Based on the research questions, this study investigates the quantitative and subjective factors that influence customer selection decisions as they pertain to bank lending.

Four themes emerged from the responses from bank executives and loan officers. Theme 1 was that loan officers rely on various types of information when making a loan decision. Banks differ on what evaluative criteria are used and how these factors are assessed. These differences were especially evident in commercial lending. Some information was quantitative (e.g., borrower's credit, capacity, capital, and loan collateral) and other was subjective (e.g., character/reputation). All the banks sampled used universal quantitative measures (e.g., FICO credit score), however, these banks differed on the acceptable thresholds of these factors. Bank and individual differences in assessing criteria were most pronounced when informants described the subjective criteria in loan evaluation. The character/reputation of the customer appears to be the most subjective factor in credit evaluation because of the multiple ways that bank loan officers assess it. Character is measured by a variety of proxies including experience with the customer, credit history, and community/industry reputation. Also mentioned repeatedly was the subjective importance of the bank's relationship with the customer. The interviews suggest that loan officers give preferential treatment to existing customers with an established relationship with the bank (i.e., relationship lending versus transactional lending).

Theme 2 was that economic conditions influence the loan evaluation process. Some banks adjust their criteria depending on economic trends, whereas others are more stable and less likely to adjust their policies to these trends. Although most of the bank

informants described their bank's strategy as being conservative, some informants described bank personalities that were more aggressive and risk taking for commercial loan business during slumping economic conditions. Conditions in the local, regional, and national economy were cited as impacting the number of loan exceptions and the emphasis on bank loan portfolio growth.

Theme 3 suggested that the job description of loan officers permits individual decision-making in customer selection. The interview suggests that loan officers have the most influence when they make decisions within a prescribed lending limit or authority. Loan officers also appear to differ in how carefully they individually adhere to bank policy and procedures when making loan exceptions. The extent of the influence this chronic need for discretion has on the behavioral tendencies of commercial loan officers is explored in Study 2.

Theme 4 was that the loan evaluation and decision process is influenced by the extent to which federal and state bank examiners enforce bank regulations. Bank executives and loan officers have different perceptions of the role of regulation on commercial lending decisions. Follow-up interviews with regulators and bank examiners revealed that most consumer compliance regulations do not apply to commercial lending. Instead, the majority of the regulations in commercial lending are of the safety and soundness type.

CHAPTER IV

EXPERIMENTAL STUDY

The central focus of this research is to investigate the factors that influence seller decisions to accept or reject business from a customer. Based on the cue diagnosticity perspective (Feldman and Lynch 1988), a conceptual model is proposed and tested. Based on the cue diagnosticity perspective, it is predicted that customer quantitative merit, customer reputation, and the decision-maker's need for discretion will interact to influence customer selection likelihood. Additionally, customer risk assessment, attitude toward the customer, and perceived value of the customer are proposed to have intervening effects on customer selection likelihood.

This chapter describes the conceptual development and methodology of the experimental study to answer research questions three and four.

3. What are the joint effects of customer quantitative merit, customer reputation, and the decision-maker's need for discretion on customer selection likelihood?
4. What are the intervening effects of customer risk assessment, attitude toward the customer, and perceived value of the customer on customer selection likelihood?

This chapter begins with a discussion of the conceptual framework that supports the hypotheses derived from research question #3, followed by the experimental model with construct definitions and the proposed hypotheses. In the second section, the methodology for this study is outlined, including the steps taken to develop the experimental scenario and the need for discretion (NFD) scale, and the results of pre-tests

conducted with commercial loan officers and MBA and undergraduate students. Finally, the results of this study are presented in response to each of the research questions.

Conceptual Framework

Evaluative judgments are based on two types of cues: (1) information that pertains to the essence of the target to be evaluated (e.g., professional experience of a job candidate) and (2) information that relates to the person's subjective response to the target (e.g., charisma of the job candidate) (Pham and Avnet 2004). Information from both types of cues combines to form a judgment (e.g. to hire or not to hire the job candidate). The cue diagnosticity perspective is the framework for proposing hypotheses surrounding how information pertaining to "the essence" of the evaluative target (e.g., the customer's credit score) combines with the loan officer's subjective response to the target (e.g., the customer's reputation) to form a probability judgment of a loan decision (i.e. approval or decline).

The cue diagnosticity perspective suggests that multiple cues combine to form overall judgments and that the extent to which a specific cue is utilized varies with its diagnosticity (Feldman and Lynch 1988; Slovic and Lichtenstein 1971). Cue diagnosticity suggests that decision-makers use the available cues to place the evaluation object into a specific category (Feldman and Lynch 1988; Skowronski and Carlston 1987, 1989). Cues that suggest one categorization over alternative categorizations are referred to as diagnostic, and diagnosticity is the extent to which the cue is perceived as reliable in discriminating between alternative categorizations or interpretations (Purohit and Srivastava 2001).

The cue diagnosticity perspective was originally used to understand measurement effects on surveys, and more specifically how the answers to previous questions provides the respondent with additional information that is useful in answering subsequent questions (Feldman and Lynch 1988). Generalized beyond these measurement applications, the primary contribution of cue diagnosticity is that it suggests that individuals may selectively use information when forming judgments.

Consumer research has explored a variety of judgments using a cue diagnosticity framework, including consumer product evaluations (Aaker and Maheswaran 1997; Purohit and Srivastava 2001) and responses to advertisement (Pham and Avnet 2004). Similarly, as consumers evaluate the quality of products using a variety of cues (Cox 1962; Rao and Monroe 1988; Richardson, Dick, and Jain 1994), the quality and value of an individual customer can be evaluated using an array of cues. The generalizibility of the use of information cues in product evaluation judgments to judgments surrounding human beings is well supported by work on impression formation (Skowronski and Carlston 1987, 1989). Along these lines, Syzmanski and Churchill (1990) found that salespeople differ on the cues they utilize to classify customer prospects (e.g., into ideal, good, moderate, and poor prospects). Syzmanski and Churchill further suggest programmatic research to examine the effects of cue dissimilarities on cue usage and salespeople's customer selection.

In response to Syzmanksi and Churchill's research call, the present work seeks an explanation for when different cues are utilized in forming judgments in customer selection. Previous work describes information cue taxonomies (e.g., Purohit and Srivastava 2002; Sujan 1985); however, still absent in the literature are explanations for

why individuals use different cues. Prior research suggests that a person's motivation, ability, and/or opportunity to process information may explain why individuals differ in their reliance on objective versus subjective information in judgment formation (Pham and Avnet 2004). Pham (1998) found that judgments are more likely to be based on subjective affective cues, as opposed to objective cues, when the person has experiential motives (e.g., reading a novel to relax) than when the person has instrumental motives (e.g., reading a tax manual to prepare a tax return). Pham and Avnet's (2004) extension of this earlier work found support for individual differences in self-regulatory goal motivation (i.e., "ideal" goals versus "ought" goals, Higgins 1998) to explain why some individuals attended more to the substance of an advertisement, when others were persuaded more by subjective affective responses to an advertisement.

The present work extends the cue diagnosticity perspective to investigate whether accounting for the decision-maker's need for discretion will help explain when, and if, the customer's reputation and/or customer quantitative information are diagnostic cues in deciding to approve or decline a loan application.

Proposed Model

To address the research questions above, this study adopts an experimental scenario design. The variables for this study are based on a review of academic and mainstream literature as well as on the results of the qualitative interviews. This study proposes that the effects of customer quantitative merit, customer reputation, and the decision-maker's need for discretion influence customer selection likelihood. Furthermore, it is also proposed that accounting for the intervening effects of customer

risk assessment, attitude toward the customer, and perceived value of the customer will provide additional understanding of customer selection decisions. The remainder of this section defines the study constructs and outlines the three-way interaction hypotheses with supporting theory and rationale.

Customer Quantitative Merit and Customer Reputation

Generally, individuals attempt to learn as much as they can prior to making a decision in new and ambiguous situations (Skinner 1995). The ambiguous nature of customer selection is no exception. Decision-makers rely on evaluative cues in deciding whether to accept or reject business from a customer. Two sources of customer information were identified in the literature review and in qualitative research as influencing this decision. First, c*ustomer quantitative merit* refers to the extent to which quantitative calculations support the overall merit of the customer. In banking, the financial or credit worthiness of the customer is measured using financial ratios (e.g., debt-to-income, net worth) and credit indices (e.g., Fair Isaac Corporation (FICO) score). Beyond its application in banking, the quantitative merit of the customer is also assessed in insurance (e.g., risk scores) and educational settings (e.g., standardized testing). The prescribed application of customer quantitative merit information allows for little discretion since inputs into these ratios and indices are derived using math and computerized models. Prior research describes this type of quantitative information as "hard" information (Berger et al. 2005). Second, conceptualized as a "soft" measure of the quality of the customer, *customer reputation* is the global perception of the extent to which a customer is held in high esteem or regard (Weiss, Anderson, and Macinnis

1999). This type of information is very discretionary since the characteristics of the individual evaluating it influence its assessment.

Previous research in finance has explored the main effects of hard and soft cues on loan evaluation decisions. Cole et al. (2004) reported anecdotal and empirical evidence that small and large banks utilize different information cues. They found that for decisions regarding extending or denying credit to small business customers, large banks took a "cookie-cutter" approach and relied more on "hard" cues to prevent agency conflict and to maintain consistent loan standards and procedures than they did on "soft" or qualitative cues (e.g., reputation). On the other hand, small banks relied more on "soft" cues. Based on loan officers' personal interactions with and assessment of loan applicants, small banks took a "character" approach or one that relied heavily upon pre-existing relationships that provide insights into the character of the customer, and assigned less weight to formal financial data. Carter and McNulty (2005) describe the differences between these two approaches, which result in a competitive advantage for small banks to do small business loans. The research of Cole et al. and Carter and McNulty are important to the present work because they found that banks differ on whether they primarily rely on "hard" or "soft" measures in evaluating and forming loan judgments. However, rather than focusing on the main effects of "hard" and "soft" cues at the bank-level, the present research investigates the joint influence of quantitative merit, reputation, and the decision-maker's need for discretion on individual decisions regarding whether to accept or reject business from a customer.

Need for Discretion

The next independent variable is the decision-maker's need for discretion. This variable was identified based on a review of the literature and qualitative interviews. Service delivery processes have been described along two dimensions – complexity and divergence (Shostack 1987). Complexity refers to the intricacy of the script or steps required to perform a service, while divergence is the level of discretion allowed or inherent in service delivery (Kelley, Longfellow, and Malehorn 1996). According to interviews with bank executives and loan officers, the role of the commercial loan officer is fairly flexible and open to discretionary judgment, and the loan officer's willingness and ability to use discretion varies across loan officers. These individual differences were most apparent when commercial loan officers faced situations in which approving a customer for a loan required an exception to bank policy. Similar to other service contexts in which the seller must decide whether to accept business from a customer, the service delivery process of banks is complex in that bank employees follow prescribed steps to perform their jobs. Such steps notwithstanding, circumstances do arise when loan officers have to decide whether to deviate from policy to approve a loan. Whether a loan officer makes a policy exception is influenced by many contextual and individual factors, including how comfortable the loan officer feels operating "outside" bank policy. Therefore, the present work attempts to capture the individual differences in the enduring propensity of loan officers to seek autonomy from organizational norms when making loan decisions. In addition to qualitative research, previous literature on discretion usage supports the notion that this individual difference variable is important in understanding

how customer contact personnel perform their jobs (Kelley, Longfellow, and Malehorn 1996).

Human motivation and decision-making processes are inherently linked to individual traits and goals (Chi 2001). Chi (2001) suggests that accounting for how people prioritize goals, seek feedback, and regulate themselves will provide insight into how individual differences influence decision-makers' cognitive processes. Kelley, Longfellow, and Malehorn (1996) investigated the extent to which organizational support, formalization, and centralization influenced three types of discretionary behaviors among front-line employees—routine discretion, creative discretion, and deviant discretion. They found that organizational support encouraged routine and creative discretionary behavior across samples of both bank employees and insurance agents. They also reported that the level of organizational formalization inhibits deviant discretionary behavior among bank employees and insurance agents. These authors also called for research to investigate whether the exercise of discretion might be a predictor of employee performance. The present work proposes that an individual's need for discretion, or in other words to what extent individuals follow the rules prescribed in their job, will influence an important performance behavior: how they decide to accept or reject business from a customer.

Related research in organizational behavior has directed attention toward understanding the importance of process orientation (versus a results orientation) in organizational practice, and specifically how it relates to an employee's behavior and psychological welfare (Hofstede et al. 1990; Verbeke 2000). Conceptualized as one end of a continuum, with results orientation on the opposite end, process orientation is

defined as management's desire for employees to engage in business processes that span several functions and departments. It is the process-oriented organizational culture that reflects what Verbeke (2000, p. 591) describes as "employees strict and rigid adherence to their own responsibilities within those processes."

Singh, Verbeke, and Rhoads (1996) created configurations or archetypes based on five dimensions of organizational practices including the process-results orientation dimension. They concluded, based on a study of customer contact personnel (i.e., customer service, salespeople) in a U.S. and Dutch multinational company, that a procedural-oriented environment was dysfunctional because it engendered higher levels of role stressors, reduced job performance and job satisfaction, and increased turnover intentions. However, Singh and colleagues mentioned the following limitations to their study. First, the procedural orientation archetype was created using cluster analysis and thus reflected not only the process-oriented dimension but other distinct organizational cultural dimensions (i.e., internal-oriented versus customer-oriented, open versus closed, employee versus job, organizational versus professional, loose versus tight). Second, although the research of Singh and colleagues accounts for perceptions of the organizational environment, it does not account for how an individual's process orientation influences that person's perception of the organization's process orientation. This raises the question of whether their results can be explained in part by the independent nature of the sample population of service workers and salespeople, who resent process-oriented work environments.

Within the tradition of the 3M Model of Motivation and Personality developed by Mowen (2000), the current work proposes that the need for discretion is a situational trait.

The 3M model defines situational traits as enduring tendencies to express consistent patterns of behavior within a general situational context. Other situational traits important in the organizational setting include job resourcefulness (Licata et al. 2003), results orientation (Harris 2001), and productivity orientation (Harris 2001). Based on theoretical specification, the need for discretion as a personality trait does not refer to any particular behavior or set of behaviors, but instead reflects an internal motivation that drives the performance of such behaviors over time (Licata et al. 2003).

Customer Selection Likelihood

The central focus of this study is on predicting customer selection likelihood. The remainder of this section is dedicated to defining this dependent variable and stating the theory-driven hypotheses.

Customer selection likelihood refers to the perceived probability that the seller will accept business from a customer. In the context of this study, customer selection likelihood is the probability that the loan officer will approve the customer for the loan.

Individuals who determine whether to accept business from the customer look to customer-specific cues to help them appraise or evaluate the customer. Two such cues are the quantitative merit and the reputation of the customer. The present work advances the cue diagnosticity perspective by suggesting that individual differences in the need for discretion will influence how information is weighted. According to the diagnosticity perspective, depending on the decision-maker's need for discretion, either customer quantitative merit or customer reputation could serve as the diagnostic cue in making a customer judgment. Because the need for discretion concentrates on following the rules

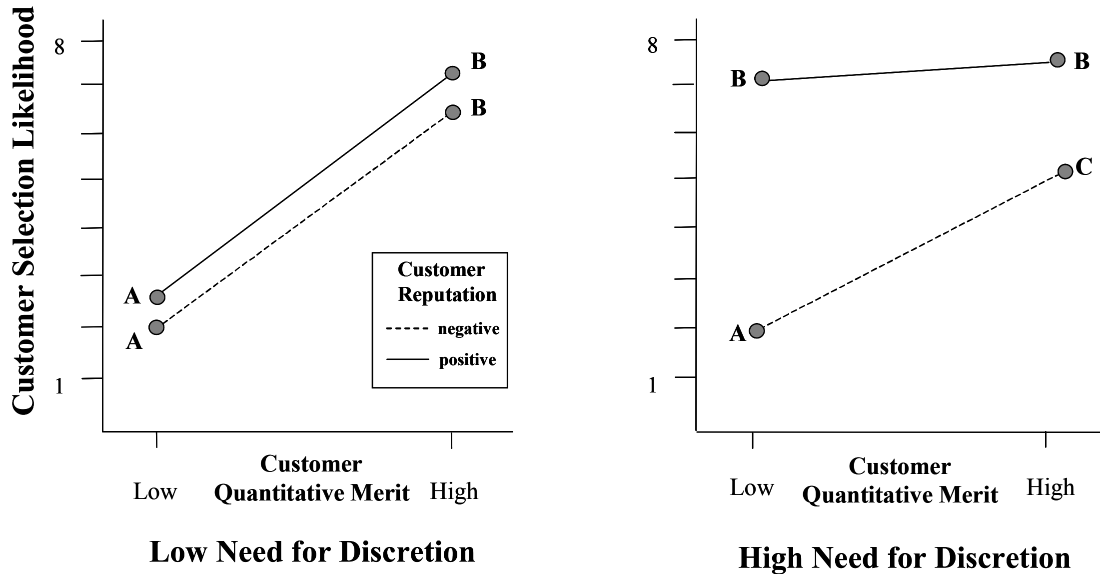
associated with the job, decision-makers with high-discretion needs are likely to weight more heavily the evaluative cue that affords the most flexibility in interpretation. Decision-makers with low discretion needs, however, will base their decision on the customer's quantitative merit because this cue requires the least amount of discretionary interpretation. Therefore, as it pertains to making a customer judgment, customer quantitative information is posited to be diagnostic for low-need-for-discretion (NFD) decision-makers, and customer reputation information will be diagnostic for high-NFD individuals.

Based on this conceptual framework, three-way interaction hypotheses were developed for customer selection likelihood. The predictions are derived from the following logic. Low-NFD individuals focus on the quantitative merit of the customer as the diagnostic cue because it is precise and allows little room for discretion. As a result, only quantitative merit will impact customer selection and the reputation of the customer will have no significant effect.

High-NFD individuals will employ both cues, but the customer's reputation will be the dominant cue. When the customer's reputation is positive, quantitative merit will have no effect on the dependent variable. In contrast, when the customer's reputation is negative, quantitative merit will influence the dependent variable in such a way that low-quantitative-merit will result in a lesser likelihood of customer selection. Based on this logic, the following hypotheses are proposed. Interaction plots for these hypotheses are shown in Figure 4-1.

Figure 4-1

Customer Quantitative Merit, Customer Reputation, and Need for Discretion on Customer Selection Likelihood (Hypotheses)



H1: There will be a three-way interaction between customer quantitative merit, customer reputation, and the decision-maker's need for discretion on *customer selection likelihood*.

H2: When the need for discretion is low, there will be a main effect for customer quantitative merit such that customer selection likelihood will be higher when customer quantitative merit is high rather than low.

H3: When the need for discretion is high, customer quantitative merit will interact with customer reputation. (a) When customer reputation is positive, there will be no effect for customer quantitative merit. (b) When customer reputation is negative, customer selection likelihood will be higher when customer quantitative merit is high rather than low.

In addition to customer selection likelihood, two other selection judgment variables were explored in this research-- magnitude of resource allocation and quality of the terms given to the customer. No formal hypotheses are stated for these two dependent variables because it was anticipated that they would follow the same pattern of relationships as customer selection likelihood.

Intervening Effects

To the researcher's knowledge, this is the first study to explore the individual decision-making process in customer selection. In response to the research question to identify and test the intervening effects of "process" variables in customer selection, three variables were proposed to influence customer selection likelihood—customer risk assessment, attitude toward the customer, and the perceived value of the customer. These variables were chosen based on the literature review and the qualitative interviews with bank executives and regulators. The remainder of this section defines each variable, and describes its importance in the decision-making process of customer selection.

Customer risk assessment refers to the decision-maker's perception of the degree to which the individual customer presents a threat to the welfare of the firm. Assessing the risk of the customer has been proposed as an important part of managing a customer portfolio (Ryals 2003). Many companies assess the risk of the customer using some form of risk or credit scoring system. Risk scoring is an effective way of evaluating specific types of risk in a customer relationship. For example, banks attempt to assess the risk of loan default prior to making a loan decision. It is proposed when deciding to accept or

reject business from a customer, decision-makers will first assess the risks associated with the customer's request.

Attitude toward the customer refers to the decision-maker's overall evaluation of the customer. Attitude toward the customer captures the decision-maker's affective responses (i.e., like – dislike, favorable – unfavorable, good – bad) toward the customer. It is proposed that these affective responses will influence customer selection likelihood. To the author's knowledge, this is the first study to consider how an employee's attitude toward a specific customer influences his or her decision to do business with that customer.

Perceived value of the customer refers to the customer's contribution to the overall welfare of the firm. Customer value is the central component in assessing customer profitability. For example, firms may use the customer lifetime value (CLV) metric to predict the future profitability of the customer by accounting for purchase frequency, predicted contribution margin, customer retention, and the marketing resources allocated to the customer's relationship (Venkatesan and Kumar 2004). This research proposes that the subjectivity of inputs into perceptions of the value of a customer will influence the decision-maker's behavioral intentions to accept or reject business from a customer. Therefore, it is believed that the perceived value of the customer will have a main effect, and possible mediating effects, on customer selection likelihood.

Methodology

The following section outlines the methods used to test the hypotheses. First, the process of developing the need for discretion (NFD) scale is outlined. Second, the procedure for drafting and pre-testing the experimental scenario is discussed. Third, the experimental design and administration procedure is described. Finally, the results of this study are discussed in response to the research questions.

Scale Development: Need for Discretion

The scale development procedure outlined here follows the guidelines set forth by Churchill (1979) and Hinkin (1998). Support for creating a NFD scale is based on a literature review and the qualitative interviews that suggest that defining and measuring this construct is worthwhile for theory-building and managerial practice.

Following the guidelines of Churchill (1979), an initial set of items was developed (see Appendix A). Items were both drafted and adapted from existing scales to reflect the underlying NFD construct supported by the review of the literature; the results of the qualitative interviews with bank executives, loan officers, and regulators; focus group sessions with bank executives and loan officers; and consultation with expert academic researchers.

Following the domain sampling model for measurement developed by Nunnally (1967), nine items were initially drafted to measure the NFD construct. This scale was administered in a survey to 178 MBA and undergraduate students with work experience in jobs that involved some degree of autonomy in decision-making. In addition to the nine NFD items, other existing scales were administered to assess the discriminant

validity of the measure. Prior to analysis, missing data were replaced via mean substitution.

First, an exploratory factor analysis (EFA) was conducted to assess the dimensionality of the measure. The sample was randomly split into estimation and validation sub-samples. The quality of the random split was determined to be adequate based on non-significant t-test comparisons and similar R-squared values. The Kaiser-Meyer-Olkin measure of sampling adequacy (KMO-MSA) index for the items was assessed. For both sub-samples, the KMO-MSA index was above .87, suggesting that the data sets were appropriate for an EFA. Additionally, Bartlett's Test of Sphericity was significant in both sub-samples, indicating that the population correlation matrix was significantly different from zero (Hair et al. 1998). For both sub-samples, EFA[1] results revealed a two-factor solution where six of the nine items loaded on one factor with factor loadings greater than .80 and three other items had strong cross-loadings or clearly loaded on a second factor. For both the estimation and validation sub-samples, the explained variance of the two-factor solution was above 68%. The pattern of the two components was generally consistent across the two samples. After closely examining three poorly performing items, the researcher concluded that confusion with item wording (e.g., negative wording) was likely influencing the response patterns on these three items. At this stage of the analyses, the three items were retained. A final EFA was estimated on the combined estimation and validation samples. The results of this EFA confirmed earlier results, revealing a two-factor solution based on the "eigenvalue greater than one" rule. The first factor explained 53% of the 65% of the variance in the data set.

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[1] All the exploratory factor analyses reported used a principal component extraction method with promax rotation.

The pattern of the factor loadings was similar to that in earlier EFA runs where the second factor consisted of the same three items with problematic wording. These items were dropped from future analyses.

Second, a confirmatory factor analysis was conducted to assess the dimensionality of the NFD scale and to test for construct validity using LISREL 8.71 (Jöreskog and Sörbom 1996). The first CFA model included the six items proposed to capture the NFD construct. The six items were forced to load on a single factor. The CFA results indicated that the NFD items loaded as predicted with minimal cross-loadings, providing evidence of unidimensionality (Gerbing and Anderson 1988). For the NFD model, χ^2 = 49.75 (degrees of freedom [d.f.] = 9, $p < .001$); goodness-of-fit index (GFI) = .91; normed fit index (NFI) = .96; nonnormed fit index (NNFI) = .94; and comparative fit index (CFI) = .96[2]. Although the model fit of the six-item NFD scale followed published recommendations, CFA fit statistics suggested that further improvement to the scale was possible. In addition to improving the fit of the scale, another aim was to reduce the scale's length while maintaining its psychometric properties. Following guidelines outlined by Voss, Spangenberg and Grohmann (2003), a series of shortened versions of the scale were compared using χ^2 difference tests and goodness-of-fit indices (i.e., GFI and adjusted goodness-of-fit index (AGFI)). Following decision rules outlined by Voss and colleagues, the researcher halted item removal iterations when one or both of two possible results occurred: (1) the χ^2 difference tests showed no difference and/or (2) the AGFI did not increase. The following describes the procedure for item removal. First, one of the items of the six-item scale was dropped because its factor loading was

[2] As Bollen (1989) outlines, the χ^2 test for CFAs has many limitations, and therefore even though the researcher presents the χ^2 test, the researcher relied primarily on GFIs in assessing model adequacy.

considerably lower than the remaining five items. Modification indices revealed that eliminating this item would have a significant improvement (i.e., reduction) on χ^2. Therefore, a second CFA model was assessed on the five remaining items. For the five-item NFD model, $\chi^2 = 21.45$ (d.f. = 5, $p < .001$); GFI = .95; NFI = .97; NNFI = .96; and CFI = .98. The researcher then conducted a χ^2 difference between the six item and the five item scales. χ^2 difference test results ($\chi^2_\Delta = 28.30$ [d.f. = 1, $p < .001$]) revealed that the five-item scale is a better fitting model than the six-item scale. AGFI for the five-item scale (.85) was higher than that for the six-item scale (.78). The significant χ^2 difference test and the increase in AGFI, taken together, support the five-item scale. However, modification indices did reveal that dropping an additional item might improve the fit of the scale. The researcher elected to drop the item and reestimate the model and to compare this model to the five-item scale using the χ^2 difference test and AGFI guidelines. For the four-item NFD model, $\chi^2 = 12.04$ (d.f. = 2, $p < .01$); GFI = .96; AGFI = .82; NFI = .97; NNFI = .94; and CFI = .98. Item removal iterations were discontinued because of the decrease in AGFI when estimating the four-item scale.

Third, a coefficient alpha was calculated to measure the internal consistency of the NFD measure. Alpha for the five-item scale was .91, and all item-to-total correlations were greater than .50.

Construct validity refers to the face, convergent, discriminant, trait, and nomological validities of the new measure (Peter 1981). Traditionally, convergent and discriminant validity have been assessed using the multitrait-multimethod matrix proposed by Campbell and Fiske (1959). However, recent developments in structural

equation modeling (SEM) have provided additional methods for assessing convergent and discriminant validity.

The variance-covariance matrix for the items comprising the need for discretion scale was used as input into SEM using Lisrel 8.70. The results supported convergent validation of the measure with all items loading significantly on one factor with all t-values greater than 12.0. Furthermore, the fit indices were acceptable, $\chi^2 = 21.45$ (d.f. = 5, $p < .001$); GFI = .95; NFI = .97; NNFI = .96; and CFI = .98. Table 4-1 presents the factor loadings, item-to-total correlations, means, and t-values for each item of the scale. The composite reliability (CR) was .91 and the average variance extracted (AVE) was .68.

Table 4-1

Factor Loading, Item-to-Total Correlations, Means, and T-Values for Need for Discretion Items

Item	Loading	Item-to-Total	Mean	t-value
1. In my job I follow strict operational procedures at all times.	.78	.74	6.03	11.98
2. I follow all the rules associated with my job.	.84	.76	6.54	13.52
3. I never make exceptions to policies and procedures in my job.	.83	.81	5.25	13.30
4. I pride myself on following rules and procedures with my job no matter what.	.82	.83	5.61	13.00
5. I believe it is better to never step out of policy to make things happen in my job.	.84	.72	4.71	13.34
(α = .91, Composite Reliability = .91, AVE = .68)				

Discriminant validity was assessed for the NFD measure using guidelines outlined in the literature (Anderson and Gerbing 1988; Bagozzi, Yi, and Phillips 1991; Fornell and Larcker 1981). This process involved comparing the NFD measure with another measure with which discriminant validity should be expected. The measure used for these comparisons was a deviant discretion usage scale (Kelley, Longfellow, and Malehorn 1996). The purpose of this analysis was to support the theoretical assertion that the individual difference trait, NFD, does indeed differ from the behavioral outcome, deviant discretion usage (DDU). First, the researcher estimated a single-factor model with the five items of the NFD scale loading on the same factor as the five items from DDU and compared the fit of the model with a two-factor model where the NFD items loaded on a separate factor from the DDU items. If the two-factor model is superior, there should be a reduction in the χ^2 statistic relative to the single-factor model. The results of the χ^2 difference test ($\chi^2_\Delta = 154.91$ [d.f. = 1, $p < .0001$]) revealed that, in fact, the two-factor model has vastly superior fit. Because the NFD and DDU scales were correlated, another step was taken to ensure that construct correlations were less than unity (Anderson and Gerbing 1988; Bagozzi, Yi, and Phillips 1991). The researcher fit a two-factor CFA model with the correlation between the two constructs fixed at 1.00 and found that the construct correlation was less than one ($\chi^2_\Delta = 98.14$ [d.f. = 1, $p < .0001$]). Finally, the researcher compared the AVE of NFD with the squared correlation between the constructs, and AVE exceeded the squared correlation (Fornell and Larcker 1981). Taken together, these results suggest that when used to measure an individual's tendency to seek autonomy from organizational norms when making decisions, NFD captures information different from the work behaviors captured by deviant discretion usage.

Experimental Case Scenario

The researcher followed the guidelines from White, Varadarajan, and Dacin (2003) to compose a case scenario. The first step was to identify a realistic situation where individual employees exercise discretionary judgment in selecting customers to receive a product offering. Commercial lending was chosen as the setting for the scenario because of the significant amount of discretion commercial loan officers use when approving new loans, renewing existing lines of credit, and pricing the interest rate and fee terms for each loan. The qualitative interviews and literature provided additional reasoning for selecting commercial lending as the context for the scenario.

The second step was to draft a realistic and controlled case scenario. A preliminary scenario using the appropriate industry language and loan criteria as described in the qualitative interviews was presented to academic researchers with experience and research expertise in banking. Their feedback was incorporated into a revision of the scenario, which addressed concerns regarding the presentation of the loan scenario and the customer quantitative merit and customer reputation manipulations. The revised case scenario was piloted in focus group interviews with commercial loan officers. Nine loan officers participated in two different focus groups. The researcher identified five objectives for the focus group sessions: First, evaluate the plausibility and realism of the scenario; second, probe whether any important or necessary information had been left out of the scenario; third, consider whether the context of the scenario (e.g., warehouse purchase) was plausible across industries, banks, and loan officer expertise; fourth, determine how much time was needed to answer the questions on the survey

including reading and responding to items pertaining to the scenario; and fifth, probe what meaningful incentives might increase the likelihood of respondent participation.

The following outlines the format followed for these focus groups. Participants were selected from four banks from a Midwestern U.S. state. Participants were recruited by telephone and were invited to a luncheon meeting. The focus group sessions followed a one-hour format. Participants were greeted and served a light lunch. The moderator briefly introduced the participants and the research study. One of four versions of a survey containing the scenario and important personality, organizational, and demographic variables was then administered to each participant. The moderator noted the start and finish times of the participants. The time required to complete the survey ranged from 20 to 25 minutes. The researcher observed that while completing the scenario portion of the survey, participants flipped back and forth from the scenario to the questions that followed. This observation resulted in a modification to the format of the survey so that the scenario and the questions appeared on adjacent pages in booklet form.

Upon completion of the survey the moderator probed first, the plausibility and realism of the scenario; second, whether the information was comprehensible and sufficient for making a loan judgment; third, whether the warehouse context was universal across industries, banks, and the capabilities and expertise of loan officers; and finally, the amount of time required to complete the survey and possible incentives to offer survey participants. The discussions with the focus groups yielded valuable insight into improving the case scenario. The consensus among the participants was that the scenario was extremely plausible and similar to those experienced in their jobs, that describing the prospective borrower's cash flow history should be added, that the

manipulation of the borrower's credit score as a proxy for customer quantitative merit should be balanced to reflect low (i.e., 610) and high conditions (i.e., 690) while still falling within a range of questionable or ambiguous levels, and that the customer reputation manipulation should be modified to reflect specific attributes of the customer's reputation – civic reputation (i.e., serves (refuses to serve) on the boards of many local charities) and professional reputation (i.e. no reports (numerous reports) of the borrower having serious disputes with his customers and employees). Finally, an unexpected finding from these sessions was that the narrative format of the scenario was similar to the format that commercial loan officers use when drafting loan reports in their jobs.

Based on the findings from the focus group sessions, the scenario was modified and the revised instrument was administered to two commercial loan officers for their review and feedback. Their feedback confirmed that the scenario adequately reflected a plausible commercial loan request. The final case scenarios (see Appendix B - E) profile one of four versions of a commercial loan customer with different combinations of customer quantitative merit and customer reputation information.

Study Overview

An experimental study was designed to assess how real commercial loan officers evaluate customers and make decisions regarding customer selection. As described earlier, the scenario for this study is based on a situation in commercial lending. The sample population for this study consists of commercial loan officers. Commercial lending was selected as the context of this study over other types of lending (e.g., consumer lending, primary and secondary residential mortgage) first because, higher

amounts of discretion are utilized in evaluating commercial loans and second because from a policy perspective, there are fewer compliance regulations for commercial loans. Support for this rationale was drawn from the qualitative interviews with bank executives, loan officers, and regulators. The reminder of this section describes the complete methodology employed in this study, including the analytical techniques used to assess the research hypotheses.

Sample and Data Collection

Banks were selected using two lists: a list of alumni from the business school alumni at a large Midwestern university who were known to be serving in executive positions in banking and a list of bank officers who participated in continuing education sponsored by a large Midwestern university. The researcher telephoned the individuals from both of the lists. The researcher first introduced the study by emailing the bank contact person a one-page summary of the research purposes and procedures, and the benefits to the bank for participating (see Appendix F). If the bank contact did not have the authority to accept or decline the invitation to participate, the researcher contacted the responsible executive directly or requested that the bank contact person forward the one-page summary to that person. Once permission was granted by the bank executive, the researcher requested a roster of all the bank's commercial loan officers. Once survey materials were prepared and ready for delivery or mailing, an email memorandum was sent by the bank executive to survey participants endorsing the project and encouraging their participation. To reduce the time and effort required to draft a memo, the researcher provided the bank executive with a sample memorandum (see Appendix G). Depending

on the preference of the bank, surveys were either mailed or delivered to each branch. Each questionnaire was labeled and delivered separately to each commercial loan officer. A postage-paid, business reply envelope was included with each survey. The loan officer survey took approximately 20 minutes to complete. (See Appendix H for a sample of the survey.)

Surveys were either mailed or delivered to 328 loan officers in nine banks. Two weeks after the initial delivery of the survey, a reminder email was sent to all loan officers in the sample. A total of 262 surveys were completed and returned, an 80% response rate. Less than 5% of the returned surveys had missing data.

Characteristics of the Sample

The sample for this study was the 262 loan officers currently working in commercial lending across nine banks with operations in five U.S. states who responded to the survey. The average of total bank assets for the nine banks was 1.8 billion. The range of total bank assets among the nine banks was 36.7 million to 7.5 billion, representing a wide spectrum of small, mid-size, and large community banks.

Of the 262 respondents, 77% were male. The average age of respondents was 46.1 years. Their average loan portfolio size was $24.6 million and the average loan limit or loan authority of respondents was $221,000. The average industry tenure for the sample was 20.3 years, and average bank tenure was 8.4 years.

Non-Response Bias

A threat to the validity of the findings in any survey design is non-response bias (Pedhazur and Schmelkin 1991). The primary concern of non-response bias is that the researcher may draw inferences based on the sample that responded to the survey, ignoring the possibility that such individuals may be different from those who chose not to respond to the survey.

For this study, the concern of non-response bias is whether the random assignment to the treatment conditions had any bearing on whether respondents were early or late respondents. The method for assessing the possibility of non-response bias in this study is based on the assumption that those who responded late to the survey are similar to those who did not respond at all. To test whether there were differences in the response patterns across the experimental conditions, a variable was coded based on whether respondents returned the survey prior to the email reminder (i.e., "early" respondents) or whether they returned the survey after the email reminder (i.e., "late" respondents). Of the respondents that received a scenario with the low-quantitative-merit-condition, 117 were early respondents and 20 were late respondents. Of those that received the high condition, 113 were early respondents and 12 were late respondents. The Pearson chi-square test results ($\chi^2 = 1.52$, $p < .22$) revealed that the response pattern of early and late respondents did not differ across the treatment levels of customer quantitative merit. The same procedure was followed for customer reputation. Of those who received the negative reputation condition, 115 were early respondents and 19 were late respondents. Of those that received the positive reputation condition, 115 were early respondents and 13 were late respondents. The Pearson chi-square test results

($\chi^2 = .99$, $p < .32$) revealed that the response pattern of early and late respondents did not differ across the treatment levels of customer reputation. A similar procedure was followed for NFD; however, the response pattern was assessed across a median split of NFD. Of those respondents in the high-level of NFD, 103 were early respondents and 17 were late respondents. Of those respondents in the low-level of NFD, 127 were early and 15 were late respondents. The Pearson chi-square test results ($\chi^2 = .79$, $p < .38$) revealed that the response pattern of early and late respondents did not differ across the median split of NFD. Taken together, these results suggest that there were no differences in the response patterns across the treatment conditions, satisfying the concern about non-response bias in reporting results based on this sample.

Design and Measures

This study employs a 2×2×2 between-subjects design. The manipulated independent variables are customer quantitative merit and customer reputation. Customer quantitative merit was manipulated using the Fair Isaac Corporation credit (FICO) score, which is used across many industries (e.g., banking, insurance) to evaluate the credit history of the customer. FICO scores range from 300 to 850, and a score of 650 or higher is considered excellent by most lenders (Fair Isaac Corporation 2005; Forsman 2001). Customer quantitative merit was manipulated across two levels, a high score (i.e., 690) and a low score (i.e., 610). Since the focus of this study is on decisions within the "gray" or ambiguous range, the two scores were carefully selected to reflect this middle range of credit scores that commercial loan officers encounter in their job. Earlier versions of this manipulation included a high-level of 725, and a low-level of 625;

however, seasoned commercial loan officers in the focus groups expressed concerns that these two scores were not equally balanced. Therefore, additional one-on-one interviews were conducted with commercial loan officers and based on recommendations from these officers and academic experts, the scores were restricted to the 600 range to minimize the perception that a score in the 700 range is disproportionaly higher than a score in the 600 range. The ambiguity associated with the range of these two levels is consistent with the steps taken by White, Varadarajan, and Dacin (2003) to draft an ambiguous decision scenario.

Customer reputation was manipulated across two levels (i.e., positive reputation and negative reputation). Information regarding the prospective borrower's civic and professional reputation was presented in the final paragraph of the scenario. The positive condition included the following wording: *"The prospective borrower serves on the boards of many local charities. There have been no reports of the borrower having serious disputes with his customers and employees. The prospective borrower is positively regarded by others in the community."* The negative condition included the following statements. *"The prospective borrower has refused to serve on the boards of many local charities. There have been numerous reports of the borrower having serious disputes with his customers and employees. The prospective borrower is negatively regarded by others in the community."* The need for discretion was measured using the new scale and was included in the analysis as a blocking factor.

Each loan officer was given one of the four versions of the scenario embedded in a survey that included a variety of other items. Loan officer subjects were randomly

assigned to one of the four treatment conditions. An equal number of subjects was assigned to each of the four treatment groups.

Prior to reading the case scenario, the loan officers were given instructions which stated that each of them had lending power to approve loans up to $250,000 and that each loan officer was individually responsible for collecting each of the loans he or she approved. The loan officers were then asked to imagine that they were reviewing a loan profile documenting a small-business loan request from their actual bank. Then the loan officers were asked to carefully consider questions regarding this loan file.

Items were either drafted or adapted from literature to measure the following dependent and intervening variables: customer selection likelihood, customer risk assessment, attitude toward the customer, and the perceived value of the customer.

Customer selection likelihood was measured using a three-item scale. Respondents answered the first item of the scale (i.e., "How likely are you to approve this customer for this loan?") using an eight-point scale anchored with 'very unlikely - very likely.' For the remaining two items of the scale (e.g., "I would definitely approve this customer for this loan.") responses were given using an eight-point scale anchored with 'strongly disagree – strongly agree.'

Customer risk assessment was measured using a three-item scale (e.g., "What is the level of risk to your bank in doing this loan?"). Respondents were asked to indicate their responses on a nine-point scale anchored with 'very low - very high.'

Attitude toward the customer was assessed using four semantic differential items (i.e., good-bad, favorable-unfavorable, strong-weak, like-dislike). The perceived value of the customer was measured using a three-item scale (e.g., "In the future this customer

will contribute additional profits to my bank that far exceed the costs."). Responses were given on nine-point scales anchored with 'strongly disagree – strongly agree'.

Control Variables

A number of control variables were included on the survey. First, it was anticipated that differences in banks' adherence to policy and procedures might impact the results. This variable was accounted for by measuring the loan officer's perceptions of the extent to which the bank uses credit score and reputation in making loan decisions. Also measured and included in analyses was the bank's procedural orientation. Items were adapted from existing scales to measure this organizational personality variable. Based on the literature and theory, other variables were also measured and considered in the analyses: job self-efficacy, perceived control over the situation, decision confidence, loan officer portfolio size, and loan officer industry tenure.

Manipulation Checks

Questions on the survey verified the magnitude of the manipulations for customer quantitative merit and customer reputation. For customer quantitative merit, respondents were asked to rate on a nine-point scale "the customer's credit score" (unfavorable - favorable). For customer reputation, respondents were asked to rate on a nine-point scale "the overall reputation of the borrower in the community" (unfavorable - favorable). These manipulation checks were analyzed using simple t-test comparisons of the different treatment groups.

Analysis

Pretest

Prior to being administered to the commercial loan officer sample, the survey was pre-tested using a sample of 178 MBA and junior/senior-level undergraduate students at a large Midwestern U.S. university. Responses from fourteen subjects were not included in the pretest sample, because these subjects did not have work experience and/or decision autonomy in their jobs. The usable sample size for the pre-test was 164.

Because the student subjects for this pretest were unlikely to have experience evaluating commercial credit, the instructions were modified to, "please imagine that you are a commercial loan officer at a bank as you the read the following story and customer description." Subjects were then presented with a brief explanation of the factors and ranges of loan characteristics. Following the narrative loan scenario, subjects responded to items measuring the key dependent variable (i.e. customer selection likelihood), intervening variables, manipulation checks, and other related control variables.

The effectiveness of the customer quantitative merit and customer reputation manipulations was assessed using the prescribed manipulation checks. As expected, subjects rated the customer with a 690 credit score significantly more favorable ($M = 6.41$) than the customer with a 610 credit score ($M = 5.41$, $t = -4.68$, d.f. = 162, $p < .001$). Also as anticipated, the positive level of the customer's reputation was perceived more favorably ($M = 7.33$) than the negative reputation level ($M = 3.43$, $t = -13.96$, d.f. = 161, $p < .001$). As another test of the effectiveness of the manipulations, univariate analyses were conducted to assess the between-subjects effects of the experimental conditions on

the manipulation checks. As expected, when assessing the between-subjects effects of the perceptions of the customer's credit score, quantitative merit had a significant main effect ($F = 18.80$, $p < .001$) and the main effect for customer reputation was not significant ($F = .30$, $p < .59$). Furthermore, when testing the between-subjects effects of the perceptions of the customer's reputation, customer reputation was significant ($F = 185.79$, $p < .001$) and quantitative merit was not significant ($F = .54$, $p < .47$). Taken together, the manipulations for this data performed as the researcher expected. Also, responses to the question related to the perceived purpose of the study suggested that no participants were aware of the experimental hypotheses.

Assumption Testing

Prior to testing the research model using the data collected from the sample of commercial loan officers, the data was subjected to tests of the assumptions of the ANOVA framework. The following section outlines the tests and results of the assumptions.

The research design of this study satisfies the ANOVA requirement of interval scaled dependent variables and categorical independent variables. A median split was performed on the NFD scale to satisfy this requirement. The normality of the error terms distribution was assessed using normal probability plots (Hair et al. 1998), that is, by plotting the standardized residuals along a diagonal line representing the normal distribution. Satisfying the normality assumption, the line of the plotted error terms closely resembled the distribution diagonal. Independence of error terms was assessed using the Durbin-Watson statistic. The Durbin-Watson statistic was close to 2.0,

providing support that the observations are independent of one another. Finally, the homoscedasticity assumption was tested using boxplots and Levene's test. Homoscedasticity refers to the assumption that dependent variable(s) exhibit equal levels of variance across the range of the predictor variables (Hair et al. 1998). For ANOVA, the focus becomes the equality of the variance/covariance matrices across the different groups of the nonmetric variables (Hair et al. 1998). The boxplots and results of Levene's test revealed a violation of this assumption (i.e., heteroscedasticity). Following the recommendations of Hair et al. (1998) to remedy this assumption violation, the dependent variable (i.e., customer selection likelihood) was transformed. Following guidelines in the literature for selecting a transformation, customer selection likelihood was transformed by taking the logarithm of the variable (Hair et al. 1998). The results of Levene's tests revealed that the transformation remedied the heteroscedasticity and that the data conformed to the homoscedasticity assumption.[3]

Measurement Model

The measurement model of the scaled variables in this study, including the intervening effect variables, was examined using EFA, reliability tests, and CFA analytics. First, separate EFAs were conducted for each of the measured scales to assess scale dimensionality. For NFD, EFA results revealed a single-factor solution where all five items of the NFD scale loaded on one factor with factor loadings greater than .80.

[3] Although a logarithm transformation was performed on customer selection likelihood, Hair et al. (1998) suggests that the researcher carefully consider the change in the interpretation of the variables. Since the transformation did not change the results of the a priori predictions, the results and corresponding statistics presented and discussed are for the non-transformed dependent variable.

The explained variance of the single factor solution was 71.2%. The coefficient alpha for the five-item NFD scale was .89 and all item-to-total correlations were greater than .70.

For customer selection likelihood, EFA results revealed a single-factor solution for the three-item scale. The three factor loadings were greater than .90. The explained variance of the single factor solution was 86.2%. The coefficient alpha was .92 and all item-to-total correlations were greater than .70.

For customer risk assessment, EFA results revealed a single-factor solution for the three-item scale. The three factor loadings were greater than .79. The explained variance of the single factor solution was 72.8%. The coefficient alpha was .81 and all item-to-total correlations were greater than .50.

For attitude toward the customer, EFA results revealed a single-factor solution for the four-item scale. The four factor loadings were greater than .80. The explained variance of the single factor solution was 78.2%. The coefficient alpha was .91 and all item-to-total correlations were greater than .70.

For the perceived value of the customer, EFA results revealed a single-factor solution for the three-item scale. The three factor loadings were greater than .80. The explained variance of the single factor solution was 79.3%. The coefficient alpha was .86 and all item-to-total correlations were greater than .65.

Next, a CFA model was estimated with the respective items measuring NFD, customer selection likelihood, customer risk assessment, attitude toward the customer, and perceived value of the customer loading on each of the separate latent constructs. The results of the model revealed acceptable model fit ($\chi^2 = 439.58$ (d.f. = 125, $p < .001$); GFI = .85; NFI = .94; NNFI = .94; and CFI = .95). Table 4-2 presents the construct

measures and CFA factor loadings. Composite reliability (CR) for each of the scales was greater than .80 and the average variance extracted (AVE) calculations for all the scales was greater than .60.

Table 4-2

Construct Measures and CFA Factor Loadings

	Loadings
Need for Discretion	
In my job I follow strict operational procedures at all times.	.75
I follow all the rules associated with my job.	.76
I never make exceptions to policies and procedures in my job.	.82
I pride myself on following rules and procedures with my job no matter what.	.88
I believe it is better to never step out of policy to make things happen in my job.	.78
Customer Selection Likelihood	
How likely are you to approve this customer for this loan?	.85
I would definitely approve this customer for this loan.	.91
Approving this loan demonstrates my good judgment.	.87
Customer Risk Assessment	
What is the level of risk to your bank in doing this loan?	.66
What is the likelihood that the bank is going to lose money on this loan?	.89
What is the likelihood that this customer will repay this loan? (R)	.79
Attitude toward the Customer	
Bad – Good	.91
Unfavorable – Favorable	.93
Weak – Strong	.77
Dislike – Like	.76
Perceived Value of the Customer	
Approving this customer for this loan will be extremely profitable for my bank.	.86
In the future this customer will contribute additional profits to my bank that far exceed the costs.	.92
This customer will refer new business to my bank.	.72

Manipulation Checks

Prior to testing the research hypotheses, the quality of the customer quantitative merit and customer reputation manipulations was assessed. For customer quantitative merit, as expected, subjects rated the customer with a 690 credit score significantly more favorable ($M = 5.86$) than the customer with a 610 credit score ($M = 2.72$, $t = -19.40$, d.f. = 260, $p < .001$). For customer reputation, as expected, the positive level of the customer's reputation was perceived more favorably ($M = 7.18$) than the negative reputation level ($M = 2.40$, $t = -36.65$, d.f. = 260, $p < .001$). As another test of the effectiveness of the manipulations, univariate analyses were conducted to assess the effects of the experimental treatments on the two manipulation checks. As expected, when assessing the between-subjects effects of the perceptions of the customer's credit score, quantitative merit had a significant main effect ($F = 373.29$, $p < .001$) and the main effect for customer reputation was not significant ($F = 2.24$, $p < .14$). Furthermore, when testing the between-subjects effects of the perception of the customer's reputation, customer reputation was significant ($F = 1339.16$, $p < .001$) and quantitative merit was not significant ($F = .82$, $p < .36$). These results suggest that the manipulations of the experimental conditions for this data performed as the researcher intended.

Hypothesis Testing

A 2 (customer quantitative merit: high vs. low) × 2 (customer reputation: positive vs. negative) × 2 (need for discretion: high vs. low) between-subjects ANOVA was run with customer selection likelihood as the dependent variable. Complete results of this ANOVA are found in Table 4-3. The purpose of this first ANOVA was to test the three-

way interaction of customer quantitative merit, customer reputation, and the decision-maker's need for discretion (NFD). The results of the ANOVA reveal that the three-way interaction (F = 4.54, d.f. = 1, 261, $p < .03$) was significant, providing support for H1. To interpret the significant three-way interaction, a 2 (customer quantitative merit) × 2 (customer reputation) ANOVA was calculated for both low-NFD individuals and high-NFD individuals, and the group means were plotted (see Figure 4-2). Complete ANOVA results for the NFD group analysis are found in Table 4-4.

Table 4-3

ANOVA Results for Customer Selection Likelihood

EFFECT	*SS*	*df*	*F-stat*	*p-value*
Customer Quantitative Merit (Quant)	16.32	1	9.83	.01
Customer Reputation (Reput)	73.79	1	44.43	.001
Need for Discretion (NFD)	.001	1	.00	.99
Quant × Reput	1.14	1	.69	.41
Quant × NFD	.12	1	.07	.79
Reput × NFD	6.61	1	3.98	.05
Quant × Reput × NFD	7.55	1	4.54	.03
Error	422.86	254		

Table 4-4

ANOVA Results for Customer Selection Likelihood (High/Low Need for Discretion Groups)

Group: Low Need for Discretion

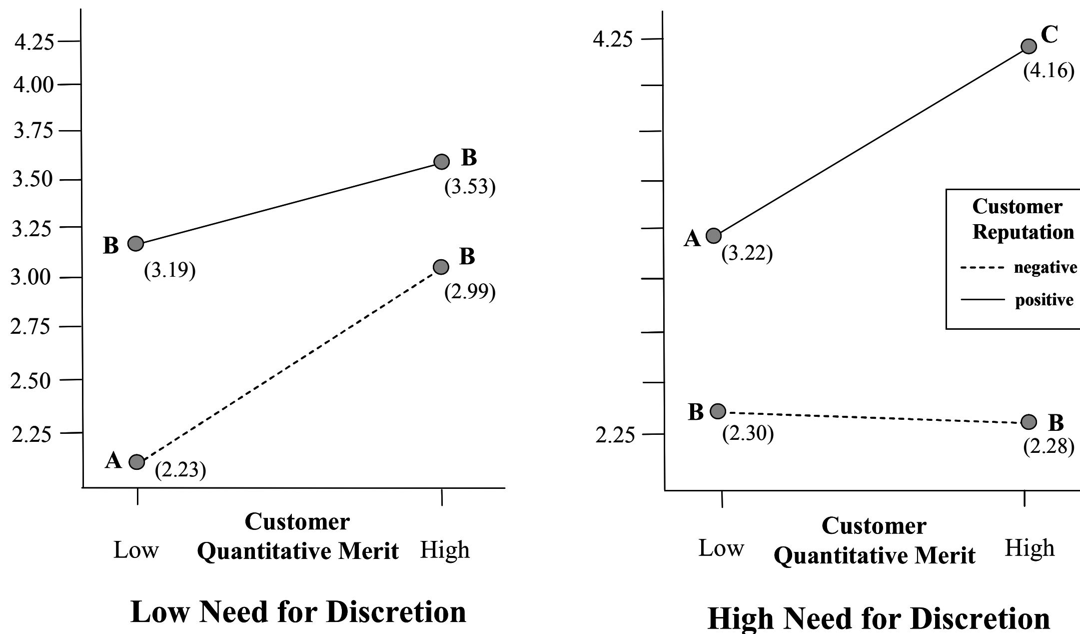
EFFECT	*SS*	*df*	*F-stat*	*p-value*
Customer Quantitative Merit (Quant)	10.63	1	5.39	.02
Customer Reputation (Reput)	20.04	1	10.17	.01
Quant × Reput	1.56	1	.79	.38
Error	272.04	138		

Group: High Need for Discretion

EFFECT	*SS*	*df*	*F-stat*	*p-value*
Customer Quantitative Merit (Quant)	6.23	1	4.83	.03
Customer Reputation (Reput)	56.82	1	43.99	.001
Quant × Reput	6.64	1	5.14	.03
Error	149.83	116		

Figure 4-2

Customer Quantitative Merit, Customer Reputation, and Need for Discretion on Customer Selection Likelihood (Results)



First, for low-NFD individuals, the results revealed a main effect for customer quantitative merit (F (1, 141) = 5.39, $p < .02$). H2 proposed that for low-NFD decision-makers the diagnostic cue in making a customer selection decision would be customer quantitative merit information and that customer reputation information would not have a main effect on customer selection likelihood. This prediction was based on the logic that low-NFD decision-makers, in an effort to seek congruence between their personality and cue preference, would rely on the cue that requires the least amount of discretionary judgment. To support this prediction, ANOVA results would need to demonstrate a non-significant two-way interaction between customer quantitative merit and customer reputation, a significant main effect for customer quantitative merit, and a non-significant main effect for customer reputation. ANOVA results revealed that the customer quantitative merit × customer reputation interaction was not significant (F (1,141) = .79, $p < .38$). Consistent with the prediction, the main effect for customer quantitative merit was significant (F (1, 141) = 5.39, $p < .02$). Contrary to the prediction of H2 however, the main effect for customer reputation was significant (F (1, 141) = 10.17, $p < .01$). The results of the main effect for customer reputation alone do not reveal whether the pattern of the main effect is consistent across low and high levels of quantitative merit. A priori contrasts of the group means were calculated for each treatment combination. Pairwise comparisons of the means of the low-quantitative-merit/positive-reputation group (M = 3.19) and the low-quantitative-merit/negative-reputation group (M = 2.23) were tested. The results of this contrast test revealed a significant mean difference (t = 2.87, $p < .01$) for the two groups. Next, the means for the high-quantitative-merit/positive-reputation group (M = 3.53) and the high-quantitative-merit/negative-reputation group (M = 2.99)

were tested. Contrast test results revealed no mean difference between these two groups ($t = 1.63$, $p < .11$). Taken together, these findings provide partial support for H2.

For high-NFD individuals, as expected, the two-way interaction of customer quantitative merit × customer reputation was significant ($F\ (1, 119) = 5.14$, $p < .03$). H3a predicted that for high-NFD individuals, customer reputation would be the dominant cue when the information about the customer was positive. In other words, positive information about the customer's reputation would be the primary information used by high-NFD individuals to make a customer selection decision (Herr, Kardes, and Kim 1991). H3b predicted a different pattern of cue diagnosticity for high-NFD individuals as compared to low-NFD individuals. H3b proposed that when negative, customer reputation would not be the dominant cue in assessing the likelihood of customer selection; instead, quantitative merit would be weighted more heavily than reputation. Planned comparisons were employed to test H3a and H3b. First for H3a, the means of customer selection likelihood for the positive-reputation/low-quantitative-merit group ($M = 3.22$) and the positive reputation/high-quantitative-merit group ($M = 4.16$) were compared. Contrary to the prediction made in H3a, pairwise comparisons revealed a significant difference in the means of customer selection likelihood for these two groups ($t = 2.97$, $p < .01$). For H3b, the means of customer selection likelihood for the negative-reputation/low-quantitative-merit group ($M = 2.30$) and the negative reputation/high-quantitative-merit group ($M = 2.28$) were compared. Contrary to the prediction in H3b, pairwise comparisons of the mean difference in customer selection likelihood for these two groups was not significant ($t = -.05$, $p < .96$). Taken together, these results provide partial support the predictions made in H3a or H3b.

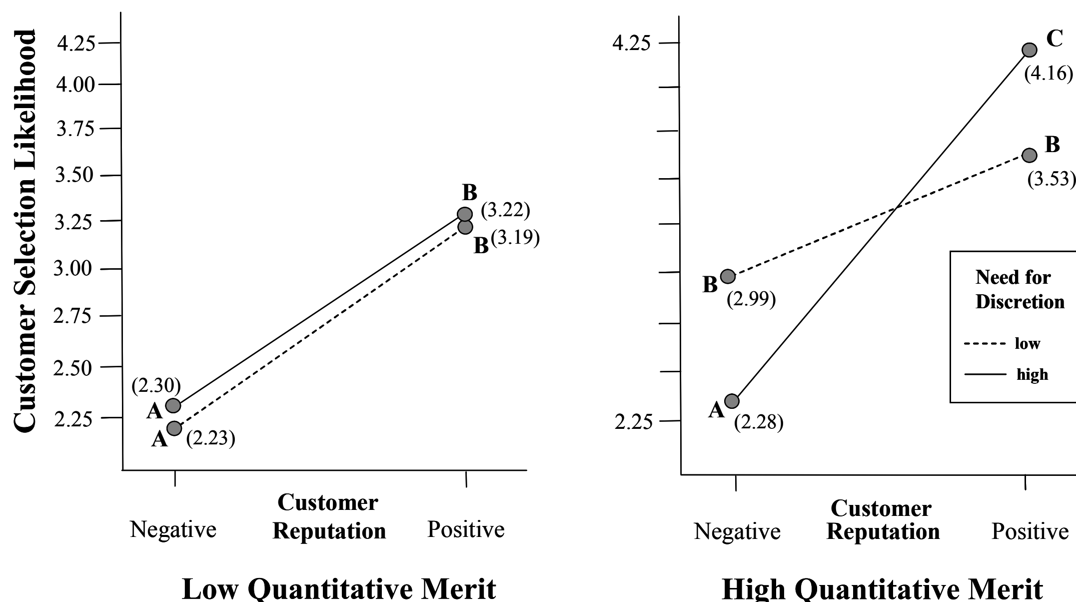
An ANOVA was also conducted for each of the two additional dependent variables – the magnitude of resource allocation and the quality of the loan terms. It was believed that the patterns of results for these two variables would resemble those of customer selection likelihood. Results of these analyses revealed main effects for customer quantitative merit and customer reputation on both magnitude of resources allocation and the quality of the loan terms. The three-way interactions, however, were not significant.

In summary, the results of the ANOVA and planned comparisons across low-NFD and high-NFD conditions provide some evidence that accounting for the individual's chronic need for discretion explains differences in information diagnosticity in customer selection decisions. Generally consistent with the predictions derived from the cue diagnosticity perspective, quantitative merit information was highly diagnostic for low-NFD decision-makers and customer reputation information was highly diagnostic for high-NFD decision-makers. Further examination of the group means, however, provides an additional interpretation of the three-way interaction. The planned comparisons and plots of the group means for the customer reputation × NFD interaction reveals insights about the information preferences of low-NFD and high-NFD individuals (see Figure 4-3). First, in the low-quantitative-merit condition (i.e., 610 FICO score), there was only a reputation effect; in other words, there was no mean difference when customer reputation was negative or positive among low- and high-NFD individuals. When customer reputation information was negative, the mean difference between high-NFD individuals ($M = 2.30$) and low-NFD individuals ($M = 2.23$) was not significant ($p < .81$). Also when customer reputation information was positive, the mean difference

between high-NFD individuals ($M = 3.22$) and low-NFD individuals ($M = 3.19$) was not significant ($p < .94$). In the high-quantitative-merit condition, however, customer reputation information has a strong influence on high-NFD individuals, and no influence on low-NFD individuals. In other words, when quantitative merit is high, the mean difference between negative and positive customer reputation for high-NFD individuals ($p < .001$) was significant, and for low-NFD individuals ($p < .10$) was not significant. Taken together, these results suggest that when customer quantitative information is high, the high-NFD loan officer is more likely to approve the loan when the customer's reputation is positive and reject the loan when the customer's reputation is negative, whereas the low-NFD loan officer's decision is not influenced at all by the customer's reputation. Plausible explanations for these results are discussed in the final section of this chapter.

Figure 4-3

Customer Reputation × Need for Discretion
for Low and High Customer Quantitative Merit Conditions



Covariate Tests

ANCOVA analyses were conducted to assess whether situational, individual, and demographic control variables influence the three-way interaction. The situational variables included the loan officers' perceptions of (1) the importance of credit score to their bank, (2) the importance of reputation, (3) their bank's adherence to policy and procedures, (4) control over the situation, and (5) confidence in their decision. Individual differences in self-efficacy on the job were analyzed. Finally, industry tenure, loan portfolio size, and bank size were the demographic control variables analyzed.

Each of the control variables was included as a covariate in separate ANCOVA runs. The primary focus of each of the ANCOVA models was to determine the impact of the covariate on the three-way interaction. F-tests, p-values, and interaction plots were used to interpret the influence of the control variables.

For the situational variables, the results revealed that the loan officer's perceptions of the importance of reputation (F (1, 260) = 3.88, $p < .05$), control over the situation (F (1, 259) = 23.95, $p < .0001$), and decision confidence (F (1, 260) = 11.22, $p < .001$) influenced customer selection likelihood. The loan officer's perceptions of the importance of credit score (F (1, 260) = .94, $p < .33$), and their bank's adherence to policy and procedures (F (1, 261) = .25, $p < .62$) were not significant predictors. Accounting for the variance in customer selection likelihood stemming from these variables had little significant impact on tests and patterns of the three-way interaction. Only in the case of loan officer decision confidence was there an identifiable difference in the three-way interaction, and in that case the F-statistic and p-value were slightly

diminished (F (1, 260) = 3.64, $p < .06$) and the overall pattern of the interaction plot remained the same.

Next, job self-efficacy (F (1, 260) = .43, $p < .52$), loan officer industry tenure (F (1, 260) = 1.35, $p < .25$), and loan officer portfolio size (F (1, 248) = .75, $p < .39$) were analyzed as covariates. Results reveal that none of these variables predicted customer selection likelihood, nor did they impact the nature of the three-way interaction.

Intervening Effects Tests

It was proposed that customer risk assessment, attitude toward the customer, and the perceived value of the customer would influence customer selection likelihood. The following section describes the tests of these variables.

ANCOVA analyses were calculated for each of the three variables to test for main effects and mediating effects of these variables. First, a 2×2×2 ANCOVA for customer selection likelihood was calculated with attitude toward the customer as the covariate. Results revealed a significant main effect for attitude toward the customer (F (1, 252) = 69.89, $p < .0001$). The three-way interaction was also significant ($p < .03$) and the pattern of the plotted interaction was unchanged. Taken together these results suggest that attitude toward the customer does not mediate the effects of the three-way interaction on customer selection likelihood.

Second, a 2×2×2 ANCOVA for customer selection likelihood was calculated with customer risk assessment as the covariate. Results revealed a significant main effect for customer risk assessment (F (1, 260) = 100.01, $p < .0001$). The three-way interaction was slightly affected ($p < .11$); however, the pattern of the plotted group means remained

the same. Because of the change in the *p*-value of the three-way interaction, further analyses were conducted to investigate the possibility of mediation. A 2×2×2 ANOVA was calculated for customer risk assessment. Results reveal that the three-way interaction was not significant ($p < .20$). Together these results suggest that customer risk assessment does not mediate the effects of the three-way interaction on customer selection likelihood.

Lastly, a 2×2×2 ANCOVA for customer selection likelihood was calculated with perceived value of the customer as the covariate. Results revealed a main effect for perceived value of the customer (F (1, 261) = 216.90, $p < .0001$). The three-way interaction again was slightly affected ($p < .15$) and the plotted interaction resembled the same pattern. Because of the change in the *p*-value of the three-way interaction, further analyses were conducted to investigate mediating effects. A 2×2×2 ANOVA was calculated for perceived value of the customer. Results revealed that the three-way interaction was not significant ($p < .12$). Together these findings suggest that perceived value of the customer does not mediate the effects of the three-way interaction on customer selection likelihood.

Discussion

An experimental design was employed to answer research questions #3 and #4. A measure of the individual's chronic need for discretion (NFD) was introduced and guidelines were followed to validate the NFD scale. Exploratory factor, reliability, and confirmatory factor analyses were applied to data collected from a sample of MBA and undergraduate students with at least two years of work experience. The prediction of the

three-way interaction of customer quantitative merit, customer reputation, and the decision-maker's NFD was derived using the cue diagnosticity perspective. Cue diagnosticity proposes that multiple cues combine in forming judgments, but that one of the cues might be weighted more heavily than other cues when forming a judgment. This research proposed that low- and high-NFD individuals would rely on different cues when forming a customer-selection decision. Research hypotheses were tested using data from a sample of commercial loan officers (N = 262). As predicted, the results of a 2 (customer quantitative merit: high and low)× 2 (customer reputation: positive and negative)×2 (NFD: high and low) ANOVA on customer selection likelihood revealed a significant three-way interaction. For low-NFD individuals, it was proposed that customer quantitative merit information would be diagnostic for a likelihood of customer selection judgment because it is the piece of information that requires the least amount of discretionary judgment. As predicted, the results of a 2 (customer quantitative merit) × 2 (customer reputation) ANOVA on customer selection likelihood for the low-NFD group revealed a main effect for quantitative merit on customer selection likelihood. In an unexpected finding, however, the main effect of reputation on customer selection likelihood was also significant. These results, together with results of pairwise comparisons of the group means, provide partial support for the prediction that customer quantitative merit information is diagnostic for low-NFD individuals. For high-NFD individuals, it was proposed that customer reputation information would be diagnostic when reputation was positive, but that when customer reputation information was negative, customer quantitative merit would be diagnostic. Contrary to this prediction, the results revealed a different pattern of the customer quantitative merit× customer

reputation interaction for high-NFD individuals. That is, when customer reputation information was negative, customer quantitative merit information did not influence customer selection for high-NFD individuals. When customer reputation was positive, customer quantitative merit did influence customer selection decisions, such that when the customer's credit score was higher, so too was the likelihood of customer selection. In summary, the difference between the hypothesis and these empirical results is that customer reputation information is diagnostic for high-NFD when customer reputation is negative instead of when it is positive.

An alternative perspective into these results was found when plotting the customer reputation × NFD interaction for low-quantitative-merit and high-quantitative merit-treatment conditions. For the low-quantitative-merit conditions, the results revealed a main effect for customer reputation and no main effect for NFD. In other words, there was only a reputation effect and it did not differ for high- and low-NFD decision-makers. This result might be explained using the logic of "floor effects." That is, the 610 credit score used to manipulate the low-quantitative-merit condition is close to bank guidelines for the minimum standard for acceptable credit scores. The nearer to the minimum standard or "floor," the more concrete or automatic the decision is to reject the loan for both low- and high-NFD individuals. There is no "floor effect" for customer reputation because there are no concrete guidelines for evaluating this customer factor. Based on this logic, it should be expected that differences among low- and high-NFD individuals in their weighting of customer reputation information would be more apparent when the customer's credit score is farther removed from the "floor" imposed by bank standards. The results of the customer reputation × NFD interaction for the high-

quantitative-merit condition support this logic. In the high-quantitative-merit condition, customer reputation, both in positive and negative forms, greatly influences the likelihood of customer selection for high-NFD individuals. Under the same conditions, customer reputation has no influence on low-NFD individuals.

Taken alone, the cue diagnosticity perspective does not explain these findings. An alternative theoretical explanation for these findings may be the dual-processing models of persuasion (e.g., ELM model, Heuristic-Systematic Model). The argument for this theory's premise is that the low-quantitative-merit condition results in a low-involvement task because the decision to reject the loan is more automatic when the customer's credit score is nearer to the bank's minimum standard for acceptable credit scores. On the other hand, the high-quantitative-merit condition results in a high-involvement task because the decision to approve a loan is less automatic since there are no guidelines for approving customers with a higher credit score, and to justify approving loans, loan officers will scrutinize the customer's credit score and other information (e.g., customer reputation/character). Because of this increased cognitive processing of information in the more highly involved, high-quantitative-merit condition, it is likely that individual differences in NFD will influence the extent to which the peripheral customer reputation information affects customer selection likelihood. Subjecting this alternative theory explanation to an empirical test is beyond the scope of the current project; however, future research should develop and test predictions of customer selection decision-making using information processing models. These and other directions for testing theory-based hypotheses of customer selection are noted in the future research discussion of the following chapter.

The final research question sought to explore the intervening effects of customer risk assessment, attitude toward the customer, and perceived value of the customer on customer selection likelihood. ANCOVA results revealed that all of these variables were significant predictors of customer selection likelihood. Additional testing found that none of these variables mediated the impact of the three-way interaction on customer selection likelihood.

CHAPTER V

DISCUSSION AND CONCLUSIONS

Chapter V contains a discussion and synthesis of the findings of this research and of the implications of the findings. The chapter concludes with potential limitations of the research, an agenda for future research, and a general conclusion.

Overview of Dissertation

To the author's knowledge, this dissertation represents the first work to explore how situational factors and personality interact to influence individual decisions to accept or reject business from a customer. More specifically, this research is the first attempt to test whether differences in an individual's chronic need for discretion influence how different types of information are processed in forming a customer selection judgment. This dissertation employed two methods – in-depth interviews and experimental data – to address four research questions:

1. What quantitative and subjective factors influence customer selection decisions in the bank lending industry?
2. What influence do loan officers have on customer selection judgments?
3. What are the joint effects of customer quantitative merit, customer reputation, and the decision-maker's need for discretion on customer selection likelihood?

4. What are the intervening effects of customer risk assessment, attitude toward the customer, and perceived value of the customer on customer selection likelihood.

Research questions 1 and 2 were addressed using a qualitative methodology. Research questions 3 and 4 were addressed using an experiment. A discussion of the results from these two studies follows.

Discussion

The Qualitative Study

A qualitative study (i.e., Study 1) was employed to answer the first two research questions. Sixteen in-depth interviews with bank executives and loan officers and five interviews with state and federal bank examiners and regulators were conducted. Interpretation of interviews revealed four themes central to customer evaluation and selection practices in banking: the different types and interpretations of information used in customer evaluation, the role of economic conditions on loan decisions, the loan officer's role in loan decisions, and the impact of bank regulations on customer selection practices.

Theme 1 suggested that loan officers rely on various types of information when making a loan decision. Bank executive and loan officer informants discussed using information that is both quantitative, or precise, and information that is subjective, or open to individual interpretation. When discussing the importance of a prospective borrower's character, informants provided a number of examples where information pertaining to the borrower's reputation was used to assess the individual's character. Emerging from these interviews was evidence of individual differences among bank

officers in their chronic need to use discretion when evaluating customer loan requests. Two groups of bank officers were represented. One group discussed loan decision-making practices that strictly followed bank policy and guidelines. A second group of bank officers discussed loan decision-making practices that embody individual interpretation or discretion and flexibility in making exceptions to bank policy and guidelines. Based on this important finding, an experimental study was developed to test whether individuals with different levels of a chronic need for discretion weight quantitative information and customer reputation information differently when forming a customer selection judgment.

Theme 2 suggested that economic conditions influence the loan evaluation process. Based on the interviews, the economic environment influences bank customers selection practices at the bank level with adjustments to the guidelines enforced for the customer's quantitative information (e.g., credit score, loan-to-value ratio). Economic conditions also influence bank customer selection practices at the loan officer level. Loan officer informants discussed how individuals' perceptions of economic conditions influence the extent to which they impose additional requirements on loan customers to be credit worthy.

Theme 3 suggested that the job description of loan officers permits individual decision-making in customer selection. Contrasted to other bank employee job descriptions, the role of commercial loan officers involves more decision autonomy. This autonomy is translated into loan officers' managing a loan profile where loan decisions can be made within a lending limit or a loan authority. Commercial loan officers also influence loan decisions through their research on the borrower, their preparation of a

loan presentation, and their professional approach to presenting the loan file to a bank loan committee or supervising authority.

The final theme (Theme 4) emerging was that the loan evaluation and decision process is largely influenced by the extent to which federal and state bank examiners enforce bank regulations. This conclusion was drawn from discussions among informants on the differences in regulation enforcement in small community banks versus larger regional banks. Informants from the larger banks described bank examinations that were more intensive and covered a broader review of bank records than did examinations of their smaller counterparts. Follow-up interviews with federal and state examiners probed more extensively into the differences in the approaches and guidelines followed by examiners when reviewing files of different bank products (e.g., consumer loans vs. business loans) and examining different categories of banks (e.g. community banks vs. national banks). These interviews provided insights into important policy issues pertaining to customer selection in the banking industry. One of the important policy issues emerging from these interviews was that state and federal consumer compliance regulations are not enforced on bank products offered to small business customers. The general consensus among these informants was that the consumer compliance regulations were enacted to protect customers who could not protect themselves from discrimination based on the customer's race, color, religion, national origin, sex, marital status, and age. This raises the question of whether small business owners have the ability to protect themselves. The vulnerability of small business customers, along with limited resources to protect their own interests, raises the question of whether these disadvantages result in exploitation of or discrimination toward these

customers. The managerial and policy implications of these findings will be discussed in a later section, especially as they pertain to the vulnerability of small business owners seeking financing from banking institutions.

The Experimental Study

An experimental study (i.e., Study 2) was conducted to address research questions three and four. The results of Study 1 were used to develop the experimental design and the experimental scenario. The experiment investigated the joint effects of customer quantitative information, customer reputation information, and the decision-maker's need for discretion on individual decisions to accept or reject business from a customer. Hypotheses were proposed for a three-way interaction involving customer quantitative merit, customer reputation, and the decision-maker's need for discretion on the decision-maker's behavioral intentions to accept or reject business from a customer (i.e., customer selection likelihood). Hypotheses were tested using responses to an experimental scenario about a fictitious small business customer's loan request. Customer quantitative merit was manipulated in the scenario using two levels (i.e., high – low) of the customer's FICO credit score. Customer reputation was manipulated in the scenario using statements describing the civic and professional reputation of the small business customer. The experimental scenario was embedded in a survey containing measured variables, including the newly validated measure of the need for discretion (NFD), and the key dependent variable, customer selection likelihood.

The survey was delivered to 328 commercial loan officers across nine community banks. Completed surveys were returned by 262 loan officers (80% response). The high

response rate is attributed to measures taken by the researcher to develop a partnership with each of the banks, including gaining the endorsement of a senior bank executive. Incentives were also given to reward loan officer participation, including a humanitarian donation (i.e., $2.00 donated to a hurricane relief fund for each survey completed) and a summary of the research results.

ANOVA results supported the omnibus three-way interaction hypothesis. The pattern of the interaction, however, was different from the prediction derived from the cue diagnosticity perspective. It was proposed that the customer quantitative merit information and customer reputation information cues would influence the formation of customer selection likelihood judgments. This research sought to extend the cue diagnosticity perspective by proposing that accounting for the loan officer's need for discretion (NFD) would explain under what conditions quantitative information or reputation information is the dominant piece of information for deciding whether to approve or reject a customer's loan request. For low-NFD individuals, it was proposed that customer quantitative merit would be the dominant information cue. The results supported this hypothesis. For high-NFD individuals, the prediction was that customer reputation would be the dominant information cue and that quantitative merit would not matter when the customer's reputation was positive. When the customer's reputation was negative, however, quantitative merit would be diagnostic. The results, however, revealed an opposite effect. That is, when customer reputation was negative, customer quantitative merit did not matter. When reputation was positive, quantitative merit information mattered, as supported by the finding that customer selection likelihood was

significantly greater in the high-quantitative-merit condition than in the low-quantitative-merit condition.

Taking an alternative perspective to the three-way interaction can provide additional insight into the behavioral tendencies of low- and high-NFD decision-makers. The customer reputation × NFD interaction was plotted for the low-quantitative-merit and high-quantitative-merit treatment conditions. These plots revealed an interesting pattern. When quantitative merit was low, there was a main effect for customer reputation and no effect for NFD. This suggests that for evaluation of a customer with a credit score at the lower end of the acceptable range, NFD did not influence the use of reputation information. Thus, when the customer's reputation was negative, the likelihood of customer selection was much lower than when the customer's reputation was positive, and NFD did not moderate the effect. This finding may be the result of a "floor effect." That is, the lower credit score is nearer to the minimum acceptable standard for bank scores, which makes a rejection decision virtually automatic for both low- and high-NFD loan officers. In contrast, when quantitative merit was high, low- and high-NFD individuals did differ in the extent to which reputation influenced customer selection likelihood. That is, when the customer's credit score was higher, NFD moderated the impact of customer reputation, such that customer reputation mattered for high-NFD individuals and did not matter for low-NFD individuals. The possibility that there is a "floor effect" for credit score provides an alternative explanation for these results. The "floor effect" for credit score is caused by bank policy and guidelines to reject loans with low credit scores. However, there is no "ceiling effect" for accepting loans with high credit scores. In other words, the decision to reject a customer

with a low credit score is a more automatic decision than the decision to approve a customer with a high credit score.

This post-hoc explanation may be supported theoretically using the dual-processing theories (e.g., elaboration likelihood model, heuristic-systematic model). Based on the tenets of these theories, the low-quantitative-merit-condition may be a low-involvement situation where rejecting the loan is a more automatic decision. As a result, reputation is used as a peripheral or heuristic cue to influence the selection judgment. In contrast, high-quantitative-merit-conditions may place respondents in a high-involvement state that results in more extensive systematic information processing. As a result, individual differences become salient and moderate the extant to which customer reputation influences the loan decision. Future directions to empirically test hypotheses derived from the dual-processing theories are discussed in the future research discussion.

ANCOVA analyses were also conducted to control for situational, demographic, and individual trait variables. The results revealed that the loan officer's perceptions of the importance of reputation, control over the situation, and decision confidence were significant predictors of customer selection likelihood. However, the loan officer's perceptions of the importance of credit score, the bank's adherence to policy and procedures, job self-efficacy, industry tenure, and loan portfolio size did not have a significant influence on customer selection likelihood.

A separate set of ANCOVA analyses was conducted in an exploratory manner to test the impact of customer risk assessment, attitude toward the customer, and the perceived value of the customer on customer selection likelihood. ANCOVA results revealed that all three were strong predictors of customer selection likelihood; however,

none of the variables mediated the effects of the three-way interaction on customer selection likelihood. These results suggest that customer selection likelihood ratings are fundamentally different from customer risk assessment, attitude toward the customer, and the perceived value of the customer.

Managerial Implications

This research has a number of implications for managers. First, individual differences in the need for discretion influence how employees process different types of information when making a customer selection decision-- particularly when the customer's quantitative information is high enough that it does not lead to an automatic rejection judgment. Managers should be aware of these behavioral tendencies to assist them in managing their customer portfolio. When the quantitative information of the customer is more ambiguous and the employee's decision requires additional information processing, high-NFD individuals may be more attune to making a customer selection decision based on the customer's reputation, whereas low-NFD individuals appear to weight their decision on the customer's quantitative information. Managers should consider these tendencies when training and monitoring employees who make customer selection decisions. These ideas suggest that formalized training should be considered for new employees in job roles that involve decision-making autonomy in customer selection decisions. The objectives of such training may: (1) help employees recognize their unique level of need for discretion, and (2) demonstrate the individual and firm-level consequences of these individual tendencies in customer selection. Upon completing a formalized training program, managers should ensure that on-going training

and education are conducted with each employee to monitor changes in the employee's need for discretion and behavioral patterns in evaluating customers.

Second, managers should clarify organizational norms and guidelines for how quantitative and reputation information are to be used when making customer selection decisions. Managers should clearly communicate to employees the organization's perspective and standards for customer quantitative information. Managers need to also address policies for making exceptions to these rules.

Third, managers need to examine the possibility of their organization's adopting standards for how and to what extent employees should evaluate a customer's reputation. Managers must also give careful consideration to any measure to standardize customer selection to prevent such steps from becoming discriminatory practice. These and other policy-related implications are discussed in the next section.

Policy Implications

In addition to implications for managers, this research raises some important public policy issues in customer selection practices. The results of qualitative interviews with federal and state bank examiners suggest that commercial customers are not protected under federal and state consumer compliance regulations. This finding raises the question of whether some classes of commercial customers (e.g., small business customers) are particularly vulnerable to bank customer selection practices. This finding has important implications for policy makers as they consider ways of promoting small business growth. Future research should explore whether the lack of consumer protection of small business customers hinders these growth initiatives. Findings from the

qualitative interviews also raise questions regarding differences in the enforcement and interpretation of customer acquisition policies across different categories of banks (e.g., small banks versus large banks, community banks versus national banks). Policy-makers should consider whether these differences have detrimental consequences on markets and vulnerable customer segments (e.g., minority small business customers).

Limitations

There are limitations with this research. One limitation is the generalizibility of these findings. The current work tested a model of key factors influencing customer selection decisions in a small commercial banking context. The experimental scenario involved a business owner, not a company guaranteeing repayment of the loan. The scope of commercial lending situations involving an individual loan guarantor limits the generaliziblity of these findings across all commercial banking contexts. Future work might consider whether behavioral tendencies exist in evaluating the quantitative merit and reputation of borrowing companies. In addition, future research should strive to replicate the three-way interaction of customer quantitative merit, customer reputation, and the decision-maker's need for discretion in other seller-choice decision contexts (e.g., insurance, education, healthcare).

Another limitation of this research is that loan officers evaluated a fictitious scenario involving a prospective borrower. Future research should strive to replicate the findings having loan officers report on loan decisions based on actual customer requests. Loan officers could then provide a direct measure into the actual customer's quantitative merit and reputation. Such an effort to measure actual loan decisions might address

another possible limitation of this work, which is that responses to the customer selection likelihood scale items were for the most part below the scale's midpoint, possibly because of conservatism among sample respondents evaluating the information in the scenario. Another factor that might explain this response pattern is that the information (held constant across the four versions of the experimental scenario) pertaining to the customer's cash flow was inadequate, causing respondents to be conservative in their evaluation and likelihood judgment.

It should also be noted that loan officer data was obtained at one point in time. It is possible that a portion of the results may be attributed to the common method variance problem. It is possible that the self-report items for the need for discretion may have affected how loan officers evaluated and responded to questions about the customer scenario. The survey was organized so that items assessing the individual's NFD were collected early in the survey and the experimental scenario was presented much later in the survey. However, ideally, the items measuring the NFD would have been administered at a separate time to minimize the potential of common method problems.

Future Research

The implications and limitations of this work provide a number of ideas for future research. The first research direction should seek to replicate these findings using actual customer loan decisions. Also, future work should test the effects of the three-way interaction on customer selection practices in other seller-choice decision contexts. These relationships could be tested in a number of other seller-choice decision contexts. For example, future work should explore the effects of customer quantitative merit and

customer reputation information on customer selection practices in the insurance, healthcare, and educational services industries. Natural extensions to this work would be to explore other types of information that influence customer selection in these industries.

Future research should explore other theoretical explanations for the supported three-way interaction of customer quantitative merit, customer reputation, and the decision-maker's need for discretion on customer selection likelihood. One conclusion from the results of the experimental study is that cue diagnosticity perspective alone does not explain individual differences in how cues are weighted in customer selection decisions. Other models of information processing, including the dual-processing models (i.e., elaboration likelihood model, heuristic-systematic model) should be tested to determine which of these theories best explains the behavioral tendencies in customer selection decision-making.

Future research should further establish the nomological validity of the NFD construct using the newly developed NFD scale to predict its antecedents and consequences. Research should compare the job performance of low- and high-NFD individuals. Work in this area should explore organizational, cultural, and environmental moderators to these relationships. Consistent with research using the 3M model (e.g., Harris, Mowen, and Brown 2005; Licata, Mowen, Harris, and Brown 2003; Brown et al. 2002), future work should explore the trait predictors of NFD and how it is related to other situational and surface-level traits of customer contact personnel (e.g., customer orientation, productivity orientation, job resourcefulness).

An important area of future research is to address the public policy implications of customer selection practices. Recent enthusiasm surrounding customer relationship

management raises the question of whether possible discrimination results as conscious effort is taken to avoid adverse customer selection. Future work should consider the role of regulation and public policy in protecting the interests of all consumers of financial services, including small business owners. Also, the competitive and economic consequences of different interpretations and enforcement of bank regulations should be explored further. One possible question might address the impact of differences in the enforcement of regulations between smaller community banks and larger national or regional banks. To the researcher's knowledge these issues and research directions have not yet been addressed.

Conclusion

In conclusion, this dissertation has shown, in a commercial lending context, that individual differences in the chronic need for discretion explains the behavioral tendency of high-need-for-discretion loan officers to weight more heavily customer reputation information, and low-need-for-discretion loan officers to rely more heavily on quantitative information when forming a customer selection decision– particularly in situations when evaluating customers with higher quantitative merit. Customer risk assessment, attitude toward the customer, and the perceived value of the customer were shown to be strong predictors of customer selection likelihood. A discussion of the managerial and policy implications of these results from the experimental study, and the findings from the in-depth interviews with bank executives, bank loan officers, and bank examiners was presented. Limitations and future research directions were also discussed.

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APPENDIXES

APPENDIX A

NEED FOR DISCRETION – INITIAL SET OF ITEMS

1. In my job I believe in doing things "by the rule book."
2. In my job I follow strict operational procedures at all times.
3. I follow all the rules associated with my job.
4. I never make exceptions to policies and procedures in my job.
5. I pride myself on following rules and procedures with my job no matter what.
6. I believe it is better to never step out of policy to make things happen in my job.
7. I enforce policies and procedures in my job.
8. Following policies and procedures is important to me.
9. I ignore the rules and reach informal agreements to handle some situations. (r)

APPENDIX B

CASE SCENARIO: LOW CUSTOMER QUANTITATIVE MERIT, NEGATIVE CUSTOMER REPUTATION

Loan Decision-Making Exercise
Assume that as a commercial loan officer at your bank you have been given the loan profile of customer #222-4. Imagine you have been given lending power to approve loans up to $250,000. You are responsible for collecting on each of the loans you give your customers. Please carefully read the loan profile and answer the questions on the next two pages.

Profile of Loan #222-4

This customer has come to you for a loan to purchase a warehouse to be used for their expanding business. The total purchase price of the warehouse is $250,000. The prospective borrower is willing to invest 15% of the borrower's own cash toward the purchase of the warehouse and you have verified that in fact, these funds are available for this purchase. Therefore, the total requested loan amount is $212,500.

You have been authorized by the customer to review his credit report from the credit bureau. After reviewing the credit report, you learn that this customer has a FICO score of 610.

The cash flow of the customer's business has rebounded from a negative trend over the two years previous to a positive trend over the last year. The customer has consistently maintained average monthly deposit balances of $30,000.

Since the loan amount is below $225,000, your bank's policy does not require that an independent appraisal be performed on this property. However, you are expected to have an informal appraisal of the real estate location and the overall condition of the warehouse to provide an assessment of the liquidity of the collateral in the case the bank has to foreclose and resell the property. You have a colleague from your bank conduct an inspection of the warehouse and compare this warehouse to others in the market you serve. Your colleague determines that the real estate location and overall condition of this warehouse is below average.

The prospective borrower has been a customer of the bank for 10 years. The prospective borrower has refused to serve on the boards of many local charities. There have been numerous reports of the borrower having serious disputes with his customers and employees. The prospective borrower is negatively regarded by others in the community.

APPENDIX C

CASE SCENARIO: LOW CUSTOMER QUANTITATIVE MERIT, POSITIVE CUSTOMER REPUTATION

Loan Decision-Making Exercise
Assume that as a commercial loan officer at your bank you have been given the loan profile of customer #222-4. Imagine you have been given lending power to approve loans up to $250,000. You are responsible for collecting on each of the loans you give your customers. Please carefully read the loan profile and answer the questions on the next two pages.

Profile of Loan #222-4

This customer has come to you for a loan to purchase a warehouse to be used for their expanding business. The total purchase price of the warehouse is $250,000. The prospective borrower is willing to invest 15% of the borrower's own cash toward the purchase of the warehouse and you have verified that in fact, these funds are available for this purchase. Therefore, the total requested loan amount is $212,500.

You have been authorized by the customer to review his credit report from the credit bureau. After reviewing the credit report, you learn that this customer has a FICO score of 610.

The cash flow of the customer's business has rebounded from a negative trend over the two years previous to a positive trend over the last year. The customer has consistently maintained average monthly deposit balances of $30,000.

Since the loan amount is below $225,000, your bank's policy does not require that an independent appraisal be performed on this property. However, you are expected to have an informal appraisal of the real estate location and the overall condition of the warehouse to provide an assessment of the liquidity of the collateral in the case the bank has to foreclose and resell the property. You have a colleague from your bank conduct an inspection of the warehouse and compare this warehouse to others in the market you serve. Your colleague determines that the real estate location and overall condition of this warehouse is below average.

The prospective borrower has been a customer of the bank for 10 years. The prospective borrower serves on the boards of many local charities. There have been no reports of the borrower having serious disputes with his customers and employees. The prospective borrower is positively regarded by others in the community.

APPENDIX D

CASE SCENARIO: HIGH CUSTOMER QUANTITATIVE MERIT, NEGATIVE CUSTOMER REPUTATION

Loan Decision-Making Exercise
Assume that as a commercial loan officer at your bank you have been given the loan profile of customer #222-4. Imagine you have been given lending power to approve loans up to $250,000. You are responsible for collecting on each of the loans you give your customers. Please carefully read the loan profile and answer the questions on the next two pages.

Profile of Loan #222-4

This customer has come to you for a loan to purchase a warehouse to be used for their expanding business. The total purchase price of the warehouse is $250,000. The prospective borrower is willing to invest 15% of the borrower's own cash toward the purchase of the warehouse and you have verified that in fact, these funds are available for this purchase. Therefore, the total requested loan amount is $212,500.

You have been authorized by the customer to review his credit report from the credit bureau. After reviewing the credit report, you learn that this customer has a FICO score of 690.

The cash flow of the customer's business has rebounded from a negative trend over the two years previous to a positive trend over the last year. The customer has consistently maintained average monthly deposit balances of $30,000.

Since the loan amount is below $225,000, your bank's policy does not require that an independent appraisal be performed on this property. However, you are expected to have an informal appraisal of the real estate location and the overall condition of the warehouse to provide an assessment of the liquidity of the collateral in the case the bank has to foreclose and resell the property. You have a colleague from your bank conduct an inspection of the warehouse and compare this warehouse to others in the market you serve. Your colleague determines that the real estate location and overall condition of this warehouse is below average.

The prospective borrower has been a customer of the bank for 10 years. The prospective borrower has refused to serve on the boards of many local charities. There have been numerous reports of the borrower having serious disputes with his customers and employees. The prospective borrower is negatively regarded by others in the community.

APPENDIX E

CASE SCENARIO: HIGH CUSTOMER QUANTITATIVE MERIT, POSITIVE CUSTOMER REPUTATION

Loan Decision-Making Exercise
Assume that as a commercial loan officer at your bank you have been given the loan profile of customer #222-4. Imagine you have been given lending power to approve loans up to $250,000. You are responsible for collecting on each of the loans you give your customers. Please carefully read the loan profile and answer the questions on the next two pages.

Profile of Loan #222-4

This customer has come to you for a loan to purchase a warehouse to be used for their expanding business. The total purchase price of the warehouse is $250,000. The prospective borrower is willing to invest 15% of the borrower's own cash toward the purchase of the warehouse and you have verified that in fact, these funds are available for this purchase. Therefore, the total requested loan amount is $212,500.

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The prospective borrower has been a customer of the bank for 10 years. The prospective borrower serves on the boards of many local charities. There have been no reports of the borrower having serious disputes with his customers and employees. The prospective borrower is positively regarded by others in the community.

APPENDIX F

Dissertation Research Request for Assistance

RESEARCH QUESTIONS

1) What are the personal, organizational, and environmental factors that influence the job performance of commercial loan officers?
2) What are the factors that influence the degree to which a commercial loan officer employs "soft, qualitative" criteria (e.g., borrower's reputation) as compared to "hard, quantitative" criteria (e.g., borrower's credit score) in making a commercial loan decision?

RESEARCH PROCEDURE

This research would involve participation of all the commercial loan officers in the bank and the immediate supervisor to these loan officers. A brief questionnaire – taking approximately 20 minutes to complete – would be distributed to the commercial loan officers. A separate questionnaire would be given to the immediate supervisor of the commercial loan officers. The employee questionnaire would include a variety of measures designed to understand factors that motivate performance and the evaluation of loan officers. The questionnaire given to the immediate supervisor will include a few brief measures of the organization and the industry environment. The immediate supervisor(s) will also be asked to assess the performance of each of their loan officers responding to a few brief questions (i.e., 1 minute per loan officer evaluated).

DELIVERABLES

Research Team Commitments:

- Provision of a written summary of the factors that influence commercial loan officer success based on the findings from the survey. Professor Mowen has performed numerous studies on the characteristics of successful customer contact personnel, including bank officers.
- Presentation of findings if desired by senior management.

Corporate Participation:

- Permit access to commercial loan officers (and all others that do commercial lending) and their supervisor to complete 20-minute surveys.
- Provide information, if available, regarding the objective performance of each of the loan officers (e.g., portfolio growth, net charge offs, fee income generated, loan exceptions, etc.).
- Help facilitate the distribution of a survey by: providing a roster of the loan officers and supervisor, and transmitting an email memo from a top executive prior to survey distribution to endorse the project and to request participation (note: a sample memo will be provided by the research team).

We would like to stress that all responses will be kept confidential. To ensure confidentiality, an outside researcher will collect all questionnaires directly. A summary of findings (and if desired a presentation of the findings) will be provided to the senior manager. All names will be removed

prior to the report of findings. All funding for this project is provided entirely by the Department of Marketing at Oklahoma State University or through personal sources.

CONTACT INFORMATION

Primary Contact: Sterling A. Bone, Doctoral Candidate
Spears School of Business, Oklahoma State University
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Spears School of Business, Oklahoma State University
Phone: 405-744-5112; Email: jcmmkt@okstate.edu

APPENDIX G

SAMPLE MEMORANDUM

December 9, 2005

TO: Commercial Loan Officers and Commercial Loan Officer Supervisors

FROM: __Name__, CEO

RE: Request for Participation in Research Study

The management would like to invite you to participate in a research study directed by Sterling A. Bone and John C. Mowen at Oklahoma State University's Spears School of Business. The focus of this research is to investigate the motivation and performance of bank loan officers. This research is being conducted in partial fulfillment of Mr. Bone's PhD degree in marketing.

Your participation involves taking 20 minutes to answer questions on a survey that will be delivered to you during the week of December 12th, and then mailing the completed survey by December 19th. For taking the time to answer and return the completed survey, a $2.00 donation will be made by the researchers to the hurricane recovery efforts of Habitat for Humanity. Additionally, you will have the option to request a summary of the survey findings to be sent to you.

I personally would like to encourage you to participate in this study. Not only will this assist Mr. Bone in completing the requirements of his doctorate degree, it will also assist our bank in improving the quality of the service we offer our customers and enhancing the working conditions of our loan officers.

If you have any questions or would like additional information, please contact Sterling A. Bone at 405-744-3201 (e-mail: sterling.bone@okstate.edu).

Thank you in advance for your assistance with this research study.

APPENDIX H

1-1

Loan Officer Motivation Survey

Dear Bank Officer,

Thank you for participating in this 20-minute survey. The survey has five parts. In the first two sections, we are collecting information on the personality characteristics of bank officers. In the next three sections we are collecting information about your bank's culture, the marketplace, and your job performance. We then collect information on the decision-making process of bank officers. In the last section, we are collecting information on the demographic characteristics of bank officers.

For taking the time to answer the questions in this survey, a $2.00 donation will be made for each completed and returned survey to the hurricane recovery efforts of Habitat for Humanity. Also, at the conclusion of this survey you may request a summary of the results.

Once you have completed the survey, please use the self-addressed stamped envelope to return your survey directly to us at Oklahoma State University.

Your responses will be kept completely confidential!!!

As part of this study, your supervisor will evaluate your performance using a short series of questions. It is important for you to know that no one from your bank will see your survey. The results are tabulated so that no names are included. After coding the data, this sheet will be detached and separated from the remainder of the survey. By signing your name below, you indicate that you understand the study and give us permission to code your responses.

Your Name: Signature: ____________________

Printed Name: ____________________

If you have questions, please contact Sterling A. Bone at Oklahoma State University (phone: 405-744-3201; e-mail: sterling.bone@okstate.edu). This project has been approved by the Institutional Review Board of Oklahoma State University. For information, call Dr. Sue C. Jacobs at 405-744-1676.

Please turn the page, carefully read the instructions, and begin the survey. Please note there are questions on the back of each page.

Part 1: Circle the number that best describes how frequently you feel or act in the manner described in your professional and home lives. There are no right or wrong answers. Just circle the response that best describes how you feel or act in your daily life, not how you wish you would act. Please answer ALL Questions!!

How often do you feel/act this way?	Never								Always
Feel bashful more than others.	1	2	3	4	5	6	7	8	9
Introverted.	1	2	3	4	5	6	7	8	9
Quiet when with people.	1	2	3	4	5	6	7	8	9
Shy.	1	2	3	4	5	6	7	8	9
Precise.	1	2	3	4	5	6	7	8	9
Efficient.	1	2	3	4	5	6	7	8	9
Organized.	1	2	3	4	5	6	7	8	9
Orderly.	1	2	3	4	5	6	7	8	9
Frequently feel highly creative.	1	2	3	4	5	6	7	8	9
Imaginative.	1	2	3	4	5	6	7	8	9
Find novel solutions.	1	2	3	4	5	6	7	8	9
More original than others.	1	2	3	4	5	6	7	8	9
Tender hearted with others.	1	2	3	4	5	6	7	8	9
Agreeable with others.	1	2	3	4	5	6	7	8	9
Kind to others.	1	2	3	4	5	6	7	8	9
Softhearted.	1	2	3	4	5	6	7	8	9
Moody more than others.	1	2	3	4	5	6	7	8	9
Temperamental.	1	2	3	4	5	6	7	8	9
Touchy.	1	2	3	4	5	6	7	8	9
Emotions go way up and down.	1	2	3	4	5	6	7	8	9
Enjoy buying expensive things.	1	2	3	4	5	6	7	8	9
Like to own nice things more than most people.	1	2	3	4	5	6	7	8	9
Acquiring valuable things is important to me.	1	2	3	4	5	6	7	8	9
Enjoy owning luxurious things.	1	2	3	4	5	6	7	8	9
Drawn to experiences with an element of danger.	1	2	3	4	5	6	7	8	9
Seek an adrenaline rush.	1	2	3	4	5	6	7	8	9
Actively seek out new experiences.	1	2	3	4	5	6	7	8	9
Enjoy taking more risks than others.	1	2	3	4	5	6	7	8	9
Focus on my body and how it feels.	1	2	3	4	5	6	7	8	9
Devote time each day to improving my body.	1	2	3	4	5	6	7	8	9
Feel that making my body look good is important.	1	2	3	4	5	6	7	8	9
Work hard to keep my body healthy.	1	2	3	4	5	6	7	8	9
Enjoy competition more than others.	1	2	3	4	5	6	7	8	9
Feel that it is important to outperform others.	1	2	3	4	5	6	7	8	9
Enjoy testing my abilities against others.	1	2	3	4	5	6	7	8	9
Feel that winning is extremely important.	1	2	3	4	5	6	7	8	9
Enjoy learning new things more than others.	1	2	3	4	5	6	7	8	9
People consider me to be intellectual.	1	2	3	4	5	6	7	8	9
Enjoy working on new ideas.	1	2	3	4	5	6	7	8	9
Information is my most important resource.	1	2	3	4	5	6	7	8	9
Keep really busy doing things.	1	2	3	4	5	6	7	8	9
Try to cram as much as possible into a day.	1	2	3	4	5	6	7	8	9
Extremely active in my daily life.	1	2	3	4	5	6	7	8	9
Always like to be doing something.	1	2	3	4	5	6	7	8	9

Part 2: Please indicate the extent to which you agree with each of these statements.

	Strongly Disagree								Strongly Agree
In my job I feel in control of what is happening to me.	1	2	3	4	5	6	7	8	9
Once I make up my mind, I can reach my job related goals.	1	2	3	4	5	6	7	8	9
I have a great deal of will power in completing my job tasks.	1	2	3	4	5	6	7	8	9
In my job, when I make a decision, I carry it out.	1	2	3	4	5	6	7	8	9
I am confident in my ability to achieve my goals in this job.	1	2	3	4	5	6	7	8	9

	Strongly Disagree								Strongly Agree
In my job I believe in doing things "by the rule book."	1	2	3	4	5	6	7	8	9
In my job I follow strict operational procedures at all times.	1	2	3	4	5	6	7	8	9
I follow all the rules associated with my job.	1	2	3	4	5	6	7	8	9
I never make exceptions to policies and procedures in my job.	1	2	3	4	5	6	7	8	9
I pride myself on following rules and procedures with my job no matter what.	1	2	3	4	5	6	7	8	9
I believe it is better to never step out of policy to make things happen in my job.	1	2	3	4	5	6	7	8	9
I am a risk taker as far as my job is concerned.	1	2	3	4	5	6	7	8	9
I take some risk with the decisions I make.	1	2	3	4	5	6	7	8	9
I have achieved success by taking calculated risks at the right time.	1	2	3	4	5	6	7	8	9
When I feel that my approach is not working; I can easily change to another approach.	1	2	3	4	5	6	7	8	9
I like to experiment with different approaches.	1	2	3	4	5	6	7	8	9
I am very sensitive to the needs of my customers.	1	2	3	4	5	6	7	8	9
I vary my approach from situation to situation.	1	2	3	4	5	6	7	8	9
I try to understand how one customer differs from another.	1	2	3	4	5	6	7	8	9
I feel confident that I can effectively change my approach when necessary.	1	2	3	4	5	6	7	8	9
I work hard to increase my productivity on the job.	1	2	3	4	5	6	7	8	9
I enjoy using time wisely on the job.	1	2	3	4	5	6	7	8	9
I pride myself on being very productive in my job activities.	1	2	3	4	5	6	7	8	9
I hate to waste time on the job.	1	2	3	4	5	6	7	8	9
I try to help customers achieve their goals.	1	2	3	4	5	6	7	8	9
I try to get customers to discuss their needs with me.	1	2	3	4	5	6	7	8	9
I take a problem-solving approach with my customers.	1	2	3	4	5	6	7	8	9
I am able to keep the best interest of the customer in mind.	1	2	3	4	5	6	7	8	9
When doing a job, I am very clever and enterprising.	1	2	3	4	5	6	7	8	9
I can make things happen in the face of scarce resources.	1	2	3	4	5	6	7	8	9
I am very resourceful in finding new ways to reach goals.	1	2	3	4	5	6	7	8	9
When doing a job, I am a very resourceful person.	1	2	3	4	5	6	7	8	9
I use routine procedures to complete my job tasks when possible.	1	2	3	4	5	6	7	8	9
I consult other bankers for ways to complete my job tasks when necessary.	1	2	3	4	5	6	7	8	9
I consult organizational manuals for the right way to complete my job tasks when necessary.	1	2	3	4	5	6	7	8	9
I decide how to perform my job duties based on training I have received.	1	2	3	4	5	6	7	8	9
I try to develop a routine for each of the typical duties involved in my job.	1	2	3	4	5	6	7	8	9
I use creativity to complete my job tasks when possible.	1	2	3	4	5	6	7	8	9
When necessary I make an effort to develop new ways to perform my job.	1	2	3	4	5	6	7	8	9
If necessary I will go beyond what is expected of me to get the job done.	1	2	3	4	5	6	7	8	9
If there seems to be a way to perform a task that might be a little unusual I will try to find it.	1	2	3	4	5	6	7	8	9
I complete my duties the way I want to even if it is viewed unfavorably by the organization.	1	2	3	4	5	6	7	8	9
If necessary I will contradict company policy in order to satisfy a customer.	1	2	3	4	5	6	7	8	9
If I think my way is better than the organization's way then I will do it my way.	1	2	3	4	5	6	7	8	9
Sometimes I perform routine tasks differently from the way the organization recommends.	1	2	3	4	5	6	7	8	9
Sometimes I take shortcuts on the job in order to get my work done more efficiently.	1	2	3	4	5	6	7	8	9
In my job I frequently feel stressed out.	1	2	3	4	5	6	7	8	9
I feel extremely nervous while on the job.	1	2	3	4	5	6	7	8	9
I feel very anxious about things on the job.	1	2	3	4	5	6	7	8	9
It is likely that I will actively look for a new job next year.	1	2	3	4	5	6	7	8	9
I often think about quitting.	1	2	3	4	5	6	7	8	9
I will probably look for a new job next year.	1	2	3	4	5	6	7	8	9
The major satisfaction in my life comes from my job.	1	2	3	4	5	6	7	8	9
I like my job.	1	2	3	4	5	6	7	8	9
Overall, I am quite satisfied with my job.	1	2	3	4	5	6	7	8	9
I sometimes feel resentful when I don't get my way.	1	2	3	4	5	6	7	8	9
I am always willing to admit when I make a mistake.	1	2	3	4	5	6	7	8	9
I sometimes try to get even, rather than forgive and forget.	1	2	3	4	5	6	7	8	9
I am always courteous, even to people who are disagreeable.	1	2	3	4	5	6	7	8	9
I never deliberately say something to hurt someone's feelings.	1	2	3	4	5	6	7	8	9

Part 3: **Please assess the personality/culture of your bank by circling the number that indicates how much you disagree to agree with each statement.**

My bank:	Strongly Disagree								Strongly Agree
Prides itself in taking risk more than other banks.	1	2	3	4	5	6	7	8	9
Actively seeks out ways to take on high-risk business ventures.	1	2	3	4	5	6	7	8	9
Is drawn to market opportunities that have an element of danger.	1	2	3	4	5	6	7	8	9
Provides its employees incentives to work on new ideas despite the uncertainty of their outcomes.	1	2	3	4	5	6	7	8	9
Has a strong desire for high-risk, high-return investments.	1	2	3	4	5	6	7	8	9
Enjoys taking more risk than other banks.	1	2	3	4	5	6	7	8	9
Seeks an adrenaline rush.	1	2	3	4	5	6	7	8	9
Believes in doing things "by the rule book."	1	2	3	4	5	6	7	8	9
Never makes exceptions to policies and procedures.	1	2	3	4	5	6	7	8	9
Feels it's better to never step out of policy to make things happen.	1	2	3	4	5	6	7	8	9
Stresses the importance of going through proper channels to get the job done.	1	2	3	4	5	6	7	8	9
Operates in a formal way when it comes to getting things done.	1	2	3	4	5	6	7	8	9

Part 4: **Please assess to what extent do you agree with the following statements about the business environment?**

	Strongly Disagree								Strongly Agree
In my trade area there is a lot of opportunity for market growth.	1	2	3	4	5	6	7	8	9
Overall the profit and growth opportunities for commercial lending products is good.	1	2	3	4	5	6	7	8	9
In the last three years, my trade area has shown a decline in demand for the products I sell.	1	2	3	4	5	6	7	8	9
In the next three years, my trade area will show an increase in demand for the products I sell.	1	2	3	4	5	6	7	8	9
Five years from now my trade area will be served by fewer banks offering commercial lending products.	1	2	3	4	5	6	7	8	9

Part 5: **Please rate your own job performance. Remember that your answers are anonymous.**

	Among the Worst in your bank								Among the Best in your bank
Quality of my performance in meeting customer needs.	1	2	3	4	5	6	7	8	9
Quality of my performance in satisfying customers.	1	2	3	4	5	6	7	8	9
Quality of my performance in attracting new customers.	1	2	3	4	5	6	7	8	9
Overall quantity of work I perform.	1	2	3	4	5	6	7	8	9
Overall quality of work I perform.	1	2	3	4	5	6	7	8	9
My overall job performance.	1	2	3	4	5	6	7	8	9
Ability to evaluate and make a decisions on loan files.	1	2	3	4	5	6	7	8	9
Ability to collect on my loans.	1	2	3	4	5	6	7	8	9
Ability to generate sales of other bank products.	1	2	3	4	5	6	7	8	9
Ability to meet target goals and objectives.	1	2	3	4	5	6	7	8	9
Ability to grow a loan portfolio.	1	2	3	4	5	6	7	8	9
Ability to make exceptions on loan products.	1	2	3	4	5	6	7	8	9
Ability to price a loan.	1	2	3	4	5	6	7	8	9
Overall compliance with bank policies.	1	2	3	4	5	6	7	8	9
Involvement in the community.	1	2	3	4	5	6	7	8	9

Part 6: Loan Decision-Making Exercise

Assume that as a commercial loan officer at your bank you have been given the loan profile of customer #222-4. Imagine you have been given lending power to approve loans up to $250,000. You are responsible for collecting on each of the loans you give your customers. Please carefully read the loan profile and answer the questions on the next two pages.

Profile of Loan #222-4

This customer has come to you for a loan to purchase a warehouse to be used for their expanding business. The total purchase price of the warehouse is $250,000. The prospective borrower is willing to invest 15% of the borrower's own cash toward the purchase of the warehouse and you have verified that in fact, these funds are available for this purchase. Therefore, the total requested loan amount is $212,500.

You have been authorized by the customer to review his credit report from the credit bureau. After reviewing the credit report, you learn that this customer has a FICO score of 690.

The cash flow of the customer's business has rebounded from a negative trend over the two years previous to a positive trend over the last year. The customer has consistently maintained average monthly deposit balances of $30,000.

Since the loan amount is below $225,000, your bank's policy does not require that an independent appraisal be performed on this property. However, you are expected to have an informal appraisal of the real estate location and the overall condition of the warehouse to provide an assessment of the liquidity of the collateral in the case the bank has to foreclose and resell the property. You have a colleague from your bank conduct an inspection of the warehouse and compare this warehouse to others in the market you serve. Your colleague determines that the real estate location and overall condition of this warehouse is below average.

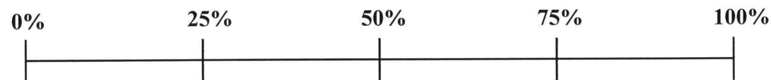
The prospective borrower has been a customer of the bank for 10 years. The prospective borrower serves on the boards of many local charities. There have been no reports of the borrower having serious disputes with his customers and employees. The prospective borrower is positively regarded by others in the community.

Now please carefully answer the following questions regarding this file.

	Very Unlikely							Very Likely
How likely are you to approve this customer for this loan?	1	2	3	4	5	6	7	8

	Strongly Disagree							Strongly Agree
I would definitely approve this customer for this loan.	1	2	3	4	5	6	7	8
Approving this loan demonstrates my good judgment.	1	2	3	4	5	6	7	8

Please draw an 'X' on the line that indicates the probability that *you will make this loan.*



Please answer this question by circling either YES or NO.

I would make this loan.	YES	NO

Please answer the questions regarding this file.

	Strongly Disagree								Strongly Agree
I am extremely confident that I made the right decision regarding this file.	1	2	3	4	5	6	7	8	9
This customer is extremely valuable to my bank.	1	2	3	4	5	6	7	8	9
Approving this customer for this loan will be extremely profitable for my bank.	1	2	3	4	5	6	7	8	9
In the future this customer will contribute additional profits to my bank that far exceed the costs.	1	2	3	4	5	6	7	8	9
This customer will refer new business to my bank.	1	2	3	4	5	6	7	8	9
I am sure to be referred new business by doing this loan.	1	2	3	4	5	6	7	8	9
I will definitely give this customer favorable loan terms.	1	2	3	4	5	6	7	8	9
I will provide the quickest turnaround possible on this loan.	1	2	3	4	5	6	7	8	9

Overall, how would you globally rate this customer?

Bad	1	2	3	4	5	6	7	8	9	Good
Unfavorable	1	2	3	4	5	6	7	8	9	Favorable
Weak	1	2	3	4	5	6	7	8	9	Strong
Unexciting	1	2	3	4	5	6	7	8	9	Exciting
Dislike	1	2	3	4	5	6	7	8	9	Like

Please rate the characteristics of this file.

	Unfavorable								Favorable
The customer's credit score.	1	2	3	4	5	6	7	8	9
The customer's invested cash flow in the project.	1	2	3	4	5	6	7	8	9
The customer's reserves.	1	2	3	4	5	6	7	8	9
The liquidity of the collateral.	1	2	3	4	5	6	7	8	9
The customer's influence in the community.	1	2	3	4	5	6	7	8	9
The bank's experience with this customer.	1	2	3	4	5	6	7	8	9
The overall character of the customer.	1	2	3	4	5	6	7	8	9
The overall reputation of the customer in the community.	1	2	3	4	5	6	7	8	9
Your overall attitude toward the customer.	1	2	3	4	5	6	7	8	9
The bank's overall attitude toward the customer.	1	2	3	4	5	6	7	8	9

Please answer the following questions regarding this file.

	Very Low								Very High
What is the level of risk to your bank in doing this loan?	1	2	3	4	5	6	7	8	9
What is the level of risk to you in doing this loan?	1	2	3	4	5	6	7	8	9
What is the likelihood that the bank is going to lose money on this loan?	1	2	3	4	5	6	7	8	9
What is the likelihood that this customer will repay this loan?	1	2	3	4	5	6	7	8	9
Compared to other loans you have made, describe the amount of resources that will be required to collect this loan?	1	2	3	4	5	6	7	8	9
Compared to other loans you have made, describe the amount of resources that will be required to manage a relationship with this customer?	1	2	3	4	5	6	7	8	9

If you were to make this loan for this customer, *to what extent would you:*

	Small Extent								Great Extent
Feel you can manage this loan rather it manage you?	1	2	3	4	5	6	7	8	9
Feel that if this loan were to go uncollected would be a matter of chance?	1	2	3	4	5	6	7	8	9

Please answer the questions regarding this file.

	Strongly Disagree								Strongly Agree
My bank encourages the use of the borrower's credit score when making commercial loan decisions?	1	2	3	4	5	6	7	8	9
My bank encourages the use of the borrower's reputation when making commercial loan decisions?	1	2	3	4	5	6	7	8	9
Loaning on warehouse property is a risky business?	1	2	3	4	5	6	7	8	9

Please respond to the following questions.

What were your thoughts when reading the loan profile and making your decision?

____
____
____
____
____

What types of information were most important in making your decision?

____
____
____
____
____
____

Describe the risks associated with this loan.

____
____
____
____
____

What do you think is the purpose of this study?

____
____
____
____
____
____

Part 5: **Please provide the following background information. Please fill in the blank or circle your response.**

Please print the name of your bank: ____________________

About how long have you been employed with this bank? ____ years and _____ months

About how long have you worked with your current supervisor? ____ years and _____ months

What is your job title? ____________________________________

About how long have you been in this position? ____ years and _____ months

About how long have you worked in the lending industry? ____ years and _____ months

About how long have you worked in commercial lending? ____ years and _____ months

About how many days of formal commercial loan training have you participated in? ______days

What percent of your compensation is: salary _____ commission / bonus ______

In your current job do you have a lending limit/authority? YES NO

About how much is your lending limit/authority? ____________dollars

What is the size of your current loan portfolio? ____________dollars

Circle your gender: Male Female Write in your age: _________ years

Please circle your education: high school some college college degree some grad school grad degree

I would like to receive a summary of the results of this survey. YES NO

If yes, please indicate an email address. Email:_______________________________________

Thank you for completing the survey!

Please check to make sure that you answered all the questions, and then place it in the business reply envelope and mail it.

APPENDIX I

IRB APPROVAL FORM

Oklahoma State University Institutional Review Board

Date	Wednesday, November 09, 2005	**Protocol Expires:**	**9/26/2006**
IRB Application	BU0533		
Proposal Title:	the Influence of Quantitative and Reputational Value on Customer Selection Practices: A Customer Contact Employee Perspective		
Reviewed and Processed as:	Exempt **Modification**		

Status Recommended by Reviewer(s) **Approved**

Principal Investigator(s) :

Sterling A Bone	John Mowen
311B Business	323 CBA
Stillwater, OK 74078	Stillwater, OK 74078

The requested modification to this IRB protocol has been approved. Please note that the original expiration date of the protocol has not changed. The IRB office MUST be notified in writing when a project is complete. All approved projects are subject to monitoring by the IRB

☑ The final versions of any printed recruitment, consent and assent documents bearing the IRB approval stamp are attached to this letter. These are the versions that must be used during the study.

Signature :

Sue C. Jacobs, Chair, OSU Institutional Review Board

Wednesday, November 09, 200
Date

VITA

Sterling Allen Bone

Candidate for the Degree of

Doctor of Philosophy

Thesis: TO ACCEPT OR REJECT A CUSTOMER'S BUSINESS? THE INTERACTION OF CUSTOMER QUANTITATIVE MERIT, CUSTOMER REPUTATION AND THE DECISION-MAKER'S NEED FOR DISCRETION

Major Field: Business Administration

Biographical:

Personal Data: Born in Provo, Utah, on September 2, 1976, the son of John and JoAnn Bone.

Education: Graduated from Mountain View High School, Orem, Utah in May, 1994; received a Bachelor of Arts in Liberal Arts and Sciences and a Master of Business Administration degree from Utah State University, Logan, Utah in August 2000 and May 2001, respectively. Completed the requirements for the Doctor of Philosophy degree with a major in Business Administration from Oklahoma State University in May, 2006.

Experience: Marketing Manager and Sales Associate, Carolyn Koskan Real Estate, 1997-2002. Department of Marketing Graduate Teaching Assistant, 2002-2006.

Professional Membership: American Marketing Association, Association for Consumer Research.

Name: Sterling Allen Bone Date of Degree: May 2006

Institution: Oklahoma State University Location: Stillwater, Oklahoma

Title of Study: TO ACCEPT OR REJECT A CUSTOMER'S BUSINESS? THE INTERACTION OF CUSTOMER QUANTITATIVE MERIT, CUSTOMER REPUTATION AND THE DECISION-MAKER'S NEED FOR DISCRETION

Pages in Study: 155 Candidate for the Degree of Doctor of Philosophy

Major Field: Business Administration

Scope and Method of Study: This research investigated factors that influence customer selection decisions. Two methods were employed. First, interviews were conducted with bank executives, loan officers, and regulators to identify factors that influence customer selection decisions in retail bank lending. Second, an experiment was conducted with 262 commercial loan officers to test a three-way interaction between customer quantitative merit, customer reputation, and the decision-maker's need for discretion (NFD) on the behavioral intentions to accept or reject a customer's business (i.e., customer selection likelihood).

Finding and Conclusions: ANOVA results supported the three-way interaction. The interaction pattern, however, differed from the prediction derived from cue diagnosticity theory. For low-NFD individuals, the prediction that customer quantitative merit would be the dominant information cue was supported. For high-NFD individuals, the prediction was that customer reputation would be dominant when reputation was positive. When negative, however, quantitative merit would be diagnostic. The results revealed an opposite effect. That is, when reputation was negative, there was no main effect for quantitative merit; however, when reputation was positive, there was a main effect. Additional analyses revealed that NFD did not influence the use of reputation information when quantitative merit (i.e., credit score) was low. A "floor effect" for quantitative merit was proposed as an explanation. When quantitative merit was high, however, NFD influenced the extent to which reputation information affected customer selection likelihood. That is, when quantitative merit was high, NFD moderated the impact of customer reputation, such that customer reputation information influenced high-NFD individuals but not low-NFD individuals. This research will assist managers in understanding how their customer contact personnel interpret information cues to make selection decisions. Policy implications were discussed regarding the potential for customer discrimination.

ADVISOR'S APPROVAL: John C. Mowen