The Effects of Service Guarantees on External and Internal Markets

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Executive Summary

Despite widespread use, there is a void in our understanding of why, when, and how customers use service guarantees to evaluate service firms. Most previous research has focused on the effects of service guarantees prior to purchase, ignoring their beneficial effects on customer evaluations after the service has been experienced. This paper develops three conceptual frameworks that elaborate the psychological and economic effects of service guarantees on customers, both before and after the service has been experienced. In addition, a fourth framework explains how implementing guarantees enables firms to positively influence employees and improve performance. This rather unique perspective that examines both external (customer) and internal (employee) markets contributes to a more comprehensive understanding of service guarantee effects and provides an effective basis for the design and management of service guarantees. The take-away is encapsulated in an inventory of propositions.

A review of the literature revealed lack of consensus regarding the definition of a service guarantee. This inconsistency is resolved by considering a service guarantee as comprised of two elements, a service promise and a compensation offer. Two types of service guarantees are examined in this paper: specific and unconditional. Specific guarantees promise superior firm performance on specific attributes (e.g. price, delivery), while unconditional guarantees promise performance on all aspects of service. Compensation offers may include full or partial refunds, and token awards for punitive damages.

Service guarantee research cuts across functions and disciplines, necessitating the use of multiple theoretical perspectives for inquiry. This paper utilizes four theoretical perspectives to provide deeper insights into the domain of service guarantees. Each perspective is developed into a framework containing arguments and propositions. The first three frameworks are concerned with the effects of service guarantees on customers, while the fourth describes effects on employees and firms. No specific perspective is advocated; rather we hope that these complementary frameworks will broaden and deepen the scope of future inquiry.

The customer frameworks draw on signaling, social justice, and attribution theories to ascribe reasons and describe psychological processes by which guarantees influence customer evaluations. Services are typically lower in search attributes, which increases the importance of signals provided by service firms. Service guarantees allow firms to signal higher quality when the costs of meeting guarantee obligations differs significantly for high and low quality firms. In addition, service guarantees may indirectly signal better quality by lowering perceptions of performance and financial risk.

Social justice theory suggests that service guarantees with comprehensive payouts communicate distributive justice since customers perceive that equitable, deserved, and desired outcomes will occur when service fails. Guarantees may also improve perceptions of procedural justice by promising simple, fair, and hassle-free procedures for claiming compensation.

Attribution theory suggests that service guarantees may be used to communicate firm responsibility, thereby increasing awareness and helping customers identify the cause of service failure and success. In addition, evaluations will be

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significantly influenced and customers more likely to invoke guarantees when performance is perceived to be within firm control. Further, guarantees may improve customer evaluations by communicating that service failures are an aberration.

Service guarantees also act as change stimuli. Guarantees require firms to give greater attention to customer concerns and streamline internal processes. Drawing on the literature and interrelated research streams in total quality management, service recovery, and market orientation, a framework is developed to elaborate service guarantee effects on employees and firms. Firms required to empower their employees for guarantee implementation are likely to benefit from increased employee motivation and job satisfaction, and an increase in customer focus. In addition, service guarantees often require firms to reorganize and restructure to support guarantees, thereby improving organizational efficiencies. Recent research in the area of service recovery suggests that service guarantees can spur learning by requiring firms to continuously identify sources of failure and develop recovery strategies. Finally, since implementing guarantees requires firms to collect and share information and develop appropriate responses to customer complaints, this is likely to increase market orientation. The paper concludes with a discussion of directions for future research.

THE EFFECTS OF SERVICE GUARANTEES ON EXTERNAL AND INTERNAL MARKETS

Service guarantees have become an important and effective means to signal quality (Ostrom and Iacobucci 1998), attract and retain customers (Evans, Clark, and Knutson 1996), and gain market share through differentiation (Hill, Hays, and Naveh 2000; Johnson and Watson 1998). In addition, firms use service guarantees to learn about customer needs (Hart 1993) and fine-tune internal processes to respond to service failure (Callan and Moore 1998; Rushmore 1998). In general, firms report significant gains such as premium prices (Fleet Owner 1999), positive customer attitudes and behaviors, and increased revenues from implementing service guarantees (Hart 1993).

Despite widespread proliferation, little research has addressed exactly why, when, and how different types of service guarantees influence customer evaluations of firms (exceptions include Kumar, Kalwani, and Dada 1997; Ostrom and Iacobucci 1998). For instance, it is not clear which type of guarantee is most effective for lowering customer perceptions of risk, or improving quality beliefs, or assisting service recovery. Most research has focused on how guarantees affect customer evaluations before they are purchased. However, customers may use guarantees to make attributions for failure or success after service has been experienced. Therefore, it is important to understand how guarantees influence post consumption evaluations when service has failed or succeeded. Further, potentially beneficial effects of service guarantees on employees and firms have largely been ignored (exceptions include Hart 1993; Wirtz 1998).

The purpose of this paper is to review and extend our understanding of service guarantees by using multiple theoretical perspectives. We draw on marketing, social psychology, and management literature to develop four complementary frameworks that explain the effects of service guarantees on customers and firms. Each framework includes propositions to guide empirical research. The rest of this paper is organized in four sections. The first section defines terms and concepts and reviews past research on service guarantees. The second section contains three theoretical frameworks that explain the effects of guarantees on customers before and after service has been experienced. Next, a framework is developed to help understand the effects of service guarantees on employees and firms. The paper concludes with a discussion of a potential research agenda.

Concepts and Current Research

In this section, we define concepts, review previous research on service guarantees, identify inconsistencies in definitions, and discuss the research questions addressed by this paper. Then we show how the proposed frameworks resolve these inconsistencies, extend our understanding of service guarantee effects, and provide bases for future research.

DEFINITIONS

Various definitions of service guarantees can be found in the literature. For instance, Hart, Schlesinger, and Maher (1992) define a service guarantee as "…a statement explaining the service customers can expect (the promise) and what the company will do if it fails to deliver (the payout)." Evans, Clark, and Knutson (1996) define a service guarantee as "… a policy, express or implied, advertised or unadvertised, that commits the operation to making its guests happy." Callan and Moore (1998) state that, "a service guarantee can be represented as a promise to the customer and is often advertised as such."

Further, previous research has identified four types of service guarantees: specific, unconditional, implicit, and internal (Callan and Moore 1998; Hart 1995, 1988; Hart et al 1992). A specific guarantee signals firm commitment on specific attribute performance such as delivery time or price. Specific guarantees allow customers to evaluate service by disconfirming attribute performance expectations. From the firm's perspective, a specific guarantee can serve not only as a benchmark to guide employee efforts and firm process design, but also as a performance measure. However, the narrow focus on some attributes may not be highly valued or appreciated by a heterogeneous customer base, although it may appeal to certain segments.

An unconditional guarantee promises performance on all aspects of service, and "in its pure form, promises complete customer satisfaction, and at a minimum, a full refund or complete, no cost problem resolution for the payout." (Hart et al 1992). Unconditional guarantees require a slightly different firm approach since variables that determine customer satisfaction such as affect and cognitive evaluations of attribute performance (Oliver 1993) are not within the firm's control. Implementation of unconditional guarantees requires firms to focus efforts on managing customer interactions instead of specific service attributes. The distinction between specific or overall (unconditional) performance is important as it defines the scope of the marketing effort required to communicate and support the guarantee and has widely different implications for service guarantee design and management.

As the term suggests, an implicit guarantee is an unwritten, unspoken guarantee that establishes an understanding between the firm and its customers (Bateson 1995 p.463). Customers may infer that an implicit guarantee is in place when a firm has an outstanding reputation for service quality. The focus of an implicit guarantee is customer satisfaction (Wirtz, Kum, and Lee 2000). Previous research suggests that customers are more likely to rely on explicit firm promises instead of implicit cues to make inferences about the firm (Wirtz et al 2000). An internal guarantee is "a promise or commitment by one part of the organization to another to deliver its products or services in a specified way or incur a meaningful penalty, monetary or otherwise." (Hart 1995). Since implicit guarantees are unconditional guarantees (without formal expression of explicit commitment) and the focus of internal guarantees is limited to coordinating functions and employees (Hart 1995), the subsequent discussion includes only specific and unconditional guarantees.

INCONSISTENCIES IN DEFINITIONS

Currently, a lack of consensus about what exactly constitutes a guarantee is evident. While some researchers view it as a policy, others suggest it is a firm promise. Also, confusing the scope with its elements has led to inconsistent definitions of different guarantee types. For instance, an unconditional guarantee has sometimes been used to refer to the *circumstances* under which a guarantee may be invoked (e.g. "if unhappy for any reason" Ostrom and Iacobucci 1998; "no-questions asked" Chu, Gerstener, and Hess 1998). Others have used it to refer to the firm *goal* of assuring complete customer satisfaction (McDougall, Levesque, and VanderPlaat 1998; Wirtz et al 2000), or assume that it implies *compensation* in full (Hart 1988). This confusion has led to idiosyncratic operationalization of concepts in studies (e.g. Fruchter and Gerstner, 1999 define "Satisfaction guaranteed" as a selling policy when no customer is worse off after purchase and all costs are refunded if the guarantee is invoked). This makes it difficult for researchers to compare results across studies, raises concerns about construct validity, and hinders replication.

We suggest that a guarantee contains two typical elements: 1) a *service promise* or pledge that expresses the firm's willingness to engage in behaviors considered desirable by its customers and 2) a *compensation offer* in case of service failure. Thus, unconditional and specific may be used to represent the service promise (about all or specific attributes of the service respectively) guaranteed by the firm, while compensation is separately specified. Empirical evidence shows that firms provide *full refunds* (e.g. money-back guarantees), *partial refunds* (e.g. assessment based upon damage or use, exchanges less restocking fees or shipping charges), or award *punitive damages* (e.g. token credits or payouts) when guarantees are invoked. Compensation and claim procedures may be either implied or explicitly stated in the guarantee. In addition to resolving definitional problems, this distinction potentially increases the combinations of promises and compensation schemes available for study. This allows for a richer investigation of the effects of service guarantees.

CURRENT RESEARCH

Previous research on service guarantees can be categorized into four broad overlapping areas: 1) impacts of guarantees on customer perceptions (of risk, quality, and satisfaction) and purchase intention, 2) design of service guarantees, 3) service recovery, and 4) organizational impacts.

Impacts of Guarantees on Customer Perceptions

Previous research suggests that service promises can foster and strengthen customer-firm relationships (Bitner 1995; Gwinner, Gremler, and Bitner 1998) due to their attention to specific attributes such as price or delivery time (New York Times 2001), or because of unconditional assurances aimed at increasing customer satisfaction (Broadcasting and Cable 1996). Ostrom and Iacobucci (1998) suggest that service guarantees serve as external cues (just like price or brand reputation) that are used by customers to evaluate service quality and reduce risk. In an experimental study, they found that service guarantees improved customer evaluations only in the absence of other quality information. As expected, perceptions of risk were lower when a guarantee was offered. In the same study, they also found that service guarantees had a greater impact on customer evaluations when quality variation was perceived to be high among service providers. In addition, the uniqueness of a guarantee has been found to amplify its effect on customer evaluations (Wirtz 1998). Wirtz (1998) notes that in general, service guarantees favorably influence customer attitudes and beliefs, thereby increasing purchase intention. However, Tucci and Talaga (1997) found that service guarantees did not necessarily increase subject likelihood of choice. They found that guarantees increased choice likelihood for expensive services, but negatively influenced choice when prices were low. In a later study, Wirtz et al (2000) found that the impacts of service guarantees on customer evaluations of quality, risk, and purchase intention were significantly moderated by firm reputation. Specifically, they found that change in customer evaluations was higher for a good quality provider than for an outstanding quality provider when guarantee availability was varied. This may be due to information redundancy (Innis and Unnava 1991) or a ceiling effect where a firm with a reputation for outstanding quality is unable to signal higher quality since it is already a quality leader. Consequently, Wirtz et al (2000) proposed an inverted U hypothesis suggesting that firms with moderate or good quality reputation benefit the most from service guarantees, while those at the high or low ends gain the least. They also found that explicit guarantees did not lower customer evaluations of service quality for high or outstanding quality providers as proposed earlier in the literature (Hart 1988).

In summary, these studies suggest that not all customers and firms benefit equally from service guarantees. The level of risk (which could be a function of price or degree of quality variation), availability of other information (e.g. brand, price), uniqueness of the guarantee, or firm reputation (low, high, or outstanding), may considerably moderate the ability of service guarantees to improve customer evaluations.

Design of Service Guarantees

*I*n an article summarizing past research, Wirtz (1998) proposed that well designed service guarantees should be unconditional, easy to understand and communicate, meaningful to customers, easy to invoke, easy to collect on and credible. McDougall, Levesque, and VanderPlaat (1998) found that survey respondents preferred a specific service guarantee to an unconditional guarantee when their attention was focused on invoking the guarantee. In this study, specific guarantees were preferred on three dependent measures: risk reduction, ease of obtaining refunds, and confidence in dealing with the firm. However, when it came to selecting a firm based on the type of guarantee offered, firms offering unconditional guarantees were preferred. McDougall et al (1998) concluded that a guarantee that combined the best of both types i.e. an unconditional guarantee with specific payout clauses would appeal to a broader audience. Chu et al (1998) have shown that a no-questions-asked refund policy is superior to a verifiable-problems-only or no-refund policy. They derived optimal refund policies for service firms under different conditions of salvage value, complaining costs, customer dissatisfaction, frequency of use during trial, and price. Using theoretical modeling, Chu et al (1998) showed that a partial refund policy was optimal when customer opportunism was high and an unrestricted money-back policy was appropriate when customer opportunism was low. Fruchter and Gerstner (1999) have suggested that satisfaction-guaranteed (unconditional guarantee with a full refund plus hassle costs) is optimal from a theoretical standpoint when firms are able to set high prices that equal the willingness to pay of satisfied customers. They also showed that such a guarantee would be most profitable even when returned products had no salvage value.

The evidence suggests that both, specific and unconditional guarantees have positive effects on customer evaluations. However, their efficacy differs depending upon the task facing the customer, and size, type, and procedures for claiming compensation. Firms should decide refund policies based upon the level of customer opportunism and would do well to compensate customers for inconvenience as well as basic exchanges or repairs (Tax and Brown 1998). Note that there is much scope to empirically validate the results obtained by Chu et al (1998) and Fruchter and Gerstner (1999).

Service Recovery

Service guarantees expedite service recovery. Callan and Moore (1998) used attribution theory to explain how customers evaluate service quality and failure. However, they did not discuss how service guarantees affect customer evaluations in the event of failure (or success) and how firms can design guarantees to assist in service recovery. Tax, Brown and Chandrashekharan (1998) have used social justice theory to explain how customers evaluate service complaint experiences. While their work did not focus on service guarantees per se, they provided a comprehensive discussion of the variables that influence satisfaction with complaint handling. They found that customers seek fair outcomes, fair processes, and fair interactions (Tax and Brown 1998). Their framework is very useful for reasoning how service guarantees might affect customer evaluations during service recovery.

In summary, previous research has identified theoretical approaches that explain how customers evaluate service failure and recovery. Attribution theory is useful for understanding customer reactions to service failure while social justice theory is well suited for explaining satisfaction with complaint experiences. However, there aren't any studies that specifically investigate how service guarantees affect customer evaluations in the event of failure or how they may be used to assist service recovery. Such knowledge can help firms not only conceive and design effective guarantees, but also assist in their implementation.

Organizational Impacts

While much anecdotal evidence has been cited, little formal research has addressed how service guarantees affect employees and organizations. Wirtz (1998) has suggested that service guarantees force firms to identify performance expectations of customers and the importance they attach to different elements of the service process. Citing anecdotal evidence, Wirtz (1998) also contends that guarantees cause firms to improve their service delivery processes by identifying and working towards eliminating potential fail points. Guarantees help firms set performance standards for employees. Therefore, service guarantees have positive impacts on personnel management by inducing firms to hire and train employees to deliver guaranteed service (Wirtz 1998). Hart (1995) suggests that firms can improve internal quality problems by offering internal guarantees.

To summarize, the research on employee impacts and organizational benefits is based largely on anecdotal evidence (Hart 1988, 1995; Wirtz et al 1998). There is a lack of empirical research or theory to support the hypothesized positive impacts of service guarantees on firm processes and performance.

- Need for Multiple Theoretical Perspectives
- Existing service guarantee research still leaves a number of important questions unanswered.
- When do firms benefit from service guarantees and why?
- How should guarantees be designed to minimize the effects of service failure?
- How do guarantees affect customer evaluations when service fails?
- How do guarantees affect employees and firms?

It is apparent that these questions cut across a number of functions and disciplines, necessitating a variety of theoretical perspectives for investigation. We utilize four theoretical perspectives to help researchers approach these questions more systematically and explain seemingly disparate findings of service guarantee effects. Each theoretical perspective is developed into a conceptual framework with an accompanying set of arguments and propositions. The first three frameworks pertain to guarantee effects on external markets (customers), while the fourth explains impacts of guarantees on internal markets (firms and employees). By examining different stages and facets of the consumption process, the customer frameworks complement one another. Note that we do not advocate a specific perspective; rather we hope that these multiple viewpoints will provide richer insight into the domain of guarantees. We expect these frameworks will advance existing knowledge by helping answer the following four questions.

When Do Firms Benefit From Service Guarantees and Why?

From a firm's perspective, it is necessary to understand why and how customers infer higher quality, value, and satisfaction when service is guaranteed. Although previous research has identified a number of benefits sought by customers of service firms (Gwinner et al 1998), not much attention has been given to specific relational benefits (or processes by which they are realized) of service guarantees. Our framework utilizes signaling theory to explain when and how different types of guarantees communicate higher quality and lower risk perceptions. It provides a reasonable basis for reconciling the observed findings and can guide firms seeking to incorporate guarantees into their service strategy.

How Should Guarantees be Designed to Minimize the Effects of Service Failure?
Previous research has examined guarantee design from the standpoint of choosing between service firms (McDougall et al 1998; Tucci and Talaga 1997). Consequently, design impacts on customer expectations of procedures for invoking guarantees and compensation for service failure have been ignored. Further, researchers have examined design from the firm perspective of managing resources (Chu et al 1998; Fruchter and Gerstner 1999), paying scant attention to customer psychology and the need for restoring equity and justice. Therefore, social justice theory is used to develop a framework that explains how customers judge the fairness of outcomes and resolution procedures. This is valuable for designing guarantees to mitigate the effects of service failure.

How Do Guarantees Affect Customer Evaluations When Service Fails? or When Service Succeeds?
Much work has focused on improvements in prepurchase customer evaluations of quality and satisfaction. Service guarantees have been viewed almost exclusively as marketing tools and most research has focused on how customers use them to reduce risk perceptions (McDougall et al 1998; Ostrom and Iacobucci 1998; Wirtz et al 2000), or choose between competing providers (McDougall et al 1998; Tucci and Talaga 1997). Failure to recognize post consumption guarantee effects has diminished their worth in the services research agenda. A framework using attribution theory is developed to reason the effects of specific and unconditional guarantees on customer evaluations after service has been experienced. This is important for understanding how guarantees assist service recovery or reinforce service success.

How Do Guarantees Affect Employees and Firms?
While it is noteworthy that some researchers have recognized that service guarantees may have merit due to their beneficial impacts on both customers and firms (Kashyap and Revelas 1999; Wirtz 1998), there has been a lack of systematic effort to utilize marketing or management theories to ground future empirical investigation. Several issues bear investigation. For instance, what type of guarantee improves the market orientation of a firm? How do different types of guarantees affect the design of service delivery and recovery processes? The proposed framework uses previous research on market orientation, service recovery, and total quality management to elaborate the effects of guarantees on employees and organizations. This would help managers formulate service strategy by explaining process and resource requirements for effective support of guarantees.

Recognizing both customer and firm perspectives has two important advantages: (1) it helps researchers recognize important interdependencies among customer evaluations and firm processes, and (2) it helps managers improve service design and better implement service guarantees through a more comprehensive understanding of service guarantee effects. Each customer framework utilizes a theoretical perspective to explain why (reasons), when (conditions), how (processes), and what effects (outcomes) guarantees have on customers.

EFFECTS OF SERVICE GUARANTEES ON EXTERNAL MARKETS

The frameworks that explain the effects of guarantees on external markets are designed around three major constructs, the type of guarantee (specific or unconditional), the psychological effects on the customer (affective, cognitive), and the economic outcomes resulting from guarantee use (monetary, non-monetary). In addition, each framework elaborates the conditions under which these effects occur. Since the meaning and importance of the type of guarantee was discussed earlier, the subsequent discussion focuses on psychological effects and economic outcomes.

Psychological effects may be *affective*, such as when guarantees improve preferences, reduce anxiety, resolve dissonance, or increase trust and confidence. In addition, guarantee effects may be *cognitive,* when they allow customers to attribute causes, or reduce risk and uncertainty. For instance, the Block Buster guarantee (Kadlec 1998) of finding a new movie release in stock (or getting it free) reduces anxiety of not finding a desired title and increases customer preference. Similarly, Walgreen's offer to provide $5 to incorrectly billed customers may signal reduced risk and increase trust. Note that in some cases, guarantees may also negatively impact customer perceptions, e.g., when customers can blame the firm for service failure.

Economic outcomes refer to financial compensation received for service failure and the reduction or elimination of search, information, and hassle costs (e.g. switching, complaining). Guarantees can reduce or eliminate *monetary* and *non-monetary* costs of purchasing services. For instance, Circuit City's low price guarantee suggests that the firm is committed to providing the lowest possible price at all times. From the customer's perspective, it reduces information costs by promising the lowest possible price, and search costs by eliminating the need to shop around for the lowest price.

The proposed frameworks collectively enhance and deepen our understanding of service guarantee effects on customers. While the signaling theory framework (see Figure 1) is used to describe guarantee effects on customer evaluations prior to purchase, the frameworks developed using social justice theory (Figure 2), and attribution theory (Figure 3) are concerned with effects on customers after service has been experienced. The social justice theory framework is specifically aimed at understanding customer expectations for restoring equity after service has failed. The attribution theory framework explains how customers assign causes for service success and failure, resulting in positive or negative affect. Each framework contains propositions and in some cases corollaries.

SIGNALING THEORY

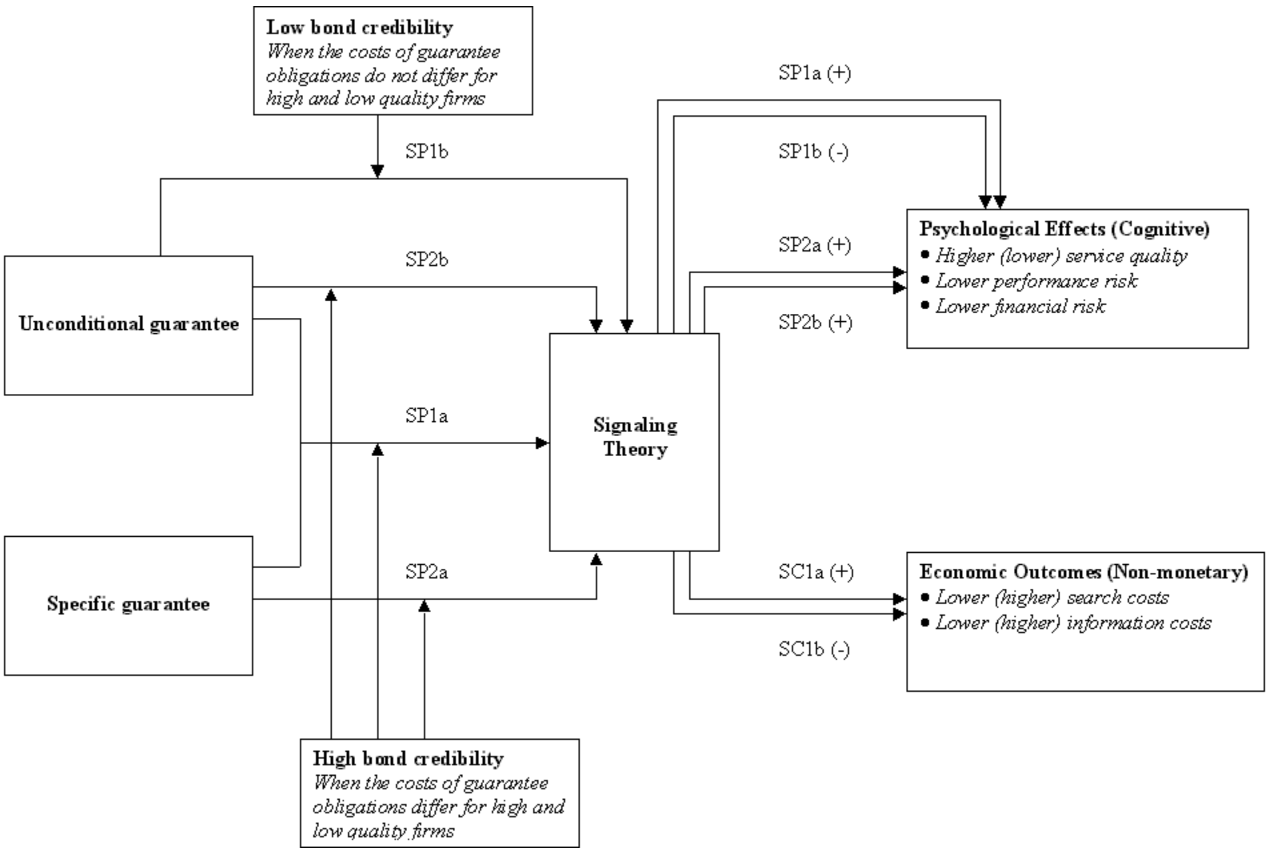
Customers have difficulty evaluating service quality prior to consumption since most services are high in experience or credence attributes. Even when search attributes can be used to distinguish between firms, customers may not have access to full information about the quality of competing services. Hence, service guarantees serve as useful signals of service quality (Note: signaling theory assumes a rational consumer, who is both, motivated and capable of decoding firm signals, see Kirmani and Rao 2000). Consequently, service guarantees that successfully signal high service quality also serve to reduce customer costs of search and information. Service guarantees may communicate higher service quality either directly or indirectly by conveying lower risk (Erevelles 1993; Shimp and Bearden 1982). Figure 1 examines the relationships among type of guarantee, and psychological effects and economic outcomes.

Figure 1 illustrates the cognitive psychological effects (changes in perceptions of service quality, SP1a and SP1b, lowered performance risk, SP2a, and lowered financial risk, SP2b) and non-monetary economic outcomes (lower search and information costs SC1a, and higher search and information costs, SC1b) resulting from the use of different guarantee types (unconditional, specific) under conditions of high and low bond credibility.

As the figure shows, both unconditional and specific guarantees signal unobservable service quality to customers (SP1a, SP1b) by informing them of (1) the firm's intention to act in a certain manner and, (2) firm resources or collateral committed to fulfilling the promise expressed in the guarantee (Herbig and Milewicz 1992). The extent to which a service guarantee may improve customer evaluations of service quality depends on its perceived credibility (Boulding and Kirmani 1993). Credible signals are perceived as "bonds" by customers (Ippolito 1990), since the firm incurs a cost if the signal is false and the guarantee is invoked. Credibility is increased when customers sense that the bond is vulnerable – that is, the firm's reputation or current or future revenues are at risk (Kirmani and Rao 2000). Boulding and Kirmani (1993) suggest that customers will use service guarantees as signals of quality only when bond credibility is high (SP1a, SP2a, and SP2b) i.e., the differences in costs or revenues for meeting guarantee obligations is significantly different for high and low quality firms.

For example, consider two airlines A and B contemplating on-time guarantees. Airline A knows that only 75% of its flights arrive on time, while Airline B has a better record with 95% on-time arrivals. Airline A would have little incentive to offer an on-time guarantee, if costs incurred when the guarantee was invoked resulted in profit erosion (i.e. could not be passed onto customers). The situation described above results in a form of "separating" equilibrium (Boulding and Kirmani 1993; Kirmani and Rao 2000), in which high and low quality service firms find it profitable to pursue different strategies. In a separating equilibrium, bond credibility is high, since costs of providing false signals are significantly higher for low quality firms. In these circumstances, customers can use guarantees as signals of quality to distinguish between high and low quality firms.

FIGURE 1
A Signaling Theory Framework for the Effects of Guarantees



Specific guarantees focus customer attention on key performance characteristics that differentiate between high and low quality firms. Specific performance guarantees set industry performance standards and allow customers to compare firms and judge quality. In addition, researchers suggest that when bond credibility is high, comprehensive guarantees (Shimp and Bearden 1982) that offer broader coverage are perceived to be more effective signals of quality (Boulding and Kirmani 1993). Therefore, guaranteeing specific attributes of service performance or providing unconditional guarantees are both likely to prove effective in signaling quality when bond credibility is high.

SP1a: Specific guarantees and unconditional guarantees signal higher service quality when costs of meeting guarantee obligations differ significantly for high and low quality firms.

SC1a: Specific guarantees and unconditional guarantees lower customer costs of search and information when costs of meeting guarantee obligations differ significantly for high and low quality firms.

However, when the costs of providing false quality signals does not affect the profitability of low quality service firms, a "pooling" equilibrium exists in which customers are unable to distinguish between low and high quality firms on the basis of signals (Kirmani and Rao 2000). In a pooling equilibrium, bond credibility is low (SP1b), since low quality firms cannot be trusted due to a short term or transaction-specific focus (e.g., they don’t care about repeat purchases). When costs of meeting guarantee obligations do not differ for high and low quality firms, customers may assume that an outstanding guarantee is "too good to be true" (Shimp and Bearden 1982). In an experimental investigation of warranties as signals, Boulding and Kirmani (1993) found that unconditional warranties significantly lowered perceptions of product quality when bond credibility was low. Therefore,

SP1b: Unconditional service guarantees signal lower service quality when costs of meeting guarantee obligations do not differ significantly for high and low quality firms.

SC1b: Unconditional guarantees raise customer costs of search and information when costs of meeting guarantee obligations do not differ significantly for high and low quality firms.

When signals credibly differentiate between high and low quality firms (SP2a, SP2b), firms may employ service guarantees to signal lower performance and financial risk (Ostrom and Iacobucci 1995). One of the biggest problems customers face when buying a service is assessing inherent performance and financial risk (Shimp and Bearden 1982). Performance risk is concerned with the likelihood of receiving desired functional benefits. Financial risk includes monetary and non-monetary costs associated with purchase, and "hassle" costs (i.e. switching and complaining costs) for invoking the service guarantee.

Service guarantees that promise performance on specific attributes such as delivery or service time can help reduce perceptions of performance risk (SP2a). However, in order to lower performance risk, a guarantee must advertise a promise about a unique or atypical attribute or promise exceptional performance on a typical attribute (Pechmann and Ratneshwar 1991). For instance, if service time is an important criterion for choice decisions, only those service guarantees that promise service delivery in times significantly shorter than competitor service times will be perceived to signal lower risk. An example is Grand Junction Restaurants, a quick service chain that offered a 60 second service time guarantee (Spinks and Kaplan 1990). This was effective in lowering perceptions of performance risk by providing a credible signal of shorter service time.

SP2a: Specific service guarantees signal lower performance risk when costs of meeting guarantee obligations differ significantly for high and low quality firms.

However, when it comes to appraising financial risk, customers may be concerned about hassle costs, types of recompense offered (full, partial, punitive), and conditions under which guarantees may be invoked (specific, all). In addition, customers perceive greater financial risk for high-ticket items or credence services. Shimp and Bearden (1982) found that consumers significantly reduced financial risk perceptions (cognitive effect, SP2b) when warranty quality (of durables) was improved. This suggests that outstanding or comprehensive guarantees that promise performance on all aspects of service will effectively lower perceptions of financial risk (SP2b). For instance, L.L. Bean’s 100% satisfaction guarantee lowers financial risk perceptions by offering customers a choice of the following: a refund of monies paid, replacement of an unsatisfactory purchase, or an issue of credit (Kotler 1997).

SP2b: Unconditional service guarantees signal lower financial risk when costs of meeting guarantee obligations differ significantly for high and low quality firms.

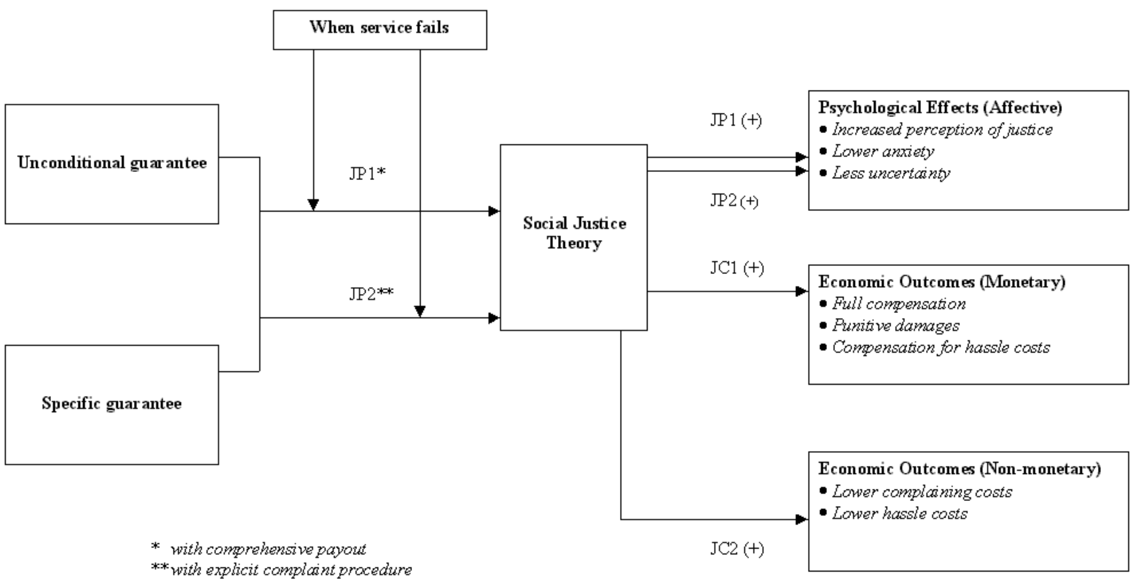
Next, we use social justice theory to investigate customer expectations for invoking guarantees and type and amount of compensation sought in case of service failure. Note that this framework complements the signaling framework described earlier by elaborating guarantee effects after service has been experienced.

SOCIAL JUSTICE THEORY

Service guarantees inform customers about how the firm expects to resolve complaints and compensate them in case of service failure. Research on customer satisfaction with complaint experiences suggests the need to give attention to elements of distributive and procedural justice (Tax et al 1998). (Note: social justice theory assumes that all complaint resolution interactions between customers and firms are perceived as distinct events. These events are evaluated with regard to outcome justness and fairness of resolution procedures, see Bies 1987). The framework is predicated on the assumption that service failure has occurred.

Figure 2 shows the affective psychological effects (increased justice perceptions, JP1) and monetary economic outcomes (full compensation, punitive damages, and hassle costs, JC1) that result from customer use of unconditional and specific guarantees accompanied by comprehensive payouts to evaluate the fairness of outcomes when guarantees are invoked. Further, social justice theory suggests that for evaluation of complaint resolution processes, unconditional and specific guarantees can lead to desired affective psychological effects (lower anxiety and uncertainty, JP2) and non-monetary outcomes (lower complaining costs and lower hassle costs, JC2), when the guarantees include explicit complaint procedures.

FIGURE 2
A Social Justice Framework for the Effects of Guarantees



Distributive justice is concerned with customer perceptions of the fairness, deservedness, and desiredness of outcomes when a service guarantee is invoked. Customers conduct cost benefit analyses to judge outcome satisfaction (Deutsch 1985). This implies that service guarantees that improve perceptions of outcome equity, equality, and need result in higher satisfaction (Tax et al 1998; Oliver 1993). The concept of fairness is central to customer evaluations of equity in transactions with firms (Oliver and Swan 1989). Fairness implies that the firm should cover all costs incurred by customers in connection with service failure. Hence, service guarantees will increase preference and perceptions of fairness when customers feel they have been adequately compensated for all their efforts and costs. For example, service guarantees that promise to compensate monetary and non-monetary costs such as search costs, costs of complaining, or even switching costs increase perceptions of fairness (JP1). In addition, customers may evaluate service guarantees favorably due to the implicit promise that all customers will be treated equally. Finally, guarantees are likely to prove more effective when they meet the needs of their customers in terms of compensation sought. Chu, Gertsner, and Hess (1998) suggest that unless considerable customer opportunism exists, a no-questions asked guarantee should be preferred to more restrictive policies as it entails the least risk of customer dissatisfaction. Consider the "Performance Guarantee" offered by the Baltimore-based Maryland National Bank that promised to pay $10 for any mistake made on a customer's account (Maher 1991). In addition, the bank promised to absorb any overdraft charges and write apologies to the customer and to any third party affected by the mistake. Customers found the guarantee attractive because it cleared their name (matched their need), handled all charges (was deserved), and paid them for their inconvenience (was equitable). This implies that all of a customer's "costs" – time, money, and effort, should be appropriately refunded (JC1).

JP1: Unconditional guarantees and specific guarantees with comprehensive payouts increase perceptions of fairness, desiredness, and deservedness of outcomes when service fails.

JC1: Unconditional guarantees and specific guarantees with comprehensive payouts provide full compensation, punitive damages, and hassle costs.

Oliver and Swan (1989) suggest that customers may also infer satisfaction from procedural policies that are set up to resolve customer problems. The focus on procedural justice is particularly important for service providers seeking to maintain a productive relationship with customers (Tax et al 1998). Service guarantees can improve perceptions of procedural justice by simplifying the procedure to rectify service failure. Service guarantees may reduce hassle costs (JC2) by providing explicit procedures that make it easier for customers to complain and receive compensation (JP2). However, research shows that when the compensation is not sufficient or requires too much effort to claim, few customers even bother to report the failure (Ettore 1994). Therefore, in order for guarantees to be effective, the procedure for claiming compensation should be relatively hassle-free (Maher 1991).

JP2: Unconditional guarantees and specific guarantees with explicit complaint procedures lower anxiety and uncertainty when service fails.

JC2: Unconditional guarantees and specific guarantees with explicit complaint procedures lower customer costs of complaining when service fails.

Next, a framework based on attribution theory is developed to explain how customers use guarantees to assign responsibility for service failure or success. This further complements the signaling and social justice theory framework by describing customers' affective responses to failure and success in the presence of different types of guarantees.

ATTRIBUTION THEORY

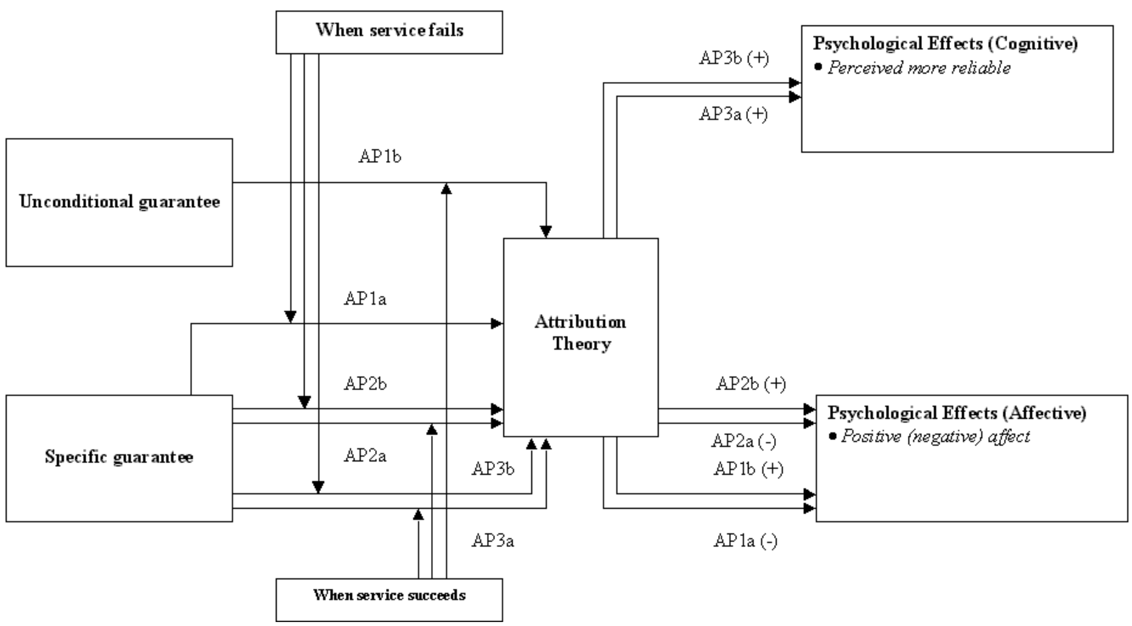
Researchers have often used attribution theory (Jones and Nisbett 1972; Kelley1973) to explain how customer attributions of success and failure influence firm evaluations (Folkes 1984, 1988' Folkes, Koletsky, and Graham 1987). (Note: attribution theory assumes that customer attributions of causes for success or failure result in increased positive and negative affect respectively). Service guarantees facilitate attribution by defining the locus of causality, increasing perceptions of firm control over the service delivery process, and by (de)stabilizing the cause of service (failure) success (Weiner 1986). Service guarantees help customers assign and evaluate attributions for success or failure (Callan and Moore 1998). While much previous research has focused on failure, attribution theory predicts similar and opposite effects for success. Hence the following discussion encompasses both types of events.

Figure 3 shows that an unconditional guarantee leads to positive affect when service succeeds (AP1b), while a specific guarantee results in negative affect when service fails (AP1a), as customers feel compelled to investigate who is responsible for success or failure. In addition, specific guarantees reinforce the notion of control over firm action resulting in negative affect when service fails (AP2a) or positive affect when service succeeds (AP2b). Finally, attribution theory also predicts that specific guarantees will have positive cognitive psychological effects (by increasing perceived reliability), whether service succeeds (AP3a) or fails (AP3b) by drawing attention to the stability of the cause of success or failure. The following discussion develops and presents supportive arguments.

Attribution theory suggests that customers will attempt to identify who is responsible for service success and failure. Customer attributions may be classified into internal (self) or external (firm related or situation related) sources. Firms may use service guarantees to inform customers that they are responsible for certain or all aspects of the service. Service guarantees heighten customer awareness and allow firms to assume responsibility for service performance. Also, service guarantees draw attention to (non) performance, increasing the salience of positive (negative) information. For instance, Oliver and DeSarbo (1988) found that individuals reported higher satisfaction with external sources when they attributed success to those sources, while Kumar et al (1997) found that service failure had more negative impact on satisfaction when waiting time guarantees were dishonored. Hence, customers are more likely to attribute firm causes to service success and failure when a service guarantee is offered.

Specific guarantees increase the perceptual salience of those service attributes for which performance has been promised. Customers find it easy to blame the firm when it fails to keep a specific promise (AP1a), as people are always searching for negative information when making judgments about negative experiences (Fiske 1980; Taylor 1991). Further, since positive experiences are less elaborated, customers may desist from pinpointing specific causes and rely instead on summary judgments of the service experience. Therefore, unconditional guarantees may be more instrumental in conveying firm concern for ensuring positive customer experiences (AP1b).

FIGURE 3
An Attribution Theory Framework for the Effects of Guarantees



AP1a: Specific guarantees increase negative affect when service fails since they allow customers to attribute firm causes for service failure.

AP1b: Unconditional guarantees increase positive affect when service succeeds since they allow customers to attribute firm causes for service success.

Service guarantees increase customer perceptions of firm control over service delivery and magnify the salience of service success (failure). Service guarantees may increase (lower) customer satisfaction by increasing positive (negative) affect. The amount of positive (negative) affect may vary depending on whether causes of success (failure) can be attributed to controllable (human, e.g. service staff or customer) or non-controllable (e.g. weather, traffic) sources (Smith and Ellsworth 1985). By explicitly guaranteeing service performance, firms may persuade customers that they have greater control over service delivery.

However, customers are less likely to hold firms responsible for failures caused by events not within the firm's control. For instance, customers may believe that a restaurant has greater control over service times than over ensuring the complete satisfaction of every customer. However, higher believability does not imply greater satisfaction. It simply suggests that customers may tend to be less forgiving when invoking a guarantee when a firm has greater control over its actions (e.g. a waiting time guarantee) than when it has less control (e.g. on-time flight arrivals). Customer evaluations of satisfaction (or dissatisfaction) arising from success (or failure) will be significantly higher (or lower) when a service guarantee is offered. Further, customers may be reluctant to believe that all aspects of service performance are within a firm's control. This suggests that specific guarantees may result in more negative (positive) evaluations when service fails (succeeds).

> AP2a: Specific guarantees increase negative affect when service fails since they raise customer perceptions of firm control over service failure.

> AP2b: Specific guarantees increase positive affect when service succeeds since they raise customer perceptions of firm control over service success.

Service guarantees may improve preference and quality perceptions by (de)stabilizing the cause of service (failure) success. Previous research indicates that when customers believe that failure is less likely to occur again in the future (i.e. an unstable cause), they are more likely to be satisfied and repurchase firm services (Smith and Bolton 1998). Service guarantees allow firms to declare to their customers that the cause of service (failure) success is (not) stable or permanent. For instance, if customers believe that a hotel often forces its guests to stay elsewhere despite holding confirmed reservations, they may attribute failure to a stable cause - the firm's practice of deliberately overbooking its rooms (Smith and Bolton 1998). Customers are likely to attribute lower variance to promised aspect(s) of service performance when a specific guarantee is offered. Hence if a firm fails to deliver on its specific promise, customers are likely to believe that the cause of service failure is an aberration or highly irregular (AP3a). Similarly, consistent success with respect to a specific service attribute may be attributed to the promise contained in a specific guarantee (AP3b).

> AP3a: Specific guarantees increase perceived reliability when service fails by allowing customers to attribute unstable causes for service failure.

> AP3b: Specific guarantees increase perceived reliability when service succeeds by allowing customers to attribute stable causes for service success.

EFFECTS OF SERVICE GUARANTEES ON INTERNAL MARKETS

The framework that explains the effects of guarantees on internal markets is designed around three major constructs, the type of guarantee (specific or unconditional), enabler (e.g., increased empowerment, top management commitment), and organizational effect (e.g., higher employee motivation and job satisfaction, improved customer orientation). It draws upon the relevant literature and previous research on total quality management (TQM), market orientation, and service recovery. Note that firm level constructs are used to develop logic and generate propositions in this framework. This aggregation was necessary to provide a more meaningful discussion and derive appropriate managerial implications. Table 1 presents the framework in terms of the constructs discussed below, i.e. type of guarantee, theory, enabler, and organizational effect. While the importance of the type of guarantee (specific, unconditional) has been discussed previously, the relevant theory is discussed during development of the organizational propositions.

Enablers are elements of firm processes (e.g., interfunctional coordination, customer complaint analysis), structures (e.g., cross functional teams), or states (e.g., top management commitment, increased empowerment) necessary and antecedent to the successful implementation of service guarantees. For instance, implementation of guarantees often requires employees to ascertain and satisfy customer needs and preferences. In addition, firms may find it necessary to coordinate diverse functions, confront deficiencies, and reorganize structurally to support these guarantees. Enablers act as catalysts for the development of organizational effects. They provide the support necessary for effective guarantee execution and facilitate the achievement of desired organizational effects.

In this framework, organizational effects refer to the impacts on firms and employees that occur as a consequence of implementing service guarantees. While some effects are employee related (e.g., higher motivation, job satisfaction), others are relevant to firm strategy and performance (e.g., improved efficiencies, better cost controls, improved design of service recovery strategies). For instance, service guarantees allow managers to translate their perceptions of customer expectations into service quality specifications and provide standards against which employee performance may be evaluated (Tax and Brown 1998).

TABLE 1
Effects of Service Guarantees on Employees and Firms

Type of Guarantee (Proposition)	Theory	Enabler	Organizational Effect
Unconditional guarantee (OP1a)	Total Quality Management Empowerment	Increased empowerment	Higher employee motivation and job satisfaction Higher Performance standards
Specific guarantee (OP1b)	Total Quality Management Organizational Reengineering	Inter-functional coordination Cross functional teams	Improved operational efficiencies Effective cost control
Specific guarantee (OP2)	Service Recovery	Customer complaint analysis	Increased customer feedback Improved design of recovery strategies Improvements in service recovery processes
Unconditional guarantee (OP3)	Market Orientation	Market Intelligence Top Management Commitment	Improved customer orientation Increased resource availability

TOTAL QUALITY MANAGEMENT: EMPOWERMENT

Service guarantees necessitate the relinquishment of control and the empowerment of contact staff for successful implementation. Empowerment requires a clear definition of organizational goals so employees do not misutilize the discretionary resources at their disposal (Dean and Evans 1994). Service guarantees give managers the opportunity to empower employees by providing a clear vision of expected results. Empowered employees have the flexibility and resources necessary to more effectively satisfy customers. For instance, Bowen and Lawler (1992) found that empowered employees responded to customer needs more quickly during service delivery and recovery and displayed more warmth and enthusiasm in their interactions with customers. Increased empowerment also results in increased intrinsic motivation and job satisfaction (Chebat and Collias; 2000; Dean and Evans 1994). In a recent study of best practices in service quality in the hospitality industry, Enz and Siguaw (2000) found that an empowered service force was a critical antecedent to service excellence. Due to the emphasis on guaranteed satisfaction, unconditional guarantees require firms to manage customer interactions and relationships rather than specific aspects of service performance. Unconditional guarantees require that employees be highly empowered and capable of customizing service to meet guest needs.

OP1: Unconditional service guarantees increase customer orientation through increased employee empowerment.

TOTAL QUALITY MANAGEMENT: ORGANIZATIONAL REENGINEERING

Some service guarantees also necessitate a high level of inter-functional coordination for successful implementation. Internally, service guarantees benefit firms by providing opportunities to make operations more efficient. Such reengineering efforts often require restructuring or at least the formation of cross functional teams and coordination of diverse functions and technologies (Weiss and Hartle 1997). Consider for instance, the service guarantee offered by

Rally's Restaurants that promised "Get it Right or Get it Free!" This guarantee required extensive coordination between the production and service staff, especially given the broad set of options on the Rally's menu. Or take the case of Oakley Millwork Inc., of Frankfort, Illinois. The company created a "No Backorder Guarantee" – if any item ordered from its catalog was out of stock and unavailable for immediate delivery, the customer would get the item free (Ettore, 1994). This guarantee required the firm to reinvent its distribution system and slash costs through more efficient inventory management. The emphasis on specific aspects of service performance drives firms to concentrate their efforts on improving inter-functional and inter-departmental coordination.

OP2: Specific guarantees improve organizational efficiencies by requiring extensive coordination between various functions and departments in a firm.

SERVICE RECOVERY

Service guarantees provide firms with opportunities to sense market conditions and facilitate service recovery (Tax and Brown 1998). They stimulate feedback because they give customers an incentive to identify service that does not measure up. Since much research indicates that a majority of customers don't complain (Andreasen 1988), a service guarantee provides benefits by serving as an effective forum for listening to the voice of the customer. Implementing a guarantee also helps the firm understand why it may have failed because the expense of guarantees provokes remedial action to investigate service failure. Consider Grand Junction Restaurants who use service-time guarantees as a performance objective for employees. The company uses failure (which occurs about 7% of the time) as an opportunity to elicit critical feedback from its customers. Service guarantees encourage firms to develop recovery strategies so that employees have explicit mechanisms for service recovery. Specific guarantees focus employee attention on service failure with respect to a key performance attribute. Specific guarantees encourage firms to codify remedial actions as general procedures to help employees recover from service failures. Thus, service guarantees not only help establish mechanisms for routine checks on performance, but also create a regular feedback loop between the firm and its customers to facilitate organizational learning.

OP3: Specific guarantees improve service recovery by continuously identifying sources of failure and stimulating the development of recovery strategies.

MARKET ORIENTATION

A service guarantee encourages a firm to be market oriented. In order to design and implement service guarantees, firms have to determine highly valued service attributes and develop programs to more effectively meet customer needs. Often, line employees may be reluctant to share customer complaint information with their supervisors for fear of retribution (Gilly, Stevenson, and Yale 1991). Service guarantee implementation requires that such information be shared within the organization, resulting in a strongly customer focused culture. In addition to mechanisms for the collection and dissemination of market information, a market orientation also implies top management commitment (Jaworski and Kohli 1993). Service guarantees require top management to commit firm resources necessary to implement the guarantee. Examples of such resources include training programs, new technology or equipment, new hires, changes to distribution systems, and so forth. At Hampton Inns, a 100% customer satisfaction guarantee required management to reorganize its infrastructure, while a satisfaction guarantee at Choice Hotels Sleep Inn brand required the development of a field education program. An unconditional service guarantee requires the firm to focus on understanding its customers and their expectations. In addition, guaranteeing all aspects of service performance requires the development of explicit mechanisms to share information among employees and develop response initiatives that are highly customer oriented.

OP4: Designing and implementing unconditional service guarantees increases firms' market orientation.

Note that the above discussion does not imply a causal chain wherein guarantees precede market orientation, employee empowerment, and organizational learning. In truth, the relationships may be much more complex, with service guarantees stimulating continuous and synergistic interaction among different organizational processes (Ostrom and Iacobucci 1998). The above framework simply provides a firm basis for systematically analyzing service guarantee effects.

CONCLUSIONS AND FUTURE RESEARCH

In conclusion, it is evident that service guarantees are more than just marketing devices for firms. They can also assist service recovery, improve operational efficiencies, and increase a firm's market orientation. Our framework deepens and broadens our understanding of this critical service asset by examining the psychological processes by which guarantees affect customers before and after service is experienced. By resolving definitional inconsistencies and generating an inventory of propositions, this paper suggests new research directions. Next, some more general research themes are discussed.

Moderating Influences of Guarantees on Customer Evaluations

Previous studies suggest that external cues such as brand and price may interact with service guarantees and moderate their ability to improve customer evaluations. It would be interesting to study how these interactions influenced evaluations for different types of guarantees (specific, unconditional) and services (experience, credence). Also, the extent of competition may moderate the effect of a service guarantee. If one firm already offers a competitive guarantee, benefits to other firms offering similar or matching guarantees may be minimal. However, whether there will be any benefit to other firms offering improved performance on the same attributes or superior performance on other highly valued attributes is not clear, and bears further investigation.

Mediational Influences of Service Guarantees

Attribution theory suggests that service guarantees may magnify the effects of service success and failure on customer evaluations. Most empirical research so far suggests that defaulting on performance leads to poorer evaluations when a guarantee is offered (Kumar, Kalwani, and Dada 1997; Smith and Bolton 1998). This presents an interesting dilemma for researchers and firms: how can a balance be struck so that the benefits from implementing guarantees compensate for loss of customer goodwill when firms fail to deliver? Future research may also address service failure and recovery issues in the presence of service guarantees. For instance, do service guarantees mediate the effects of service recoveries on satisfaction and retention?

Measuring Guarantee Impacts

From an organizational perspective, it would be interesting to estimate the size of effects of service guarantees on different aspects of organizational learning. This might include a study of guarantees that facilitate organizational communication, teamwork, and the development of market driven capabilities. In addition, it might be useful to conduct a cost benefit analysis of service guarantees by comparing the cost of implementation with returns from increases in new trials, improvements in retention rates, and other performance measures.

Perhaps, most interesting of all would be studies aimed at simultaneously examining the effects of service guarantees on customers and firms. There is also scope to examine the relative importance of various organizational benefits provided by service guarantees. For instance, guarantees that flow naturally from a firm's intrinsic capabilities may provide it with little but promotional value, whereas guarantees that direct a firm towards a market based re-organization may be more beneficial in the long run. This implies a need to investigate the strategic aspects of service guarantee design in regard to ongoing firm development. Most service guarantee research has focused almost exclusively on transactions between customers and firms. However, guarantees may be useful in stimulating change in customer evaluations over time. More longitudinal research is required in this regard.

We conclude that a perspective that recognizes the effects of service guarantees on customers and firms extends our understanding of service marketing. Additional inter-disciplinary research is needed to help service firms understand the implications of offering service guarantees and better manage the service process.

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