The thrill of victory, the agony of defeat

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Abstract. This paper presents experimental evidence from a rent-seeking exercise where the highest bidder wins the rent, but all bidders, including the winner, lose their wagers. This exercise closely resembles the rent-seeking dilemma facing agents in many settings. There are two main conclusions from the results. First, there is a tendency towards overdissipation of the rent. Second, some individuals are willing to pay more for a rent than its face-value would warrant. We attribute this phenomenon to a "thrill of victory" effect.

1. Introduction

The simplest model of rent-seeking hypothesizes that any artificially contrived rents will be exactly dissipated by competing parties seeking to secure a share of such rents. We will attempt to demonstrate that within an experimental environment typifying rent-seeking the collective behavior of subjects results in overdissipation.

Our exercise is modeled after the game proposed by Brennan (1980), which we believe closely resembles the actual rent-seeking dilemma facing agents in many settings. In Brennan’s game, participants are asked to make a sealed bid for a prize (the rent) under three conditions: (i) no collusion exists among the bidders, (ii) bids are not refunded, and (iii) the highest bidder wins the prize. Clearly, this has all the characteristics of rent-seeking. Brennan noted that there was no systematic tendency for participants to collectively over, under or exactly dissipate the rent.

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Moreover, there is no pure strategy for an individual to follow when faced with this type of rent-seeking problem. Consider a simple example of two individuals, A and B, who are offered a $100 rent. It is not clear what either should bid without knowledge of what the other will bid. Tullock (1980, 1987, 1989) notes that any pure strategy would inevitably break down because of the paradox of the liar. If A knows that B is going to bid $20, then A will bid $21; but if B knows that A will bid $21, then B will want to bid $22, and so on. ¹

Since no well defined theoretical model has emerged, our experimental results should shed considerable light on the rent dissipation process.

2. The experiment

In keeping with the spirit of Brennan’s game, we specified a consistent set of guidelines for the in-class administration of our exercise. The exercise was performed on four campuses and consists of 20 economics classes with 499 students.² Each exercise begins with the administering instructor displaying the rent where all class members can see it. Each student was handed a Student Bid Form and the administering instructor then gave a verbal explanation of how the exercise should proceed.³ The students were asked to list their major, GPA, gender, to formulate a bid for the rent, and to sign the Student Bid Form. The range of rents offered at sealed auctions was largely determined by what we felt were the students’ effective budget constraints. Therefore, each student was given a chance to wager for a rent of anywhere from $1.00 to $20.00. The forms were then collected and a winner announced.

It is worth taking some time to fully explain the mechanics of our approach.⁴ Care was taken to ensure that the results we received would not be biased towards over, under, or exact dissipation. In order to avoid biasing our results toward underdissipation, all winnings and losses incurred were settled at the start of the next scheduled class meeting. Without this provision, many students would have been forced to sit on the sidelines for lack of correct change or cash-on-hand. Furthermore, since our exercise is admittedly contrived we placed special emphasis on convincing the students that their wagers would be confiscated. Without this provision, rational students would have bid higher amounts for the rent thereby biasing the results of the experiment toward over-dissipation.⁵

The winner of the exercise was defined as the person who made the highest bid. In the event of a tie, all persons who bid the highest amount would be entered into a lottery. Only the lottery winner would receive the rent. All other participants, including those who lost in the lottery, lost their wagers.

Another element in this discussion involves the dispersion of the money collected. Here care was taken to inform the students that all revenues collected