

Moral Hazard with Multiple Agents and Hierarchy Structure*

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Abstract

This paper addresses the effects of hierarchy structure under moral hazard with multiple agents. Specifically, we compare the horizontal structure in which each agent takes an action simultaneously with the vertical structure in which each takes an action sequentially. Relative to the horizontal structure, the vertical structure imposes an additional incentive constraint on the follower agent but may relax the incentive constraint on the leader agent due to punishment by the follower. We show that the vertical structure outperforms the horizontal structure if the optimal contract in the horizontal structure exhibits joint performance evaluation. Conversely, the horizontal structure is better than the vertical structure if the follower's punishment in the vertical structure is implemented *via* relative performance evaluation.

JEL Classification: D86; J41; D20

Keywords: moral hazard with multi agents; hierarchy structure; sequential move;

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