The Cost of Gaming in Quota Contract

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Abstract

Gaming is an important problem when firms use a nonlinear incentive contract. Previous empirical researches show that gaming reduces firm's profit. This paper derives the cost of gaming in a dynamic moral hazard model and show that this cost is higher when the employee is more productive. Moreover, we compare a liner contract and a quota-based contract and show that even when an employee can game the incentive system,a quota-based contract is more profitable than a linear contract.

Keywords: Quota-based contract; Gaming; Moral-hazard

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