Employee Referrals and Incentive Schemes*

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[**Very Preliminary**]

Abstract

This study investigates advantages and disadvantages of referral hiring, recruitment through the current workers' referral, in a framework of moral hazard with multiple agents. We assume that the current worker has an advantage on information about competence of potential workers outside of the organization. To give the current worker an incentive to recommend an competent worker to the employer, the incentive payment must be more positively correlated to the new workers' performance. Consequently, the referral hiring system is disadvantageous as relative performance evaluation is more effective to induce the current worker to work hard than joint performance evaluation.

JEL classification: D86; J41; D20

Keywords: recruitment system, multi-agent moral hazard, joint performance evaluation, relative performance evaluation