

Incentive Design and Distorted Behaviour

by

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22.04.2013

Abstract

Incentives often distort behavior: they induce agents to exert effort but this effort is not employed optimally. This paper proposes a theory of incentive design allowing for such distorted behavior. At the heart of the theory is a trade-off between getting the agent to exert effort and ensuring that this effort is used well. The theory covers various moral-hazard models, ranging from traditional single to multi-task models. It also provides —for the first time— formalization and proofs for various common wisdoms about incentive design and distorted behavior.