

Altruism, Corruption, and Relative Performance Evaluation*

ALEXANDER HENKE†

Department of Economics

Grand Valley State University

Abstract

I construct a principal – agent – supervisor inspection model where the supervisor is altruistic towards the agent and therefore wishes to alter the signal in the agent’s favor. Even when side-contracting between the supervisor and the agent is infeasible, the threat of unilateral report manipulation from an altruistic supervisor leads to low-powered incentives and large transfers to the supervisor to induce truthful negative reports. When there are multiple agents whose production and related signals are entirely independent, the principal can use relative performance evaluation to mitigate the effect of the supervisor’s altruism, reducing wage compression and supervisor transfers. The power of relative performance evaluation diminishes when the supervisor is biased towards one agent and vanishes completely when the bias is completely in favor of one agent, as this eliminates the principal’s ability to balance the supervisor’s desires to see both agents do well. I show that a corrupt supervisor who bargains with all agents as a coalition presents an equivalent problem to a special, costly case of the problem with altruism, and I find that changes in a corrupt bargaining structure between agents and supervisor can alter incentives significantly.

Keywords: Relative performance evaluation, altruism, corruption, multiple agents

JEL Codes: D86, D74, L51, I21

* I would like to thank Lin-chi Hsu and Quan Wen for helpful comments. All errors are my own.

† Email: henkeale@gvsu.edu