

## 334.111/112 Organizational Design and Incentives in Firms 1/2

**Univ.-Prof. Dr. Michael Kopel**

Institute of Organization and Economics of Institutions

<http://www.uni-graz.at/organisation>

Office Hours: see UGO



*„For two hundred years, the basic economic model of a firm was a black box: labor and physical inputs went in one end; output came out the other, at minimum cost and maximum profit. Most economists paid little attention to the internal structure and functioning of firms or other organizations.”*

*(Robert Gibbons: Why Organizations are Such a Mess and What an Economist Might Do about It, 2000)*

### Course description

This is a Master-level course in *Organizational Economics*. The course draws heavily on insights from Transaction Cost Economics, Property Rights Theory, and Principal-Agent Theory. It develops concepts and theoretical constructs that provide the basis for the formulation of innovative solutions for managers in today's business environment. The general manager is seen as a designer of a firm's strategy and the organizational structure to implement the strategy. In this course we will address the following key topics: Coordination and motivation in organizations; Incomplete contracts; Make-or-Buy; Risk-sharing and incentive contracts; Ownership and property rights; Rents and efficiency.

### Previous knowledge expected (Prerequisites)

It is expected that you have mastered the concepts and analytical methods in intermediate courses on Microeconomics, Game Theory, and Statistics. A prerequisite for this course is that you have taken 334.101 Masterkurs Management.

### Objective

After this course, students should have a deeper understanding of key issues in Organizational Economics. The concepts and frameworks introduced in this course will help the participants learn to put structure on complex and unstructured problems in business firms, in particular with regard to decisions that concern the efficiency of transactions within and between firms.

### Language of instruction:

This course will be held in English.

### Teaching and learning method

The course consists of a mix of lectures, group discussions, case studies, and video lectures.

### Exam information

Assessment is based on (i) active involvement and participation in class (please note that class attendance is mandatory!), performance of tasks, group assignments, presentations, etc. in class, problem sets and (ii) a written exam. In-class performance and problem sets account for 40% of the grade. The written exams account for 60% of the grade.

## ECTS

This double-course has  $4+4 = 8$  ECTS = 200 hours. Since you will spend  $13 \times 3 = 39$  hours in class, you should spend approx. 160 hours outside of class for reviewing material, reading the cases/exercises, preparing for exams, and so on. Therefore, please reserve at least 12 hours outside class for each in-class lecture.

## Required readings

We will rely on the textbook, *Economics, Organization, and Management* by Paul Milgrom and John Roberts (1992) for the theory and on several case studies and video lectures for applications.

## Additional readings

Besanko, D., D. Dranove, M. Shanley, S. Schaefer (2007), *Economics of Strategy*, 4<sup>th</sup> ed., Wiley.

Brickley, J.A., C.W. Smith, J.L. Zimmerman (2009), *Managerial Economics and Organizational Architecture*, 5<sup>th</sup> ed., McGraw-Hill.

Hendrickse, G. (2003), *Economics and Management of Organizations*, McGraw Hill.

Kräkel, M. (2007), *Organisation und Management*, Mohr-Siebeck.

## Topics

- Chapter 1: Does Organization Matter?
- Chapter 2 Economic Organization and Efficiency  
Efficiency. Coordination and Motivation. Transaction Cost Analysis. Value Maximization. Coase Theorem
- Chapter 3 Coordination: Markets and Management  
Prices and Coordination. Incentives and Information on Markets. Market failures. Transfer Prices in Organizations.
- Chapter 4 Coordinating Plans and Actions
- Chapter 5 Bounded rationality and private information  
Perfect, complete contracting. Relational contracts. Implicit contracts. Investment and specific assets (hold up problem). Prisoner's dilemma. Reputation. Private information. Economizing on information costs (block booking). Adverse selection (market failure). Signaling. Screening
- Chapter 6 Moral Hazard and Performance Incentives  
Key factors of Moral Hazard. Evidence of Moral Hazard. Case: Savings&Loan-Crisis. Controlling Moral Hazard. Influence activities.
- Chapter 7 Risk sharing and incentive contracts  
Risk and incentives. Efficient risk sharing by groups. Model of incentive compensation: informativeness principle, incentive-intensity principle, monitoring intensity principle, equal compensation principle. Ratchet effect.
- Lincoln Electric: Harvard Business School Case 9-376-028 (Fast and Berg 1975)
- RKO Warner: Harvard Business School Case 9-190-067 (Shimer and Baker 1989)
- Chapter 8 Rents and efficiency  
Problems with the value maximization principle. Efficiency wages. Reputation revisited. Repeated transactions; Rent-Seeking and Influence activities.
- Chapter 9 Ownership and Property Rights  
Concept of Ownership. Coase-Theorem revisited; Property Rights. Assigning Property Rights.

# Institut für Organisation und Institutionenökonomik

Institute of Organization & Economics of Institutions

Leiter: Univ.-Prof. Dipl.-Ing. Dr. Michael Kopel

## Richtlinien für den Besuch von Lehrveranstaltungen des Institutes

Für Lehrveranstaltungen mit immanentem Prüfungscharakter gilt, entsprechend der gesetzlichen Bestimmungen und den einheitlichen Regelungen an der SOWI, folgendes:

- Abmeldungen von Lehrveranstaltungen im laufenden Semester werden, wenn diese bereits begonnen wurden, ausnahmslos nicht durchgeführt.
- Bei prüfungsimmanenten Lehrveranstaltungen beginnen der immanente Prüfungsakt und somit auch die Beurteilung mit der ersten mündlichen oder schriftlichen Teilleistung bzw. mit der Übernahme eines Referatsthemas, Problem Sets, od. dgl.
- Bei bereits erbrachten Teilleistungen (Mitarbeit, Gruppenarbeit, Kurztests, Übernahme Referatsthema etc.) und einer Versäumnis der Zwischen- und/oder Abschlussklausur muss mit einer negativen Beurteilung gerechnet werden.
- Zudem wird auch darauf hingewiesen, dass bei prüfungsimmanenten Lehrveranstaltungen innerhalb eines Semesters keine Wiederholungsprüfungen angeboten werden, da dies letztendlich auch dem Typ der prüfungsimmanenten Lehrveranstaltung widersprechen würde.
- Die Anwesenheit wird bei allen Lehrveranstaltungen überprüft. Bei laufenden Lehrveranstaltungen dürfen max. vier Einheiten (d.h. 3 Stunden á 60 Minuten) versäumt werden, sonst ist eine positive Beurteilung nicht möglich.

Für alle Lehrveranstaltungstypen gilt:

- Anmeldungen nach dem LV-Beginn gibt es an der Fakultät grundsätzlich nicht.
- Die Beantwortung von Einzelanfragen per E-Mail ist nicht möglich.