

Finding the Hidden Cost of Control

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Abstract:

An increasing literature has demonstrated that psychological factors (such as fairness, trust, norms and intrinsic motivation) interact with explicit incentives (such as contracts, fines and monitoring regimes) in complicated ways. Empirical and experimental evidence has demonstrated that, for many individuals, intrinsic motivation and/or social norms can lead to costly pro-social behavior in the absence of explicit incentives, and that perversely interventions such as increased monitoring and/or fines can destroy intrinsic motivation and lead to worse behavior. In particular, Falk and Kosfeld (2006) show that in a principal agent setting the average agent effort is lower when the principal controls the agent by imposing a minimum action than if he leaves the agent free to choose any action – attributing this result to agents feeling mistrusted by the principal. By contrast, Kessler and Leider (2012) show that when prosociality is supported by informal agreements, having a mutually agreed upon minimum action often does not diminish effort. In this paper we replicate Falk and Kosfeld’s “hidden cost of control” result for a setting with informal agreements, and demonstrate that the hidden cost is eliminated when the binding minimum affects both parties and reversed when both parties must agree upon the minimum. Additionally, we show that individual differences in the propensity to use the minimum as a principal affects the likelihood of reacting negatively to having a minimum imposed as an agent.