

Collusion and Strategic Favouritism in Organizations

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BACKGROUND

- Objective measures of employee performance are rarely available in organizations like firms and bureaucracies. Instead these organizations rely on subjective assessments by supervisors, which may cause serious incentive problems.
- Rank-order tournaments are widely adopted to resolve these incentive problems. However they are vulnerable to collusion or collective sabotages. The phenomenon of collusion is indeed quite common in organizations, which is widely documented in literature.
- On the other hand subjective assessments of employee performance open the door to favouritism, where employers act on personal preference toward subordinates to favour some employees over others. Favouritism becomes one of the most important sources of conflicts in organizations, and its harmful effects on the design of incentives are widely discussed in the existing literature.
- This research bridges the phenomenon of collusion and strategic favouritism.

METHODOLOGY

- The author builds a simple model of tournaments, by taking into account the possibility that the employer might bring some bias in performance evaluation.
- The paper focuses on the case of perfect collusion where collusive agreements between employees are enforceable by some forces like social norms and reputations.
- The author compares explicit discrimination and implicit discrimination, and also analyzes more sophisticated and strategic use of favouritism with manipulation of information revelation by the employer.

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KEY FINDINGS

- The paper shows that favouritism cannot benefit organizations where collusion is not a serious concern; meanwhile explicit favouritism is not effective in dealing with well-organized collusion.
- However, strategic use of favouritism can bring conflicts among collusive subordinates and undermine collusion. It is therefore effective in fighting collusion.

POLICY IMPLICATIONS

- Fighting collusion has long been a challenge in organizations; on the other hand, favoritism in organizations has long been condemned as one of the most important sources of workplace conflicts and stress. While most studies of favoritism focus on its harmful effects on organizations, our analysis shows that strategic favoritism can improve the efficiency of organizations where collusion is a serious concern.
- The research also highlights the complicated relationship between the supervisor and subordinates in organizations where personal relations among co-workers, bosses, and subordinates constitute an important component of many workers' daily lives. Unfortunately, they are rarely addressed by economists.
- These relationships are built mainly for coordination but they also play an important role in facilitating collusion. Meanwhile, subordinates often invest many resources in the relationship with the superior to seek favoritism in promotion. These relations act as informal mechanisms which affect the effectiveness of incentive schemes, and they can be also utilized strategically to benefit organizations.

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The full working paper (CCP Working Paper 08-27) and more information about CCP and its research is available from our website: www.ccp.uea.ac.uk

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