Adverse selection, 4, 11–13, 52, 97
in annuity market, 220
and auction theory, 65–73
and auditing of agent, 89–91
and bilateral private information, 82–88
and collusion among organization members, 73–75
and equilibria, 98
exercises on, 40–42, 91–93
and informed Principal, 86–88
in insurance market, 213, 220
and insurer as monopolist (example), 51–56
in intertemporal price discrimination, 168–78
and least-cost separating equilibrium, 107
and mechanism design, 13–18
and moral hazard problem, 184, 188, 213–14
with multidimensional characteristics of Agent, 26n.11, 78–82
and multiple Principals, 61–65
and optimal taxation (example), 47–51
and perfect competition in contracts, 57–60
and price discrimination, 18–27
and regulation of firm (example), 43–47
and renegotiation, 181
and risk-averse agents, 76–77
Rothschild-Stiglitz model of, 219
standard model of, 27–39, 71–72, 89
and type-dependent reservation utilities, 88–89
underproduction from, 107n.10
Agency problem, 6, 120n.2. See also
Moral hazard
Agent, auditing of, 89–91, 140
Annuity markets, 220
Asymmetric information. See also Moral hazard
and adverse selection, 21–27
and adverse selection (exercise), 92–93
and general equilibrium models, 1–2
in insurance markets, 218–21
and secondhand-car market, 98–99
study of bargaining under, 5
Auctions, theory of, 65–73
and correlation of bidders' valuations, 71–73
and empirical contracts literature, 216–18
and optimal auction, 70, 70n.13, 71
and revenue equivalence theorem, 69
shading bid in, 68
Auditing, of Agent, 89–91, 140
Authority, formal and real, 115–16
Automobile insurance, and adverse selection vs. moral hazard, 213–14
Babbling equilibrium, 107, 109, 113
Backward induction, Kuhn's algorithm of, 226
Banking
and adverse selection, 12
example of, 207–208
Barriers to entry, 164–67
Bayesian consistency, 228, 230
Bayesian equilibrium, 226–27
and contract models, 3
perfect, 3, 5n.2, 104, 105, 110–11, 227–29, 231
refinements on, 229–32
Bayesian updating, 228
Behavioral norms, contract expressed in, 3
Bilateral private information, 82–88
Borch’s rule, 129n.11
Bounded rationality, 193, 194, 207
Breach of contract, 162
Bribe, for supervisors, 73, 73n.14, 74–75
Brownian motion, 145, 145n.22
Bunching, 51, 77, 78, 81–82
Bunching equilibria, 107
Bunching optimum, 38–39
exercise on, 40–41
Buyer–seller relationship. See also
Signaling models
and incomplete contracts, 196–97
in secondhand car market, 98–99
CARA (constant absolute risk aversion), 145, 146, 188n.23, 189, 206–207
Causality, problem of, 212
CDFC (convexity of the distribution function condition), 131–32, 132n.14, 133, 136, 140, 150
exercises on, 157
Center, 15–16, 204–205, 206, 207
Cheap talk, 97, 114
and Crawford-Sobel model, 107
in worker-and-manager example, 115
Chicago school, 165, 166n.5
Cho-Kreps intuitive equilibrium, 105, 114
Coase theorem, and bilateral private information, 86
Coinsurance, 150
Collusion
exercise on, 92–93
among multiple Principals, 62
and optimal contract, 74
among organization members, 73–75
Collusion-proofness principle, 74
Commitment, 162–64
absence of, 163, 176–77, 185
full, 163, 164, 170–72, 178, 188
long-term, 163, 172–76, 178, 188
short-term, 163, 177–78, 178–79
spot, 163
strategic, 164–68
Common agency model, 61, 142
Common priors, 227n.2
Common value auctions, 65
Common values model, 53
Communication game, 232
Comparative statics
and continuous-action model, 136
and unique equilibrium, 104–105
Compensation. See Incentives(s); Wage determination
Competitive equilibrium, Wilson, 91–92
Complete contracts, 161–62, 197. See also
Commitment
assumption of, 193
and property rights, 197, 207
and renegotiation, 162, 207
simple, 207
Complex goods, and contracts, 198
Concavity of the distribution function condition, 131n.13
Consumer surplus, in regulation of natural monopoly, 44
Consumption paths, 174
Consumption smoothing, 184–85, 190
Contracting literature, and interaction between theory and empirical studies, 221
Contracts, 3
accounting for specific form of, 212
adverse selection and moral hazard distinguished in, 213
Subject Index

breach of, 162
and commitment, 162–68
complete, 161–62, 193, 197, 207 (see also Complete contracts)
exclusive, 165
fixed-price, 197
fixed-rent, 214
implicit, 3
incentive effect of, 212, 213
incomplete, 161, 193–208 (see also Incomplete contracts)
insurance, 180
long-term, 194
optimal, 74, 90, 129, 141, 144
option-to-sell, 200–204, 208
perfect competition in, 57–60
and renegotiation, 162 (see also Renegotiation)
robustness of, 144–45
short-term, 177
side-contracts, 74, 75
simple, 207, 208
spot, 185, 190
Contract theory(ies), 2–3, 211–13
adverse selection models, 4 (see also Adverse selection)
classification of, 3–4
and empirical observation on asymmetric information in insurance markets, 218–21
and empirical observation on auctions, 216–18
and empirical observation on unobserved heterogeneity, 212–16
explosive development of, 211
factual data lacking in, 211
institutions in, 162
moral hazard models, 4 (see also Moral hazard)
and private information, 82
signaling models, 4 (see also Signaling models)
spot, 185
Control rights, property rights as, 198
Convergence, to first-best, 181–83
Convexity of the distribution function condition (CDFC), 131–32, 132n.14, 133, 136, 140, 150
exercise on, 157
Cooperation, and piece-rate wage, 151.
See also Teamwork
Coordination problem, in stag-hunt example, 108
Corporate shareholding, 187–88
Corporate scandals, and managerial compensation, 154
Costless signals, 107–108
general model of, 109–14
in stag-hunt example, 108–109, 118
Costly signals, 99–107
Cost-plus contract, in regulation of firm, 47
Crawford-Sobel model, 97, 107, 109–14
and equilibria, 98
exercise on, 117–18
and treacherous-journalist example, 115
Credit market, and finitely repeated moral hazard, 183, 184n.17, 187, 188–89
Cutoff rule, 108
Direct truthful mechanism, 17–18, 87
and competition among Principals, 61
and full commitment, 170
and informed Principal, 87
and optimal auction, 70
and optimal taxation, 48
“Dominated,” 231
Doyle, Arthur Conan quoted (A Scandal in Bohemia), 211
quoted (A Study in Scarlet), 223, 226n.1
Dutch auction, 66
Dynamic programming, 205
Econometricians, and endogenous selection, 213
Economics of information, 2
and theory of contracts, 6
Education, and productivity (signaling models), 100–101, 102, 104, 105
Subject Index

Efficiency-wage model, 153
Efficient investment incentives, restoring of, 200–204
“Effort,” 120
and managerial incentives, 154, 155
Empirical contracts literature
on asymmetric information in insurance markets, 218–21
on auctions, 216–18
and unobserved heterogeneity across agents, 212–16
Empirical observation, correlations not causation as object of, 212
English auction, 66
Entry, barriers to, 164–67
Equilibrium(a)
babbling, 107, 109, 113
Bayesian, 3, 226–27
Bayesian (perfect), 3, 5n.2, 104, 105, 110–111, 227–29, 231
Bayesian (refinements on), 229–32
bunching, 107
Cho-Kreps intuitive, 105, 114
intuitive, 230–32
least-cost separating, 106–107, 116
multiple, 104–105
Nash, 224, 225
partial, 2
partition, 111
pooling, 60, 102, 103, 104
selection of, 103–107
separating, 107, 117
subgame-perfect, 224–26
trembling-hand perfect, 230
Walrasian, 14, 16
Exclusion phenomenon, 26n.11
Exclusive dealing, 165
Extensive form of game, 224–25
observation of difficult, 97

Federal Communications Commission, spectrum auction by (1994), 66
Fines, and renegotiation, 206
First-best, convergence to, 181–83
First-order stochastic dominance (1SD) in exercise, 159
First-price sealed bid auction, 66–73
Fisher Body–GM relationship, 195–96
Fixed-price contract, 197
Fixed-rent contracts, 214
Forward induction arguments, 232, 232n.7
Franchises, 152
Freedom of choice, limitation of, 163–64
Free riders, 140, 152
Fubini’s theorem, 36, 36n.25, 49, 50
Full commitment, 163, 164, 170–72, 178, 188
Functional analysis, and moral-hazard outcomes, 138

Games
extensive form of, 97, 224–25
of incomplete information, 226–32
of perfect information, 224–26
preplay communication, 114
Game theory
and limitations of general equilibrium models, 2
Prisoner’s Dilemma, 163–64
Game tree, 224
General equilibrium theory and models, 1, 2
and contract theory, 2
limitations of, 1–2
GM–Fisher Body relationship, 195–96
Government-regulated firms, and adverse selection, 13
Grossman-Hart approach, to moral hazard, 128–29

Hazard rate, 35, 35n
Health Insurance Experiment (HIE), Rand, 215–16
Heterogeneity across agents, unobserved, 212–16
Holdup problem, 194
GM–Fisher Body as example of, 195–96
Subject Index

“Hostages,” 162
_Huckleberry Finn_ (Twain), quoted, 119, 121
Hunting (stag hunt) story, 108–109
exercise on, 110n.13, 118

IC constraints. See Incentive compatibility constraints
Imperfect information. See Asymmetric information
Incentive(s). See also Wage determination
contracts as providing, 212, 213
investment, 200–204
and law of large numbers, 181
managerial, 154, 155
provided by two Principals, 144
Incentive compatibility (IC) constraints, 22, 28, 29–33, 174
and auditing of agent, 89
and informed Principal, 87
and insurance market, 60
and moral hazard, 122, 123, 125, 127, 135, 137, 147, 189
and moral hazard (exercise), 158
and multidimensional characteristics of Agent, 79–80
and relaxed program, 80
and revelation principle, 90
Incentive-compatible contract, exercise on, 93
Incentive-compatible functions, 83
Incentive-compatible mechanisms, 84
Incentive problem, in mechanism design, 15
Incentive schedules, real-life vs. theoretical, 149
Incomplete contracts, 161, 193–95, 205–208
and buyer–seller model, 196–97
and holdup problem, 194
irrelevance theorems on, 200–205, 206–207
and political economy, 205
and property rights, 198–200, 205
Independent private values auctions, 65
Individually rational functions, 83
Individual rationality (IR) constraints, 22, 28, 34, 174
and informed Principal, 87
and moral hazard, 122, 123, 126, 137
and moral hazard (exercise), 158
and multidimensional characteristics of Agent, 79–80
and optimal taxation, 48
and relaxed program, 80
and trading mechanisms inefficiency, 86
and type-dependent reservation utilities, 88
Induction
backward, 226
forward, 232, 232n.7
Informational asymmetries. See Asymmetric information
Informational rent, in adverse selection models, 26, 34, 36, 55n.4
Informed Principal, 86–88, 116
Institutions, in theory of contracts, 162
Insurance contract, 180
Insurance markets
and adverse selection vs. moral hazard, 213–14
asymmetric information in, 218–221
moral hazard in, 120, 149–51, 220
and types of Agent, 60n.8
Insurance model, vs. standard adverse selection model, 60
Insurer as monopolist, as adverse-selection example, 51–56
Intertemporal moral hazard, 179–90
Intertemporal price discrimination, adverse selection in, 168–78
Intuitive criterion, 230–31
Intuitive equilibrium, 230–32
Investment, lack of. See Underinvestment
Investment, specific, 196
Investment incentives, restoring as efficient, 200–204
Subject Index

IR constraints. See Individual rationality constraints
Irrelevance result, 59–60
Irrelevance theorems, 195, 200–205, 206–207
Iterated logarithm, law of, 182

Jensen’s inequality, 186, 186n.21
Joint ownership, 200
and option-to-sell contract, 201

Labor markets, and adverse selection, 12–13
Labor supply in autarky, elasticity of, 50–51
and correlation of bidders’ valuations, 71–73
Laffont-Tirole model of regulation, 45, 46, 47
exercise on, 93
Law of iterated logarithm, 182
Law of large numbers, in incentive problem, 181
Least-cost separating equilibrium, 106–107, 116

“Lemons.” See Secondhand cars, market for
Lender-borrower relationship, and auditing, 90, 90n.19
Life insurance, and adverse selection, 12. See also Insurance markets
Limited commitment, 163
Limited liability model, and moral hazard, 136, 138
Long-term commitment, 163, 172–76, 178, 188
Long-term contracts, renegotiation of, 194

Managerial compensation, 153–56
Market foreclosure, 167
Maskin-Tirole mechanism, 205, 206–207, 207
Mechanism, 15
optimal, 26–27, 41

Mechanism design
and adverse selection, 13–18
for incomplete contracts, 204–205
Memory effect, 184–85, 190
Message game, 15–16, 207, 208
Mixed strategies, 190, 223

MLRC (monotone likelihood ratio condition), 130–31, 136, 140, 150
exercises on, 157, 159
Monopolies. See Natural monopolies
Monopolist insurer, as adverse-selection example, 51–56
Monotone likelihood ratio condition (MLRC), 130–31, 136, 140, 150
exercises on, 157, 159
Moral hazard, 4, 119–21
and adverse selection, 184, 188, 213–14
and agency problem, 6
and continuum of actions, 135–36
and “effort,” 120
example in, 122–24
exercises on, 156–59
finitely repeated, 183–90
and imperfect performance measurement, 140, 158
and infinity of outcomes, 138–39
informativeness of value for, 134–35
in insurance, 120, 149–51, 220
intertemporal, 179–90
intuition untrustworthy on, 133
and limited liability model, 136–38
multisignal case for, 139–40
and multitask model, 146–49
and robustness of contracts, 144–45
and several Agents, 140–41
and several Principals, 142–44
standard model in, 124–33
and “technology,” 124
and wage determination, 123–25, 125n.9, 151–56

Multidimensional characteristics, and
Principal–Agent model, 26n.11, 78–82
Multiple equilibria, undesirability of, 104–105
Multiple (several) Principals, 142–44
Subject Index

competition among, 61–65
Multiprincipals model, 61
exercise on, 92–93
“Multiprincipals with symmetric information,” 142
Multisignal case, for moral hazard, 139–40
Multitask model, 146–49

Nash bargaining solution, 199
Nash equilibrium, 224, 225
Natural monopolies, 43n.1
and adverse selection, 43–47
Noncooperative game theory, 223
and contract models, 3
games of incomplete information, 226–32
games of perfect information, 224–26
Nonverifiability assumption, 195n.2

Optimal auction, 70, 70n.13, 71
Optimal contract, 74, 90
and Agents helping each other, 141
and long-term commitment, 175n.12
and moral hazard, 129–33, 144
and renegotiation, 180–81
Optimal control theory, 38
Optimal mechanism, 26–27
exercises on, 41
Optimal reserve price, exercise on, 92
Optimal taxation
as adverse-selection example, 47–51
exercise on, 91
Optimal wage schedule, 144
Option-to-sell contract, 200–205, 208
Organizational behavior, and collusion, 75

Pareto optima
and equilibria, 1
and Principal–Agent paradigm, 5
Partial equilibrium models, in contract theory, 2
Participation constraints, 22, 76
Partition equilibria, 111

Perfect Bayesian equilibria, 3, 5n.2, 104, 105, 110–11, 227–29, 231
Perfect competition, in contracts, 57–60
Performance measurement
imperfect, 140, 158
for teamwork, 140
Piece-rate wage, 151
Political economy, and incomplete contracts, 205
Politicians, and incomplete contracts, 205n.8
Pontryagin minimum principle, 76n.15
Pooling equilibria, 60, 102, 103, 104
Precommitment effects on third party, 164
Predation, and auditing, 90n.19
Preplay communication game, 114
Price-cap contracts, in regulation of firm, 46–47
Price discrimination
discrete model of, 18–27
first-degree, 11n.2, 20
Price system, and strategic interactions, 1
Principal–Agent model, 3, 5–6
and adverse selection, 11–12, 16–17
(see also Adverse selection)
and auditing of Agent, 89–91, 140
and informed Principal, 86–88, 116
and moral hazard, 119–21 (see also Moral hazard)
with multiple Principals, 61–65, 142–44
and unobserved heterogeneity across agents, 212–16
Prior beliefs, 227, 227n.2
Prisoner’s Dilemma, 163–64
Private information, 2
bilateral, 82–88
in classification of contracts, 4
Private values model, 53
Privileged information, in signaling-models example, 115
Productivity, and education (signaling models), 100–101, 102, 104, 105
"Profitable entrant," 58
Promotions, 152
Property insurance, moral hazard in, 120. See also Insurance markets
Property rights
and Anglo-Saxon law, 198n.5
and complete contracts, 197, 207
and incomplete contracts, 198–200, 205
Roman law on, 198
Public goods
and incentives provided by two Principals, 144
and mechanism design (bridge example), 14, 16, 17
Pure strategies, 190
Rand Health Insurance Experiment (HIE), 215–16
Ratchet effect, 176, 177n.15, 179
Rational expectations equilibria, 2
Rationality, individual. See individual rationality constraints
Rationality, sequential, 228
Regulation of firm, as adverse-selection example, 43–47
Renegotiation, 162
and complete contracts, 207
after effort, 179–81
and incomplete contracts, 164, 194, 205, 205–206, 207, 208
long-term commitment with, 163, 172–73
for option-to-sell contract, 203
and public contracts, 167–68
secret, 168
of short-term contracts, 177
Renegotiation-proofness principle, 173–74, 194
Reservation utilities, type-dependent, 88–89
Residual control rights, property rights as, 198
Revelation, and adverse selection problems, 12
Revelation principle, 17–18, 90, 91
and full commitment, 170
and long-term commitment, 173
in multidimensional settings, 79
and multiple Principals, 62
and no commitment, 177
Revenue equivalence theorem, 69
Risk
and adverse selection, 51–56, 60
and fixed-rent contracts vs. sharecropping, 214–15
and incomplete contracts, 205
and insurance, 51–56, 60, 149, 220, 221
and moral hazard, 121, 125, 129, 136–37
and renegotiation after effort, 180
Risk-averse agents, 76–77
Robustness of contracts, 144–45
Rothschild-Stiglitz equilibrium, 58–59, 59–60
exercises on, 91, 92
Rothschild-Stiglitz model of adverse selection, 219
Rousseau, Jean-Jacques, 108n.12
Scarcity constraint, 48, 49
Sealed-bid auction, 66–73
Secondhand cars, market for, 98–99
Second-price sealed bid auction, 66
Self-fulfilling prophecies, 104
Self-protection efforts, vs. self-insurance efforts, 150n.26
Self-revelation, and adverse selection problems, 12
Semiseparating equilibria, 107, 117
Separating equilibria, 60, 102
least-cost, 106–107, 116
Separating optimum, 37–38
Sequential efficiency constraints, 174
Sequential equilibria, 117, 230
Sequential rationality, 228
Service activities, moral hazard in, 120
Shapiro-Stiglitz model of unemployment, 152–53, 153n.28
Sharecropping vs. fixed rent contracts, 214
Subject Index

<table>
<thead>
<tr>
<th>Term</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>and moral hazard, 120, 187</td>
<td>120</td>
</tr>
<tr>
<td>Shareholding, corporate, 187–88</td>
<td>187</td>
</tr>
<tr>
<td>Shares in firm, as managerial compensation, 153–54</td>
<td>153</td>
</tr>
<tr>
<td>Short-term commitment, 163, 177–78, 178–79</td>
<td>163</td>
</tr>
<tr>
<td>Short-term contracts, renegotiation of, 177</td>
<td>177</td>
</tr>
<tr>
<td>Side-contract, and collusion, 74, 75</td>
<td>74</td>
</tr>
<tr>
<td>Signal(s)</td>
<td></td>
</tr>
<tr>
<td>Apple’s Macintosh factories as, 162</td>
<td>162</td>
</tr>
<tr>
<td>outcomes as (moral hazard), 130</td>
<td>130</td>
</tr>
<tr>
<td>Signal-extraction problem, in managerial incentives, 155</td>
<td>155</td>
</tr>
<tr>
<td>Signaling models, 4, 97–98</td>
<td>4</td>
</tr>
<tr>
<td>and costless signals, 107–14</td>
<td>107</td>
</tr>
<tr>
<td>and costly signals, 99–107</td>
<td>99</td>
</tr>
<tr>
<td>and informed Principal model, 116</td>
<td>116</td>
</tr>
<tr>
<td>and risk-averse-entrepreneur model, 114–15</td>
<td>114</td>
</tr>
<tr>
<td>and secondhand-car market, 98–99</td>
<td>98</td>
</tr>
<tr>
<td>and treacherous-journalist example, 115</td>
<td>115</td>
</tr>
<tr>
<td>and warranty, 114</td>
<td>114</td>
</tr>
<tr>
<td>and worker-and-manager example, 115–16</td>
<td>115</td>
</tr>
<tr>
<td>Simple contracts, 207, 208</td>
<td>207</td>
</tr>
<tr>
<td>Single-crossing condition, 31</td>
<td>31</td>
</tr>
<tr>
<td>Social choice problem, and mechanism design, 13–14</td>
<td>13</td>
</tr>
<tr>
<td>Social surplus, 25, 25n.10</td>
<td>25</td>
</tr>
<tr>
<td>in regulation of natural monopoly, 44</td>
<td>44</td>
</tr>
<tr>
<td>and socially efficient auction, 70</td>
<td>70</td>
</tr>
<tr>
<td>and virtual surplus, 25–26, 36</td>
<td>25</td>
</tr>
<tr>
<td>Social welfare, in regulation of natural monopoly, 46</td>
<td>46</td>
</tr>
<tr>
<td>Sorting condition, 31</td>
<td>31</td>
</tr>
<tr>
<td>Specific investment, 196</td>
<td>196</td>
</tr>
<tr>
<td>Spence-Mirrlees condition, 19, 31</td>
<td>19</td>
</tr>
<tr>
<td>and adverse selection, 169</td>
<td>169</td>
</tr>
<tr>
<td>and education as signal for productivity, 100</td>
<td>100</td>
</tr>
<tr>
<td>and incentive constraints, 31, 32–33, 33n.18</td>
<td>33</td>
</tr>
<tr>
<td>and insurer example, 53, 54</td>
<td>53</td>
</tr>
<tr>
<td>and multiple Principals, 63</td>
<td>63</td>
</tr>
<tr>
<td>and optimal taxation, 48</td>
<td>48</td>
</tr>
<tr>
<td>and pure strategies, 190</td>
<td>190</td>
</tr>
<tr>
<td>Spence’s signaling model, 100–102</td>
<td>100</td>
</tr>
<tr>
<td>exercises on, 117</td>
<td>117</td>
</tr>
<tr>
<td>and informed Principal model, 116</td>
<td>116</td>
</tr>
<tr>
<td>overproduction in, 107n.10</td>
<td>107</td>
</tr>
<tr>
<td>and risk-averse-entrepreneur model, 114</td>
<td>114</td>
</tr>
<tr>
<td>and warranty, 114</td>
<td>114</td>
</tr>
<tr>
<td>Spot commitment, 163</td>
<td>163</td>
</tr>
<tr>
<td>Spot contracts, 185, 190</td>
<td>185</td>
</tr>
<tr>
<td>Stackelberg game, Principal–Agent game as, 5, 6</td>
<td>5</td>
</tr>
<tr>
<td>Stag hunt story, 108–109</td>
<td>108</td>
</tr>
<tr>
<td>exercise on, 110n.13, 118</td>
<td>110</td>
</tr>
<tr>
<td>Statistical inference, and moral hazard problem, 135</td>
<td>135</td>
</tr>
<tr>
<td>Stochastic matrix, 134, 134n.16</td>
<td>134</td>
</tr>
<tr>
<td>Stock options, as managerial compensation, 153–54</td>
<td>153</td>
</tr>
<tr>
<td>Strategic commitment, 164–68</td>
<td>164</td>
</tr>
<tr>
<td>Strategic interactions, and general equilibrium model, 1</td>
<td>1</td>
</tr>
<tr>
<td>Strategies</td>
<td></td>
</tr>
<tr>
<td>mixed, 190, 223</td>
<td>190</td>
</tr>
<tr>
<td>pure, 190</td>
<td>190</td>
</tr>
<tr>
<td>Stylized facts, 211</td>
<td>211</td>
</tr>
<tr>
<td>Subgame-perfect equilibrium, 224–26</td>
<td>224</td>
</tr>
<tr>
<td>Sufficient statistic theorem, 139, 140, 141, 144</td>
<td>139, 140</td>
</tr>
<tr>
<td>Symmetric information</td>
<td></td>
</tr>
<tr>
<td>for multiple Principals, 62</td>
<td>62</td>
</tr>
<tr>
<td>and unforeseen contingencies, 208n.13</td>
<td>208</td>
</tr>
<tr>
<td>Symmetric information assumption, 195</td>
<td>195</td>
</tr>
<tr>
<td>Taxation, optimal, 47–51, 91</td>
<td>47</td>
</tr>
<tr>
<td>Taxation principle, 18, 27</td>
<td>18</td>
</tr>
<tr>
<td>Teamwork. See also Cooperation</td>
<td></td>
</tr>
<tr>
<td>creating conditions for, 141</td>
<td>141</td>
</tr>
<tr>
<td>and performance measurement, 140</td>
<td>140</td>
</tr>
<tr>
<td>“Technology,” 124, 144</td>
<td>124</td>
</tr>
<tr>
<td>Theory of contracts. See Contract theory(ies)</td>
<td></td>
</tr>
</tbody>
</table>
Theory of games. See Games; Game theory
Third party, 3. See also Center
Tournaments, 141, 152
Trading mechanisms, inefficiency of, 82–86
Transaction cost economics, 194
Trembling-hand perfect equilibrium, 230
Truthful mechanism, direct. See Direct truthful mechanism
Twain, Mark (Huckleberry Finn), quoted, 119, 121n.5
Type-dependent reservation utilities, 88–89
UMTS auctions (2000), 66
Uncertainty, about quality of good, 98
Underinvestment, 194, 199, 200, 202 deterrence of, 201

Unemployment, Shapiro-Stiglitz model of, 152–53, 153n.28
Unobserved heterogeneity across agents, 212–16
Updating, Bayesian, 228
Vickrey-Clark-Groves mechanisms, 83
Virtual surplus, 36, 85, 89
Virtual valuation, 71
Wage determination and moral hazard, 123–25, 125n.9, 151–56
and moral hazard (finitely repeated), 184
Wage schedule, optimal, 144
Walrasian equilibrium, 14, 16
Warranty, 114
“Weighted utilitarian” criterion, 47–48
Wilson competitive equilibrium, 91–92