

# Aggregation and Convexity in the Provision of Dynamic Incentives

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## Abstract

In this paper I identify an alternative preference structure that preserves most of the cherished simplicity of the formulation of the Principal-Agent problem pioneered by Holmström and Milgrom (1987). The main advantage of my approach is in relation to the structure of the optimal contract: it adds a convex component to their optimal linear contract. This provides new opportunities to revisit empirical predictions and studies based off of their linear formulation and to demonstrate how the empirical irregularities may be at least partially explained by this one additional component identified here.