



**5076 Human Resource Management (ST 2005) – Retake Final Exam**

**Final Exam**

In the final Exam to this class, you will have 2 hours to solve the problems with a maximum of 70 points. There are a few pieces of general advice we can offer at this stage:

1. Use the theoretical tools and terminology you have learned in class and from the textbook.
2. Make sure there is a clear structure in your argument. (Use some time to sort your ideas before you start writing the version you want to submit, esp. if you answer B).
3. Use the time you have! If you are ready much earlier than we planned you should wonder if you forgot something.
4. Remember: people have to be able to decipher what you write.
5. Leave a margin for our comments, so we can give you a more detailed feedback than just the number of points.

Here is the set of problems:

Please solve *either* problem(s) A *or* B (maximum 70 points):

You are welcome to use a dictionary and a calculator.

**A) Answer question only 7 of the following 9 questions:**

1. **Hiring the Right People (max. 10 points)**  
Suppose that your firm is in financial trouble. Nevertheless you have to hire new workers for your firm. Assume you have the choice between students with an academic degree (D) and applicants with a highschool degree (H). A D will generate a revenue of 5,000 € per month, a H generates a value of 4,580 € per month. The market wage for Ds is 15 € per hour and Hs make 14,50 € per hour (they work 176 hours per month).  
a) By which criterion should your firm decide which type of workers to hire in that situation?  
b) Calculate the marginal profits of both types. Explain your findings.
2. **Motivation (max. 10 points)**  
We can distinguish two types of motivation. Describe them, and use your own examples to illustrate the difference. Why is it so important to distinguish these forms when designing a compensation structure?

**3. Compensation Schemes and Institutional Framework (max. 10 points)**

Explain how the principle of cost-utility-arbitrage can be used to design efficient cafeteria plans. Explain three institutional rules that influence the composition of such plans.

**4. Tournaments and Promotions (max. 10 points)**

- a) What are the basic principles of the tournament theory? Explain.
- b) Assume there are 10 Vice President positions in a company with an annual salary of 160,000 € each. On the next higher level of the hierarchy there are 5 Executive Vice President positions with salaries of 310,000 € each. The President receives a compensation of 360,000 € per year. Calculate the strength of incentives for VPs and EVPs resulting from this design. Why could such a structure make sense in reality?

**5. Fluctuation of Employees (max. 10 points)**

Suppose the demand for the products of your firm decreases. In order to avoid making losses you have to “downsize”. You will need to separate from the least productive employees, which happen to be the oldest. Your idea is to offer those employees a buyout plan that will induce them to quit voluntarily. The following dataset is provided by your personnel department:

Age	Present value of decreased productivity	Present value of wages	Present value of alternatives
59	51.000	51.000	49.000
60	49.000	49.800	48.500
61	47.000	48.600	47.000
62	45.000	47.400	45.500
63	43.000	46.200	44.000

- a) Which variables determine your firm’s buyout offer? Explain the logic of calculating such offers.
- b) Calculate the efficient buyout offers for each age group using the dataset above. Who will accept the buyout offer? Explain.

**6. Absolute or Relative Performance Measurement (max. 10 points)**

Discuss the pros and cons of an absolute or relative performance measurement. When should relative over absolute compensation be used as a motivator? You are welcome to use examples for explanation.

**7. Trust (max. 10 points)**

Explain the notion of “trust” from an economic perspective. What consequences could arise for a firm’s owner if he only trusts in the “good-will” of his employees? Explain three alternative solutions to avoid that problem.

**8. Motivation and Efficient Use of Limited Resources (max. 10 points)**

What information do you theoretically have to know about your workforce in order to design an efficient incentive scheme? Is it always useful to acquire all this information? Please explain what HR-managers could do to solve that problem.

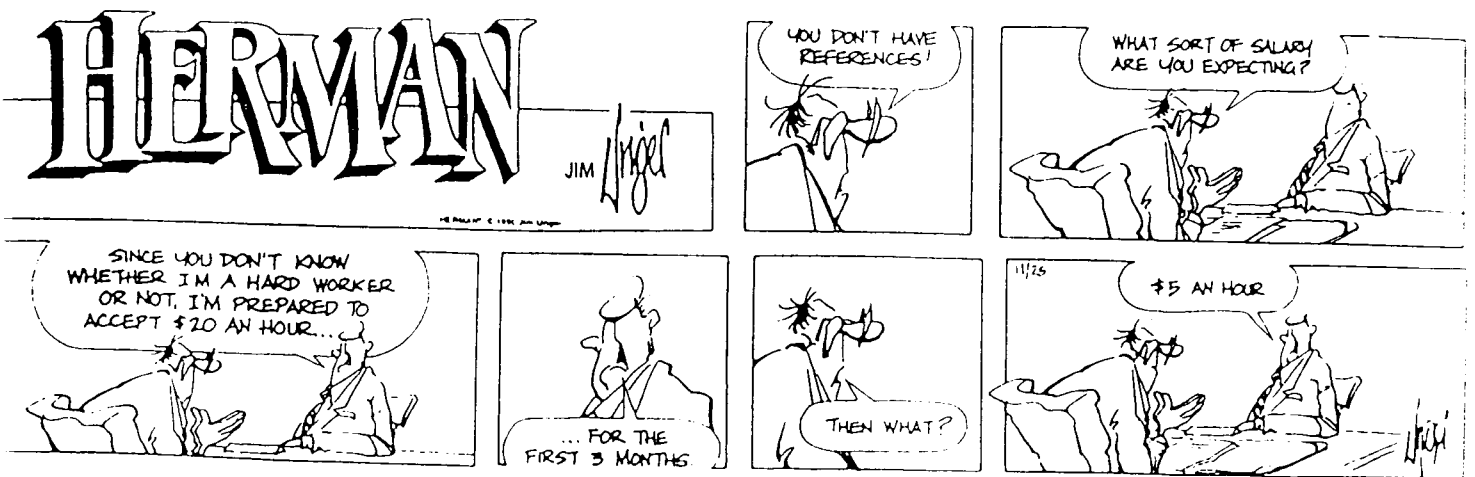
9. Reengineering (max. 10 points)

Please describe the notions of 'collective efficiency' and 'incentive-compatibility'. Subsequently, elaborate on the implications of incentive-compatibility on the success of reengineering projects. Please do not forget to explain how and under which conditions incentive-compatibility may be established. You may refer to a game-theoretic example of your own choice if it helps to clarify your explanation.

B) Essay (max. 70 points):

Which model from personnel economics is the cartoon on the opposite page referring to? Explain the theoretical logic underlying this cartoon. What is the employee in the cartoon revealing about himself? What contract would you offer that employee?

Good Luck!



Jim Unger. HERMAN is printed with permission from Laughingstock Licensing Inc., Ottawa, Canada