

“Win-win Cooperation” Between Government and the Third-party Education Evaluation Agency—Enlightenment from Incentive Compatibility Theory

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Abstract: With the separation reform of supervision, running and evaluation in education in China, the government and the third-party evaluation agency begin to cooperate to conduct education evaluation. Obviously, the government and the third-party education evaluation agency have “different” interests demand because of the differences in identity. Existing research has recognized the the problem of “damage of public interest” that may arise from conflicts of interest and incompatibility between the two and the scholars also tried to solve the conflicts to realize the ideal expectation and vision of “win-win cooperation”. However, how can “win-win cooperation” of the government and the third-party evaluation agency be realized? This is the goal of the research. By using critical discourse analysis, this paper intends to clarify the interests compatibility between the government and third-party education evaluation agency, based on which, effective measures are proposed to avoid the moral hazard behaviors generated by the third-party education evaluation agency pursuing “selfish interests”. Consequently, the study finds that constructing relevant systems based on the “truth telling mechanism” of Incentive Compatibility Theory enables the third-party education evaluation agency to pursue its own interests through “legitimate ways” rather than “unjustified opportunistic ways”, thus, enhancing “collective value” while increasing “private interests”.

Keywords: Incentive Compatibility, Win-win Cooperation, Third-Party Education Evaluation

1. Introduction

With the gradual development of the separation of supervision, running and evaluation in education, the education evaluation entered the stage of commissioned evaluation [1]. The government acting as the principal and the third-party evaluation agency acting as the agent work together to complete the education evaluation tasks. As is known to all, under the commissioned evaluation mode, the interests of “government” and “the third-party agency” may present both “same” and “different” aspects. Therefore, stakeholders have reached a consensus: noticing rather than “ignoring”, affirming rather than “denying” the “different” interests of both parties. However, of particular concern is that when there are “different, conflicting and incompatible” [2] interests in education evaluation, how can the third-party education evaluation agency give up the “dangerous and

improper” ways of “infringing on the interests of the government” voluntarily and choose the “legitimate ways” to “do not harm government’s interests” when pursuing its own interests?

If the third-party evaluation agency “acts in a dangerous and unfair manner to make an opportunistic behavior against others in order to maximize its own interests” [3], there will be moral hazard to jeopardize the impartiality of education evaluation. Conversely, if the third-party evaluation agency pursues “private interests” in “legitimate ways” and “does not exclude the interests of other parties including the government”, it will be beneficial to the realization of the “collective interests” of the participants. This is a “reciprocity” and “win-win” situation.

It should be said that the “reciprocity” and “win-win” relationship between the government and the third-party agency is the ideal vision that the scholars [4, 5] expect.

However, easier said than done. Opportunistic behaviors are human nature. How can third-party education evaluation agency pursue their own interests in “legitimate ways” rather than “unjust opportunistic ways”? According to Incentive Compatibility Theory, the system based on “truth telling mechanism” can solve this problem effectively. If the participants gain more from telling the truth (legitimate ways) than from telling lies (opportunistic ways), they will take the initiative to choose the “legitimate ways” of “telling the truth” rather than the “opportunistic ways” of “saying lies.” It is precisely because the “legitimate ways” are recognized by both parties, it will not bring “deliberate damage” to the interests of both parties, and “win-win cooperation” may be realized.

Based on the “truth-telling” mechanism in Incentive Compatibility Theory, this paper analyzes the respective interests of the government acting as the principal and the third-party education evaluation agency acting as the agent, and then analyzes the compatibility and incompatibility of the interests of the two; Moreover, this paper proposes to construct a corresponding system based on “truth-telling” mechanism so that the third-party education evaluation agency can actively avoid moral hazard and seek benefits in legitimate ways, thus leading to the compatibility of the government and the third-party evaluation agency and achieving “win-win cooperation”.

2. Literature Review

Previous research has established that it has triggered the phenomenon that the third-party education evaluation agency harm public interests when pursuing their private interests because of the inconsistencies, contradictions and conflicts between the education evaluation agency and the government.

For example, study by MAO (2006) noted that in order to seek maximum benefits, social agencies and interest groups will inevitably adopt rent-seeking behavior in the face of the temptation of a large number of institutional rents [6]; Study by HAN (2014) also proposed that rent-seeking phenomenon in education evaluation “is usually to obtain private benefits at the expense of the interests of others... the starting point is to maximize private interest” [7]; XI (2009) demonstrated that rent-seeking phenomenon in higher education evaluation can be understood as the behaviors of relevant stakeholders “gaining excessive interests for organizations or individuals” [8]; WANG and YANG (2018) noticed the “credibility crisis” encountered by third-party education evaluation and questioned that the third-party evaluation agency may be “selfish” when it issued evaluation reports and “may provide evaluation reports that may be contrary to the public interests” [9]; Study by WANG and ZHANG (2006) showed that some third-party evaluation agencies “may disregard the facts for their own interests and get inappropriate evaluation results” [10].

In exploring how to address the moral hazard arising from conflicts of interest, several studies have proposed the basic viewpoint of “coordinating interest relations” and “promoting

the balance of interests”, and have imagined “reciprocal” and “win-win” vision. For instance, XI (2009) proposed some ways to strengthen institutional construction and “coordinate the conflict of interest” when exploring how to prevent rent-seeking problems; WANG and ZHANG (2006) suggested that the government should sort out the current situation of the third-party agency’s interests dispute in the evaluation process, meet the rationality requirements of the stakeholders, and promote the “rebalance of interests”.

Together, these studies indicate that in response to the loss of collective value and public interest caused by conflicts of interest, the concept of “reciprocal and win-win” cooperation, that is, the idea of not neglecting the reasonable interests of either party, has been proposed. However, the studies mentioned failed to specify how to realize “reciprocal and win-win” cooperation. Therefore, this study proposes that the construction of the interest-consistent system from Incentive Compatibility Theory is a possible solution.

3. Theoretical Basis

Incentive Compatibility Theory [11] was originally proposed by American economist Havertz K. who pointed out that under the assumption of economic man, individuals in the market act in accordance with the rules of “self-interest”, if there is a mechanism that enables participants’ behaviors of pursuing “private interests” integrate with the goals of “collective interests”, this is a system arrangement of incentive compatibility. Generally speaking, incentive compatibility is to take the interests of all parties as the starting point and the foothold, and to pursue the interest compatibility of all parties, so that each participant does not exclude the realization of the interests of other parties while pursuing “self-interest” and the integration of the participants’ “collective interests” and “institutional cooperation” [12] could be achieved.

3.1. Incentive Compatibility

The term “incentive compatibility” and the term “incentive incompatibility” [13] are a pair of corresponding concepts. The term “incentive incompatibility” refers to the phenomenon that “private individual interests” is incompatible with “collective value”. Both the disregard of individual interests and the neglect of collective values in a system are manifestations of incompatibility in which the goal of “collective action” cannot be achieved. Institutional arrangements of “incentive incompatibility” can lead to a range of moral hazard behaviors and consequences (see Table 1). Table 1 compares the difference on moral hazard avoidance between incentive compatibility and incentive incompatibility. First of all, if the institutional arrangements only pays attention to public value and “collective interests” and ignores private interests, it will result in the phenomenon that individuals with “high quality” are “unwilling to participate” but the individuals with “low quality” take advantage of a weak point. Secondly, if institutional arrangements only focus on “individual interests” and lack

institutional constraints to achieve “public interest”, then the individual may “damage” the collective value and interests based on the motivation of “self-interest” when pursuing the

maximization of self-interest, and a series of moral risk behaviors occur.

Table 1. *Difference on moral hazard avoidance between unilateral incentive and incentive compatibility.*

	Focus on public value	Focus on individual value	Interest compatibility
Incentive objects	Collectivity (unilateral) Incentive incompatibility	Individuals (unilateral) Incentive incompatibility	Collectivity & Individuality (bilateral) Incentive Compatibility
Incentive effects	Ignoring individual value	Ignoring collective value	Emphasizing collective interests & individual interests
Risks	The premium does not participate; Moral hazard occurs	Seeking individual interests excessively; Moral hazard occurs	Actively avoiding moral hazard

3.2. “Truth Telling Mechanism” in Incentive Compatibility

Incentive Compatibility Theory focus on the institutional design function and believes that using “institutional rules” [14] can “beneficially guide” [15] stakeholders, so that participants who are “Economic Man” can “continue to adjust and correct their own actions and rules” [16], thus taking “legitimate ways” to pursue their individual interests.

The “truth telling mechanism” is such an institutional rule. It can be learned from Incentive Compatibility Theory that whether a participant “tells the truth” [17] depends on the “utility”. If “telling the truth” makes the utility far greater than the utility of “saying lies”, the participants will choose to tell the truth naturally, “show all the information truthfully” and take proper actions instead of choosing to risk “losing more” [18] of implementing opportunistic behaviors. In this way, “telling the truth” becomes the best choice for participants and “dominant strategies”. [19] Thus it can be seen that “telling the truth” is a “legitimate way” to gain interests while “saying lies” is an “improper way” to gain interests. Only when the benefits and effects of legitimate ways are greater than the benefits and effects of the “improper ways”, the legitimate ways will be adopted first. The key of incentive compatibility system is that the utility of “telling the truth” is greater than that of “saying lies”.

Under the separation system of supervision, running and evaluation, the government commissioned the third-party agency to carry out education evaluation. In the education evaluation, it is necessary to realize the public interest of the government as well as the interests of third-party education evaluation agency. If the third-party evaluation agency cannot obtain benefits through legitimate ways, it may obtain benefits through “improper ways”. Therefore, it is very important to construct a “truth-telling” mechanism of incentive compatibility to provide “legitimate ways and approaches” for the third-party evaluation agency to obtain legitimate interests.

4. Analysis on the Interests Compatibility Between Government and Third-party Evaluation Agency

The premise of designing the “truth-telling” system is to know the interests of the government and the third-party

education evaluation agency. After clarifying the interests of both of them analyzing “which interests are compatible and which interests are incompatible”, we can find the internal reasons that lead to the “incompatibility” in order to promote the “incentive compatibility” system design.

4.1. Interests Demand of the Government and the Third-party Education Evaluation Agency

The government acting as the principal and the third-party evaluation agency acting as the agent have different interests demands.

4.1.1. Government’s Interest Demands

Demand on high-quality results. The government’s major interests demand on education evaluation is the fair, objective, and true evaluation results. After the separation reform of supervision, running and evaluation, the government no longer participates in the evaluation process directly—The government supervises education evaluation in a “decision-making” manner while the third-party agency carry out education evaluation in a “executive” role. It is precisely because of the “speciality” and “professionalism” of the third-party education evaluation agency that the government entrusts it to carry out education evaluation. Therefore, the government expects that the third-party evaluation agency can provide “high-quality” evaluation results to reflect the actual school-running level “objectively and realistically”, thus providing a reference for education management decisions.

Demand on appropriate investment. “Appropriateness” and “appropriate principles” in the “funding investment” of education evaluation are pursued by the government. First, the “costs and subsidies” given to the agent should be able to meet the costs of the third party’s education evaluation; Second, it is necessary to give the third-party agency a certain “profit space” to enable them to maintain their own operations and “expand reproduction”; In addition, public education funding should not be wasted for the improving usage of financial resources.

4.1.2. Third-party Evaluation Agency’s Interest Demands

Demand on profession. “Demand on profession” is the foundation of the third-party evaluation agency. With professional appraisers, professional evaluation techniques, and professional evaluation methods, the third-party evaluation agency is specialized agency engaged in education evaluation, which has a “professional” requirement for the quality of education evaluation work it engages in. Because

only when it reaches a certain level of professionalism, it can be recognized by peers, clients and evaluation targets in the field so as to occupy a position in the competition of the industry. In short, a higher “professional level” is the “core competitiveness” of the third-party education evaluation agency.

Demand on reputation. Demand on reputation is the interest demand in “non-economic form” and an additional product of the “professional demand” of the third-party evaluation agency. Good credibility and reputation which have an important impact on their foothold and development are the hidden capital of third-party evaluation agencies. Therefore, the third-party evaluation agencies need a large amount of trust, affirmation and praise from the government and universities to form a reputation effect to help them improve industry status and social reputation.

Demand on income. Demand on income is an important interest demand of the third-party evaluation agency. The third-party agency need to obtain “funds” in the form of direct investment or subsidies by government. These funds are used to cover the cost of education evaluation and to maintain the basic needs of assessing the operations and expanding its development. Moreover, as homoeconomicus, third-party evaluation agency will certainly never be satisfied with the amount of funding.

4.2. Interest Compatibility Between the Government and the Third-party Education Evaluation Agency

4.2.1. Consistency and Compatibility on Profession Demand of The Third-party Education Evaluation Agency and Objective Results Demand of Government

The professionalism and specificity of the third-party agency in education evaluation is the most important reason why the government is willing to transfer education evaluation power to the third-party agency. In the government’s expectation, entrusting the third-party agency to conduct education evaluation will result in high-quality results. Coincidentally, the third-party education evaluation agency also value their professional competence that will directly affect their own survival and development, and will make them competitive. If a third-party agency is unable to meet profession needs, it will slowly lose competitiveness in the industry and even “disappear” from the evaluation market. Consequently, there are consistency and compatibility between “profession demand” of third-party education evaluation agency and “objective results demand” of government. In other words, the more the evaluation agency pursues the “profession” and “reputation”, the more the government will be able to obtain “objective and fair evaluation results”. Both are mutually reinforcing in “in the same direction”.

4.2.2. “Connection Point” for the Construction of the Incentive Compatibility Mechanism: The Consistency and Compatibility

With “consistent interests” as the “connection point” of the “win-win” institutional arrangement, it is possible to “guide” the evaluation agency to pursue “quality” of presenting

“objective and fair evaluation results”, which will allow them to obtain “legitimate benefits” to make incentive compatibility possible. Conversely, without a “connection point” of interest compatibility, third-party education evaluation agency may obtain “unfair income” through other moral risk behaviors such as “deception, inaction, rent-seeking, and collusion”. Correspondingly, the “win-win cooperation” system is difficult to construct.

4.3. Incompatibility on Interests Between Government and the Third-party Education Evaluation Agency

4.3.1. Incompatibility on Economic Interests

The third-party education evaluation agency are eager to “maximize” the benefits while the government tends to invest “appropriately” that compensate for the cost of third-party education evaluation and enable it to obtain appropriate economic benefits, to meet the needs of maintaining operations and expanding development but not causing waste. That is to say, the demand for “maximizing” economic returns by the third-party agency is “incompatible” with the demand for “appropriate investment” by government. Because the investment from government is not certain to meet the economic benefits of the third-party agency, there is interest conflict between the two. If the investment from government is not enough to meet the expected benefits of the evaluation agency, the third-party agency may abandon the “profession demand” and ignore the government’s “objective results” demand and take unfair behaviors. Thus, “moral hazard in two directions” [20] occurs: On the one hand, education evaluation agency may abuse powers. If the evaluation agency encounter the “rent-seeking” circumstance in the work, it may be unable to withstand the temptation of “high rent” and be “captured”; In addition, it is possible for the evaluation agency to “collaborate” with the school to seek “unfair” interests; On the other hand, it is highly probable that the evaluation agency will “deliberately reduce costs” and “make low-level efforts”. Anyhow, these two kinds of moral hazard behaviors will cause serious harm to the government’s pursuit of “objective and fair results”.

4.3.2. Make the Incentive Compatibility Realize: Taking the “Incompatible Interests” as the “Pointcut” of Construction Mechanism

It should be noted that the problem should be solved from the place where the problem occurs. Therefore, we should proceed from the “incompatibility” between the government and the third-party education evaluation agency to design a compatible system. For one thing the government must grasp the “standards” of “moderate investment”, meet the “reasonable demands” of the third-party evaluation agency to enable them to achieve expected benefits through “legitimate ways” rather than “unfair ways”. For another the government must clarify the rules for rewards and punishments. If the evaluation agency performs well, the government can reward it and, if there is moral hazard, punish it. From these two aspects, the third-party education evaluation agency can be induced to adjust and correct their actions and behaviors

constantly, to obtain their own interests in "legitimate ways" and to achieve the compatibility of their interests.

5. System Construction on "Win-win Cooperation"

The "truth-telling" mechanism in Incentive Compatibility Theory is the basis for the institutional construction of "win-win cooperation" between the government and the third-party education evaluation agency. According to the principle of comparing the utility of "telling the truth" with "saying lies", to establish a system of "win-win cooperation" between the third-party evaluation agency and the government, three conditions need to be met. First, ensure that the third-party education evaluation agency is willing to participate in the education evaluation and become agents. Second, encourage the third-party education evaluation agency to "tell the truth". In other words, third-party agency's incomes should be directly proportional to their efforts. Third, punish the behaviors of "saying lies" by the third-party education evaluation agency. It is necessary to form a regulatory effect that "saying lies" is proportional to punishment and "loss". In short, "truth-telling" mechanism can play the role of "benign induction" that enables the third-party agency to obtain interests through "legitimate ways" rather than "dangerous and unfair methods", thereby prompting the third-party evaluation agency to give up moral hazard behavior voluntarily.

5.1. Provide Reasonable Funding to Ensure that the Third-party Evaluation Agency "Participate into" the Education Evaluation

The premise and basis for the operation of the incentive compatibility mechanism is to "participate" "premium" participants and expel "low-grade" participants. If the utility of "participation" is greater than "no participation", then the participants will choose to "participate" and vice versa. What is even worse is that if the "inferior" agencies that "maliciously reduce costs and make little efforts" enter education evaluation field, the possibility of moral hazard behavior will exacerbate greatly. Therefore, in order to construct an incentive system with a compatible interest, we must involve high-quality agents in order to prevent the phenomenon of "strong agency not competing" and "weak agency flooding the market".

As an agent, the third-party evaluation agency has certain income "expectations". Although the evaluation agency can not "profit for the purpose", it can "profit" in its operation process because third-party evaluation agency not only need to make money to cover the cost of the normal work and operation, but also need to pay for development funds in the future "expanded reproduction". If the third-party evaluation agency finds that the "income" is not within the "reasonable" scope, that is, the income cannot meet its own development needs, the "premium" third-party agency may not participate in the government's commission task, instead, it will be

involved in other evaluation tasks. It is clear that the benefits of participating in government mandates are far less than the benefits of participating in other works.

Under this circumstance, the "inferior" evaluation agency with low-level personnel quality, skills and cost is easily satisfied by the "investment" from the government and actively participate in the evaluation. Undoubtedly, the evaluation market will be occupied by "inferior" evaluation agencies in the long run and there will be terrible education evaluation quality received by the government. Therefore, it is important that the government determine a reasonable "investment standard" to ensure that "premium" third-party agencies participate in the education evaluation.

5.2. Establish a Statute Mechanism to Avoid Moral Hazard of the Third-party Evaluation Agency

In all systems, the third-party agency, "economic man", will adjust action rules to achieve the goal of maximizing benefits. If there is an institutional arrangement that enables the evaluation agency to find that the true evaluation results rather than the false evaluation results could obtain the maximum benefit, then the third party agency will choose the true evaluation results as action criteria, because this is the most beneficial to itself. Conversely, if the third-party agency finds that false evaluation could maximize the profit, the agency will abandon the true evaluation criteria. Hence, the government must construct the institutional rules of "legitimate returns more than the opportunistic gains" and form a benign situation in which the evaluation agency maximize profits through "legitimate ways".

But sometimes, people often take chances. Even if "legitimate income" is greater than "rent-seeking income", when there is an opportunity to reap some "rent-seeking benefits", the third-party evaluation agency still have such an attempt. At this time, the comparison on the "cost and benefit" of rent-seeking will work. Based on the nature of maximizing benefits, third-party education evaluation agency will certainly calculate the benefits and gains. If the evaluation agency finds that its rent-seeking behaviors are recognized but not be punished and suffers large losses compared to the gains obtained in rent-seeking, it will feel that rent-seeking is "worthy to risk", of course, if rent-seeking behaviors are not recognized, its "gains" will be even greater. On the contrary, if the evaluation agency finds that rent-seeking behavior will cause very serious losses, then it will recognize that rent-seeking is very undesirable. At this time, moral hazard behaviors will be greatly reduced. Therefore, from the perspective of punishment, the introduction of relevant policies to make the cost of rent-seeking greater than the benefits of rent-seeking will help prevent the moral hazard of third-party education evaluation.

5.3. Establish a "Performance Reward" Mechanism to Inspire the Third-party Evaluation Agency

If the interests obtained by the third-party education evaluation agency can only meet the "reasonable expectation",

it will complete the evaluation tasks to meet the “bottom line” defined by the government, that is, it only meets “pass” standard. In fact, there is limited incentive for the third-party education evaluation agency. Because if the “enthusiasm” of the third-party evaluation agency of completing the tasks is not motivated, it will lead to a “low level of competition” among the education evaluation agencies and a negative psychology that passes if it is qualified. At this time, the “performance reward” mechanism, also known as “superior mechanism” that the harder you work, the higher the quality of the task you complete, and the more reward you get, is necessary. In this rule, in addition to the rewards of the economic form, there will be non-economic forms of rewards such as “trust and reputation”. Together, all the rewards will inspire the third-party evaluation agency to complete the evaluation tasks “excessively”, obtain satisfactory evaluation quality, and form a virtuous cycle of “pursuing excellence”. Therefore, the “performance reward” mechanism is an important part of the “win-win cooperation” system between the third-party evaluation agency and the government.

In short, this study has identified that the establishment of an incentive-compatible system makes it possible to achieve “win-win cooperation” between the government and the third-party education evaluation agency. Establishing a dynamic and adjustable “true-telling” incentive mechanism that is compatible with all parties by unblocking the communication channels of stakeholders, understanding the reasonable expected returns of all parties and estimating the possible moral hazard can “collective action” [21] be possible. Furthermore, the “win-win cooperation” between the government and third-party evaluation agencies can be achieved.

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