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Abstract

We study how agents decide between working for firms with profit sharing and firms in which pay is based on individual productivity. Profit sharing has the disadvantages of free riding and adverse selection. The benefit of profit sharing is that it makes easier for agents to signal their productivity. We show that in equilibrium skilled agents are more likely to belong to profit sharing organizations. The analysis provides a framework for understanding the market structure of industries like law, accounting and consulting services in which both profit-sharing partnerships and "eat-what-you-kill" firms co-exist and compete with each other.

KEYWORDS: Partnerships, Companies, Equal Sharing, Professional Services.

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