CONFLICT BETWEEN OWNER AND AGENT CAUSE AND SOLUTIONS

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The promulgation of the Companies Law makes the number of companies skyrocket. This situation leads to more goods and services on the market but it also gives birth to many problems, including the agent one. This paper will present two solutions to the problem by using financial measures.

1. Cause of the agent problem

The agent problem arises when conflicts between interests cause the agent to stop acting for interest of the owner. The problem takes place when: (1) the agent and the owner are two separate entities and (2) there are conflicts between their interests. When it happens, the agent's actions aim at protecting his interests and thus causing harm to the owner's interests.

In Vietnam, the problem easily takes place in two kinds of company: joint stocj and state-owned ones where the owner and agent are two different entities and no proper attention is paid to conditions for the harmony of their interests. When conflict takes place the business performance will inevitably go bad.

2. Solutions

There are many solutions to the problem. We want to discuss here two of them. The first one is the effective salary scale and the second is the use of options as a bonus. The first one could be applied to the two above-mentioned kinds of company while the second one is applied to the joint stock company only.

a. Effective salary: The reason behind this model is a salary scale that encourage the agent to work for the owner's interest instead of his/hers. To work out this scale, we must consider the following inequations:

g (w - w') [1], where w is the salary for the agent, w' is the average wage offered on the labor market and g is benefit for the agent when he work for his interest. This equation means that the difference between w and w' must be big enough to prevent him from working for his interest.

However, it's possible for him to work for his interest in spite of big difference between w and w' if he thinks that his acts won't be discovered. So the probability of discovery P must be included and we have g P (w – w') [2]. In addition, the agent may expect a long-term employment from the company and the variable N for his expectation is also included and we have g P (w – w') N [3].

The inequation [3] helps us realize the following measures:

- Paying salary high enough to ensure reasonable difference between w and w'.
- Increasing the value of P by carrying out regular inspections, audit and evaluation.
- Increasing the value of N by giving priority to young people who want get long-term employment.

b. Options: The company could give call options to employees instead of bonuses in cash. The value of call options equals the difference between the market price of stock and its exercise price (price the agent pays if he choose the options instead of cash). Benefit he enjoys depends on the market price of the stocks (because the exercise price is unchanged while the market price fluctuates). This solution encourage employees to work for the interests of the company with a view to enhancing the market price of the company's stocks, and thus increasing the value of stocks he is awarded. In short, the use of call option as a reward could link the employee's interest with the company's ones and remove all potential conflict between them. ■