

QUALITY, PLATFORM CONTRACTING, AND MARKET DESIGN

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Abstract

Platform markets (two-sided markets) tend to be analyzed in the context of pricing frameworks. Scant attention has been paid to a complementary line of thought, based on the observation that in many cases, the quality of goods and services running on the platform may be as important for the market as “getting the prices right.”

This paper offers an analysis on how to optimally govern the contractual relationships between the platform and the developer (seller) side so as to solve inherent problems of moral hazard and adverse selection when the seller needs to be incentivized *ex ante* to invest in quality development, which is not observable. In line with the ideas of the new literature on platforms rules and regulation we show that platforms may typically use two forms of governance that differ in their degree of vertical integration. The contractual mode used will furthermore decide whether the revenue of the platform will be collected from sellers or from buyers. Our findings are novel in that we show how contract design solves the problem of getting consumers to join the platform that care about quality.

JEL classification: *L14, D82, C72.*

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