Alternative Institutional Structures

Evolution and impact

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10 On Institutional Individualism as a *middle-way* mode of explanation for approaching organizational issues

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Introduction

For approaching organizational issues, is there any mode of explanation that provides a *middle way* between methodological individualism (MI) and methodological holism (MH) in their several varieties? To provide an answer for this question is the basic purpose of the present article. Because many contributions have been published on the comparative virtues of these two modes, my aim here is not to deal with these debates but to focus on Institutional Individualism (II), a different *hard core* methodological principle that allows for building explanatory analyses of such a middle way.

The chapter is organized as follows. After pointing out the positions held by some scholars who are not satisfied with holist, nor with reductionist analyses, I provide a brief and synthetic demarcation of MH and MI in order to show that a substantial gap between the two exists. Next, I go on to explain what Institutional Individualism (II) consists of and why it can be characterized as a middle way mode of explanation. In order to present it, the contributions of J. Agassi (1960, 1975) himself are considered, also indicating why II is not the same thing as the so-called Popperian program of situational analysis. Lastly, the paper points to some explanatory analyses that may be deemed to be reasonably good institutional individualist analyses. The examples are mainly about the organization of policy tasks and other public sector organizational affairs. Because these issues have been much debated, several comments and references will be provided in footnotes as a way to complement the mean line of arguing and account for the many contributions published since the 1960s.

The ultimate purpose of the article is to show that it is possible to make analyses that are based on the rules of Institutional Individualism as well as on those other methodological foundations often found in the OIE (Old Institutional Economics) and NIE (New Institutional Economics) traditional contributions. Several examples of analyses so built will be offered from both camps. To prevent any misinterpretation, I must clearly state that this does not necessarily mean that a kind of convergence is occurring between different approaches in institutional analysis. No statement in favor of such a convergence is made in

the present article. The sharp differences in approach and substance that can easily be found in many OIE and NIE published papers may be maintained even if a similar mode of explanation is adopted. The rules of Institutional Individualism do not preclude the possibility of accounting for power influences, distributional conflicts, inequalities, etc. as institutionalists in the OIE tradition often do. Nor does it prevent new institutionalists from adopting a voluntary conceptualization of economic transactions, using transaction cost concepts, accounting for efficient or inefficient institutional changes etc., as they often do. Some hybrid, but methodologically consistent, institutional individualist analyses can also be built, and some examples will be mentioned.

I like to state clearly also that, in accordance with the dictates of methodological pluralism, the purpose of the present article is, rather, to show that a new alternative exists than to argue against methodological holism and methodological individualism. Epistemological issues are not addressed in the paper either, as my aim is not to deal with questions about the empirical truth or falsity of different economic explanations. These are nevertheless complex issues to be collectively determined and no general agreement is expected to occur. However, disagreement in the social sciences does not necessarily mean bad research performance if aims and/or interests differ, including those of the agents being studied and those of the researchers, whatever the natural scientists say about explanations of chemical reactions, for example. Although they are necessarily interwoven, the present article also places special emphasis on separating the mode of explanation issue from the many other methodological issues at stake, such as those concerning the rationality assumption, the mode of interaction assumed, the intended/designed versus unintended/evolutionary conceptualization, the assumed level of uncertainty, etc.

What the former introductory comments help me to stress is that on the rules of Institutional Individualism it is possible to account for many aspects depending on the situation investigated and the research purpose at hand. Institutional Individualism is simply a *middle way* mode of explanation that yields non-systemic and non-reductionist explanations at the same time as it allows for the incorporation into economic theories and models of the many formal and informal institutional aspects surrounding all human interactions, whether these interactions take place under stable structures of legal rules and social norms or whether they attempt to change them.

Who cares about middle way economic analyses?

Who cares about economic explanations of a middle way? As regards analyses aiming at building general economic theories, I believe that it is not difficult to agree that both holist and methodological individualist explanations abound.[1] However, if we look at those applied economic papers and reports published in many business oriented journals or in the applied economics ones, these two methodologically more extreme types of explanations are not so easily found. The same seems true concerning the stories of human affairs recounted by journalists. This is particularly so in the local press stories about organizational and institutional change issues. The way most of us think about our real case independent or collective decisions is not so extreme either, I believe. If this is so, can any complaint in the economic literature be found about the way many general economic analyses are built? Many complaints can always be found, of course.[2] Some complaints relate to the fact that general economic analyses are becoming more and more abstract and sophisticated because they increasingly incorporate mathematical models or econometric equations looking for statistically significant correlations, but this is not the issue I want to address here.[3]

The existence of both holist and reductionist analyses in economics has been paralleled by a never ending debate on the comparative explanatory relevance of both of them, let aside other comparative *virtues* from an ideological, political, or any other explicit normative stance. Concerning the institutionalist literature, this debate may be introduced by reference to representative papers that were published almost 20 years ago by Langlois (1989) and Rutherford (1989). Langlois did not like the holist explanations that were so abundant among OIE contributions of the time. Rutherford, in contrast, did not like the reductionist requirement that a strict interpretation of methodological individualism imposed upon many of the NIE analyses published over the 1970s and 1980s. In the philosophy and the sociology of science camps, this and related debates took place much earlier.[4]

Among economists and economic methodologists it was during the 1980s and 1990s that a significant number of articles and books on methodological and epistemological issues, on rhetoric and realism, on persuasion, etc. were published. If these debates had to be summarized in only one word, "confrontation" is the one I would choose. In most cases, confrontations between those endorsing an anti-holist approximation and those others endorsing an anti-reductionist one responded, in part, to deep ideological differences, let aside other explanatory factors.[5]

Although my purpose is not to argue in favor or against MH or MI, a few demarcating comments on these two modes of explanation may be helpful for a better understanding of the following sections. The comments will show that a substantial gap between the two exists. This is not an easy task because not only confrontation, but also a great deal of confusion, has surrounded these and related debates.[6] Concerning methodological holism, several versions have been suggested and used.[7] However, according to the classic and much cited contribution by Wilber and Harrison (1978), and also according to Rutherford (1994), it is not only accurate but also helpful for the purpose of the present chapter to state that when authors adopt a holist mode of explanation they usually presuppose that individual actions can only be understood and explained properly if agents involved are considered as elements or components of some other *social entities* and *systems* (this is the terminology often employed). The position agents occupy in these *social wholes* is considered a basic factor that determines the values, ideas, knowledge, preferences, purposes, and constraints they face. Therefore, in order to analyze human interactions and the events generated,

these authors often pay special attention to the so called *social entities* (*groups, associations, corporations, political parties, churches, states, etc.*) to which many individuals mainly belong as passive members who internalize or assume (let us disregard now how it is said to occur) the purposes, values, norms, etc. which have usually been established long before as distinguishing marks of the said *entities*. It is because of the aforesaid presupposition that these factors occupy such a central position in the holist OIE contributions, for example. In holist analyses, it is also frequently assumed, explicitly or implicitly, that these *social entities* and *systems* possess a kind of systemic force or logic which drives events in such a way that it is difficult for the analyst to discover personal responsibility for what is going on. Events such as continuous changes in prices, increasing unemployment, technological changes, etc. and, indeed, institutional reforms, all tend to be explained by way of revealing which systemic and impersonal forces are in place and how they operate, besides accounting for some other complementary aspects.[8]

Of course, this is a stylized and brief presentation. Not all holist analyses are so to a similar degree. Not all are subject to the charges of functionalism, ontological holism and organicism.[9] Some analyses incorporate functionalist explanations in order to show the presence of a stabilizing force without referring to any causal mechanism, but others do not. Not all of them attribute such an insignificant role to human action.[10] And of course, not all OIE contributions are built on these holist principles and presumptions. Non-calculated human actions and norm-guided behavior through internalized habits and routines also form a part of many of these analyses.[11] As Rutherford stated:

> This social whole is seen as influencing and conditioning individual behavior. However, the strength with which the social is seen as conditioning or determining behavior of the individuals varies substantially between holists. ... In some cases, holists do seem to imply that macro or social entities have some sort of agential power of their own, but this is by no means a universal characteristic of the genre.
>
> (Rutherford, 1994: Chapter 3)

In contrast, methodological individualism as a mode of explanation is usually associated with a claim for reductionism, though some controversy has always existed on this.[12] Although several versions of methodological individualism have been suggested, it is quite frequent among scholars in economics to refer to a version that has been much promoted through neoclassical articles, books and handbooks since Lionel Robbins (1932) seminal definition of *the economic problem* as a matter of allocation of scarce means among alternative competing ends.[13] Gary Becker has also promoted it through his efforts to extend *the economic approach* based on the "neoclassical maximization assumption", as Boland (1981) and others called it, to the analysis of almost all human *choices*.[14] This is also the version characterizing many current rational choice economic analyses in the standard game theory literature in which some competing

optimizing *individuals* calculate their best choices in stylized situations that have been deprived of much of their formal and informal institutional content, except for the rule of competition and some other well-defined (not always well-enforced) conventions known by the *players*.[15]

According to this much endorsed interpretation, which is also the most useful one for my purpose here, it can be said that adopting this mode of explanation requires that social economic events (inflation, increasing unemployment, organizational changes, evolution of cultural norms, etc.) be explained in terms of individual actions and their preferences and purposes, incorporating into the analysis the relevant material constraints that affect participants (natural, technological, monetary, and the like) but minimizing the use of *social* explanatory factors. If some concepts and arguments referring to *social factors* are in fact used for elaborating the explanatory causal reasoning, this should only be a shorthand for referring to the individual actions and interactions that create them. The researcher should be able to reduce or break down these concepts and argumentations into the actions of the relevant participants if an acceptable methodologically individualist explanatory analysis has to be constructed. If team action is concerned, collective decisions adopted and implemented through *organizations* should be consistent with, at least, the actions of some members.

Recently Boland has referred to the "Principle of Substitution" of Marshall's *Principles of Economic* as a pioneer endorsement of the reductionism claim. Boland writes:

> At the other extreme is Marshall's approach which is the foundation of virtually all neoclassical analyses of institutions ... As explained before, the latter presumes that anything than can be varied in the given amount of time must yield to the Principle of Substitution, that is, can be itself explained as a matter of optimizing choice.
>
> (Boland, 2006)

He also writes:

> [E]xogeneity may depend on the amount of time under consideration.... There is nothing in Marshall's method which prevents any neoclassical economist from attempting to explain inter-generational changes in such variables as long-run prices or long-run distribution of resources. But, if changes in the long-run variables are to be explained as the results of changes in institutions (as elements of the 'social conditions'), the question is begged as to whether changes in the institutions are themselves the result of additional applications of Marshall's Principle of Substitution...
>
> (Boland, 2006)

This may be a reason why, over the 1970s and 1980s, several NIE oriented authors constructed explanatory analyses of institutional changes that were based on the rules of methodological individualism and on the rational choice

assumption.[16] In fact, these contributions suffered from such a high degree of reductionism that they could hardly be considered economic analyses of an institutionalist kind.[17] Paradoxically, and surely as a result of the reductionist claim already mentioned, institutional changes tended to be explained through analyses much deprived of institutional content. Several contributions over those years attempted to explain institutional evolution, particularly in western countries, as a result of changes in relative prices. Whatever the cause, these changes in prices were assumed to create powerful incentives for participants to devise and collectively implement new, more efficient organizational formal structures for governing their interrelationships. This "efficiency view" was subject to charges of functionalism,[18] and was explicitly abandoned by many authors, including North (1990: 7), during the 1990s.

Of course, not all NIE oriented contributions suffered, not even in those years, from such a high degree of reductionism. Already in 1993, after the Seminar Series on the New Institutional Economics held at Saar, Furubotn (1993: 8) wrote in his final remarks summarizing conclusions the following:

> If it was thought previously that the work of the new institutional economics could be accomplished simply by extending neoclassical theory, there is reason today to believe that something more is required.... Some insights yielded by neoclassical analysis will continue to be valuable, but theoretical movement seems likely to be in the direction of a more flexible and comprehensive model of political economy.
>
> (Furubotn, 1993: 8)

However, nine years before, Furubotn, E. (1984: 3) had identified the methodological foundations of the new institutional economics with the "traditional foundation stones of neoclassical theory – viz., methodological individualism and the self-interest principle".

That is enough, no doubt, for a contestable demarcation as the present one is. It has been offered not to close any debate, of course, but as a useful presentation of the issue, mainly thinking about those research scholars in economics who find the writings of methodologists extremely boring and sophisticated.[19]

What does Institutional Individualism consist of?

The above comments clearly show that some demand for these middle way analyses exists and that there is also enough room for Institutional Individualism, even if the gap seems shorter when some soft interpretations of MI and MII are considered. In fact, such a middle way mode has been already presented and is being used, explicitly or implicitly. To the best of my knowledge, it was Agassi (1975) who first named it Institutional Individualism (II) and who offered a pioneering systematic presentation of it. In this section I attempt to provide an innovative presentation of Aggassi's ideas taking advantage of the demarcation previously made. It will be argued that II is not the same thing as

the so-called Popperian program of situational analysis, even if there is a common ground between the two. For elaborating situational analyses, researchers have to adopt not only an institutional individualist mode of explanation but also some other complementary assumptions such as the rationality assumption. In contrast, it is possible to make institutional individualist explanations of different types of non-calculated behavior (rule-following behavior, norm-guided behavior, ideologically committed behavior, behavior based on habits and routines, etc.). Situational analysis may be best characterized as a program of analysis in which several *hard core* methodological principles or assumptions are established. Institutional Individualism is only one of these methodological principles. However, Institutional Individualism, as a mode of explanation, may be used in combination with many alternative *hard core* methodological assumptions, not only those ones usually chosen by Popper and others when defining the program of situational analysis.[20]

This section is intended to offer a definition and presentation of Institutional Individualism that covers the essentials and avoids some complementary aspects that are not very useful for non-methodologists as myself, as already mentioned. Because Popper's written ideas about situational analysis are not very precise, N. Koertge's (1975, 1979) interpretation of that program[21] has often been used as a substitute. Although I have deliberately altered the order of elements and made the role played by Institutional Individualism explicit, the ultimate elemental components and structure of a situational analysis, following Koertge's interpretation as closely as possible, should resemble the following:

1. *Rationality assumption*:
   Agents always act appropriately (rationally) in their situations.
2. *Description of the situation*:
   Agent A is in type C situation.
3. *Institutional individualist analysis under the rationality assumption*:
   In a type C situation, the appropriate (rational) thing for agent A to do is X.
4. *Explanandum*:
   Therefore, A does X.

Using Lakatos' concepts to characterize scientific research programs, it may obviously be said that this rationality assumption or principle represents something close to a *hard core* methodological foundation that should not be subject to discussion among those who accept the program. The type of rationality to be assumed is a different issue. What we all know as standard rational choice theories should be considered only as the most popular and extended way of defining rationality. The rationality principle need not be defined as it often is, that is, as a full rationality assumption. As OIE and NIE oriented scholars know well, it may also be defined as a bounded rationality assumption that incorporates a cognitive limitation in human processing abilities, following Herbert Simon's seminal contributions.[22] Of course, although the above elemental schema contains no indication in this respect, such a program also enables strategic interactions among

agents or groups of agents to be accounted for. Some characteristics of the situation, when present, might induce agents to act strategically when dealing with others, through individual or team/collective strategic actions.

However, what is important here is that the aspects of the situation (proposition 2) which this program of situational analysis makes it possible to incorporate as explanatory variables include not only the preferences, aims and interests of the relevant agents plus the relevant material conditions (natural, technological, monetary and the like), *but also all other relevant institutional or social aspects* that might characterize the situation in which agents interact. This means that situational analyses, so constructed, are not of a reductionist nature.[23] In this respect, Blaug (1980: 145) offers the following quotation from Popper (1976: 117): "this program consists of building a model *of the social situation, particularly incorporating the institutional situation the agent confronts* when acting, so that the rationality of his action may be accounted for."

In contrast, J. Agassi's (1975) presentation of Institutional Individualism makes no reference to the rationality principle.[24] Agassi's main task is to specify which role should be attributed to "social" or "institutional" factors when analyzing human interactions and their consequences, rather than dealing with the mental processing issue. For Agassi, both are interwoven aspects that every social researcher should consider and take a position on, but they may be conceptually demarcated. Neither was he in this article interested in adopting a position on the many other methodological assumptions that social researchers have to make in order to elaborate their analyses of human affairs. The instrumentalism/realism debate concerning assumptions was also out of Agassi's research concerns in the said paper.[25] Institutional Individualism is just a mode of explanation that may be incorporated into different research programs.

What, then, characterizes Institutional Individualism? Although Agassi (1975) defines it from a comparative point of view, I shall define it autonomously from the beginning. I shall, however, follow a similar schema to that employed by Agassi, and also by Rutherford (1994), to define methodological holism and methodological individualism in their most endorsed and used versions already indicated.[26] In order to characterize Institutional Individualism, a central question is whether "social/institutional" elements may be incorporated into the analyses/models as explanatory variables regardless of the remaining methodological assumptions adopted. A complementary question is whether "social/institutional" conditions affect the behavior or even the preferences, mental models, etc. of participants. A third question is whether particular institutional/organizational changes always take place under the umbrella of broader formal and informal institutional frameworks. The rules of Institutional Individualism provide for a straightforward answer to these three questions. Institutional individualist explanations require that three rules be obeyed. These rules establish the way in which institutional aspects may be incorporated into the theory as explanatory variables. The rules also specify the way in which institutional conditions may be assumed to affect human interactions if the author believes that they may be relevant factors, whatever the way he uses to reach this conclusion.

However, for making an explanatory analysis of any human collective affair, as economic transactions usually are, several other methodological principles (conceptualizations, assumptions, criteria, etc.), are needed in order to consistently proceed and build the *explanatory picture* to be tested.[27] Which type of rationality and preferences are going to be attributed to participants and how this is going to be decided? Which mode of human interaction is going to be adopted and therefore emphasized? What of intended/designed versus unintended/evolutionary conceptualizations? What of the level of uncertainty different agents are supposed to experience in each situation? And so on. Institutional Individualism, as a mode of explanation, does not determine the answers to these other questions because it is compatible with many, if not all, of the possible alternatives.

Though Agassi (1975) does not explicitly adopt the following schematic presentation, I believe that it incorporates all his basic ideas and arguments about Institutional Individualism. In accordance with this schema, Institutional Individualism may be defined as containing the following three rules:

1 *Only persons can pursue aims and promote interests.*
(They can act individually or coordinated in groups of individuals; the aims may be perceived as their own or as those of others; the aims may or may not be set out in written documents; the aims may be stable or subject to changes when preferences and mental models change or when the situational circumstances change, for whatever cause.)

2 *Those sets of institutional rules and norms affecting interactions among persons must be part of the explanatory variables, together with some non-institutional variables if considered relevant.*
(These sets of common formal rules and informal social norms are a variety of kinds. Common ideological principles, common cultural norms, shared social values and conventions, shared-behavioral routines, etc. are examples of these informal institutional structures under which different groups of people interact. Personal expectations about the behavior of others are not informal institutional structures as they may differ from person to person. Formal institutional rules are those written legal rules that go from constitutional rules to the written procedures established in a contract. Institutional (legal or social) structures may be part of the exogenous situational conditions that influence the opportunities faced by participants but not their fixed preferences, or they may affect the preferences of those who spontaneously try to conform or adapt themselves to the prevailing social and legal institutional environment created by others; or the institutional situation may also affect the preferences of some because others deliberately persuade them to conform and adapt to the said institutional environment; etc. Of course, non-institutional *circumstances* should not be disregarded either if considered relevant.)

3 *Marginal institutional changes always result from the independent or collective actions of some persons and always take place within wider institutional frameworks.*

(These independent or collective actions may be guided by unbounded rational and strategic calculations of self-interest on the part of all relevant participants – case by case strategic maximization – or by bounded rational and strategic ones, or by bounded rational but not strategic ones (rational rule-following, satisfying, rational adaptation by imitation, etc.), or by other deliberately chosen considerations of morality, solidarity, etc. Some agents may have higher abilities for rational strategic calculations than others. In these processes of independent or collective action some persons may attempt to persuade others to internalize certain social norms or conventions, to vote sincerely in favor of certain legal reforms they believe to be fair, etc. Such independent or collective actions may result in intended or unintended consequences, etc. When an institutional framework is changed or reformed, not only human agency but also the other legal rule structures and social norms that are not being changed must be taken as explanatory variables if they influence the process of reform. Of course, non-institutional *circumstances* should not be disregarded either if considered relevant.)

The comments below each rule must be considered as examples of the potential and flexibility of Institutional Individualism. They do not exhaust all the possibilities. Institutional Individualism is a methodological principle that may pertain to the *hard core* of different programs of analysis. Rule 1 makes this a different mode of explanation from that of methodological holism, particularly in the much endorsed and used version previously depicted. Making models and analyses according to this rule means that *no impersonal active entity with apparent aims, interests and driving forces of its own is included in the discourse as an explanatory variable, nor is any other impersonal systemic factor that possesses its own dynamics for which the responsibility may not, even indirectly, be attributed to any person*. Many and diverse sets of social norms and legal rules exist, though some only in the participant's head. They usually form informal and formal institutional structures that may be included in the model or discourse according to the dictates of these three rules. These rules determine nothing concerning the many complementary assumptions that researchers also have to make in order to construct their analyses, as the examples depicted below each of the said rules show. Rule 2 makes this a different mode of explanation from that of methodological individualism one depicted in the previous section. Therefore, for those elaborating analyses according to this rule, no requirement to eliminate or break down all "social/institutional" explanatory terminology exists.

Rule 3 requires not only that concrete institutional or organizational changes be explained as resulting from the independent or collective actions of some persons but also that those other legal rules and social norms that are influencing the said process of change be incorporated into the analysis as exogenous or endogenous explanatory variables, together with some other non-institutional factors of course, if considered relevant. This incorporation should be consistent

with dictates of rules 1 and 2 if an Institutional Individualism explanatory analysis is to be made. There are few options not allowed by the rules of Institutional Individualism. Those conducting institutional individualist analyses should not *assume that only preferences and material conditions (natural, technological, monetary and the like) are sufficient exogenous explanatory variables for making economic analyses*. Among many other alternatives, it is possible to account for a change in preferences or mental models and then use this change as an explanatory variable of another event or phenomenon in what, therefore, becomes a dynamic theory or a theory of a process of change.[28]

Compared to the presumptions and rules of methodological holism and methodological individualism, at least in their most endorsed and used versions previously mentioned, there is no doubt that the three rules of Institutional Individualism make it a *middle way* mode of explanation that yields non-systemic and non-reductionist explanations at the same time as it allows for the incorporation into economic theories and models of the many formal and informal institutional aspects surrounding all human interactions, whether these interactions take place within stable structures of legal rules and social norms or whether they attempt to change the said rules and norms.

Some examples of institutional individualist analyses from the OIE camp

At this point, a new question arises: are there any examples of institutional individualist explanatory analyses in the OIE and NIE traditions? Of course there are. As my purpose here is not to carry out a survey of these contributions but to persuade readers that a *middle way* alternative exists and is being used, only some examples will be mentioned. In this section, I will consider some analyses that are constructed on the traditional methodological principles much used in the OIE camp but not on the holist mode of explanation. In the next section, I will turn to the NIE camp. For my purpose in the present chapter, questions about the empirical truth or falsity of different economic explanations are irrelevant and will not be asked, nor answered, as previously mentioned.

Schmid (1987, 2nd edn.) is an outstanding example from the OIE perspective. Of course, the reference to this classic book in no way implies that all Schmid's contributions are so constructed. Although I will concentrate on those of Schmid's institutional individualist analyses that are based on the "lenses of conflict and power", it must be emphasized that he also pays attention to many other aspects such as transaction and production costs, economies of scale, profitability of transport segments, etc. when his research purpose makes him think that these are relevant factors to be considered. Attempting to summarize some of the Schmid (1987, 2nd edn.) analyses as accurately as possible to avoid charges of re-interpretation or rewriting,[29] it can be said that among many other institutional individualist analyses, in this book he showed how people in feudal Europe had a traditional right to use certain land for cultivation and had common access to certain pastureland. If someone could not make use of his

entitlement, the land was simply absorbed by others. There was no way for a person to transfer rights explicitly to some specific other person. There was a right of use but no right to exchange or grant. Schmid writes that's the transformation from use rights to markets in many resources may be considered one of the many painful and misery-producing periods of history if we pay attention not to the total wealth created but to the huge number of people whose living conditions became extremely poor during those years as a result.

This transformation severely altered the prevailing institutional framework. The right to transfer means that it becomes possible to gain assets by withholding what you own from others even when you cannot make use of it yourself. This is a proprietary scarcity. The right to withhold from others what they need but do not own is the potential substance of market income. Coupled with the right to transfer, it is the engine by which it is possible for some people to accumulate great wealth and, in effect, to have other people work for them. In a non-transfer economy, Schmid writes, some people are more energetic and skilled than others and many have access to the use of rights to natural resources that are more productive than the resources of others. Differential access to resources means that some people still have more wealth than others, but differences are limited. In an exchange economy, the differences can be and are extreme. In a non-transfer economy with given use rights, the only cleverness that counts is that which competes with nature, but in an exchange economy, cleverness against other people redistributes assets even where the total wealth remains unchanged. If one party can be kept in ignorance, the other may make a more advantageous bargain. In a modern market economy, a good deal of talent and energy goes into manipulation of paper assets and tax avoidance, which have little to do with the production of wealth. Much effort also goes into creating scarcity to increase prices.

Schmid also showed, for example, how there is a set of property-rights issues that can best be understood as boundary questions if an institutional individualist analysis is to be made. In one way or another they all involve the issue of how a person, in his capacity as consumer or voter, is grouped with other people. For example, in a number of situations the scale of product Y has some influence on the profitability of making product X because both products are segments of a larger product sought by certain consumers. An example may be seen in the different links that exist in a transport network, such as main lines and feeder lines. A problem of interdependence arises when not all people have the same interest in each segment of the product. Some people ride a long distance over many segments and others only use a portion. When the segments are provided by different firms, the existence of a feeder line may affect the number of customers and the profitability of the company that owns or operates the main line.

This interdependence may be accounted for in several ways in Schmid's view. The main line firm might offer the feeder firm a payment to help it to stay in business. The external effect would in this case be internalized by market bargaining. Another possibility is an expansion of the size of the firm to include both segments of its interconnected route. It is possible that the integrated firm

will suffer losses on certain portions of its system, but the existence of the feeder routes may still contribute to overall profitability. If the contractual costs or internal information costs were not too high, the selection of either alternative would cover the entire route. However, there is an interdependence between customers which raises the distributive issues so often emphasized by institutionalists from the OIE tradition. Schmid clearly made an institutional individualist analysis. He said that if a person rides the whole route he will pay for its total cost regardless of how the portions are priced. But some riders may only ride the feeder route and some only the main route. The feeder-route riders get a reduced-cost ride compared with the marginal cost of that portion of the route. The integrated firm might charge a flat price per mile regardless of the portion of the route used. Customers would be treated as one large group, to the advantage of those riding the higher-cost feeder routes exclusively. The firm, in arriving at its profit-maximizing pricing scheme, does not care about someone getting a reduced-cost ride. It might not profit the firm to try to charge more for the feeder route and lose customers on the whole system.

The possibility of contracting or creating a single firm may make the maintenance of the whole system possible, but it does not address the question of how different portions of the system are of interest to different groups. If each separate product "should stand on its own feet", that is, each portion should cover its own marginal cost, then the person who rides only the main line would have his fare reduced if he did not have to help pay for the feeder line. What Schmid's institutional individualist analysis shows is that there are several options which all affect different groups of people in different ways. The institutional structure of the market affects its profitability and affects who gets what. Besides individual action (rule 1 of Institutional Individualism), this institutional structure must be taken into account if a relevant institutional individualist analysis is to be made (rule 2 of Institutional Individualism).

What is true for market boundaries is also true for political boundaries, as the famous Lake Michigan national park case shows. According to rule 2 of Institutional Individualism, making institutional individualist analyses of political behavior means considering the relevant formal rules and informal norms that affect the participants in every collective decision making process as explanatory variables. That is what Schmid did in order to explain why a political representative acted differently on the same political issue depending on which group of constituents he was representing. The issue arose in connection with a proposal to create a type of national park on a peninsula in Lake Michigan. Many of the local people near the proposed park opposed it because they feared congestion and loss of private ownership of individual cottage sites. The U.S. Congress representative from this district reflected this dominant interest and opposed the park. Later, when he became a U.S. senator for Michigan, he supported the park. The dominant interest in a state-wide vote was the people of Detroit, who wanted a public recreation area away from the busy city. It is also interesting to note that the park was originally proposed by a senator from the neighboring state of Illinois, where the largest city was within easy driving distance of the park.

The Michigan Congressman and, later, Senator was democratically elected, but he changed his mind when the electoral boundary changed the character of the majority. It seems that power to the people does not acquire its full meaning until we inquire: which people? If the people in the vicinity of the park had the right to make the decision, Schmid writes, they would have furthered their interests at the expense of lost opportunities for more distant people. The reverse is also true. The establishment of the federal park created costs for the local people for which they received no compensation. If the right to decide had been assigned to the local people, a compensation payment could have been designed or a market for negotiation could have been established, with representatives from both parties, in order to reach an agreement on such a compensation payment. There must be no doubt that Schmid (1987, 2nd ed.) conducts an institutional individualist analysis in which distribution conflicts and power influences are also taken into account, as is usual in the OIE tradition.[30] Recently, Schmid (2004: 257) has explicitly stated, concerning his analysis of institutional change in Chapter 13, that "It employs three principles that Toboso (2001: 773–774) calls Institutional Individualism". This indicates that we both agree on how these analyses are built from a methodological point of view,[31] but some other colleagues may not.[32]

What about an example dealing with institutional reform issues? An excellent one is the classic article by W.J. Samuels (1981a) that contains an analysis of the Miller and Shoene Virginia Court case. Of course, what has been said of Schmid's book must be mentioned again: taking the said paper as an example does not imply that all Samuels' works are built on the requirements of Institutional Individualism. In fact, they are not.[33] Briefly, and attempting also to accurately summarize what Samuels exactly wrote, the Miller and Shoene' Virginia Court case was a case which involved red cedar and apple trees and their respective owners concerning a plant disease that developed in two different phases. In the first phase the fungus lived on the ornamental red cedar tree without any adverse effect on it. During the second phase it could severely damage the apple trees that were sufficiently near, causing complete destruction of the fruit and leaves.

In 1914, the legislature of the state of Virginia passed a statute which empowered the state entomologist to investigate and, if necessary, condemn and destroy without compensation any cedar tree that had the fungus within a two-mile radius of an apple orchard. This was an institutional reform that changed the legal rules governing the red cedar and apple trees conflict. Warren Samuels gave an institutional individualist explanation of the consequences of these two different institutional frameworks for the income and wealth of conflicting parties. He also made an institutional individualist analysis of the process leading to such a change, as well as of the reaction by cedar tree owners who, unsuccessfully, first brought a suit in the state courts and then sued to reverse the unfavorable decision of the Supreme Court of Appeal of Virginia.

The thrust of the cedar tree owners' argument as a whole was that the statute was an unconstitutional exercise of police power by virtue of its violation of the due process clause of the Fourteenth Amendment. However, the Supreme Court affirmed the judgment of the lower state courts, denying the challenge to the statute on the grounds of unconstitutionality. The legislature was under the necessity of making a choice between the preservation of one class of property and that of the other wherever both existed in dangerous proximity. It would have been none the less a choice if, instead of enacting the new statute, the legislature, by doing nothing, had permitted serious injury to the apple orchards within its borders to go unchecked. When forced to make such a choice the legislature does not exceed its constitutional powers by deciding upon the destruction of one class of property in order to save another.

The new statute altered the effective assignment of rights upon which market transaction might be made. It was of course possible to allow for private agreement among conflicting parties, but the result of such a negotiation process would have been different depending on the legal framework in place. Without the new statute, only by paying the red cedar owners for cutting down the affected trees might the apple owners avoid damage if the fungus were to reach them. With the new statute in place, it is the red cedar owners who are forced to offer a compensation payment to the apple trees owners if they want to avoid cutting down their red cedar trees when the fungus appears. Market forces emerge and take on shape and direction only within legal frameworks. Since, Samuels writes, relatively effective rights are a partial function of law, the bargaining strength or power, the distribution of the relative risk, the level of business costs, resource allocation, income distribution, etc., are law dependent variables.

The apple and cedar trees court case also shows how the relevant issue is not whether the government has to intervene or not but who will influence government decisions. Apple orchards were a major *industry* in Virginia. Red cedar trees were of primarily ornamental use, with some little use and value as lumber. The apple owners were organized and influential whereas the red cedar owners were not. The case also shows how marginal institutional changes, that is, changes in specific legal rules and social norms, always result from processes of human interaction that take place in specific situations in which certain other legal rules and social norms remain unchanged (rule 3 of Institutional Individualism).

Of course, several other examples could have been mentioned. M. Rutherford (1983, 1984, 1987, 1989), for example, has persistently searched the old institutionalist pioneers' contributions, by Commons, Veblen, Mitchell, etc., to find these institutional individualist explanations wherever they might be found and whatever the significance or weight that is attributed to them in those contributions. V. Vanberg (1989) has given a presentation of some central ideas contained in Commons' *Economics of Collective Action* where the arguments and explanations are of a non-reductionist individualist type rather than holist. Biddle (1990) and Ramstad (1987, 1989, 1991) also emphasized the analyses by Commons in which human action appears to function as an explanatory variable, whatever the degree of discretion attributed to it. The book by R. Bartlett (1989)

is another excellent example in which the concept of *mutual power influences* among persons and groups of persons is included in his institutional individualist models.

Finally, let me just mention some books and articles that cannot be easily classified into the OIE or NIE camp but that are also examples of institutional individualist analyses in which distributive issues and non-voluntary influences are systematically accounted for when considered relevant for the research purpose at hand, together with many others aspects, of course. Barthan (2004) and Knight (1992) are the books. Greif (2005) and Kruse (2005) are the articles.[34] It must be clear by now that it is possible to conduct analyses that retain many of the conceptualizations, assumptions and criteria frequently found in the OIE camp but are built upon Institutional Individualism rather than methodological holism.

Some examples of institutional individualist analyses from the NIE camp

Turning now to the new institutionalist camp, some examples of analyses that conform to the three rules of Institutional Individualism can also be mentioned. This fact as previously said does not mean that a kind of explanatory or prescriptive convergence between the OIE and NIE perspectives is being reached. No statement in favor of such a convergence is made in this paper, though several authors such as Rutherford (1995), Groenewegen *et al.* (1995), Vandenberg (2005) or Zouboulakis (2005) ask themselves whether some bridges can be built. Again, no attempt is made here to answer any question about the comparative degree of empirical truth or falsity of different economic explanations.

Although the number of examples has grown recently, let me start by pointing out some of the latter works by D.C. North in the *political economy* oriented branch of NIE, as compared to the *industrial organization* one. By the late 1980s, North had already written:

> The major focus of the literature on institutions and transaction costs has been on institutions as efficient solutions to problems of organization in a competitive framework – Williamson, O.E. (1975), (1985) ... Valuable as this work has been, it leaves out the most important contribution which institutional analysis can make to economics ... The formal economic constraints, property rights, are specified and enforced by political institutions and the literature that characterize modern industrial organization takes these as given. What we must do is to explore political institutions as well as economic institutions.
>
> (North, 1989: 240)

As already mentioned, not all North publications are built on exactly the same methodological principles.[35] It seems evident to me that in North (1990, 1988, 1991a, 1991b, 1993, 1995, 2005a, 2005b), for example, he abandons the

efficiency view that characterized *some* of his previous explanatory analyses. He also abandons his previous purpose of explaining all institutional changes in terms of self-interested human actions responding mainly to changes in prices, technologies and other material conditions (natural, technological, monetary, and the like). Furthermore, he also provides preliminary answers to the question of what explanatory role mental models and ideologies may play in explaining changes in formal institutional structures. His concern with cultural inertia and path-dependence should not be surprising given that North is an economic historian. In North (1990), he dedicated a full chapter to emphasizing a number of basic behavioral assumptions by which his theory departed from the standard neoclassical theory. In North (2005) he states that

> in contrast to standard (neoclassical) theory that draws its inspiration from physics, modeling the process of change must derive its inspiration from evolutionary biology. But in contrast to Darwinian theory in which the selection mechanisms are not informed by beliefs about the eventual consequences, human evolution is guided by the perceptions of the players in which choices – decisions – are made ... in pursuit of their goals.
>
> (2005: 21)

According to North, a main source of contrasting economic performance between societies lies within the institutional structures that define incentives for saving, investment, production and trade and that also influence production and transaction costs. Because in standard neoclassical analyses zero transaction costs are usually assumed and many, if not all, institutional factors are removed, these analyses are of little help to North for the said task of explaining the source of contrasting economic performance. Although North's analyses in the said papers and books may be characterized as (new) institutional analyses, in the sense that he pays attention to the formal and informal institutional structures that influence the situation under investigation, his analyses are nonetheless of an individualist kind in the sense that individual action remains essential for his explanations (rules 1 and 2 of Institutional Individualism). As is obvious, and North (1990) stresses, we all can act alone with no explicit coordinated plan with others, or in groups (organizations and teams) through the informal or formal arrangements created for collective action. People acting in a coordinated way through organizations always try to profit from the existing broader institutional environment but also to lobby, some groups or organizations more than others of course, in order to obtain a more favorable one. Individual perceptions, much influenced by their mental models and ideologies, are also an essential part of the indicated North's analysis. Formal institutions such as constitutions and other legal rules must be reformed through political decisions, while efficient changes in those institutions are not guaranteed by political competition. Efficient changes are sometimes promoted and sometimes blocked in the political arena. Sometimes, North writes, they are blocked for centuries, as the case of the medieval manor institution shows.

North's research efforts are often mainly directed to evaluate the degree of efficiency characterizing alternative institutional settings in different periods of history, or to explain why the total output grew much more in some countries that in others. Little attention is usually paid to the distributional impacts those frameworks produce, or to how distributive conflicts among relevant participants may influence the institutional reform that is agreed or voted on. But what is relevant for my task in the present paper is that in the said contributions North does not conduct a methodological individualist analysis in which only preferences and material conditions (natural, technological, monetary and the like) are taken into account as explanatory variables in order to achieve the reductionist claim usually associated with MI. Much to the contrary, he adopts an institutional individualist mode of explanation similar to the one previously outlined.

Little attention to distributive issues and power influences does not mean a complete disregard of it. When a detailed (new) institutional historical analysis is made by North some non-voluntary inter-relationships are sometimes emphasized. In North (2005: 112), for example, he points out the "violent struggle among competing groups for control of the polity and economy" that took place in all new Latin American republics created after the defeat of Spanish armies and the independence movements. Even if many adapted a version of the United States Constitution as a model for independence, the consequences were radically different, he says, because of the colonial heritage they suffered from. The entire pattern of settlement, trade, and development was geared to the extraction of precious metals for the Spanish Crown. Through an authoritarian system not based on self-government, the Crown, North says, granted exclusive monopoly privileges to selected merchants, and trade was confined to a small number of ports in the whole of South America. The evident and well documented purpose was to facilitate the extraction and sending of precious metals to Spain, not to promote the development of people living there.

Without a heritage of democratic self-government with well-defined and enforced political and market rules, and a legitimated distribution of property and economic assets, independence disintegrated in a violent battle between groups for capturing the polity for controlling economic transactions. Those groups that emerged victorious established authoritarian regimes to secure order and the phenomenon of "caudillismo" became pervasive, North says. But new conflicts appeared with those who had inherited rights from the royal regime as they were in fundamental conflict with the interests of the new governing elites and their supporters. Huge land grants had been given to wealthy individuals as well as to the church elites. A series of local monopolies in production and trade had also been authorized to be managed by some family groups. The result was, and still is, continuous political instability, extensive rent-seeking behavior at expense of productive activities, adverse income distribution, a really poor provision of public goods, and a huge number of people suffering from an extreme poverty situation. North concludes that the endowment arguments for explaining growth and development must be fundamentally supplemented by the powerful

consequences the path dependent colonial heritage have on both informal and formal institutional arrangements.

All these arguments are, of course, debatable. However they reveal that some of the institutional individualist analyses by North also contain references to distributive issues, conflict of interests, and groups of people with diverging capacities to influence the rules of the political and economic games being played, setting aside their differences as players under the existing rules. In North (2005: 165) he writes: "As noted above, alteration of the economic rules entails winners and losers and it is essential to be aware of them...". In 1990, North had already explicitly stated: "Institutions are not necessarily or even usually created to be socially efficient, rather they, or at least the formal rules, are created to serve the interests of those with the bargaining power to devise new rules"[36] (1990: 16).

In fact, though most authors often concentrate on revealing how formal and informal institutional structures affect transaction costs and the total output achieved by participants, more and more attention is being paid to distributive issues. This is particularly so in the political economy branch of NIE. If team action is considered, now it is also stressed by several self-labeled new institutionalists that arrangements used for organizing team action also influence the share in the efforts and costs needed to accomplish the common purpose as well as the share in the total output achieved. As several existing alternatives for reducing production and transaction costs will expectedly produce different distributional impacts on the affected participants, proposals for organizational reform are always a source of some dispute. In the polity this often causes conflict ending not in a general agreement but in a final vote with winners and losers, as Libecap (1993: 32) wrote. In NIE camp, several analyses containing explanations of why some groups of people oppose to a specific market institutional reform even when it is a generalized perception that total transaction costs could be reduced as a result can also be found.[37] In a similar sense, Horn states that due to the fact that

> enacting legislators' commitments, as well as the benefits provided to their constituents, are uncertain when subsequent legislatures come, they may have an incentive to protect those benefits by even attempting to implement inefficient institutional arrangements that increase the transaction costs of reversing those policies.
>
> (Horn, 1995: 16)

Let me just end these comments by referring to Eggertsson, who explicitly commented on this aspect when he stated that the NIE perspective

> also provides an opportunity for explaining the institutional arrangements than affect the relative power of workers and employers, and exploring how these power relationships emerged and how they are maintained ... The framework does not suggest that all institutional change is explicitly designed to increase aggregate wealth as many critics seem to believe.

> Purposive institutional change reflects both the power and interests of those who control institutional change and the process for making decisions in the political sphere.
>
> (Eggertsson, 1996: 16)

Turning again to those more traditional analyses in which many NIE standard assumptions and criteria are combined with an institutional individualist mode of explanation, North and Weingast (1989), Weingast and Marshall (1988), and Kiewiet and McCubbins (1989) could also be mentioned as examples. In Weingast (1989), for example, he examined the workings of the legislative committee system of the USA Congress. He attempted to show that this system is significantly less plagued by problems of ex-post facto enforceability than a pure vote-trading system (logrolling or market for votes system). In so doing he performs an institutional individualist analysis that follows the three rules already mentioned, and at the same time, retains many of the conceptualizations, assumptions, etc. frequently found in NIE contributions.

Of course, Weingast was basically concerned with efficiency, as new institutionalists usually are. Is this system more efficient than the logrolling system in the sense that it generates lower transaction costs for legislators in their tasks of reaching agreements on the policy actions that are being implemented day after day? If the answer is yes, Weingast said, legislators who are seeking re-election from their constituents would have an interest in creating and maintaining the legislative committee system if they were faced with a choice between this and the traditional logrolling system. This is an example of the comparative static type of analysis so often adopted by new institutional economists over the 1970s and 1980s. The mechanism that links this reasonable outcome (more efficient rules in which legislators have an interest) to the process of human interaction that is necessary to achieve this outcome collectively must be indicated to avoid charges of non-intended but actual functionalism, as previously indicated. Weingast assumed that political competition for votes in legislators' constituencies was that mechanism. Legislators from different constituencies have considerable incentives to exchange support so as to provide benefits to their supporters. Because the value of today's legislative bargains depends on actions taken in future legislative sessions, legislators have incentives to devise institutions that provide today's bargaining with durability.

For Weingast, repeat play among legislators was not sufficient to prevent the breakdown of co-operation under certain circumstances. Legislative rules could not be considered as substitutes for the reputation building and the trigger strategies commonly used in repeat play. Rather, rules complement the use of these strategies and, in particular, prevent the breakdown of co-operation in precisely those circumstances under which these other strategies fail. It is obvious that this argument parallels that of vertical integration, in which reputation effects are also insufficient to police co-operation between firms' owners. In both cases, potential contractual problems lead to the design of institutions that substitute

for market exchange (vote trading in the legislative arena). In so doing participants improve ex-post facto enforceability of agreements in Weingast's opinion.

The diversity of interests among legislators creates gains from exchange within the legislature. But under a logrolling system, votes are usually *sold* and *bought* for a *price*, with the equilibrium prices determining vote trades and hence the set of bills passed. Legislators are better off, Weingast says, by giving away votes on issues that have lower marginal impact on their districts (and therefore on their electoral fortunes) in exchange for votes on issues having larger marginal impact. But what if bills that are going to come are not known in advance? Or what if future events modify the payoffs of bills already exchanged? Or what if a legislator changes his mind and his perceptions of an issue that was previously subject to exchange? In a pure exchange system or simple logrolling the time dimension cannot be fully taken into account, consequently the enforcement of agreements remains exogenous. It is unlikely that agreements will cover more than one legislative session. A variety of exchange problems arises because, as Weingast writes, the value of today's legislation significantly depends on next year's legislative events.

Even if no change in seats has occurred, members of future sessions may face different incentives from those faced when the trade occurred and may seek, for example, to amend, abolish, or simply ignore previous agreements. Moreover, these settings inhibit the ability of reputation to serve as the sole enforcement tool. Weingast first depicted a model of an idealized legislative committee system and then argued that evidence found in the USA Congress *was consistent*[38] with that model. In his model, legislative committees are composed of a number of seats, each held by an individual member who has a property right over his seat, based on the so-called "seniority system", that allows him to remain on the committee for as long as he chooses. Associated with each committee is a specific subset of policy issues over which it has jurisdiction, and therefore the monopoly right to bring alternatives to the status quo up for a vote before the legislature. Whenever a member leaves a committee his seat becomes vacant and is assigned to other congressmen through a bidding mechanism based on the preferences previously revealed by legislators and on the "seniority system" of those who placed it as first choice.

The control over the agenda within its jurisdiction implies that a committee has veto power over the proposals of others. Agenda power allows committees to bias the outcome in favor of the alternatives they prefer most. The agreements made among members of a committee or between members of different committees are simply enforced by the property rights over seats system already mentioned. A legislator on committee i gives up influence over the selection of proposals in the area of committee j in exchange for members of committee j's giving up their rights to influence proposals in the area i. Institutionalizing control over the design and selection of those proposals that will come to a vote substitutes for purchasing the votes of others in an explicit market. Since committees afford their members a disproportionate influence over the policy choice within their jurisdiction, representatives from farm districts, for example, are

much more likely to bid for seats on agriculture committees than they are for seats on urban, housing, or merchant marine committees. The more competition for seats, the less likely the bid will be successful, however.

All these are the reasons why, in the USA Congress, representatives from farming districts usually dominate the agriculture committees and oversee programs that benefit farmers. Members from urban districts usually sit on the banking, housing, and welfare committees that provide benefits to an incredible array of urban constituents, etc. USA representatives opt for committees that are relevant to their constituents' interests and their doing so leads to committees composed of legislators with considerable support for policies within their jurisdictions. Weingast offered some figures showing how this support by committee members was indeed significantly above the mean for the entire Congress. Finally, the pattern of campaign donations by firms provides additional evidence, in Weingast's opinion, on the accuracy of his model in representing the basic working of the USA committee system. Because of their influential position, the probability that a committee member will receive a donation from a firm was at those years 0.34 times higher than that of a nonmember, according to the figures provided by Munger (1984).

As is usual among many new institutionalists, in this article Weingast makes a comparative institutional analysis mainly focusing on organizational aspects and their impacts on transaction costs and efficiency. Several comments are made, however, on how different rules attribute differential capacities to act, to control the agenda or to veto participants. The legislative committee system of the USA Congress seems, to Weingast, more efficient than a pure vote trading system (standard logrolling) in the sense that it generates fewer transaction costs for participants since it is significantly less plagued by problems of ex-post facto enforceability.[39] For the purpose of the present chapter, it is not relevant whether this is true or not, or whether different accounts might emphasize aspects that Weingast disregarded. What must be clear now is that Weingast and North, as well as others, have conducted analyses of organizational issues and institutional changes that are in accordance with the rules of Institutional Individualism, as a mode of explanation, and are also based on the rest of the assumptions, conceptualizations and criteria usually adopted by self-labeled new institutional economists. The above examples are analyses that do not follow the reductionist claim usually associated with methodological individualism.

Although this is not the place to carry out a survey, some other examples from the NIE camp could be mentioned. In fact, my impression is that a turning point took place over the 1980s once the international seminar series on the New Institutional Economics began in 1983 and these debates were published in the Journal of Institutional and Theoretical Economics.[40] In 1997, when the International Society for the New Institutional Economics (ISNIE) was launched, a long way had already been traveled by those hundreds of scholars from economics, political science, history, organization and public administration studies, etc. who participated in the inaugural ISNIE meeting. Ronald Coase and Douglass North had already received the Nobel Prize award, which helped to attract

more scholars with different intellectual backgrounds.[41] Since 1997, it seems to me that the NIE approach is being made wider and wider, as the papers presented at ISNIE meetings indicate, and the ISNIE website explicitly stresses.[42] In North (2005a), Ménard (2000) and (2004a), Ménard and Shirley (2005), Eggertsson (2005), and Toboso and Arias (2006), for example, many analyses are now being built on a much more comprehensive approach, as Furubotn (1993: 8) was able to envisage in the early 1990s, as previously indicated.

And it has turned to be so in the two main branches of NIE: the one dealing with political economy issues and that addressing industrial organization issues. Although my previously declared purpose was to focus on examples from the first strand, some brief comments on the latter may complement the paper. In this sense, Williamson (2003: 921) has recently stressed that, in contrast to the neoclassical resource allocation approach in economics, what NIE represents is a move from the orthodox lenses of choice optimization under physical, monetary and technological constraints to the lenses of contract by which organization issues become salient and governance structures can be approached. Governance structures at the firm level may serve as coordinating devices, no matter how efforts-costs and results are shared, in part, as a result of the formal and informal contractual arrangements implemented. Again, Williamson and others in the industrial organization branch of NIE often focus on transition costs and the degree of efficiency of alternative institutional arrangements. Similarly, inter-firm coordination arrangements such as those examined by Williamson and Ménard are usually implemented because firm's owners think that they will be beneficial in comparison to the feasible alternatives each of them confronts. Mutually beneficial under the circumstances does not mean equally beneficial. The way efforts and results are shared is always an issue that has to be negotiated to some extent among partners, and sometimes the controversy so generated creates problems to finally reach the required coordination agreements, or breaks them when new circumstances emerge.

Again, the "lenses of contract" and related conceptualizations often used by the NIE researchers for approaching organizational issues at the firm or industrial level very much influence the explanatory *pictures* they build. But the same is true for those other *pictures* on similar organizational issues many OIE scholars build on the "lenses of power" and related conceptualizations. As indicated, my purpose here is not to make any qualitative judgment on which analyses are more relevant for explaining some issues in specific circumstances, nor to perform any comparative empirical test. My point is, again, that even in the industrial organization branch of NIE, more and more analyses are being published since the mid-1990s which are not of a reductionist kind. Williamson (1991, 1993, 1996, 2003) and Ménard (1996abc, 2004b and 2006) are examples containing institutional individualist analyses while retaining many other conceptualizations and assumptions often associated with NIE analyses. Besides many other organizational details influencing the economic transactions under analysis, these authors often take into account relevant aspects from the general formal and informal institutional environment in which people through firms

(with different hierarchical capacities and responsibilities) as well as through other hybrid organizational forms operate.

Traditional firms and other hybrid modes of governance such as cooperatives, subcontracting, supply-chain systems, distribution networks, franchising, partnerships, alliances, etc., are all institutional structures for organizing production and distribution. These authors often attempt to reveal how these arrangements affect transaction costs and the total output reached by participants, and little attention is usually paid to distributive issues and conflicts associated with alternative contractual specifications. Again, little attention does not here mean no attention at all. Williamson and Ménard sometimes refer to control aspects, conflict relationships, safeguards, penalties, hierarchical relationships, discretionary commands and even discretionary power.[43] Concepts such as transaction costs, opportunism, assets specificity, human assets, adverse selection, moral hazard, contractual safeguards, surrounding uncertainty, monitoring costs, incentives to collude, enforcement mechanisms, asymmetric information, strategic behavior, bounded rationality, credible commitments, and modes of governance are now much used in the said and similarly oriented analyses when considered relevant for the research task at hand, even if some concepts abound more in some research areas than in others. As it was the case with the examples mentioned in the previous section, it must also be evident that it is possible to conduct analyses that retain many of the conceptualizations, assumptions and criteria frequently found in the NIE camp but are built upon Institutional Individualism rather than methodological individualism.

Final remarks

The arguments and citations of the present chapter reveal that economic researchers do not necessarily have to build their explanatory analyses on the two traditional modes of explanation already mentioned. A middle way alternative exists which allows for taking into account many and diverse aspects depending on the situation investigated and the research purpose at hand. Individual agency and social structure can then be combined in a way that assigns analytical primacy to both of them, not to one or the other as is usually done in reductionist and holist economic explanations. As questions about the empirical truth or falsity of alternative analyses have been explicitly excluded from consideration, obviously my purpose here has been, rather, to show that a new alternative exits than to argue against methodological individualism or methodological holism as modes of explanation. Some explanatory analyses built on the three rules of Institutional Individualism *might* be more inaccurate or irrelevant than some competing explanations built on these alternative modes. Why not?

The articles and books here examined show that the *pictures* of reality transmitted through these new institutional individualist analyses are not exactly the same as those others offered in the more traditional contributions. As previously stressed, these *images* are all theory laden to some extent due to the

analytical categories, assumptions, rules and criteria that the researchers use for constructing their neoclassical, marxian, new institutional, etc. analyses (or even some hybrid ones). Though epistemological issues have not been addressed in the chapter, I want to end it by emphasizing that these explanatory *images* are also influenced by the specific and differentiated procedures each group of researchers follow, if any, in order to *test* and refine their analyses. These procedures also influence research results. Of course, some explanatory analyses may be more biased than others and therefore have less explanatory relevance. But, which are they? We will never know because this is a complex issue to be collectively determined and no general agreement is expected to occur. Whatever the natural scientists say about explanations of viruses, infections and the like, disagreement in the social sciences does not necessarily mean bad research performance if aims or interests differ. And interests often differ, both the interests of the agents being studied and those of the researchers. New criteria are also needed, of course, when the task requires making assessments and policy or institutional reform recommendations, no matter whether this is done for free, as many scholars do as a part of their research duties, or for those who pay for an economic advice in order to better pursue their purposes, whatever they are. In the so-called social sciences, including economics, these are basic aspects characterizing research tasks. Biologists also have interests, as do the owners of pharmaceutical corporations, but viruses do not. Viruses may also be brought to the laboratory for repeated experimentation as they often perform the same way, just like rats. How could research on people's economic affairs be evaluated in the same way as research on virus infections?

Moreover, things concerning economic research are even more complicated because many economic articles, books and reports are being elaborated by authors who explicitly do not even try to play the *scientific game* of trying to find the most relevant explanation for the human affairs under analysis. In no part of this chapter have I said that they should do so. If economic transactions are always very much influenced by participants' expectations of future personal gains, then it seems straightforward that relevant participants will be interested in getting useful reports to advance their purposes in specific circumstances rather than just *true* reports. And so will their advisers, as well as similarly committed scholars. This applies to both scholars sympathetic to union leaders' bargaining strategies and scholars writing reports on alternative ways to reduce those transaction costs suffered by, for example, some cooperating entrepreneurs wanting to coordinate their strategies against competitors. Many other examples could be mentioned.

If economic theories and reports must be relevant, instructive and useful from the point of view of different participants in markets, governments, firms, etc., it seems difficult that all analyses can be built on an identical ex ante *methodological jacket* when their aims, interests or views differ. Accounting for relevant and useful particularities and revealing how different interests count in each situation, or how each could be differentially affected by a suggested reform,

requires, of course, a methodologically consistent approach or research program formed by a set of basic *hard core* conceptualizations, principles, and criteria, together with a varied and wide set of *protective belt* concepts to choose from depending on the situation under investigation at the research task at hand. But if views, aims or interests differ, as is often the case, differentiated research programs will always emerge in the social sciences, particularly in the realm of economic studies. Concerning people's economic affairs, too much unanimity on the part of the specialists may be suspicious. That is why the spirit of the present chapter is at odds with technocratic or (natural) scientist stances in economic research.

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Notes

1 This is evident, and no citation is needed, if we consider that methodological individualism (and the often associated claim for reductionism) constitutes an explicit methodological foundation for many traditional neoclassical articles, books and handbooks. The principles, rules and presumptions associated with holism are much favored by many self-labeled heterodox economists.

2 Samuels (2004: XI) has recently stated that what Frank Knight told in a class in 1933–34 still applies to economics as a whole, and I agree. What Knight, more than 70 years ago, said is: "There is no established economic usage for anything in economics." Davis (2006) refers to the growth being registered in the number of non-mainstream publications in economics that add more diversity.

3 Already in 1991, even the mathematician Debreu (1991) expressed similar concerns. In Blaug (1998), Stigler (1988), Buchanan (2001), and Coase (1974, 1982, 1992) similar statements can also be found. Recently, the legendary Kurt W. Rothschild (2006) also complains about this.

4 Examples of these debates are the collections of papers on methodological and epistemological issues published in Krimmerman, E. (1969), Brodbeck, M. (1968), O'Neill, J. (1973), and Lakatos, I. and Musgrave, A. (1968). And also Harsanyi, J.C. (1969), Machlup (1961), Blaug (1975), Popper (1968) Lakatos (1978), Katouzian (1980), Feyerabend (1975), McCloskey (1985), to mention but a few. No doubt a year on leave from teaching that I enjoyed in 1988 for completing my PhD Dissertation helped me very much to look deeply into these debates, as did also comments by Viktor Vanberg who was the Public Choice Center visitors program coordinator.

5 For those who might like to go into these confrontations, some contributions covering many aspects are: Bush (1981a, 1981b), and Seckler (1980, 1981), Hutchison (1984), Langlois (1986), Bush, P.D. (1991), Ramstad, Y. (1989), Gruchy, A. (1989, 1990), Whalen, O. (1989), Tool, M.R. (1987), Samuels, W.J. (1988, 1989), and Hodgson (1985, 1986), Coase (1984), Dugger (1990, 1995), Gunnarsson (1991), Andersen and Bregn (1992), Rutherford (1995), Stanfield (1995), Medema (1995), Groenewegen and Vromen (1996), Boland (2001), McCloskey (1990, 1993 and 1994), Hausman (1998 and 2001), Backhouse (1997), Parsons (1997), Mäki (1993a), 1993b and 1998), Wang (2003), and Howard and King (2001).

6 Similar statements can be found in Rutherford (1994: 27) and Mäki (1993: 26). See also the recent paper by Hodgson (2007). This is not surprising when an on-going debate also exist between philosophers and sociologists of science. See a recently written passage by Boland (2003) related to the Popperian situational analysis I will assess later: "Clearly, the Popper outlined in the LScD is neither the Popper promoted by Blaug (following Lakatos), nor the one suggested by Friedman.... Almost without exception today if you dare mention Popper's name in a philosophy seminar the reaction will almost always be 'oh, you mean Karl Popper the falsificationist' – they will rarely recognize 'Popper the critical rationalists'".

7 See for example, Klein (1993), Bush (1981a, 1981b and 1993), Hodgson (1993a and 1998). Some connections between OIE holist approach and Durkhemian positive economics were shown in Gislain and Steiner (1999). Boyland and O'Gorman (1995, 1997 and 2006) refer to causal holism.

8 For a deeper examination of the mode of analysis characterizing holist OIE contributions see Ramstad, Y. (1989), Wilber C.K., Harrison R.S. (1978), and Langlois, R. (1989). See also Danto, A.C. (1973), Hempel, C.G. (1968), and Harsanyi, J.C. (1969), and Cohen, G.A. (1982).

9 See Mäki (1993a: 27). See also Boyland and O'Gorman (1995, 1997 and 2006).

10 Rutherford (1983), Whalen (1989), Biddle (1990), Ramstad (1987), Vanberg (1989) and others refer to those contributions on the so-called "*Commons tradition*" that are less holist.

11 See, for example, Hogdson (1985, 1993a, 1993c, 1993d and 1998) who always refers to Veblen works.

12 See the classical presentations and debates contained in Brodbeck (1954) and Watkins (1969a, 1969b and 1969c).

13 For critical assessments of these analyses based on the *neoclassical optimization assumption*, see the contributions by such diverse authors as Schmid (1987, chapter 1), Buchanan (1975), Toboso (1993), and Williamson (2003). Game theory conceptualizations and mathematical tools are being increasingly used as I am going to comment next.

14 Becker (1976, 1981 and 1993).

15 This added also some controversy as standard game theory models contain some rules and conventions among the explanatory variables that influence the behavior of players through the payoff structure of games. Riis and Vislie (1995) contains a didactic but comprehensive non-mathematical presentation of main game theory conceptualizations and types of games. Vega-Redondo (1993), and (1998) contain sophisticated game theory models that use a kind of evolutionary mathematics which incorporates several institutional variables. Schotter (1983) is also a classic statement endorsing an institutional approach based on game theory conceptualizations and tools. As more and more rules, conventions and interdependencies are introduced in the models as explanatory variables the analyses depart from the reductionist claim of methodological individualism and get closer and closer to the requirements derived from the three rules of Institutional Individualism that I am going to examine next.

16 See, for example, Davis and North (1971), North and Thomas (1973), Hayami and Kikuchi (1981), Sudgen (1989) Axelrod (1984), (1986), Schotter (1981), Vanberg, V. (1988a), (1988b), Ault, R.W. and Ekelund, R.B. (1988), Furubotn (1989), and Witt (1989).

17 That is what Dugger (1983) emphasized even in his paper's title.
18 See Basu, R. *et al.* (1987), and Binger, B.R. and Hoffman, E. (1989). For a further and more critical examination of these "efficiency view explanations" see Dugger, W.M. (1983, 1990), and Schmid, A.A. (1987, chapter 11).
19 Surprisingly to me, as Boland embarked over the 1980s and 1990s in big-M methodological debates, Boland (2001) advocates a practical approach to methodological and epistemological issues when he emphasizes that small-m methodologists asking practical questions can be more useful for economists studying real economic cases. Debates by small-m methodologists concerning the way those economists build their models and attempt, or not, to test them might be more interesting for economic researchers, he says.
20 See Boland (1998).
21 B. Caldwell (1991), Hands (1992) and Mäki (1993a) are examples of such a presentation. See also Oakley (1999).
22 See Simon (1979).
23 See the coincident position held on the issue by such diverse authors as Blaug (1980: 71), Caldwell (1991: 14) and Langlois (1989: 278), Langlois and Csontos (1993: 122) and Rutherford (1989: 304).
24 However, in a much earlier article, Aggassi (1960) gave a preliminary, more ambiguous, presentation of Institutional Individualism that I will not consider here.
25 Of course, this is a central methodological issue that has created a never ending controversy since the very beginning when the seminal paper by Friedman in the 1960s was published. As previously indicated, I do not either intend in the present chapter to say that the analyses built on the rules of Institutional Individualism will be more accurate or "empirically" more relevant than those built on alternative modes of explanation. They may be so, or they may not. And, of course, no general agreement is likely to emerge, not even among those scholars with an institutionalist orientation. On the instrumentalism debate see, for example, Boland (2003, 2001, 1983, 1981 and 1979), and Caldwell (1983).
26 Though Rutherford (1994: 28–35) makes a similar characterization to that of Agassi (1975), he uses the definitions of methodological holism and methodological individualism contained in Agassi (1960) that are much less precise than those others contained in Agassi (1975).
27 As indicated in the introductory section, explanatory economic analyses are all theory-laden or methodologically biased to some extent. Those epistemological issues related to how researchers proceed to test their analyses, in case, are not addressed in the present chapter as explicitly mentioned. Those who try to perform these econometric tests still seem to do it in a pre-lakatosian naive way and also frequently speak about "corroboration" instead of "falsification" or "sophisticated falsification". Many other epistemological debates in social science research also seem to be disregarded. Whether this is done intentionally in some cases and unintentionally in others is a different issue.
28 It seems evident to me that participants in any democratic process aiming at collectively reforming an organizational setting always enter into political debate and persuasion and sometimes the preferences and mental models of some participants (or the way they apply them and the conclusions they reach) may be affected by such strategies. Hodgson (1985, 1986, 1989 and 1998) has insisted on the limitations of those rational choice analyses that assume fixed/exogenous preferences for explaining these processes.
29 I received this charge from an anonymous referee of my Toboso (2001) paper. I will say more on another referee later on.
30 See also Schmid and Sorokob (1997).
31 It could not be otherwise as I very much enjoyed finding Schmid's book (a book from the OIE traditions that did not contain holist explanations). I ordered it at the George Mason University book store in 1988 during my one year stay at the Public Choice Center for the purpose of completing my PhD Dissertation on "The Methodological Foundations of the Public Choice Research Program". In 1985 I had already worked on many holist OIE contributions for making a thesis for my economics degree on the topic: "Power influences in market economies and the limitations of the neoclassical research program."

32 This was the case concerning another referee for my Toboso (2001) paper. I keep his report in a safe place. He said:

> I doubt that Schmid and Samuels would agree that their work is not informed by holist explanation, even if it is not apparent in these Works ... From my familiarity with the writings of Schmid and Samuels I doubt either would say anything remarkably has been added to what they regard as intrinsic to OIE, other than the emphasis on Agassi.
>
> (Taboso, 2001)

33 Samuels (1981b) is a holist contribution on power influences that caused me some unrest 23 years ago. As student of Economics in my third year I had to participate in 1984 in a presentation of these really abstract and holist ideas to my fellow students. I still can visualize the moment and how uncomfortable I felt when both preparing and delivering the presentation. One year later, when completing a thesis for my economics degree on precisely those power influences that exist in market economies, I supplemented OIE explanations, mainly from JEI published papers, with final comments to some groups of actors and some causal mechanisms here and there. The director of my thesis, Juan A. Tomás, who had recently published a holist paper on related issues liked the extensions anyway.
34 See also Knight and North (1997), and Barthan (2000, 2001 and 2005). Barthan and Greif have participated in several collective books edited by Ménard under the title of "new institutional economics".
35 David and North (1971), North and Thomas (1973) are well-known examples of his more neoclassical approximation to economic change issues.
36 In the political economy branch of NIE, some other non-orthodox institutional individualist analyses containing references to conflict, distributive issues or power relationships are Libecap (1989 and 1993) Eggertsson (1995 and 1996), Horn (1995) and Greif (2005).
37 See Libecap (1989a and 1989b), Winiecky (1994, 1996 and 1998). Of course, those contributions mentioned in the last paragraph of the previous section could also be mentioned here as the said authors actively participate in the ISNIE conferences and NIE oriented collective books. These contributions are: Barthan (2000, 2001, 2004, 2005), Greif (2005), Knight (1992) and Knight and North (1997).
38 In fact, if attention is paid to the epistemological debates previously mentioned, it would be more appropriate for Weingast to say (and this is, I think, what he really wants to say) that the (to some extent) *theory-laden* evidence gathered does not seem *to refute* this particular model whereas alternative models are in fact refuted, in his opinion, by the same evidence. This is what I understand that Lakatos (1978) referred to by his situational and interpersonal *sophisticated* refutation procedures. However, Boland (1998: 1) speaks against the Lakatos's contribution saying that it (through Blaug presentations) misled many young methodologists over the 1980s concerning what Popper really wrote about these issues. Lakatos in fact differentiated between Popper 1, Popper 2, and a Popper 3, saying that the third one never came into being. But going into this will also divert me from achieving my purpose here.
39 Recently Caballero (2006) has made a comparative institutional analysis of the USA and the Spanish congresses showing that hierarchical relationships predominate in the mode of governance characterizing both the working of parliamentary groups in the Spanish congress and the working of the Spanish political parties. This is in part due

to the Spanish general constitutional rules and other pieces of legislation. On different types of hierarchical modes of governance see Ménard (1996a).

40 A list of participants and topics debated in these seminars can be seen at www.mpp-dg.mpg.de/oekinst.html.

41 Some very much cited, but not always well-understood, contributions by Coase are Coase, (1937, 1974, 1982, 1992). See also Toboso and Compés (2003).

42 At www.isnie.org it can be read:

> The New Institutional Economics (NIE) is an interdisciplinary enterprise combining economics, law, organization theory, political science, sociology and anthropology to understand the institutions of social, political and commercial life. It borrows liberally from various social-science disciplines, but its primary language is economics...

43 See Williamson (1996b, 1997). In Ménard (1997) he says:

> Forms of discretionary power. This capacity to command requires a formal status base on rights and rules defined at the level of the 'institutional environment' ... But the exercise of this discretionary power and the related modalities of control vary significantly from one organization to another.
>
> (1997: 36)

See also Ménard (2004b: 39–45).

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