



The Theory of Institutional Design by Robert E. Goodin

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Robert E. Goodin (Ed.), *The theory of institutional design*. New York: Cambridge University Press, 1996. x + 288 pages. \$49.95 (cloth).

This first offering in the series titled “Theories of Institutional Design” from Cambridge University Press, edited by Robert E. Goodin of the Australian National University, contains ten decidedly cross-disciplinary essays, each of interest in its own right and which together provide a valuable introduction to the institutional design literature. The following paragraphs are not a review of this book so much as a summary of the arguments and issues raised by each of the authors.

Robert Goodin’s introductory essay, “Institutions and Their Design,” is quite useful for several reasons, not the least of which is how well it sets the stage for the subsequent chapters. Goodin describes the variety of institutions on which the various chapters will focus and examines the difficulty of drawing lessons for institutional design from other disciplines. I especially benefitted from the thumbnail sketch of the history and status of “institutionalism” within history, economics, political science and sociology.

Phillip Pettit contributes “Institutional Design and Rational Choice.” His first tasks are to define what he means by rational choice and to defend its use in this context. He argues that rational choice means that individuals are self-interested but that self-interest includes both desires for economic gain and for social acceptance. Moreover, he suggests that rational individuals might behave in certain ways without having to weigh costs and benefits. For example, Pettit argues that a strict accounting of economic gains does not provide the full explanation for one choosing to help one’s parents. He suggests there are other motivations.

Pettit goes on to discuss institutional design that focuses on controlling deviant behavior versus design that strengthens and reinforces non-deviant behavior. Sanctions imposed on deviant behavior, he contends, may induce people who would otherwise not deviate to alter their behavior. For instance, when one hears of the tough new sanctions on slackers, the awareness of the benefits of slackness rises. Noncompliance becomes a viable option, and compliers begin to weigh the costs and benefits of compliance rather than comply simply out of habit. Pettit recognizes that his assertions are subject to empirical verification. However, he argues that the possibility that non-compliance might rise because of deviant-led institutional design should be enough to lead to rejection of that style of design.

Bruce Talbot Coram addresses the implications of theories of the second best for institutional design. Coram defines the second best problem as focusing on what to do when all the rules or conditions required for first best institutions cannot be obtained or do not exist. Note that what Coram defines as the first-best differs from the usual notion of first-best in economics, a point that he recognizes. His notion is that the first-best is the situation or outcome that designers of the institution would like to attain; it is a benchmark. The second-best is, therefore, the situation or outcome that is most like the goal.

Coram argues that thinking in these terms, one recognizes two possible errors that must be accounted for in the process of institutional design. First is the fallacy of continuity. This he likens to the mathematical notion of continuity of a function. Coram presents the Condorcet voting paradox as an example of when small changes in initial conditions within a given set of institutions might have large consequences for the outcomes. The second pitfall is the fallacy of stretchability. This Coram describes as the belief that small changes in the institutions will have only small consequences. Political conservatives, Coram says, often assume that small changes in institutions have small impacts on outcomes. He demonstrates using the well-known pirates game how small changes in the institutions may cause dramatic changes in outcomes. He also presents a real world example: what many saw as merely a technical change in the rules governing elections to the Australian Senate produced a dramatic shift in the power of small parties and independent senators and in the way the body conducted its business.

In "The Informal Logic of Institutional Design," John S. Dryzek argues that institutional designers must be aware of the manner in which "discourses" are influenced by the interventions. Dryzek defines a discourse as "a framework for apprehending the world embedded in language, enabling its adherents to put together diverse bits of sensory information into coherent wholes." In my view, this is infelicitous terminology. Paradigm, world-view, and system of beliefs, even "ideology," all connote "a framework for apprehending the world" and substitution of any one of them for "discourse" would make the paper a far easier read.

Making the paper easier to read is valuable, however, because I believe Dryzek's main point is especially important. If the world-view of the people who will live under the newly designed institutions is not amenable, or is hostile, to the paradigm implicit in the design, acceptance of the new institutions will be problematic or worse. Dryzek points to the failure of market type incentives to supplant "command and control" methods of environmental regulation. Use of the market simply contradicts the world view of most environmentalists and much of the general population for whom pollution is morally wrong. Market incentives can never replace direct regulation while

that world-view holds. The difficult transition to market economies in Eastern Europe is another case in point.

Claus Offe's essay, "Designing Institutions in East European Transitions," complements Dryzek's chapter. Offe discusses the tendency for institutional designers to imitate institutions from other times or places. He makes it clear that imitation is problematic if it is necessary to simultaneously undertake "efforts to 'reeducate' people so as to make them fit for their roles in the new institutions." To be successful, the people living under the new institutions must have a "congruent spirit" with the institutions. At the same time, designers play down their authorship of the new institutions preferring instead to give the sense that these institutions are the brainchild of some great statesman, classical thinker, or have simply evolved. To do otherwise is to make the population too aware of the tinkering, increasing the likelihood that the citizens demand still more adjustments and undermining trust in the institutions. Moreover, because the institutional changes will have lasting and significant impacts on the prospects of all individuals, it is doubtful that anyone can design the institutions in a completely impartial, disinterested manner. It may be, Offe suggests, that "the greatest damage one can inflict upon an institutional system is an attempted large-scale repair operation performed in public."

Russell Hardin writes about "Institutional Morality" and, specifically, "the problem of relating institutional to individual action." To make sense of "institutional morality" one must decompose institutional responsibility into individual responsibility and ultimately to causation. Can an individual be responsible if neither action nor inaction by that individual determines the choices or behavior of the organization? In a classic public goods type setting, Hardin poses the question of whether causation and responsibility can be ascribed to an individual French soldier who deserted Napoleon's army retreating from Russia. Had all the soldiers stayed at their posts, the outcome might have been different for France. Yet does the responsibility for the tragedy rest with the deserters?

Hardin stresses the fallacy of composition, the idea that responsibility for the actions of the institution can be apportioned to the constituents such that total responsibility is simply the sum of the individual responsibilities. The bottom line for Hardin is that "institutional morality is a design issue: Morality must be built in." Moreover, Hardin concludes that "the moral theory of institutions and of the behavior of institutional office holders must be derived from the purpose of the institutions." He does not say as much, but it is natural to infer that institutions must be designed with moral purposes if they are to be moral, though that is only a necessary not a sufficient condition.

David Luban's "The Publicity Principle" presents an informative and highly readable discussion of Kant's "transcendental formula of public law" that "all actions relating to the rights of other human beings are wrong if their maxim is incompatible with publicity." Luban's interpretation of this phrase might go as follows: If the government cannot trust the judgment of ordinary citizens to affirm a policy, that policy is probably bad government and unjust. The presence of the qualifying "probably" is very important. Luban recognizes that situations exist when full public disclosure regarding a policy may not be beneficial. (He suggests the announcement of the date of a currency devaluation or the removal of price controls.) He also cautions against the implicit tyranny of the majority (though he does not use that term) that might arise if "judgement of the ordinary citizens" is taken to mean some sort of plebiscite or other opinion polling. (The South African government's decision to end apartheid likely would have failed a plebiscite in which only whites were allowed to vote.)

In the end, Luban offers a defense of the "publicity principle" that rests on the nature of selection of individuals for the government. If the method can pick only "the Wise" who will act in the public's best interest, then adherence to the publicity principle is unwarranted. So, if the selection method can identify only the benevolent, omnipotent, philosopher king of old-style welfare economics for government service, then there is no cause to object if that person is able to hide things from us for our own good. However, if the process of choosing people to make policy selects individuals who have no more claim on intelligence, benevolence or infallibility than the rest of us, then the publicity principle stands as a useful guide for those in public service to follow while designing institutions or making policy.

Kenneth Shepsle writes about "Political Deals in Institutional Settings." Shepsle describes both formal and informal enforcement mechanisms as a forecast by one agent "of what the other party to a deal will do." Beliefs, then, "provide a forecast of the manner in which the deal will actually be implemented." Individuals acting within a government will use whatever discretion they have within the institutions to move policy in directions favorable to their constituents or, presumably, their own preferences. Knowledgeable individuals, Shepsle argues, will anticipate the real policy effects of this discretion. In the parliamentary system, this information influences the types of government that can be formed. Shepsle shows how imperfect enforcement and the beliefs about the nature of discretion will alter the feasible set of outcomes. "The short-circuiting of comparisons (between alternative policies) owing to discretion and the institutional deal-making technology may create equilibrium where none otherwise would have existed."

In "Self-inventing Institutions: Institutional Design and the U.K. Welfare

State”, Rudolf Klein recalls the manner in which redesign of British health care institutions proceeded from a conjunction of Thatcherite ideology and small political support for the complete privatization Mrs. Thatcher might have preferred. The outcome was the creation of “mimic markets” which Klein describes as competition grafted onto hierarchical organizational structures. Because these two forms are inconsistent with one another, the system is inherently unstable. However, Klein sees this instability as a good thing because it is the result of the institution redesigning itself in response to changes in its environment. Indeed, these environmental changes are often the result of actions taken by the health care system. The mimic markets, then, are able to assure that health care is available to all while at the same time effectively generating the information vital for efficient allocation of resources. At least this is the theory. Klein suggests that the system has been in place too short a time to fairly judge it. Klein also argues that this move toward self-designing institutions, accidentally hit upon in Britain, is making headway elsewhere. The impetus for self-designing institutions is strongest where hierarchical structures held most power, such as Britain and Sweden, but relatively less influential where government services were (are) provided in a more decentralized way, such as Germany and, one presumes, the United States.

Geoffrey Brennan contributes “Selection and the Currency of Reward.” The selection to which the title refers is the selection of individuals into particular activities or employments. Brennan argues that virtue is a resource, like any other, which individuals hold in varying degrees. Optimality requires that people with greater supplies of virtue be selected into those jobs where virtue produces the greatest social rewards. The currency of reward, that is, the form that compensation takes, may be used as a selection device to assure this optimality. In the case of academic positions, selection of candidates who are in it for the love of scholarship is valued over selection of those whose motives are predominantly pecuniary. Extending the point, Brennan suggests that for positions in the government it might be valuable to search for the appropriate “currency of reward” so as to induce people with the desired attributes to self-select into those activities. Interestingly, though on the job consumption is generally viewed as inefficient, this currency of reward argument is a defense of on the job consumption as an enhancement to efficiency. Brennan is quick to point out, however, that the beneficial selection effects of on the job consumption may not surpass the costs.

In sum, the essays in this book are informative and thought provoking. The authors, the editor and Cambridge University Press are to be commended for this effort. I look forward to the next installment in the series.

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