On fuzzy frontiers and fragmented foundations: Some reflections on the original and new institutional economics

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ABSTRACT

These reflections are prompted by the papers by Claude Ménard (2014) and Claude Ménard and Mary Shirley (2014). Their essays centre on the path-breaking contributions to the 'new institutional economics' (NIE) by Ronald Coase, Douglass North and Oliver Williamson. In response, while recognising their substantial achievements, it is pointed out that these three thinkers had contrasting views on key points. Furthermore, Ménard's and Shirley's three 'golden triangle' NIE concepts – transaction costs, property rights, and contracts – are themselves disputed. Once all this is acknowledged, differences of view appear within the NIE, raising interesting questions concerning its identity and boundaries, including its differences with the original institutionalism. There are sizeable overlaps between the two traditions. It is argued here that the NIE can learn from the original institutionalism, particularly when elaborating more dynamic analyses, and developing more nuanced, psychologically-grounded and empirically viable theories of human motivation.

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The stimulating papers by Claude Ménard and Mary Shirley (2014) and by Ménard (2014) provide an opportunity for assessing their claims that the 'new institutional economics' (NIE) as a 'movement' has made some major advances, and is making a significant impact on economics.[1] They rightly note its broad successes, and the award of four Nobel prizes since 1991 to 'new institutional economists'. Thanks to these achievements, institutions are back on the agenda of economics and other social sciences.

This special issue is on the future of institutional and evolutionary economics. The papers by Ménard and Shirley are confined to the NIE. One of the aims of this comment is to complement their contributions and bring the original institutional economics into the picture,

[1] I thank David Gindis, Richard Langlois, and Jan-Willem Stoelhorst for very helpful comments on earlier drafts of these reflections. It is submitted in the name of an individual, and represents neither the editorial policy of this journal nor necessarily the opinion of its other editors.

alongside the NIE. This comment is plea for a broader and more inclusive critical understanding of the contributions of institutional researchers of all types.

I must emphasise that this is not an attempt to undermine the genuine achievements of the NIE, or a move to promote the original institutionalism as an alternative. Instead, one of the most important arguments raised below is that the identities and boundaries of both the NIE and the original institutionalism are now unclear; there is a sizeable overlap between them. Hence this comment is not divisive: it is an appeal for mutual understanding of both traditions, recognising the merits of each, so that these may be jointly deployed in future enquiry.[2]

Ménard and Shirley (2014, p. 2) note that the NIE is a 'decentralized field of inquiry' and 'in some ways new institutional economics is still more of a movement than a field' with 'glaring gaps still to be filled'. Ménard (2014, pp. 1-2) in particular refers to 'black holes' in the 'Williamsonian' branch of the new institutional economics.

In response I wish to survey some of these gaps and add a further assessment of what has and has not been achieved, to consider major differences within the (even narrowly defined) NIE 'movement'. I also raise the question of how it defines itself, especially given the major rifts within its own intellectual core.

I acknowledge the important previous theoretical developments discussed in these two papers, including the path-breaking works of Ronald Coase, Douglass North and Oliver Williamson. Nevertheless, these three thinkers expressed contrasting views on key points. Furthermore, what is described as the 'golden triangle' of three core concepts – transaction costs, property rights, and contracts – is itself disputed and problematic. Once this is acknowledged, profound differences of view appear within the NIE, in turn raising questions of its identity and boundaries.

Once this question of the identity and boundaries of the NIE is raised, we are back to the related question of its core differences (if any) with the original institutionalism. Hence, as important background to this question of identity and limits, I later consider the frontiers of the original institutionalism. I argue that there are overlaps between parts of the NIE and the original institutionalism, and the NIE can learn in part from the original institutionalism, particularly when addressing some of the 'glaring gaps' within.

The next section discusses the alleged 'golden triangle' of core concepts. It is argued that they still lack clear and satisfactory definitions, and more work is needed on these central ideas. This is followed by a section discussing the differences between Coase, North and Williamson. Two further sections discuss the nature, boundaries and potential relevance today of the original institutionalism.

Assaying the 'golden triangle' within the NIE

I first turn to the accounts by Ménard and Shirley of key NIE contributors and core concepts. One of my aims will be to show – even with their relatively narrow definition of its scope and

[2] I have explored the limitations of the original institutionalism elsewhere, and outlined its internal contradictions and differences (Hodgson 2004). A possible feature distinguishing it from the NIE was its treatment of individual dispositions and preferences as endogenous (Hodgson 2000). But some work in the NIE now acknowledges endogenous preferences (Dequech 2002). North (1994) has long emphasised the dependence of individual attitudes on factors such as ideology.

mentors – there is huge diversity within this camp. I also appeal that more attention should be given to the tasks of conceptual and definitional clarity.

Ménard and Shirley focus on Coase, North and Williamson. This is understandable and acceptable, given their constraints, but what about other achievements by post-1970 institutional economists? The extensive and path-breaking work of Daron Acemoglu and his co-workers is quickly passed over as 'mainstream'. Other major but less-discussed names include Yoram Barzel, Harold Demsetz, Mancur Olson, Elinor Ostrom, Richard Posner and others. Of course, Ménard and Shirley could not review all this work adequately in the space provided. My point here is to show that if such names were included, then even more diversity would have to be acknowledged in the NIE.[3]

Ménard and Shirley (2014, p. 4) explained: 'Three key concepts – transaction costs, property rights and contracts – became the "golden triangle" of NIE. … These three concepts … encapsulate the central core of NIE and make its paradigm so distinctive.' In both their papers, they then go on to discuss these three concepts. But their accounts overlook several major problems.

Transaction costs

For example, the history of the transaction cost concept reveals considerable ambiguity over its meaning (Klaes 2000a, 2000b). Another critic, Stanley Fischer (1977, p. 322), observed:

> Transaction costs have a well-deserved bad name as a theoretical device, because solutions to problems involving transaction costs are often sensitive to the assumed form of the costs, and because there is a suspicion that almost anything can be rationalized by invoking suitably specified transaction costs.

Williamson (1985a, p. 1) defined a transaction as occurring 'when a good or service is transferred across a technologically separable interface.' This suggests that transaction costs emerge through the physical transfer of goods or services. Unlike John R. Commons (1924, 1934), Williamson makes no mention here of agreed, legal, contractual obligations, or transfers of legal rights. Controversies over the so-called Coase Theorem have further dramatized the need for clarification of the concept (Barzel 1985, Allen 1991, 2000).

While the intuitive notion that transacting activities involve intrinsic costs is unassailable, and the importance of this real-work fact has been established by Coase and others, definitional vagueness and terminological confusion endure. For example, Williamson (1985a, p. 19) wrote: 'Transaction costs are the economic equivalent of friction in a physical system.' But Douglas Allen (2014, p. 3) pointed out that 'defining a transaction cost as a simple friction that happens within an exchange is inadequate … and simply leads to an analysis not unlike a simple treatment of taxation.' Allen (2014, p. 3) added:

> Looking for a transaction cost definition in Coase's writings is futile on several grounds. First, and unfortunately, Coase did not fully understand the concept himself, and is often led astray in many of his arguments defending his work. Second, Coase simply never defined the term, and even years later only resorted to the use of examples.

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[3] In a classic collection of essays, Langlois (1986) included the work of 'evolutionary economists' Nelson and Winter (1982) within the NIE. But Nelson (1996) went so far as to write: I now 'understand fully that I am part of the old institutional economics'. Given the copious possible boundaries of both the original institutionalism and the NIE, it is possible to be in both camps (Dequech 2002). North is another possible example of dual occupation (Groenewegen et al. 1995).

Allen's (2014, p. 4) solution was to define them as follows: 'transaction costs are *the costs of establishing and maintaining economic property rights*.' This is a cue to move to another apex of the golden triangle.

But before moving on, it must be emphasized that problems of definition and measurement do not mean that a concept should be abandoned. The notion of transaction costs has brought major insights. Nevertheless, serious definitional and conceptual problems at the foundation require urgent attention. Otherwise further progress in transaction cost analysis may be impaired.

Property rights

Arriving at the concept of property rights, this is also highly problematic. Ménard and Shirley (2014, p. 5) wrote:

> As Coase (1959) explained what people really trade are rights, the rights to perform certain actions. The concept was further developed by Armen Alchian (1965), who defined property rights as a set of rights to take permissible actions to use, transfer, or otherwise exploit or enjoy the property.

What are these 'rights'? Coase (1959, p. 25) saw property rights as determined 'not by the forces of supply and demand but by the law of property … One of the purposes of the legal system is to establish that clear delimitation of rights on the basis of which the transfer and recombination of rights can take place through the market.' When this notion of property rights was 'further developed' by Alchian and others, it meant the progressive dilution and eventual removal of Coase's insistence that property essentially involves a legal system run by the state.

Alchian (1965) defined private property rights in terms of the assignment of the 'exclusive authority' and ability to choose the use of goods (without affecting the property of other persons). He mentioned the possible role of law alongside a greater stress on custom and convention. But rather than an institutional means to constitute or legitimate rights, law was treated as just one possible mechanism alongside others (such as custom and convention) to ensure that a *de facto* exclusive assignment remained in place. Furthermore, his definition was largely in terms of (constrained and assigned) *de facto* powers of control rather than legal or moral rights. Later Alchian (1977, p. 238) defined the 'property rights' of a person in universal, ahistorical, and institution-free terms including 'the probability that his decision about demarcated uses of the resource will determine the use.' Alchian's definitions of property neglect the essential concept of legitimated, rightful ownership. They denote possession rather than property.

Consequently, Ménard's and Shirley's (2014, p. 5) claim that Alchian's definitions are about 'rights to take permissible actions' fudges the meanings of 'rights' and 'permissable'. The *Oxford English Dictionary* defines 'right' (as a noun) as 'that which is morally correct, just, or honourable' or 'a moral or legal entitlement to have or do something'. Alchian and subsequent NIE scholars have removed morality from the picture and downgraded the role of law, from being the source of legitimate authority concerning rights to one means among others for enforcing possession and control. When we refer to legal rights, we again do not simply mean *de facto* ability to control resources. Similarly, the relevant meaning of 'permissible' in the context of real-world property rights is to simply what we are able to do or control. It refers to actions that are legally or morally legitimate.[4]

Other NIE definitions of 'property rights' are no less defective. For example, Barzel (1994, p. 394) defined property as:

> an individual's net valuation, in expected terms, of the ability to directly consume the services of the asset, or to consume it indirectly through exchange. A key word is *ability*: the definition is concerned not with what people are legally entitled to do but with what they believe they can do.

The upshot of this is that if a thief manages to keep stolen goods then he acquires a substantial property right in them, even if, on the contrary, legal or moral considerations would suggest that they remain the rightful property of their original owner. Elsewhere Barzel (1997, p. 3) made it clear that his version of 'the economics of property rights' is not about legalities. This removed the question of legal title from his definition of property. But it is misleading to describe 'the ability to enjoy' something as a 'right.' Enjoyment can exist without rights, and rights without enjoyment. Rights result from institutionalized rules involving assignments of benefit and duty. The 'ability to enjoy' may not involve more than an individual's relationship with an object.

The above NIE definitions of 'property rights' conflate property with possession. Possession is principally a relation between a person and a thing. It does not amount to legal ownership. As the historian Richard Pipes (1999, p. xv) put it: 'Possession refers to the physical control of assets, material or incorporeal, without formal title to them.' Property often implies but does not necessitate possession, and some laws recognize possession as a separate right *in rem* (regarding things). But the two are not the same: '*Property* refers to the right of the owner or owners, formally acknowledged by public authority, both to exploit assets to the exclusion of everyone else and to dispose of them by sale or otherwise' (ibid.).

The contractual exchange of property involves a minimum of not two parties but three, where the third is the state or a 'superior authority' (Commons 1924, p. 87). The basis of a right of ownership of a resource is an acknowledgement of that right by others, through mechanisms of institutional accreditation and legitimation. As the legal theorist Antony M. Honoré (1961, p. 115; 2013) wrote: 'To have worked out the notion of 'having a right to' as distinct from merely 'having' … was a major intellectual achievement. Without it society would have been impossible.' The distinction between property and possession is ignored within much of economics, yet it is of enormous analytical significance (Heinsohn and Steiger 2013, Hodgson 2015, Deakin et al. unpublished).

In its view of property, the NIE is strangely close to Marxism. Marx's numerous discussions about property had little to say about legal rights, and he too conflated the matter of property with possession. Hence Marx (1975, p. 351) in 1844 addressed 'private property' and argued that 'an object is only *ours* when we have it – … when we directly possess, eat, drink, wear, inhabit it, etc., – in short, when we *use* it.' Marx also relegated law. In his 1859 Preface to the *Contribution to the Critique of Political Economy*, Marx (1971, p. 20) depicted law as part of the 'superstructure' and not of the economic 'base'.

Similarly, some NIE writers emphasized custom and private ordering, seeing formal law as an *étatiste* stamp upon the more 'basic' world of individuals beneath. With both Marx and

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[4] I sidestep here the important, complex and unresolved debate within the philosophy of law on the relationship between law and morality. Classic (but different) statements on this include Hart (1958) and Fuller (1964).

these NIE writers, effective power over something, i.e. might, makes a *de facto* right. Legal and moral aspects of property are overshadowed. Writers in both these schools of thought downplayed the role of the legal apparatus in establishing and legitimizing rights.

The mistaken removal of legal rights from the definition of property cannot be justified on the ground that they are unnecessary to predict behaviour. Any explanation of dispositions, choices or preferences must take such factors into account. If economists are interested in predicting behaviour, then they must take legal matters of motivation, possibility and constraint into account. The focus on control is descriptive rather than explanatory. It takes as given what has to be explained. Such predictive power is based on extrapolations of superficial observations, with inadequate explanation of what is observed. More reliable predictions require fuller theoretical explanations.

Williamson's focus on private ordering is relevant here. Ménard and Shirley (2014, p. 5) wrote that Williamson 'showed that private arrangements are usually less costly than the legal system in enforcing rights.' This statement is ambiguous. If it simply means that agreeing a deal privately is generally cheaper than involving lawyers and courts, then this is obviously true. But Williamson had a different agenda. He suggested that contracting does not generally require the existence of courts. Consequently, 'private ordering … is the world with which transaction cost economics is concerned' (Williamson 1985b, p. 184). But the idea that contracting is possible, in a large-scale, complex market economy, without a state legal apparatus will find no substantial empirical or theoretical support in Williamson's work. It is entirely unproven.

Williamson rightly pointed out that recourse to litigation and the courts is always costly, and that disputants have strong incentives to reach mutual agreements without using the full force of the law. But in practice, at least in developed capitalist countries, these private agreements are always under the shadow of the state legal apparatus. Negotiators know that if they fail to meet a private agreement, then the full threat of law may be used. As Avner Greif, et al. (1994, p. 746) put it, 'the effectiveness of institutions for punishing contract violations is sometimes best judged like that of peacetime armies: by how little they must be used.' Where the rule of law prevails, the mere possibility of access to the courts is sufficient for the legal system to bear down upon contractual agreements. Hence many apparently self-enforcing agreements are actually contracts made 'in the shadow of the law' (Mnookin and Kornhauser 1979). Like Marx, Williamson downplayed formal (state) law and its mechanisms of legitimation and enforcement.

Institutional economists need to take much more account of legal theory. As Dean Lueck and Thomas J. Miceli (2007, p. 187) concluded, much of the literature in economics on property rights 'remains ignorant of property law'. As Benito Arruñada (2012, p. 24) pointed out, much economic analysis treated property as a relatively unproblematic distribution of entitlements and quickly moved its analytical attention toward contracting difficulties and transaction costs. The standard 'economics of property rights' miss-specifies an ability as a right. The ability to use something means possession, not property. Strange as it may seem, the 'economics of property rights' is about neither property nor rights. This is not to deny important insights in this stream of research. But the above issues need to be taken into account for a fuller understanding of both real-world property and the complexities of individual motivation.

Contracts, firms and markets

Taking law seriously has a number of implications, including within the theory of the firm. Both Coase (1937, 1988a, 1988b) and Williamson (1975, 1985a) neglected the matter of legal personality in their work in this area. While they considered contracts, they focused on entrepreneurial contracts with agents within the production process, largely ignoring contracts between the firm (as a legal entity) and its customers and outside suppliers (Hodgson 2015).

Recent research on legal personality and legal incorporation suggests that major problems within the Coase-Williamson theory, including the specification of boundaries and the determination of the 'glue' that holds the firm together, can be resolved when legal factors can be taken into account (Hodgson 2002, 2015, Hansmann et al. 2006, Gindis 2009, Robé 2011, Deakin 2012). This work draws a clear line between the firm and the market, and hence puts into question the idea of a 'continuum' between firms and markets, with 'a host of hybrid modes of organizing' in between (Ménard and Shirley 2014, p. 17), and undermines the concept of 'hybrid forms' (Ménard 2014).

Muddying the distinction between firms and markets involves a confusion of singular with multiple traders and legal persons. Both the identities and rights of the respective legal agents and property owners then become vague. This imprecision, created through inadequate attention to key concepts, has spread elsewhere. In particular, the notion of a market is eviscerated. Given that the market is a vital institution in modern economies, this is a serious impairment.[5]

Consider two examples. First, following Aaron Director (1964), Coase (1974) advocated a 'market for ideas.' In their important book on China, Coase and Wang (2012, pp. 190-207) repeated the term about 30 times, and the 'market for goods and the market for ideas … together in full swing' is their main policy recommendation, neglecting other needed Chinese institutional reforms in land tenure, corporate law, finance, or the polity (Hodgson and Huang 2013). Does their proposal for a 'market for ideas' literally mean that full property rights in ideas should be established (as with goods) and they should all become priced and traded on a market for money? Not so, it seems. They referred principally to the need for 'freedom of speech and expression' and for 'the creation and transmission of knowledge' through educational institutions. By misleadingly describing all this as a 'market,' Coase devalued his previous insistence on the importance of property, and on the non-universality of the price mechanism. Coase (1974, p. 384) wrote earlier: 'in the market for goods, government regulation is desirable whereas, in the market for ideas, government regulation is undesirable and should be strictly limited.' My quarrel with Coase is not on these matters of regulation, but on his loose basic concepts of *property* and *market*. What is consistent in his position, from his earliest to his latest works, is his failure to distinguish between possession and property (we *have* ideas, but we do not necessarily *own* them in a legal sense), his relative neglect of legal *rights* (beyond the capacity to impose costs or penalties on others), and his insufficient acknowledgement of the economic importance of corporate legal personality.

A second example comes from the work of North. Despite North's (1977) valid complaint that economists have neglected the true nature of markets, North (1990a, 1990b) promoted an untenable idea of a 'political market.' This concept was not clearly defined. It might refer to party competition in democracies, or perhaps any struggle between individuals or groups for political power. Such processes are poorly described as markets. Voting or consent to authority involve neither exchanges of property rights nor commercial contracts. A danger in the term 'political market' is that it stretches the concept of the market so widely that it loses

[5] Contrary to the suggestion by Ménard and Shirley (2014, p. 18), I do not define the market simply as an institution. It is important to differentiate between definitional and descriptive statements. See Hodgson (2008a, 2008b, 2015) for definitions of a market. Ménard (1995) similarly described markets as institutions.

much of its meaning, particularly in relation to property rights and contractual exchange. The notion of 'political market' is strangely indifferent between less corrupt democracies and others (such as India) why the buying of popular votes and the votes of elected politicians is commonplace.

Given these problems, if terms such as 'market for ideas' or 'political markets' are merely intended as metaphors, then that must be made absolutely clear. Furthermore, the characteristics of real markets must be established, including exchanges of genuine property rights.

The problematic definitions of both transaction costs and property rights, and the consequent over-widening of the concept of the market, mean that the 'golden triangle' is not so glittering as claimed. Their gold is mixed with baser metals. My recommendation is not that the core ideas of transaction costs, property rights and contracts should be abandoned, but that they should be treated much more seriously and carefully within the NIE. Fake alternatives should be avoided.

Coase, North and Williamson de-homogenized

Turning from the 'golden triangle' of ideas I now broadly address the contributions of Coase, North and Williamson, which Ménard and Shirley place very reasonably at the centre of their accounts of the NIE. There is considerable diversity, and even some important contradictions, within this influential NIE trinity. My aim is not to undermine the importance of the work of these inspiring writers – on the contrary their contributions are highly stimulating – but to illuminate some basic differences between them. In this way I bolster my claim that the NIE is internally diverse and has unclear boundaries.

Assumptions about the nature and behaviour of individual agents are of course foundational to social science. On this there are major differences within the troika. Ménard and Shirley (2014, p. 10) rightly noted North's abandonment of 'neoclassical assumptions about human rationality', but do not mention Coase's similar qualms, or Williamson's different position. Williamson (1975, p. 255) famously emphasized 'opportunism' and 'self-interest seeking with guile', while also embracing a version of bounded rationality.[6] Williamson did not offer any empirical grounding for the assumption of 'opportunism' and there is increasing experimental and other evidence against purely self-interested behaviour (Camerer and Fehr 2006, Bowles and Gintis 2011). In later writings Williamson saw 'opportunism' as a possible threat rather than necessarily ubiquitous, but he adopted no alternative general account of human motivation.

By contrast, Coase was more open to evidence. Coase (1984, p. 231) advised that we should 'start with man as he is', thereby alluding to Alfred Marshall's (1920, p. 26) highly qualified adoption of rationality and his rounded acknowledgement of the multiplicity of human motives, including ethical intentions (Marshall 1920, p. vi).[7] On this fundamental

[6] Bounded rationality itself has several different meanings (Sent 1998).

[7] It is important to point out that on this and other issues, Marshall was heavily influenced by Gustav Schmoller of the German historical school (Hodgson 2001, 2005). In turn, Coase was a devotee of Marshall. Consequently, as Furubotn and Richter (1997, p. 34) pointed out: 'Schmoller's critique of classical economics is strikingly similar to that made recently by Ronald Coase'.

issue, there are marked differences of substance, empirical orientation, and emphasis in the works of Coase, North and Williamson.

Coase criticised Williamson's version of transaction cost analysis. Coase (1988a, p. 43-44) was 'sceptical of the asset-specificity argument' that is central to Williamson's work. There is also an important difference between Coase and Williamson on private ordering. Williamson (1985b, p. 184) argued that 'transaction cost economics' should address 'private ordering' rather than institutions such as courts. Coase (1988b, p. 10) thought differently:

> When the physical facilities are scattered and owned by a vast number of people with very different interests . . . the establishment and administration of a private legal system would be very difficult. Those operating in these markets have to depend, therefore, on the legal system of the State.

But in their studies of the firm, Coase and Williamson both sidestepped the legal personality of the firm and the significance of legal incorporation. By contrast, throughout a major volume on the development of modern politico-economic systems, North et al. (2009) gave it massive emphasis. They stressed the general role of statutory law and of the legal incorporation of business firms. The development of state-based corporate legislation was, for them, crucial for the development of capitalism. The establishment of corporate legal persons that could outlive their shareholders was both a major means of capital accumulation and a vital source of enduring, countervailing political power.

Another major difference between North and Williamson concerns the effects of competition in the evolution and efficiency of firms and other institutions. For example, when discussing the relative efficiency of cooperative and conventional firms, Williamson (1980, 1985a) argued that if worker cooperatives were more efficient, then they would be much more common in the real world. Pointing to their manifest scarcity, he concluded that worker cooperatives must therefore be of lower efficiency or profitability. Williamson assumed that competition tends to weed out inefficient firms, and consequently a rare organisational form is likely to be so because it is less efficient.

By contrast, North (1990a) embraced the concept of path dependence. Accordingly, a socio-economic system and its entangled institutions can get locked into one of several previously possible paths of development. Individual institutions are unable to search for global efficiency in the entire fitness landscape, because they are tied in with other institutions upon which their performance depends. North (1990a) gave historical examples of sub-optimal, path-dependent development in socio-economic systems. Williamson's different approach downplayed the context dependence of fitness and efficiency. Because of context dependence and complementarities, systems can evolve along different tracks (Aoki 2001, Hall and Soskice 2001). Addressing cooperatives in particular, it has been shown that their survival and efficiency may depend on the kind of financial system under which they operate (Gagliardi 2009). Efficiency and fitness are context-dependent concepts.

The original institutional economics: underestimations and mischaracterisations

In further search of meaning and boundaries, let us now consider the original institutional economics. This movement had many internal variants, all of which had serious shortcomings (Hodgson 2014). But this does not mean that it can be side-lined or forgotten. Apart from their mention of Commons, the two papers by Ménard and Shirley contain no significant discussion of the institutionalism of Thorstein Veblen, Wesley C. Mitchell, John Maurice Clark, Walton Hamilton, Morris Copeland and many others. This institutionalism was dominant in American economics in the interwar period. Several original institutionalists became presidents of the American Economic Association, from Commons in 1917 to John Kenneth Galbraith in 1972. Mitchell and Clark were the first recipients – in 1947 and 1952 – of the AEA Francis A. Walker Medal, awarded every five years 'to the living American economist who in the judgement of the awarding body has during his career made the greatest contribution to economics.' Simon Kuznets, who was Mitchell's former colleague at the National Bureau of Economic Research and was also inspired by the original institutionalism, won the Nobel Prize in 1971. If we add Gunnar Myrdal, who also aligned himself with the original American institutionalists, then we must acknowledge his 1974 Nobel Prize as well.

But the NIE 'movement' ritually dismisses the original institutionalists, often remarking, very wrongly, that they were 'anti-theoretical' (Coase 1984, p. 230, Williamson 1996, p. 1792). These claims have been easily refuted elsewhere (Rutherford 2001, 2011, Hodgson 2004).

While, to their credit, Ménard and Shirley do not repeat the false 'atheoretical' claim in their two articles, they are under another misapprehension concerning the original institutionalism. In their introduction to their useful *Handbook of New Institutional Economics*, Ménard and Shirley (2005, p. 2) stated that 'unlike old institutional economics, NIE does not abandon neoclassical economic theory. While new institutionalists reject the neoclassical assumption of perfect information and instrumental rationality, they accept orthodox assumptions of scarcity and competition.' This too is a mischaracterization.

There are two questions here, concerning the alleged abandonment by the original institutionalists of (a) 'neoclassical economic theory' and (b) 'assumptions of scarcity and competition'. While (a) depends on (b), the latter does not imply the former. For instance, Austrian school economists endorsed assumptions of scarcity and competition, while rejecting much of neoclassical analysis.[8] They typically rejected standard models of utility maximization, much equilibrium analysis, and unrealistic assumptions concerning information and knowledge in neoclassical economics. Note in particular Friedrich Hayek's (1937, 1945) forceful critique of general equilibrium theory.[9]

Did the original institutionalists abandon neoclassical theory? Without doubt, one of the most potent critics of neoclassical economics was Veblen. He forcefully criticised neoclassical concepts such as utility-maximization and equilibrium, and rejected assumptions of normal or natural levels of profits, wages, prices or employment. But even Veblen did not entirely abandon neoclassical theory. When he analysed price levels in essays published in 1892, 1893 and 1905, he acknowledged the concepts and effects of supply and demand (Camic and Hodgson 2011). In lectures delivered in 1926-27, his former student Mitchell (1969, vol. 2, pp. 685-6) pointed out that 'Veblen himself at times makes casual, implicit use of orthodox economic theory … his theory of the expansion phase of business cycles runs in terms … of changes of conditions of supply and demand.'

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[8] I define 'neoclassical' here in terms of prevalent assumptions of equilibrium and utility maximization, and the avoidance of chronic information problems.

[9] Hayek was an institutional economist, in the sense that he was much concerned about institutions. He too received the Nobel Prize in 1974. Ménard and Shirley (2014) mention Hayek only once, in passing. Adding Kuznets and Myrdal, we could say that *seven* institutional economists have won Nobel Prizes in economics – more than the four noted by Ménard and Shirley.

Prominent original institutionalists such as Mitchell and J. M. Clark endorsed aspects of Marshallian theory, which they saw as necessary for much economic analysis. They took it for granted that institutionalism had to make use of some Marshallian-type tools, while (following Marshall himself on some points) they criticized some of the more extreme or 'unrealistic' assumptions found in much of the neoclassical tradition, such as individual utility maximization, universal diminishing returns, static equilibrium, perfect competition or perfect information. Modified Marshallian notions of cost are evident, for instance, in Clark's (1923) theory of 'overhead costs'.

The leading institutionalist Hamilton (1923) criticized the idea of a natural 'law' of supply and demand. But – especially when dealing with practical matters – Hamilton (1918, 1944) adopted a concept of scarcity and accepted that supply and demand affected prices. Hamilton (1919, p. 317) wrote: 'The writings of the neo-classicists … are not without pertinent material.' Similarly, Commons (1931, pp. 648, 656) admitted elements of orthodox price theory and made scarcity a central concept (Biddle and Samuels, 1998). It is also clear from an important contemporary article by Eveline Burns (1931) that the original institutionalists did not take a rejection of neoclassical theory as canonical, and that the extent of its legitimate usage was a matter of considerable debate.

Turning to 'assumptions of scarcity and competition', these were widely accepted by the original institutionalists, typically within a Marshallian (partial equilibrium) framework. But what about Veblen, the fiercest critic of neoclassical theory? Veblen wanted to bring insights from Darwinism into economics, to turn it into an 'evolutionary' and 'post-Darwinian' science. To achieve that, he had to accept the Darwinian ideas of (local) scarcity and competition. These are central to Darwin's own paradigm (with the qualification that Darwin (1871) emphasized cooperation within groups, as well as competition and selection). Veblen used the concepts of scarcity and competition several times.[10]

The fact that Veblen was normatively against 'the competitive system' is beyond the point. He still underlined the role of competition within a market economy. Furthermore, in contrast to Veblen's normative stance, most original institutionalists – including Mitchell, Commons, Hamilton, Copeland and Clark – were in favour of a competitive but regulated capitalism.

In sum, to use exactly the same words that Ménard and Shirley (2014, p. 2) used to describe the NIE, the original institutional economists also 'accepted much of the neoclassical paradigm' albeit 'with certain important exceptions'. The same words in quotes could apply to the both the NIE and to the original institutionalists.

Ménard and Shirley (2014, pp. 2, 4, 8) and Ménard (2014, p. 1) noted the influence of Commons on the NIE, and in particular on Williamson. I would add that Commons was also a very major influence on Chester Barnard, Herbert Simon (Hodgson 2004, p. 285) and Elinor Ostrom (2004). Other connections and influences should also be noted. For instance, although he did not use the term, the original institutionalist Clark (1918) helped pioneer a concept of

[10] See, for example, the Veblen extracts in Camic and Hodgson (2011, pp. 66-74, 80, 106, 159, 162-3, 210, 215, 223, 225, 228, 280, 324, 329-330, 380, 403, 413-16, 423-38, 454-5, 495, 503, 546). On the complementarity of cooperation and competition in human social evolution see Hodgson and Knudsen (2010) and Bowles and Gintis (2011). Note that the concept of scarcity is ambiguous, and in some forms it is not universal. But local scarcity is ubiquitous (Hodgson and Knudsen 2010, pp. 33, 242).

bounded rationality (Rutherford 2001), another version of which became central in the work of Williamson (1975, 1985a).[11]

The original institutional economics: diversity and relevance

I wish to emphasise my claim that any meaningful boundary between the NIE and the original institutional economics is now very difficult to draw. As established in the preceding section, the attempt by Ménard and Shirley to make this demarcation fails. Other NIE devotees deal with this problem either by mischaracterizing the original institutionalism as 'atheoretical' or by ignoring it entirely.

On closer inspection it becomes clear that the original institutionalism was itself highly diverse (Hodgson 2004, Rutherford 2011). Furthermore, for reasons raised above and elsewhere, some elements of the NIE are very close in theoretical terms to some original institutionalists (Groenewegen et al. 1995, Dequech 2002).

Another important point is that all institutional economists can learn from the original institutionalism, including when addressing some of those 'glaring gaps still to be filled'. One of those 'glaring gaps' is the lack of adequate dynamics in transaction cost economics: it remains mostly a static analysis. Important attempts have been made to bring dynamics into the picture (Langlois 1992, 2007). Institutional and technological dynamics were also a major and enduring feature of the old institutional economics, including in Veblen's attempt to develop 'evolutionary' and 'Darwinian' ideas. Recent years have seen a revival of Darwinian ideas in the social sciences, including in evolutionary game theory and evolutionary economics (Aldrich et al. 2008, Stoelhorst 2008, Hodgson and Knudsen 2010).

To his credit, Ménard (2014) highlighted the admission by Williamson (2000, p. 600) and others that technology has been largely ignored in the transaction cost approach. Ménard starts to fill this gap. The insights of both the original institutionalism and modern evolutionary economics are relevant for this task (Dosi et al. 1988).

Another 'glaring gap still to be filled' is an adequate account of human motivation that is grounded on established scientific research in experimental economics, psychology, anthropology, primatology, biology and philosophy. Here too evolutionary ideas are making a huge comeback, and we are reminded of Veblen's attempts to combine both biological (instincts) and cultural (habits) factors in the explanation of individual motives (Bowles and Gintis 2011, Hodgson 2013).

It is also important to note that Veblen and other original institutionalists acknowledged other motives alongside self-interest (Camic and Hodgson 2011). The same is true of Marshall (1920) and leading members of the historical school (Hodgson 2001). They all wanted a more realistic and rounded theory of human motivation and behaviour, based on psychological and other relevant evidence.[12]

Contrary to much of the NIE, but more consonant with the original institutionalists, recent research undermines the notion of narrow self-interest. Instead it gives grounding for social

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[11] Clark's concept of bounded rationality was in turn inspired by Charles Horton Cooley (1902, pp. 33-34), who was also regarded as one of the 'leaders' of the emerging institutional economics (Hamilton 1919).

[12] It should be noted that within the NIE there is growing interest in psychology and cognitive science, particularly in the work of North.

preferences, cooperation, altruism and moral motivation, albeit alongside greed and opportunism (Bowles and Gintis 2011, Hodgson 2013). These additional factors are crucially important to understand human economic organization (Stoelhorst and Richerson 2013).

While they did not pass down a complete or systematic theory, it would be foolhardy to suggest that we cannot learn from the original institutionalists. While it had serious shortcomings, there are important insights within this tradition that should be addressed. We should not confine ourselves to old ideas, but much enduring wisdom does not have a sell-by date. Furthermore, if we fail to define accurately the differences between two schools of thought, we must consider the possibilities that they might be partly complementary, rather than rivalrous, and we can all learn from their achievements and mistakes.

Conclusions

My aim in this comment is neither to undermine the genuine achievements of the NIE, nor to propose its overall inferiority vis-à-vis the original institutionalism. This is not an attempt to promote one school over another. Instead I wish to make the following eleven claims:[13]

1. Both the NIE and the original institutionalism are (or were) internally highly heterogeneous in terms of their assumptions and methods.
2. Some leading researchers in the NIE have been directly or indirectly inspired by ideas from the original institutionalism.
3. There is considerable overlap or resemblance between parts of the NIE and parts of the original institutionalism.
4. Claims that the original institutionalists were 'against theory' or 'atheoretical' are false and have been decisively refuted.
5. Claims that the original institutionalists were entirely 'against neoclassical theory' are false. Most of them adopted elements of Marshallian (or similar) theory.
6. Proponents of the NIE have so far failed to provide a valid explanation of what (if anything) distinguishes their approach, in terms of assumptions, theories or methods, from the original institutionalism.
7. Proponents of the NIE have so far failed to provide a clear and convincing picture of its own conceptual and theoretical boundaries. This problem of identity and boundaries also afflicted the original institutionalism, and was one of the factors in its eventual decline.
8. Concepts identified at the core of the NIE – particularly transaction costs, property rights, and contracts – are disputed, problematic and so-far ill-defined.
9. Some NIE economists have degraded the vital concept of a market, by referring to 'political markets' or 'markets for ideas', which are not true markets.
10. Much work in (all kinds of) institutional economics suffers from a lack of clarity and consensus concerning key concepts and definitions.[14]

[13] For further arguments and evidence to support these claims see Rutherford (2001, 2011) and Hodgson (2004).

[14] An example is the ongoing confusion whether or not organisations and institutions are mutually exclusive. North is often attributed with the notion that organisations are not institutions, but Hodgson (2006) shows that North did not hold that view. Nevertheless, some passages in North et al. (2009) are ambiguous on this point (Hodgson 2015). Another definitional bugbear is the frequent failure to define the terms 'formal' or 'informal' in regard to institutions, despite the ambiguity and different usages of these adjectives.

11. All modern institutional economists can learn from original institutionalists, despite their limitations. They may even help in dealing with the acknowledged ‘glaring gaps’ and ‘black holes’ in the NIE.[15]

We all need to avoid academic tribalism and triumphalism. We should be more humble, synthetic and outward-looking. Ménard and Shirley rightly convey some of the excitement generated by the enhanced study of institutions assumed in the social sciences. After being neglected from the 1940s to the 1970s, and thanks to Coase, North, Williamson and many others, the study of institutions has moved to centre stage. But there is a great deal of conceptual, theoretical and empirical work still to be done. Some prominent empirical claims in NIE are open to dispute.[16] Definitions of key terms are often imprecise and unsatisfactory. These flaws need to be fixed. By putting forward and debating some key ideas, the contributions of Ménard and Shirley are most welcome. They have exposed both weaknesses and strengths. It is through such open and ongoing dialogue that we can make further progress.

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[15] For example, we might pay heed to the insistence of Veblen and others that economics must take account of findings from psychology and incorporate the implications of changing technology. Also inspirational are Veblen’s attempts to draw dynamic ideas from (Darwinian) evolutionary theory and to examine the natural as well as cultural bases of economic phenomena.

[16] For example, claims that Williamson-type transaction cost economics has been empirically corroborated are countered by meta-studies that show that the evidence in favour is at best mixed, and some of it could also support rival (but perhaps ultimately complementary) explanations, such as competence-based theory (David and Han 2004, Carter and Hodgson 2006).

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