DISSERTATION

PROGRESS AND REFORM: THE ECONOMIC THOUGHT OF JOHN R. COMMONS

Submitted by

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WE HEREBY RECOMMEND THAT THE DISSERTATION PREPARED UNDER OUR SUPERVISION BY THOMAS KEMP ENTITLED "PROGRESS AND REFORM: THE ECONOMIC THOUGHT OF JOHN R. COMMONS" BE ACCEPTED AS FULFILLING IN PART REQUIREMENTS FOR THE DEGREE OF DOCTOR OF PHILOSOPHY.

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ABSTRACT

PROGRESS AND REFORM:
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This study re-examines the economic thought of John R. Commons. Specifically, Commons's work is examined with a regard for his contribution to the new and original institutional schools of economic thought. Toward this end this study attempts to first, organize Commons's economic system into a workable framework, second , reconcile Commons's value conception with those of other founding authors in the original institutional tradition, and third, to show the linkages between Commons's thought and the research agenda of the newer institutional school.

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Table of Contents

Introduction

John R. Commons was arguably one of the most influential economists of the progressive era and the interwar period. His contributions to national policy included unemployment insurance, women's minimum wage, labor law, and public utility law. Additionally, his students contributed to legislation in the areas of social security, women's suffrage, interstate commerce, immigration, national banking, and worked with the Roosevelt administration during the New Deal era. Despite all of the above, his name goes largely unmentioned in current economic thought.

Commons, often forced to play the role of the wandering academic in his early years, worked for many organizations, both public and private, throughout his career. During the years 1889-1900 Commons taught at four universities and held innumerable private sector jobs. In his mature years, after 1900, Commons worked directly for the National Civic Federation, The Wisconsin Industrial Commission, The Russell Sage Foundation, and The City of Milwaukee, all the while teaching at the University of Wisconsin. In addition to the vast amount of applied work Commons achieved in his lifetime, he also left behind a significant body of theoretical writings. This is a study of those works.

Without a doubt, the aforementioned experiences had a significant effect upon Commons's written works. Throughout his career, he wrote several books dealing with theoretical and applied issues in economics. However, despite his acknowledged work with state and national government as well as private concerns, Commons's written works -- both those of an applied and a theoretical nature -- were never very well received. This seems unusual given that his work anticipated many of the economic concerns of the modern era. Modern issues such as contracting, intangible value, and expectations as an economic determinant can all be found discussed in depth in Commons's work.

Despite his neglect, Commons, along with Thorstein Veblen, is generally regarded as a founder of the school of economic thought known almost universally as "institutional economics," which, since the advent of new institutional economics (NIE) has become known as original institutional economics (OIE). More than anything else, scholars in the OIE tradition strove to explain the role of social institutions upon the development of the then current economy -- i.e., they sought to explain the economy as a socially instituted process. One would think that the role of founder of a school of economic thought would alone insure that Commons's writings would be well cited by those continuing in this tradition; however, this is not the case.

While Commons's theoretical work has remained largely ignored over the last several decades, its relevance has perhaps never been greater. The rapid growth of the NIE over the last two decades has increased the level of interest in his ideas. Specifically, it is Commons's transactional focus that is currently enjoying resurgence. Rather than a theory of economy based upon relative prices, Commons focused upon the human interactions of the wider economic process. These human interactions he termed transactions. As questions of contracting, information, and governance return to economic thought, so has reference to Commons's work. However, the references to his work are, in many cases, accompanied by the claim that Commons's written works are too personal and difficult to comprehend. That is, while Commons's name is often mentioned as a significant contributor to many current strains of thought, actual examinations of his work remain sparse. Therefore, the time is ripe for a re-examination of Commons's ideas.

Methodology

Methodologically, studies in the history of economic thought can be problematic. Specifically, those engaged in such studies can find themselves feeling like the unwanted stepchildren of the economics profession. If he is lucky, the economist engaged in studies in the history of economic thought will find himself regarded as a quaint curiosity by his peers. It seems likely that the disdain of the economics profession for its own history is, in part, a result of the purported "Popperian" nature of economics. The Popperian methodology of science suggests that current theories are the most "correct" because they have not yet been falsified.

Despite the lack of interest from within the economics profession, several reasons have been given why studies in the history of economic thought are necessary. First, studies in the history of economic thought make us better economists. In reading the thoughts of economists long gone we become more acquainted with a variety of thoughts on the economic problem. Second, the history of economic thought can teach us humility. The errors of economists past makes us aware that we can make errors and that we ought to not become overconfident. Third, studies in the history of economic thought can provide inspiration (Landreth and Colander 1994, 16). J.M. Keynes himself claimed the then long-dead thoughts of the mercantilist era as inspiration for his own work. The above three examples, however, do not necessarily make studies in the history of economic thought necessary, but merely desirable. As such, they are not investigated further.

The general methodological debate in the history of economic thought may be said to revolve around "absolutist" and "relativist" positions. The former suggests that knowledge in the economic science accrues by a process of falsification. That is, one may suggest that the current theories are, by process of elimination, the best. Therefore, by studying thought one is only likely to repeat the errors of the past. This is the position of absolutists. Such suggestions fail to explain much in the development of economic thought. One could point to the failures of falsification to explain the so-called "marginalist revolution" of the 1870s, and the "Keynesian revolution" of the 1930s. In both cases, economic thought made fairly radical departures from previous lines of thought. Given the above, it is unreasonable to suggest that falsification alone can explain all developments in economic thought (Blaug 1985, 698-699; and Spiegel 1991, xiv-xv). If internal development alone cannot explain the growth of economic thought, then one must also look to external sources. Such a focus does not imply that history is the only determining factor in the development of economic thought, but merely that it is relevant. This is the position of the relativist. While each of these approaches has merits and demerits, they both miss the point. That is, they both presume the existence of some ideal or pure correspondence; that we could – if we could only find the right method or vocabulary – discover "truth."

Instead, it is suggested here that economic thought, and science in general, is interpretive. That is, economic "science" boils down to the interpretation of meaning. Methodologically speaking, we may well say, "the price of a good and its quantity demanded are inversely related." However, this alone accomplishes nothing – what does it mean? Samuels explains,

> The problems which confront social scientists are interpretive ones. Very often they involve competing paradigms with regards to the nature of the economic system; for examples, whether it is to be comprehended as a Pareto-optimizing allocative mechanism or a conflict-ridden matter of organization and control; or whether the distributive paradigm is to be honorific productivity, immoral exploration, or non-judgmental appropriation. Such questions, and the social sciences contain many of them, are not matters of truth but interpretation (1996, 114).

Once we attempt to apply our terminology, it becomes evaluative – it is no longer value free. From Rorty,

> Suppose we picture the "value-free" social scientist walking up to the divide between "fact" and "value" and handing his predictions to the policy-makers who live on the other side. They will not be of much use unless they contain some of the terms which the policy-makers use among themselves. What the policy-makers would like, presumably, are rich juicy predictions like "If basic industry is socialized, the standard of living will [or won't] decline" (1982, 196; brackets in original).

That is, in the application of "value-free" conceptions to human endeavors they necessarily become value-laden. This does mean to say that a hermeneutic approach is necessarily the best. Like the "absolutist" and "relativist" positions as well as the "value-free" contention mentioned above, hermeneutics makes the same error. That is, they all make the same mistake in assuming that knowing something is the same as being able to deal with it. Explaining is not the same as understanding; there is a fundamental difference between the two (Rorty 1982, 198). It follows from this that traditional ideas of methodology are misleading. Rorty suggests that instead of trying to determine the correct methodology to determine "truth" we should be searching for means of coping with existence (Rorty 1982, 198). That is, instead of searching for the correct method of explaining, we should strive for understanding. The method employed in constructing theories is therefore not important; instead, the only criterion ought to be that theories "should contain descriptions of situations which facilitate their prediction and control" and second, theories "should contain descriptions which help one decide what to do" (Rorty 1982, 197). This is the pragmatic approach to science. *This does not mean anything goes or that truth is not important*. Indeed, method and truth are still important, but pragmatism suggests that truth, and consequently method, as a theoretical concept, is impossible.

From the pragmatic approach outlined above, it follows that studies in the history of economic thought are justified if they help us to cope with ongoing problems. The present study of Commons meets both these criteria. Indeed, the method of Commons's economics was to make the economic science meet the above-mentioned criteria. As such, a study of Commons's thought can be justified as an example of pragmatic economist thought. As is shown in the second chapter, Commons's theory of economy is based squarely upon the pragmatic philosophy. It does not seek to find the fundamental "truths" of the economy in a theoretical sense, nor does it paint a picture of "ideal" economic outcomes. Instead, Commons's thought attempts cope with economic activity as it exists.

The above is not meant to present a through-going study of the methodology of science; such a study would be far beyond the scope of this work. Instead, this discussion is presented in order to first, justify the study, and second, to set the philosophical tone of the work. Given this, the work that follows considers not only the words of Commons but also his actions. Indeed, the latter are taken to provide an understanding of the former. Moreover, the intention of this work is to provide the reader with the tools of social policy that Commons used with such great success.

The specific approach taken in this study is that of an intellectual portrait. This approach emphasizes the role of external influences such as society and life experiences upon the thought of the individual. Studies in this tradition have, in the last several years, been written on Max Weber, John Dewey, John Kenneth Galbraith, Karl Polanyi, and Louis Brandeis, among others (Bendix 1998; Hook 1995; Stanfield 1996 and 1986; Baskerville 1994). These studies are all done in the "great man" vein. That is, they are written with the assumption that single individuals have the power to change history and that the circumstances that surround individuals shape and change them in return. For example, in economics there can be little doubt that the circumstances that surrounded the life of Karl Marx had a great effect upon the world. One might ask the question: How would the world be different today if Marx had been able to secure an academic post? Or: What if there had been no John Neville Keynes to father John Maynard Keynes? This study concurs with the above-stated proposition that individuals are both influenced by and have influence on history (Spiegel 1991, xv). While the influence of Commons is perhaps not as great as Keynes or Marx, there can be no doubt that the world of today would be different had he not lived. As described within this work, Commons's influence on the social legislation of the early twentieth century is difficult to overestimate. As such, it would seem that a study of Commons's work is long overdue.

Structure of the Work

The thesis of this work is that, first, the combined work of John R. Commons contains a theory of value that is compatible with that generally presented in the OIE literature. Second, that Commons's work provides significant linkages to theories presented in the NIE. The former is significant by the fact that it resolves a long-standing conflict within the OIE, while the latter points to a research agenda that would likely prove fruitful to both traditions.

In the first chapter, a brief biography of John Commons is presented. This chapter incorporates the influences of Commons upon and from the wider community. This chapter paints Commons as, in part, a product of his era -- the progressive era. This chapter examines how in the late nineteenth century and the early twentieth century, Commons and his students would change the shape of American society. Specifically, Commons and his students' work had a lasting influence on progressive era reforms and aspects of Roosevelt's "New Deal." Perhaps the greatest of these was the Unemployment Insurance Act of 1932, based upon the Wisconsin act drafted by Commons and his students. The purpose of this chapter is, first, to establish the social conditions and influences of Commons's life.

The second chapter of this study outlines the philosophy employed by Commons as a basis for his economic theory. This chapter shows how Commons's view of economy is closely linked to his understanding of pragmatic philosophy. From his understanding of pragmatic philosophy, Commons developed a theory of human action that he referred to as "willingness." Willingness is the basic foundation upon which Commons's theory of economy is based. Commons's willingness principle suggests that five guiding principles, namely, custom, scarcity, efficiency, futurity, and sovereignty, guide economic action. The incentives and mores of these five guiding principles could allow the economist to predict and, if desired, reform economic action and institutions toward desired ends. Also included in this chapter is Commons's use of Weber's "ideal type" in constructing his theories. Theory, for Commons, therefore takes on a different meaning from the conventional. Most significantly, it is not reductionist; it attempts to incorporate all relevant variables into the analysis. In this, Commons's work may be described as being "holistic."

The purpose in this is discussion is that -- in the opinion of the author -- Commons's work cannot be understood without a prior understanding of pragmatism and Commons's application of it in his work. Indeed, it is likely that many of the misunderstandings about Commons's work come from the failure of his students both past and present to fully appreciate the role of pragmatic philosophy as an essential component of his theory of economy.

Having examined the method of Commons's economics, the third chapter reviews Commons's system of economy. The purpose here is not to examine or criticize Commons's work, but merely to present it to the reader so as to have a common frame of reference from which to launch a discussion -- this follows in Chapter 5. The reader should be forewarned that this chapter might come as a surprise to those trained in traditional economic thought. Commons's economic thought is significantly different from the theories embraced by the current orthodoxy of economic thought. Rather than focus on prices, as in the traditional model, Commons chose the transaction as the basis for his economic theory. Commons chose the transaction because he wished to investigate the man-to-man relationships of the economy that he felt the more traditional economists had neglected. Consequently, the reader may find much that is unfamiliar in this chapter. Despite this, the careful reader will discover within this chapter a theory of economy that is not only unique, but one that provides great insight into the inner workings of the overall economic process.

The fourth chapter reviews Commons's applied work. Specifically, this chapter focuses on Commons's role in developing the Wisconsin Industrial Commission, the American Association for Labor Legislation, and the Wisconsin Unemployment Insurance Law of 1932. These examples of Commons's work were chosen because they are typical and at the same time are exemplary. This chapter is included for two reasons: First, despite the fact that the majority of Commons's applied work occurred nearly one hundred years ago, there is much to be gleaned from his method. Second, the true meaning of Commons's theoretical works is only revealed when one considers their applications. Therefore, in this chapter, three applications of Commons's theories are given consideration. Also given here is the author's interpretation of Commons's work. This may be summarized in the following statements: Commons's value conception -- embodied in his theory of reasonable value -- is explained as embodying the fundamental vision of Commons's economic theory, and this vision can only be properly understood in light of its application.

The fifth chapter of this study attempts to place Commons's work within the school of thought collectively known as institutional economics. As mentioned above, Commons is universally named as a founder of this school of thought. However, within the literature of that tradition Commons's value conception is generally regarded as conflicting with the value conceptions of other authors in the OIE. Toward the end of resolving this conflict, this chapter analyzes the supposedly competing value conceptions. Also, toward this end, within this chapter criticisms from the secondary literature of Commons's work are reviewed and in some cases rebuffed. It is the central finding of this study that the confusion about the two value conceptions comes from the mistaken belief that variables utilized by Veblen and Commons can be directly translated into those used by the other authors in the OIE.

In the sixth chapter, this study attempts to place Commons's work within the body of economic thought generally referred to as "new" institutional economics. The recent Nobel Prize given to Douglass North -- perhaps the most famous individual within this school -- for his work on institutions more than justifies and validates the work of the newer school and its consideration here. This school of thought has in recent years focused on aspects of economy that include information failures, transaction costs, law and economics, and theories of the firm. Authors in the NIE have often acknowledged Commons as a foundational author. It is shown that there is significant overlap between some of the preeminent authors in the newer tradition and the work of Commons. Perhaps more importantly, this chapter shows that significant gains to the NIE and the OIE could be achieved through cross-pollination. It is also suggested that such cross-pollination would provide significant venues for future research.

Finally, a short conclusion section is presented. Within the conclusion the reader will find, in summary form, that which has been presented and for which resolution has been attempted in the earlier chapters. Also included in this section are some recommendations for further research in this area.

Chapter 1
Life and Times

While it is the primary concern of this study to present the economic ideas of John R. Commons, this is not its sole concern. Given that to some extent his environment shapes the ideas and actions of a man, a study of said environment becomes significant. Thus, in this first chapter an account of Commons's personal history, his influences, and his influence is given. The account of Commons's personal history is not complete, but rather is an introduction to the environment of this scholar. To attempt a more complete account would take this study too far afield from its primary purpose.[1] The second and third sections, which describe influences upon and of Commons, are not meant as definitive but, again, as an introduction to the intellectual atmosphere of the era and of important impacts Commons had on the wider social environment, respectively. Particularly brief is the section on the lasting influence of Commons's work; this topic is covered more completely in the later chapter, "The Applied Reform Method of John R. Commons."

Biographical Note

The middle years of the nineteenth century were ones of radical change on all fronts. Socially and morally, the nation was dealing with the issues of slavery,

[1] For through discussions of Commons's personal history see both his Autobiography *Myself* (1934) or the biography of Commons by L. Harter (1962).

industrialization, and a more diverse population due to increased immigration. Geographically, the United States was expanding and incorporating the lands and problems west of the Mississippi. And economically, the industrial revolution had segmented the relatively new nation into a newly industrialized East, an agricultural South, and an underutilized and geographically distant West. This all created a polarization of the nation that in part led to the Civil War.

In addition to the physical war being fought between the states, an intellectual revolution was also occurring. Darwin's *Origin of Species* had spawned a social derivative: under the pens of Herbert Spencer in England and Charles Graham Sumner in the United States, "Social Darwinism" became a significant influence on thought on both sides of the Atlantic. At the same time, radical political economy, a philosophy that was arguably a factor in the labor unrest that was also on the rise, was beginning to filter over to America from the European continent.

The Civil War, fought over many of the aforementioned issues, did little to resolve many of the underlying problems. The aftermath of the war would determine the shape of the economy for the next fifty years and arguably more. Faced with a re-integration of the Southern states, the Union had at least as many problems after the war as it did before. Economically, the nation was a disaster and poorly equipped for growth. The huge costs of the war had forced the nation to issue unbacked currency, the infamous Greenback, causing severe inflation, a high tax rate, and several years of monetary difficulty (Catton 1960, 1-3).

It was into this world that John Rogers Commons was born October 3rd 1862, to John Commons and Clara Rogers Commons in Hollandsburg, Ohio. At the time of

John Rogers's birth his father, John Sr., owned a harness shop and edited a local newspaper in his spare time. He was an armchair intellectual who was well read and had an interest in the writings of Herbert Spencer. Clara was a strict Presbyterian, college educated, and an abolitionist Republican. In many ways, she was the opposite of her husband.

The Commons household, while well educated, contained intellectual conflict. Commons would later say of his childhood that, "I was brought up on Hoosierism, Republicanism, Presbyterianism, and Spencerism" (Commons 1964a, 8). Commons felt that his childhood household contained a "rift" between the thoughts of his mother and father. While Commons never saw his parents fight, he knew that his mother strongly disapproved of his father's Spencerism and his poor work ethic. Commons knew that she desired the children to be raised in a religious atmosphere, which she was not able to provide due to her husband's ways. At the time, the writings of Spencer were quite controversial and John Sr.'s local community of Quakers also disparaged his beliefs. Concerned with his lack of faith, they would hold prayer meetings at the Commons' household for his benefit. Commons saw his mother as fighting a loosing battle to maintain a Calvinist presence in the household.

John Sr.'s amateur intellectualism oftentimes caused him to neglect his business and often forced his wife to support the family. Clara did this by constantly maintaining boarders in the family house. Despite her extraordinary efforts, the Commons family would always remain in or near poverty. Later, during high school and college, Commons and his brother worked in the harness shop in order to keep it viable. Commons wrote that his father would have little problem doing the work, but then neglected to collect the bill (Commons 1964a 11). Commons and his brother would have to take care of the bill-collecting aspect of the harness shop. Later yet in life, Commons would have to take up the role of supporting both his mother and father.

After Commons finished high school, he worked as a teacher at a local country school. Commons only lasted a few short months before he lost control of the class and was asked to leave. Commons attributed his failure to his attempts to teach through experimentation (Commons 1964a, 27). Despite his lofty educational goals, more often than not the experiments would go awry. The students eventually revolted, and, as Commons relates, "pelted me with snowballs" (Commons 1964a, 27). After leaving this position, Commons vowed that he would never teach again.

The next year, 1882, Commons was able to attend Oberlin College. At Oberlin, the works of Henry George and Herbert Spencer would influence him. While there, Commons formed the Henry George club. George's single tax theory, based upon the assumption that all the value of land is God given, Commons had always known to be flawed. Commons understood that a good portion of the value of land depended upon the farmer's cultivation of it. Despite this, he would cling to George's ideas until a visiting lecturer, one Richard Ely, would refute both the works of George and his single tax as well as Herbert Spencer and his "Social Darwinism." Ely's "new economics" was, at the time, a radical change from traditional political economy typified by the works of Ricardo and Mill. Ely held that, first, value was not a static concept; and second, that there was no "natural selection" where the economy was concerned but rather that there was an "artificial selection." Ely's economics stressed the social significance of economics in practice. As we shall see in the next section, Ely, from this time forward, would be a significant influence upon Commons's work.

During his time at Oberlin, Commons had the first of several mental breakdowns that would plague him throughout his life. While coming out of an examination, Commons felt a terrific blow to the inside his head. This first attack forced Commons to leave school after failing his examinations at the end of the term. During his three-year absence from Oberlin, Commons and his brother worked at a printing office. It was from this experience, Commons explained, that his interest in labor unions and their practices began (Commons 1964a, 18-19). Commons worked at a union printing office while his brother worked at a non-union office across town. This experience allowed Commons to observe the differences between the two shops. It was from his experience at the print shop that Commons claimed he developed his system of "working rules," the unwritten rules that guide individual behavior (Commons 1964a, 19).

Upon his eventual return to Oberlin, Commons rekindled his interest in Ely's economics. He became involved with Ely's "social gospel movement." The social gospel movement (SGM) maintained that the social sciences should be responsible for the betterment of mankind. That is, the SGM held that economic theory should work with other social sciences to present a unified social theory as well as be involved with social concerns. Most importantly, the SGM sought to use Christian ideals to reform society. From Fine,

> Rejecting any distinction between sacred and secular, social gospelers sought to apply the ethical and social principles of Christianity to all problems of the age to the end that a more just social order might be realized here on earth. Society itself was to be redeemed and

> Christianized, and although individuals were still to be converted, they were to be provided with a Christian society in which to live (1976, 171).

Moreover, the SGM would "study an evolving reality inseparably involving both what is and what ought to be, and its laws would be only historical and relative" (Gonce 1996, 654). While Commons's involvement with the SGM was limited during his time at Oberlin, it would prove to be a significant influence on his early works. Perhaps more importantly, through the SGM Commons became more thoroughly versed in the ideas of Richard Ely. Since his introduction to Ely, Commons had been enamored with Ely's new economics. During his early years, Ely was the primary influence on Commons and his career.

It was also during his last year at Oberlin that Commons pitched what he then thought was the first "curve ball." During his time at the printing house, Commons had read that Herbert Spencer said it was physically impossible to pitch a curve ball. Commons set out to disprove him. Commons realized that Spencer had neglected critical variables -- the stitching on the ball and the resistance of air. This would be a primary force driving Commons's exploration in economics -- he would try to find the "omitted factors" in the field of economics.

Despite its potential to revolutionize sport, Commons's "curve ball" was short lived. During a game at Oberlin in 1886, a player whom Commons had struck out earlier with his pitch, decided to pay him back. The player beaned Commons with the ball and knocked him unconscious. Fortunately for economics, Commons soon recovered. However, he was advised that the effects of the shock might not show up for several years and that he should give up the game of baseball. As in other realms of his life, the fruits of Commons's investigations had landed him in trouble.

In 1888, Commons earned his bachelor's degree from Oberlin. Commons admitted that his graduation was at the goodwill of his instructors. His performance while at Oberlin was worse than average. Commons would neglect his studies in order to pursue his own intellectual goals. In his autobiography, *Myself*, Commons relates the following story,

> I fell behind in Biology because I persisted in finding the heart-beat of a little red water-bug that came to life before the ice was out, in the roadside ditches. The other students went on with the regular schedule of specimens. But I stuck stubbornly to that little bug.

He continues,

> I think, (the instructors) gave me a "pass" at the end of the course, for otherwise I failed on the examination (1964a, 27).

Commons's persistence was a critical component of his personality. Time and time again, when faced with hardship he would simply press on. Commons's persistence would be his savior. Typically, Commons's methods and opinions would yield major life setbacks, but Commons, undaunted, would forge ahead. His college experience was typical of his life. While the water bug and his other researches set him behind in class, such endeavors endeared him to his instructors, who eventually moved him onward.

However poorly Commons did at Oberlin, his instructors thought highly enough of him to recommend him to Johns Hopkins for graduate work. Commons went to Hopkins in order to study under Ely. Upon his arrival, Ely immediately sent

Commons to work on "case studies" such as the Baltimore Building and Loan Association and the Charity Organization Society. Upon completion of his studies, Commons would report back to Ely and write up his findings. Commons was very excited to be working in Ely's new economics as opposed to the Ricardian economics that he had been learning at Oberlin.

In his second year of graduate study, Commons failed his history examination and lost his assistantship. Despite this setback, Ely was able to get him a teaching job at Wesleyan University. However, Commons's performance as a teacher was again less than stellar and he was asked to leave after his first year.

During his time at Wesleyan, Commons married Ella (Nel) Downey. Together they would have six children. Four died in infancy and one would remain estranged from John and Ella for most of their life. While Commons did not often speak of his wife in his professional work, it seems clear that she was a great source of comfort to him during the many trials of his life. They remained married until her death in 1928.

Upon his dismissal from Wesleyan, Commons wished to return to Hopkins to finish his doctoral degree. However, such goals were simply not meant to happen. Johns Hopkins at that time had a requirement that the last year of the degree had to be done in residence, and Commons would have to start all over again. Commons never did finish his doctoral degree, but he did remain in contact with Ely and continued to be a part of the SGM that Ely founded.

Despite this setback, Commons pressed on. Through his contacts, Commons was able to procure a job for himself at Oberlin. Happy to be back at Oberlin, Commons was able to live near his parents and take care of them. However, the pay at Oberlin was significantly less than Commons could earn elsewhere. Because of this, after a year, being faced with the increased costs of a family, he was forced to find work elsewhere, although he would like to have stayed at Oberlin.

For the 1892 school year, Commons took a job teaching at the University of Indiana, where the pay was significantly better than it had been at Oberlin. During his time at Indiana, Commons believed that his skills as a teacher began to develop. He found that students preferred to hear the stories of his investigations as opposed to a traditionally structured class. They enjoyed, more than anything else, hearing stories of his life and experiences. From that point forward, Commons taught his classes not according to any prescribed format but as a sounding board for his ideas and questions about economics. Because of this, Commons's students would gain a great knowledge of public policy, but often knew little about theoretical ideas.

The following year, Commons published his first major work, *The Distribution of Wealth* (1893). The book was less than a success. Frank Taussig of Harvard referred to it as an "unbaked" performance (Dorfman 1969, 284). Another reviewer, A.C. Miller, stated, "The logic of the essay demands socialism, and the whole essay may not improperly be regarded as a disguised attempt to found a scientific basis for a theory of socialism" (Miller 1894, 464). While it is certainly true that Commons's first attempt to develop a theory of political economy was less than perfect, it does show the early influences upon his work. Commons's *Distribution of Wealth* makes the supposition that the wealthy have a greater representation in the state. Due to unequal representation, property rights are assigned unequally, and the wealthy have greater access to economic gains, thus repeating and enhancing the cycle.

Here we can see Commons's early interest in property rights, law and the rationale for state intervention in markets, as well as the significant influence of Ely upon Commons's early work. Furthermore, the policies that Commons outlines in order to counter the aforementioned trend (the rich get richer), including a guarantee of work, are very much in line with the principles of the SGM. Commons, at this time, believed that successful reform had to be based along Christian lines, and that the church had a significant role to play in reforming the economy.

In 1895, Commons was offered a job at Syracuse University. As with Oberlin, Commons would have preferred to stay at Indiana, but the wages at Syracuse were considerably higher than they were at Indiana. Commons attempted to use the offer to bolster his wages at Indiana. However, he was told by Dr. Swain, the president at Indiana, to accept the Syracuse offer at once (Commons 1964a, 52). Commons believed that it was his reputation as a socialist that had caused him to lose his job. According to Commons, since the publication of *Distribution of Wealth*, he had been labeled by many as a socialist and thought that he was giving the school (Syracuse) a bad name. After his experience at Indiana, Commons never again asked for a raise as he thought the exposure to be too great (Commons 1964a, 52-53). Instead, he would bargain for reduced working hours and pay for assistants to help him in his work.

From 1885 to 1899, Commons taught at Syracuse in New York State. By this time, Commons had refined his teaching approach. While continuing to take a participatory approach by having his classes go into the field, his teaching techniques had become more polished. The majority of Commons's students would later say that they never really did completely understand Commons's economic theories. However, they all spoke well of his character and classroom presence. This failure to grasp his theory of economy is likely explained by his above-mentioned teaching philosophy. Commons could never understand the affection that his students would show him in his later years.

Commons would teach a different set of economics to his students each semester as he continued to improve upon his theories. Of his inconsistencies in teaching and in economic theory, Commons stated,

> Somehow they probably thought that if, during fifty years, I could work my way out by inconsistencies, then there was hope for them. Perhaps too, they liked that I did not take myself too seriously. How could I take myself seriously when I was "putting over" something grand but contradictory to what I previously or afterwards put over (Commons 1964a, 2)?

Despite his self-doubt and insecurity, Commons appears to have been well liked by both the students and his contemporaries (Dorfman 1969 287-288). Judged by the success of many of his students within their field, it would seem that he gave them a good education, but Commons's inconsistencies most likely contributed to his students' inability to understand his theoretical ideas.

Despite his good reputation with the students, in 1899 Commons was -- in his opinion -- asked to leave Syracuse for stating that opening the city parks to baseball on Sunday was a good idea. However, Dorfman believed that Commons's inflammatory comments made at the 1898 meeting of the American Economics Association had something to do with his dismissal (1969, 287-288). In a speech given that year, Commons stated that (Henry) George and (Karl) Marx represented the thought of the class that was currently rising to dominance, which, according to Dorfman, was an unpopular opinion in conservative turn-of-the-century society (1969, 288).

Whatever the case, the dismissal had a profound effect upon Commons's thought. Syracuse was a religious school with ties to the Christian church, and members of the several local denominations threatened to remove their children from the school if Commons would not leave. Commons had become the enemy of local religious authorities. This incident deeply affected Commons, perhaps because of his close ties to the social gospel movement. Afterwards, he stated that he would always be suspicious of Christian "love" of mankind as a motivator for economic change (Commons 1964a 59). Commons was truly surprised that religion would be used to manipulate his economic position. After this, Commons seems to have become aware of the dangers of using religious principles to guide economic policy, because at this time Commons began to disassociate himself from the SGM and the links between religious reform and economics in general. In many ways, Commons's departure from academia represents a turning point in his life as well as his ideas. His time away gave him a perspective and temperance that he had -- to this point -- failed to find.

During his last year at Syracuse, Commons published a series of articles entitled *A Sociological View of Sovereignty* (SVoS). SVoS outlined Commons's general theory of institutions and institutional development. Commons's second theoretical work was much better received than *Distribution of Wealth.* While one critic suggested that it be entitled "An Economic View of Sovereignty," Commons clearly meant for this work to be a general theory of how institutions come into existence, how they develop, and the conditions for their disappearance. In 1934, when writing his autobiography, he would state that the ideas in SVoS would become the basis for his magnum opus, *Institutional Economics*.

The next five years gave Commons the real world experience that he had long demanded that his students take part in. Once again, Commons found that his methods landed him in dire straits and once again his friends bailed him out. Upon reentering the private sector, Commons would later state that he was born again (Commons 1964a, 95). In 1899, Commons got a job publishing a weekly index of wholesale prices for G.H. Shibley. Shibley was an old associate of Commons's and was interested in publishing the index to advocate bimetallism. Commons had long spoken out against free silver and a pure gold standard and in favor of his own unique form of bimetallism (Dorfman 1969, 278). Shibley seems not to have cared that Commons's bimetallism was at odds with that of W.J. Bryant, Shibley's candidate for president.

Years before, in *Distribution of Wealth*, Commons had advocated a bimetallic system of monetary reform to cure the ills of the late nineteenth century economy. Surprisingly for a Midwesterner, Commons advocated a reformed and more elastic version of the old gold standard -- at least early in his career (later Commons would be an advocate of fiat money). This is surprising, because the agricultural Midwestern states had long advocated a silver standard in order to stave off deflation. In opposition, Commons's system used gold as a basis for the value of currency and exchange, while using silver sales and purchases to contract or expand the money supply. Specifically, Commons believed that international trade was an important part of the national economy and that to remove the gold standard would put the United States on a trade standard with lesser nations such as Mexico (Dorfman 1969, 278). On the other hand, Commons saw that a pure gold standard failed to allow for any flexibility for adjustment of the money supply. Commons felt that his bimetallic plan offered the stability of the gold standard while allowing for flexibility of the money supply thorough silver purchases and sale. Also, Commons's early work advocated industrial reform in the form of publicized accounts and public ownership of natural monopolies. It was Commons's theory that this would partially cure the credit cycles and the changes in the money supply that he believed were the cause of the nation's economic woes.

Due to influences external to the argument, bimetallism was already an almost dead issue doomed to failure by the time Commons went to work for Shibley in 1899. As mentioned above, the bimetallism of Shibley and his candidate Bryant differed from that of Commons. The Shibley/Bryant plan advocated the free minting of silver coin in order to widen the monetary base and mitigate the long-running deflation of the late nineteenth century. The debate between the advocates of Bryant's bimetallism and adherents to the principles of the pure gold standard pitted the agricultural West represented by the Democrats against the industrialized East of the Republicans. The long-standing deflation had severely disrupted the Western economy, and its elected officials were looking for an avenue to increase the money supply, thus prompting much-needed inflation.

However, the problem of deflation had already been largely alleviated by new gold discoveries in 1896 and by increased efficiency in the gold refining process (Vedder 1976, 187; Puth 1982, 279). It was Shibley's hope that the index that Commons was developing would bolster the bimetallic cause by illustrating falling wholesale prices. At least initially this proved to be the case; however, a few months later, the index failed to support Shibley's position when prices began to rise. Once again, Commons found himself out of a job.

After Shibley dismissed Commons, he found work with the United States Industrial Commission. Commons was immediately asked to finish an ongoing report on immigration. This report would eventually become Commons's 1907 book *Races and Immigrants in America*. This job required Commons to travel to Chicago and see firsthand syndicalism at work there. During his time in Chicago, Commons was introduced to the practical workings of Marxism through Abram Bisno, a clothing worker turned economist and labor analyst. Never an advocate of any form of Marxism, Commons began to redevelop his idea of conflicting interests as the motivation for social and economic change. Commons understood the economy to operate not in simple terms of a majority and minority between capitalists and laborers, but rather as a myriad of conflicting interests among several groups.

Upon completion of his report on immigration in 1902, Commons was again out of a job. This time he went to work for the National Civic Federation (NCF). Years earlier, a friend of Commons had said that if he ever needed a job, Commons could go to him. Ralph Easley was true to his word, and gave Commons a job working on issues of taxation and labor. Easley had recently cofounded the National

Civic Federation (NCF). The NCF was "an organization of capitalists, philanthropists, and professionals who sought to construct nonviolent solutions to labor conflicts" (Sanders 1999, 91). As an agency dedicated to peaceful labor reform, it seems likely that Commons's experience with the NCF significantly shaped his theories of collective action. The NCF was organized to promote trade agreements rather than costly strikes. The NCF originally accomplished this through collective bargaining, and, later third party arbitration. It was the hope of the NCF that these agreements would cause capitalists to better understand the position of labor and that the public would come to see organized labor as a partner in the industrial process. In this endeavor, the NCF experienced mixed results. A case in point is the 1906 steel strike. Despite the fact that the NCF helped organize the merger that formed U.S. Steel, the corporation still crushed the steel unions. Commons later blamed this loss on the "intellectuals" leading the bargaining process (Commons 1964a, 86-87).

During his time with the NCF, Commons saw firsthand, the problems associated with "academic" interference in labor issues. Commons noticed that labor leaders with academic backgrounds were often more interested in the "class revolution" than they were in the continued sustenance of laborers. As such, labor would often strike in cases where labor would have been better off not striking. Commons found that the critical criterion for a labor leader was to understand the situations and lives of the laborers, something that he believed many leaders did not do. Afterwards, Commons would insist that the conditions of change or legislation of any given transaction should come from its most immediate participants.

This experience would make Commons skeptical of intellectuals in the workplace for the rest of his life. Commons felt that they were more interested in proving their personal theories than in bettering the lives of the individuals that they were supposed to be helping. Commons would hereafter refer to these meddlers as the "fool friends" of labor. More than ever, Commons came to view the role of the economist not as a reform leader but as an advisor to the reform process.

Moreover, while with the NCF, Commons lost his faith in proportional representation (Commons had long advocated proportional representation as a way of increasing democratic participation). Collective bargaining without arbitration did not work, in Commons's opinion (Commons 1964a, 72). The third party was the role that the NCF sought to fill. More than simply a third party to labor disputes, the NCF sought to provide a forum from which disputes could be resolved (Sanders 1999, 92). Again, Commons's experience with the NCF seems have provided much of the basis for his ideas on economic reforms and reform commissions.

In late 1904 Commons -- with the help of his old friends Richard Ely at the University of Wisconsin and the then governor of Wisconsin, Bob LaFollette -- came to the University of Wisconsin. Commons continued to work for the NCF for the next several years, but the majority of his output would be through the university. Ely brought Commons on board at Wisconsin, where he had been teaching, in order to work on a study he was doing on the history of American industrial society. This study was done through the American Bureau of Industrial Research, an organization that Ely had founded.

With the help of Ely, and the resources of Wisconsin, Commons's career started to take off. Commons had long been a friend of the progressive Wisconsin politician Robert LaFollette. When LaFollette became the governor of Wisconsin, he often called on Commons to draft legislation. The first piece of legislation was the Wisconsin Civil Service Law drafted by Commons in 1905. Among other things, this law required testing of all civil service workers to ensure competence, and was one of the first of its kind. The Commons/LaFollette Civil Service Law would become the cornerstone for several later changes to state legislation. The law required civil servants to be independent, educated bureaucrats rather than cronies of the current political leaders. It was Commons's opinion that the success of LaFollette's reforms in Wisconsin owed a great deal to the reform of the civil service. The Wisconsin Civil Service Law would go on to be the model for the National Civil Service Law, a cornerstone of the progressive era reforms -- a law in place to the current day.

The following year, Commons was sent to Great Britain by the NCF, with whom Commons continued to work, as part of a committee to study the organization of public utilities there. The NCF was interested in studying the feasibility of public utilities in the United States. While in Britain, Commons and the committee were lavished with extravagant parties and dinners. The primary effect of this extra attention was to make Commons uncomfortable. The British authorities suggested to the committee that the British public utilities worked well because the nation's aristocracy controlled them, suggesting that these "gentlemen" -- as the British referred to them -- were somehow more capable than the average administrator. Commons thought the system worked well because it was treated as a business concern, with a board of directors who had to be reported to on a regular basis. Despite his admiration for their public works, Commons came back with the impression that British capitalism was decadent. He was amazed that such a system had produced such great wealth. Commons suspected that the British system was a system in decline, a system failing to create any new value; instead, resting on its past accomplishments.

The next year, 1907, while continuing at the University of Wisconsin, Commons went to work for the Russell Sage Foundation. Here Commons was asked to do a study of Pittsburgh social conditions. This work was cut short -- Commons had to leave the study early when professional tragedy struck. A Mr. Sullivan charged Commons with lack of good faith and underhanded investigations. Commons had earlier written a report on the Chicago public utilities with the aforementioned Mr. Sullivan. Inadvertently, he had forgotten to allow Sullivan to preview the report before it was submitted (Commons 1964a, 119). Commons, however, had seen Sullivan's report and had commented upon it. Sullivan in response printed a separate report lambasting Commons for his apparently inappropriate behavior. Commons felt he would be ruined. Nel, after calming her husband down, went over the paperwork regarding the report and found that a clerical worker for the project had forgotten to send a copy to Sullivan. Because the fault was not Commons's nothing came of the incident. As Commons put it, "Thus ended the tempest in my little teapot" (Commons 1964a, 120). While the experience seems to not have drastically affected Commons's thought, it clearly illustrated his concern for maintaining convention and relationships. It can be surmised that Commons was no radical and was very interested in the maintenance of social conventions and fair play.

The following years were busy ones for Commons both inside and outside the classroom. Continuing to work with the LaFollette administration, Commons drafted legislation for Wisconsin public utilities. His public utility law required investigative commissions to determine the rates and methods of production that were "reasonable" -- that is, the best available practices. This work provided the material for the below-mentioned course on public utilities that Commons frequently taught at Wisconsin. Additionally, Commons worked with the Socialist administration in the city of Milwaukee, Wisconsin, on the Council for Economic Efficiency. The Council served as a prototype for the Wisconsin Industrial Committee (WIC), of which Commons was also a member.

The WIC strove to reform workplace regulation and was successful in reforming railroads, public utilities, child labor laws, minimum wages for women, worker's compensation, and worker safety. During this same period, Commons was nominated to serve on the National Commission on Industrial Relations. Finally, in 1917, he was elected president of the American Economics Association, the largest association of its type in the United States. Commons seemed to have appeal with Progressives, Socialists, and the democratic national government under Wilson. From this, it would seem that during the early years of the century Commons's practical work enjoyed almost universal appeal. However, while Commons's prestige among working economists was on the rise, his written works continued to be largely ignored at best and at worst scorned by the academic community.

All during this time, Commons continued to teach at the University of Wisconsin. Here, Commons developed new classes to work around the issues he was currently engaged in, the first example of which was the aforementioned class on public utilities -- the first of its kind, which he developed into a class in 1907. Later, he would develop a class on public value and valuation based around the now familiar idea of socially determined value. Once these classes were developed, Commons left them to pursue whatever new ideas had piqued his interest. This was Commons's concentration on the "omitted factors." Throughout his life, Commons would find a problem of interest to him, study and analyze it, and once he was satisfied leave it and move elsewhere. Commons would refer to this as the "irritation of doubt," a phrase he had found reading Charles Peirce and his work on pragmatism. Peirce was the most-cited author in Commons's classes and would prove the most significant contributor to his method of theorizing (Parsons 1942, 246). From his constant search for the "omitted" factor Commons developed his idea of human motivation, his "strategic factor."

In 1919, Commons published his book on best labor practices. *Industrial Goodwill* represented the culmination of twenty years of on-site investigation of the labor practices of industry. While this book has been ignored by most students of Commons and wholly ignored by the profession in general, it was remarkably ahead of its time in its analysis of the intangible values of the firm. Also to be found within *Industrial Goodwill* is Commons's case for cost-reducing labor insurance and shop safety polices as well as a rudimentary discussion of the intangible values embedded in skilled labor. Within, he suggests that such reforms will result in cost savings for the firm. This last issue has become, in recent years, a significant point of discussion within the "transaction cost" literature, an issue that will be discussed in depth below.

The following year, Commons, with Wesley Mitchell and Malcolm Rorty, founded the National Bureau of Economic Research. The bureau was dedicated to the study of business cycles and to the gathering of related economic data. Despite his role as a founder, Commons had fairly little interaction with the bureau, serving as the bureau's director until 1928 only in name.

It was during this time that Commons published *The Legal Foundations of Capitalism*. It was Commons's intention that this book be his magnum opus. Within this work, Commons outlined the gradual development of the capitalist system from the feudal system that preceded it. Furthermore, *Legal Foundations* contains the first explanation of Commons's basic unit of analysis, the transaction, which is made up of no less than five parties. Finally, *Legal Foundations* gives us Commons's concept of "reasonable value" -- his theory of socially defined value. Commons's "reasonable value" explains value as a function of history and society as well as the current state of economy and technology.

Written when he was 62, Commons had originally meant for *Legal Foundations* to be his final statement on economic theory. However, both students and his peers found it difficult to understand. Because of this, Commons felt compelled to later write *Institutional Economics* (1934) and, finally, *The Economics of Collective Action* published five years after his death, in 1950. *Institutional Economics* was the work for which people would most remember Commons. While not very well received at the time, it has become an often-cited but little-understood staple in certain fields of economic study, an enigma of economic thought. At nearly 1,000 pages, and written in a difficult style, *Institutional Economics* is a challenging read for even the most interested reader. Commons's goal for *Institutional Economics* was to present a theory of economics that would be complementary to existing economic theory. Whether or not he accomplished this is a matter of much conjecture, but it seems that Commons had little interest in the issue (Commons 1990, 1; 1969, 62-64). It seems likely that Commons had no problem with a "multi-paradigm" tool-kit such as that recently outlined by Stanfield (1999). That is, he had no problem with the inconsistencies to be found between his "institutional economics" and more traditional theory using each when appropriate or convenient.

Commons's final book, *The Economics of Collective Action* – written, again, to clarify his ideas to students and critics -- is essentially a simplified version of *Institutional Economics*. However, by the time of its publication in 1950, interest in Commons's work had seriously waned and was overshadowed by the works of the new mathematical economists. This is unfortunate for potential students of Commons's work, as this is easily the most accessible of his writings. If it had been written at the beginning of his career, it seems likely that Commons's influence would be much greater today.

As with the economy as a whole, the late 1920s would be a series of highs and lows for Commons. In 1928, Commons's wife Nel passed away. Deeply affected, Commons left Wisconsin and retreated to Washington to study price stabilization. Commons, along with several other economists, including Irving Fisher, advocated a 100 percent reserve banking system in order to stabilize the rapid deflation that had been occurring. In 1922, Commons had been named president of the National Monetary Association. Fisher's group, the Stable Money Association, which was working on the 100 percent reserve program, was an offshoot of the National Monetary Association (Commons 1964a, 190). The Stable Money Association, whose main purpose was to stabilize the value of the nation's money supply, was financing Commons's work. In order to accomplish their goal, Commons spent a good deal of his time in Washington testifying to the House Banking Committee concerning the Federal Reserve. Commons was in favor of immediate emergency reinflation of the money supply and a separation of the lending and savings functions of the banks. This is now referred to as "narrow banking," a separation of the exchange function of banking from its financial function. Interestingly, this is an idea that is again gaining popularity (Phillips 1995, 175-180).

In 1930, Commons's son Jack, who suffered from paranoia following his time as a foot soldier stationed in Russia during the First World War, disappeared and would have no communication with Commons until a few months before his death in 1945. Jack was among those still fighting in Russia after the war had officially ended. Many of his company froze to death or were ambushed during the night. The experiences of his son changed Commons's attitude. Commons, who had always been a proponent of the war, found the experiences of his son modified his views.

Two years later, Commons witnessed what he believed to be his greatest achievement -- the enactment of the Wisconsin Unemployment Insurance Law. This plan would become the basis for the National Unemployment Law. The bill had been drafted in 1920, but was defeated in each legislative session until 1932. Commons's attachment to the issue of unemployment began with his dismissal from the University of Indiana and developed during his frequent bouts with unemployment at the beginning of the century. Commons saw unemployment as the critical factor affecting the development of social and economic institutions. Commons felt that the unemployment insurance law would remove the threat of unemployment and allow economic and social institutions to move to a higher level. Specifically, he believed that unemployment insurance would reduce the coercive nature of the labor contract, allowing people to work without fear of starvation.

During the same year, Commons had the most severe of his mental attacks and was forced to retire from his position at the University of Wisconsin. Upon his retirement, Commons's students donated $1,500 for travel and recovery. They also established the John R. Commons Economic Library at the University of Wisconsin, which housed all of his written works and the works of his students. With the money he had left over, Commons bought a V-8 Ford with which he would come to endear himself to the local police, as he had done for years with his bicycle (Commons 1964a, 1).

Four years later, in 1936, Commons moved from his house in Madison, Wisconsin, to Fort Lauderdale, Florida. He left behind the majority of his possessions and bought a trailer home. Commons felt at home with the "trailer folk," as he referred to them. He lived simply, returning to Madison a few times to teach summer courses. Finally, in early 1945, Commons moved again, this time to Raleigh, North Carolina, to live with a sister and his formerly estranged son, Jack. That year, while in relatively good spirits, John R. Commons passed away on May 11.

Influences on Commons's Thought

Undoubtedly, the two greatest influences on Commons's thought were Richard Ely and Charles Peirce. Richard Ely was both teacher and peer to Commons. Ely encouraged his investigative and exploratory approach to economics. Moreover, Ely taught Commons a theory of economics that was an evolutionary science. From Charles Peirce, the founder of the pragmatic school of philosophy, Commons gleaned his approach and method of investigation as well as his method of exposition.

Richard Ely was an economist in the German historical school of economic thought, educated by Karl Knies. As such, Ely was well versed in the importance of empirical investigation and fact gathering. Ely's approach to economics would always reflect his upbringing, being heavily laden with empirical evidence and experimental technique. Thus, Richard Ely gave to Commons an economics that was not a pure science but one interlaced with a myriad of social concerns. As Ely put it,

> Economics is a science, but something more than a science; a science shot through with the infinite variety of human life, calling not only for systematic, ordered thinking, but for human sympathy, imagination, and in an unusual degree for the saving grace of common sense (Ely 1926, 2).

Ely continued by defining economics as,

> *Economics is the science which treats of those social phenomena that are due to the wealth-getting and wealth-using activities of man* (italics in orig. Ely 1926, 2).

Ely would explain economics as a science that was concerned with man and his relations to others rather than man's relationship to nature, as was the case with the old Ricardian economics. This is the way in which Commons would define the economic problem. Both Ely and Commons saw economics as dealing with problems of distribution and institutional structure as well as with production. In his work, Commons would always refer to the economics of production as the "home economics" of the neoclassical economics as opposed to the "institutional economics" of man-to-man relations.

Commons's ideas about the scope of economics clearly came from the work of Richard Ely, but Commons also took from Ely the method of economics. It was Ely who pioneered the "look-and-see" approach to economics that Commons would practice throughout his career. Ely also took his classes out into the field to witness economic phenomenon first hand, another practice Commons would continue. Ely clearly believed that this was necessary because of his belief that the economy was a social phenomena with few, if any, hard-and-fast rules. As mentioned above, Ely and the SGM held that the economy was only to be explained by principles that were historical and relative. Ely, however, did not believe that there was no place for economic theory. One of his most famous works, *Outlines of Economics*, was, in fact, one of the most common economic textbooks of the era. Its content is very much in line with the marginalist analysis of the era, but it is interlaced with social concerns. It would seem that Ely meant for theory to be the starting point from which to analyze economic situations, while conclusions could only be drawn from a combination of theory and on-site investigation.

Ely also believed that economic reforms should be based on Christian ideals. He was the driving force behind the above-mentioned Social Gospel Movement. Throughout his life, Ely continued to advocate Christian ideals as a basis for reform. While Commons would not adhere rigidly to this later stance, it is very much in line with his pre-1900 attitude toward economics and economic theory. However, as time went on this would come to be a sore point between Commons and Ely.

After 1900, Ely's influence over Commons waned. After his dismissal from Syracuse, Commons's introduction to the working world made him a much more flexible and worldly man. Most importantly, his experiences jaded his view of Christian values as a basis of reform. From this point on, Commons would refer to his vision for reform as "pragmatic idealism." Specifically, Commons came to have a less antagonistic attitude toward business and its role in economic reform. It seems to have been that Commons's attitude towards social and economic reform became much more democratic rather than authoritarian (see Chapter 5). The drift of Commons away from Ely climaxed in 1909 over the issue of merging Ely's history of labor work with work being funded by the Carnegie Institution of Washington. Commons felt it necessary, while Ely was dead set against it (Miller 1986 34). After this conflict, Commons's and Ely's relationship would never be the same.

In addition to Ely, Charles S. Peirce had a significant effect upon Commons's work. Commons would take his verbose writing style, his repetitive method of explanation, and his ideas about human action that would become a component of his economic theories from Peirce. Peirce is best known as a founder of the distinctly American school of philosophy known as pragmatism -- or as he would call it

"Pragmaticism." Peirce made that distinction in order to distinguish his work from that of William James, which he felt addressed social concerns while he wished to address the methodology of science. The difference between the work of Peirce and James lies in the application. Peirce meant for his work to be a methodological test: Pragmatism, in Peirce's eyes, is a method of doing, a test of truth. On the other hand, James's (and Dewey's) pragmatism is a measurement of value and a philosophy of life and practice.

A working understanding of pragmatic philosophy is critical to understanding Commons's concepts of value and knowledge as well as his expositional form. This is because pragmatism is Commons's theory of human action, which in turn is a basis for his theory of economy. While Commons's views on human action are the focus of the second chapter, a brief digression here to review a few salient points of pragmatic philosophy is warranted.

Pragmatism is a philosophy that finds meaning and value in action; one in which concepts "are to be understood in terms of their practical applications" (Peirce 1998, 1). That is, concepts and ideas only have value or significance when they are applied in practical problem-solving. Peirce defined pragmatism as,

> The opinion that metaphysics is to be largely cleared up by the application of the following maxim for attaining clearness of apprehension: Consider what effects, that might conceivably have practical bearings, we conceive the object of our conception to have. Then, our conception of these effects is the whole conception of the object (Peirce 1998, 300).

The pragmatic philosophy is based in the concept of an active mind. That is, the mind is an active organizer and reorganizer of ideas and impressions. These impressions create a lasting image in the mind, influencing present actions and their future ramifications. Therefore, individuals utilize past experience and future expectations in order to make current decisions. Thus, the mind is constantly reforming its problem-solving apparatus with each new decision. Peirce meant pragmatism to be a test of scientific experimentation. Specifically, the scientist should question the direction and methods of his experimentation to determine whether his methodology seeks to discover new truths or merely is a function of current thought.

Later, both William James and John Dewey would apply Peirce's pragmatic method to the analysis of society. The social pragmatism of Dewey and James took Peirce's pragmatism and applied it to group and individual decision-making in a societal context rather than within the laboratory of Peirce. Dewey and James used pragmatism to determine whether choices lead to outcomes that are socially desirable; that is, to derive a theory of value and valuation. Dewey described outcomes that are socially desirable as being "instrumental," meaning that they have value in promoting the life process (Dewey's pragmatism is the *process* of determining the choices that lead to the fulfillment of the life process).[2] It is the process of using past knowledge and experience *as well as* future expectations to create a set of values that will lead to the betterment of the individual. Despite its patriarchal overtones, Dewey did not mean to suggest that the casual observer can say that any one choice is better than another without reflection or an understanding of past choices, future expectations, and their outcomes. As Dewey puts it,

> The true, real, final, or objective good is no *more* good as an immediate existence than is the contrasting good, called false, specious, illusionary, showy, meretricious, *le faux bon*. The difference in adjectives designates a difference instituted in critical judgement;

[2] For an excellent study of the life of John Dewey and the pragmatic philosophy see McDemott 1981 or Hook 1995.

> the validity of the difference between good which is approved and that which is good (immediately) but is judged bad, depends therefore upon the value of reflection in general, and of a particular reflective operation in especial. Even if the good of the reflective object is different from the good of the non-reflective object, it does not follow that it is a better good, much less that it is such a difference in goodness as makes the non-reflective good *bad*: -- except upon one proviso, namely, that there is something unique in the value or goodness of reflection (Dewey 1971, 326).

Thus, for James and Dewey pragmatism is the process of deriving value from knowledge and learning. Commons, ever the pragmatist, would follow the social pragmatism of Dewey in developing theory and proposing policy while at the same time following the pragmatism of Peirce while investigating the same theories (Commons 1990 150). A pragmatic approach to economic theories is something that Commons clearly considered. In his 1919 book *Industrial Goodwill*, Commons stated, "The fanatic, or crank, or mere 'theorist,' is brother to the autocrat -- he takes one theory and rides it to the death penalty." He continues,

> The sane man is the man of common sense, who is willing to act on different theories, or rather on all the theories, and is willing to investigate and give due weight to all the facts in the light of all the theories. Such a man is what is known in law a "reasonable" (1969, 63-64).

Here we can see both Commons's disdain for academia and his ever-practical and pragmatic attitude. It is perhaps the case that his pragmatic attitude allowed Commons to suggest that his "institutional economics" augments, rather than displaces, conventional economics, despite the fact that the contradictions between Commons's work and conventional economics are well documented (Gruchy 1987, xix-xx; Ramstad 1995, 991-1012; Yonay 1998, 70-74). Furthermore, as stated above, Commons seems to have been aware of this and had little problem with it. Thus it seems that Commons, a pragmatist in all aspects, had little problem combining different sets of theories that contradicted each other so long as they were applicable to a given problem. Pragmatism for Commons became not just a system of value or investigation but a way of life. Commons's students later would remark that Peirce was by far the most common classroom citation he used throughout his teaching career (Parsons 1942, 246; Harter 1962, 216). Peirce's influence upon Commons's work cannot be overestimated.

Besides Ely and Peirce, Commons claimed a myriad of influences. Following the pragmatic method developed by Peirce, Commons would trace all his ideas from their origin to date. That is, Commons felt it necessary within his written works to fully trace the intellectual origins of all his ideas. Commons was an extremely well-read man and took a little from everything he came in contact with. His main work, *Institutional Economics*, makes mention of innumerable economists from Aristotle forward.

Some other influences are certainly worth mentioning, the first being Thomas Malthus. Specifically, Malthus's concept of economic rent and his ideas about human nature would influence Commons. Malthus's theory of rent explained the phenomenon as being a partial function of economic power. According to Commons, Malthus's rents were the result of economic conflict rather than the harmony of Smith and Ricardo (Commons 1964a, 60; 1990, 249). Malthus, again according to Commons, saw mankind not as a creature of reason but of passion. According to Commons, Malthus's great contribution is incorporating passions into economic analysis -- a trait Commons would borrow (Commons 1990, 248).

Third, Commons would elaborate upon Thorstein Veblen's concept of intangible value and much of his general theories of economy. Veblen was the first to write on the intangible aspects of the economy and their relationship to tangible aspects. Veblen understood that the current market value of the firm is based not only on the firm's current product but also upon future expectations of the firm's profitability, and the embedded intangible capital. However, these intangible values did not create any "true" value in the sense of bettering mankind. Veblen thus believed that value could not be understood as a static concept but rather as a socially determined variable. Commons would expand this theory into his notion of "futurity," one of the five components of Commons's theory of economy. Commons's futurity would combine Veblen's theory of intangible value with the pragmatic mind. Commons's notion of futurity and Veblen's theories are discussed in depth in Chapters 4 and 5.

These four authors, while not a complete list of Commons's influences, do give an adequate image of Commons's pedagogues. While Commons was well versed in the writings of mainstream economists from Smith to Marshall, it was primarily from heterodox economists that Commons developed his ideas. Not unsurprisingly, it is with heterodox economists that Commons has had a lasting effect.

Commons's Influence on the Twentieth Century

Despite the lack of influence Commons's ideas have had upon the economics profession, his career as an economist arguably ranks as one of the most influential of the twentieth century. As has been mentioned, John R. Commons would, in name, have a lasting influence upon the "institutionalist" school of economic thought, a school dedicated to studying economics as a dynamic, social process. Along with Commons, Veblen came to be known as a founder of this school of thought. On the other hand, Commons's work has had a lasting influence upon American society as a whole. Perhaps Commons's greatest influences were the many reforms he instigated, reforms that have shaped the modern economy. Within the state of Wisconsin, Commons initiated three major reforms of lasting affect (Harter 1962, 89-129). The first two of these reformed the state's civil service law and the state's public utilities through the newly created Wisconsin Industrial Commission. The third reform created Wisconsin's unemployment compensation program. In addition to his work in the state of Wisconsin, Commons worked in an advisory position with those who drafted the Banking Reform Act of 1933, pioneered modern collective bargaining arrangements during his work with the NCF, and advised a number of graduate students, many of whom went on to do great things.

Summary

In this chapter, this work has provided an overview of Commons and the era in which he lived, specifically the concerns of the times and the working conditions of his life. Commons lived a turbulent life in turbulent times. From the aftermath of the Civil War to the Great Depression, his life was surrounded by significant historical events. Within his personal history Commons had to deal with personal tragedy, health problems, and the loss of several professional positions. Without a doubt, Commons's life affected his work, as will become apparent throughout this study. However, this study does not attempt to suggest that Commons was an intellectual slave of his era. Much to the contrary, this work will show the reader that Commons's ideas transcend his era, and that they are perhaps even more useful today than they were then.

It was Commons's lifelong effort to make that which the law deems "reasonable" more liberated and participatory. It is this that Commons is referring to when he says "I was trying to save capitalism by making it good" (Commons 1964a, 143). Commons understood that while history had shown than the economic process had greatly increased the average individual's ability to participate in the sovereign process, the current situation was less than ideal. Thus, we may safely say that the economist's role -- in Commons's system -- is a provider of information and an investigator of facts. The economist's role is first, to guide change in a way that allows for greater participation in the process of guiding the economy in a direction more accurately suiting the public purpose, and second, as a provider of information to all parties concerned in the process of collective bargaining.

Chapter 2
The Pragmatic Method of Commons's Economics

It may seem frivolous to the casual reader to devote an entire chapter in a study of economics thought to philosophy. This chapter attempts to show that such a digression from the normal subject matter of economics is in fact necessary. This is especially true with regards to Commons's work. As has been noted elsewhere, pragmatism is an essential component of Commons's thought (Ramstad 1986, 1067-1105; Albert and Ramstad 1997, 881-916).

Despite its claim to be a positive science, all theories of economy reveal an implicit philosophy of human action. For a succinct example, take a typical definition of economics: "Economics [is] the study of how people allocate their limited resources to satisfy their unlimited wants" (Miller 1999, 5). Several assumptions are implicit within this statement. The first is that the determination of wants is exogenous to the economic process. More obviously, said wants are assumed to be unlimited. On the other side, resources are also thought to be fixed and exogenous to the economic process. These are only the most obvious of the assumptions that our above-stated definition makes. Despite the fact that these assumptions underlie the majority of economic theory, the reader will be hard pressed to find any discussion of them in an introductory economics text. In fact, one may well argue that philosophical assumptions about human action such as the ones above have come to be regarded without suspicion by the majority of the economics community (and, in fact, the majority of the educated population). To introduce Commons's theory of economy without first outlining the philosophy upon which it is based dooms the study to failure.

Second, Commons's theory of economy is one based upon the idea of the will in action. As such, his theory of human action is critical to understanding his theory of economy. It is the position of this study that without such an understanding, comprehension of Commons's work becomes almost impossible. In fact, in the fifth chapter it is argued that Commons's theory of human action is more than an input to his theory of economy -- it is a component. Kenneth Parsons, a student of Commons, has stated that Commons himself repeatedly pressed this issue (Parsons 1942, 250; Albert and Ramstad 1997, 885-886).

Commons's view of humankind's drives and influences set the stage for his theories of political economy. For this reason, this study treats pragmatism not simply as an influence on his theoretical work but as a component of it. As a pragmatist, he understood that human actions have both antecedents and consequences. That is, as individuals, people are both affected by, and have an effect upon, their social environment. Thus, Commons's theory necessarily becomes an institutional one based in history and with an expectation toward the future. Moreover, economic phenomena become socially and historically relevant -- a function of their social environment. Commons would go further than other writers in the institutional tradition by explicitly examining the role of the individual in shaping institutional reform in his theory of limiting and complementary factors.

Commons gives his theoretical economic agents not only consequences but also explicitly *defined* purpose. As we shall see in the fourth and fifth chapters, Commons's work offers a more systematic discussion of individual human purpose than do other writers of the older institutionalist tradition. This chapter will attempt to show that Commons's application of pragmatism results in a theory of human action that is well developed. More than a blind process of natural selection, Commons's theory incorporates a theory of mankind as having an active role in the shaping of the economic process and the role and shape of institutions. Commons's theory is one of artificial selection, whereby change is the result of individual economic agents. His is clearly a hopeful theory, but at the same time not utopian -- a volitional theory of human action.

Human Nature and Individual Action

As the first chapter has attempted to show, Commons was an inquisitive man. From his youth, he would identify problems and pick at them until he was satisfied. Much of Commons's time as a working economist was spent investigating the economic process and encouraging his students to do likewise. Commons's ideas of human nature would be derived from his observations of his own actions and the actions of others.

Unlike the classical economists who preceded him, Commons did not paint man as the rational, calculating individual of Ricardo and Mill -- the famous lightning calculator of pleasure and pain. According to Commons, mankind was, when unchecked, "capricious, self-seeking, [and] oppressive" (Commons 1967, 60). Moreover, Commons stated that "The Age of Reason ended in the French Revolution. The Age of Stupidity began with Malthus" (Commons 1990, 244). And finally, "Man is not a rational being, as in the Eighteenth Century thought; he is a being of stupidity, passion, and mistake" (Commons 1990, 682). This was no slight on Malthus, but rather Commons's confirmation of the Malthusian view of mankind -- a view that held men as self-seeking, ruled by their passions, and largely stupid (Spiegel 1991, 271-4). This, however, seems to have been a personal view. As we shall see in the next section, Commons's theory of human action suggests an individual who, if not perfectly rational, is intendedly so. Thus, the argument may be made that Commons's view of human rationality is in some sense inconsistent with his economic theory. As we shall see in later chapters, Commons's theory is based upon a largely rational economic agent. While he acknowledges irrational action, there is no developed theory of irrational behavior like those found in the works of Veblen (1899) and Ayres (1978).

Despite the above statements concerning man's irrational and self-seeking nature, Commons was no misanthrope -- far from it, in fact. It was his concern for the well-being of humanity that drove Commons to action. To repeat an often-cited passage, Commons claimed, "I was trying to save capitalism by making it good" (Commons 1964a, 134). Moreover, Commons believed people to be naturally inquisitive beings who would seek out and attempt to correct the problems that confounded them. That is, while most of the time people resorted to general rules of thumb and habit, in the face of adversity they were capable of reasoned decision-making. This last assumption is the prime mover of Commons's economic system. Commons, in his work, suggests that individual action, motivated by adversity, both creates and modifies the existing economic system. Thus, despite Commons's dim view of human intellect and reasoning, he held humanity to be innovative and people's accomplishments worthy of praise.

John Commons's theory of human action begins with the individual in society. His individual can neither be studied solely as an individual in the true sense nor, as we shall see, can he be considered solely as a product of his environment. As Commons states,

> Individuals begin as babies. They learn the custom of language, of co-operation with other individuals, of working towards commons ends, of negotiations to eliminate conflicts of interest, of subordination to the working rules of the many concerns of which they are members. They meet each other, not as physical bodies moved by glands, nor as "globules of desire" moved by pain and pleasure, similar to the forces of physical and animal nature, but as prepared more or less by habit induced by the pressure of custom, to engage in those highly artificial transactions created by the collective human will (Commons 1990, 73-74).

The above reference to the "collective human will" should not be taken to mean that the individual is without a will of his or her own. As we shall see later, individuals have purposes that they use to manipulate institutions. As such, individual choice is a significant factor in shaping the economy, but it is far from being the only one.

Historically, economics has utilized a theory of human action based loosely upon Jeremy Bentham's famous lightning calculator of pleasure and pain. According to Bentham's theory, individuals measure the relative "good" or "bad" of an item based upon its ability to incite either pleasure of pain (Blaug 1985, 299-300). This was the prevailing theory in Commons' time. Among those in this school of thought Commons places Bentham, Senior, Gossen, Jevons, Menger, Bohm-Bawerk, and Clark (Commons 1974, 4).

Bentham's basic principle of human action was the predominant theory of the nineteenth century. Although somewhat modified from its original hedonism by J.S. Mill, the basic concept of man as a self-interested utility maximizer remains the dominant theory in economics today. Since the majority of economists today follow this tradition, this study shall refer to it as the mainstream, or traditional, line of thought on valuation.

Commons questionably traces this line of thought back to John Locke.[3] In doing so, Commons is attempting to show the intellectual reasoning for a non-institutional theory of economy. Specifically, he believed that Locke's idea of human understanding made separate the mind from the world without. Thus, the concept of knowing and hence doing can be separated from the outside world -- that is, according to Commons, in a Lockean theory of human action the tangible world is not critical to the process of deciding. As Commons puts it,

> Thus Locke makes a complete separation of the mind within from the world without. The mind observes itself operating about certain ideas which it combines and recombines from simple ideas to the highly complex ideas of substance, cause, effect, morality, divine law, and civil law (Commons 1990, 16).

Commons continues by suggesting that in Locke's concept, the mind is a mere receptacle of ideas. Thus, we can reasonably surmise that the mind takes from the

[3] I say questionably because this idea is more generally traced to Descarte. However, such points are beyond the scope of this study. For now, we shall take Commons's work as it stands.

outside world and processes, but that the process of knowing and observing has no significant effect upon the observer. If this is true, then we can see that it is reasonable to study the individual truly as an individual. This is the traditional Robinson Caruso abstraction of human action used by economists and many social theorists.

Commons saw the early economists from Locke to his time as having a static conception of thought whereby thought and ideas at any given time could be separated from their social surroundings without significant loss. In this view, neither the flow of time nor human institutions is critical to understanding the process of human action. This is not to say that causation and history are not important. Nor does it suggest individuals do not base current decisions upon the outcome of past decisions or without future expectations. What Commons wished to stress was that the naturalistic philosophy of Locke suggests that it is reasonable for current decisions to be regarded independently of other decisions.

Commons disagreed with the "passive" mind of earlier thinkers, with its naturalistic conception of economics. In its place, Commons took from Pierce and Dewey the pragmatic concept of the active mind that is constantly revising and re-evaluating its ideas. As mentioned above, the basic tenet of the pragmatic philosophy is that individuals take into consideration past and present experiences as well as future expectations in order to discern the variables relevant to current choices.

Commons uses this philosophy to create both a theory of value and a theory of economy. Commons's philosophical outlook was very likely due to Richard Ely's influence. As mentioned above, Ely taught economics as a social phenomenon (Ely

1926, 1-5). More than anything else, Commons was concerned with the interrelation of the various factors of economy. This Commons referred to as the whole-part relationships of the economy. Commons's "parts" in the whole-part relationship are the interdependent variables that make up the "whole" concept. Thus, Commons's system is composed of multi-causal endogenous variables.

In Commons's system, a change in any one of his five principles of economy -- scarcity, efficiency, custom, sovereignty, and futurity -- results in a change in the other four factors. As such, a complete understanding of the economy requires an understanding not only of all the critical components of economy but also of their interrelatedness. Thus, we can consider Commons to be a holist in the sense that he believed the economy to be best understood as a part of the social web within which it lies.

Commons's holist approach toward economic theory is, perhaps, one of the reasons why many find his ideas difficult to understand. One has to understand that Commons's "theories" are not really theories in the strict sense of the mainstream economist. This, however, does not mean that they lack explanatory power. To explain this statement requires some perspective.

Traditionally, the economics profession has taken a very formal approach with regard to the meaning of "theory." Borrowing from the physical sciences, economics and economists have taken theory to mean something that is testable and that provides explanatory power independent of circumstance. This has not always been the case. Commons and the rest of the institutional school of economic thought -- who, according to Commons, had many precursors dating back to David Hume --

took a much wider view of what theory meant. To the modern economist, Commons's ideas do not seem to contain any sort of theory in the traditional sense. His theories contain no basis for analyzing or predicting economic phenomena independent of circumstance. By the standards of modern economics, they lack scientific testability. However, this begs the question of what it means to be scientific.

An Alternative Definition of Theory

Webster's Dictionary defines a theory as "an explanation based upon scientific study or reasoning" (2001, 1485). By this relatively wide definition, Commons's "theories" apparently do fit the bill. Commons's theories are based upon study, and they provide an explanation of economic behavior. However, within the epistemology of mainstream economics, his theories are not scientific. Mainstream economics is methodologically based upon logical positivism. As alluded to above, logical positivism suggests that the validity of scientific study lies in the empirical testing and verification of theories. It is based upon the notion that there are universal truths that can be discovered. Supposedly, through testing, "laws" of economics in the "scientific" sense can be developed that are immutable and universally true. One may safely say that the economics profession sees theory as a set of laws from which we can analyze economic behavior and make predictions about things to come. For example, when economists speak of the "law" of demand, it is held to be universally true. Commons was aware that his "theories" really did not fit the traditional definition of the term, but he employed it because he felt his ideas contained a method of understanding (Commons 1990, 722-724, 730).

Since Commons's time, logical positivism has been dismissed by the majority of natural scientists (Landreth and Colander 1994, 15). In the 1930s, Karl Popper tried to show that one can never "prove" the truth of a given theory because one can never perform all the necessary tests: rather, one can only prove theories false. Thus, the theory that has yet to be proved false is the best theory. However, this begs the question: what does one do with theories that cannot be tested? Does one simply throw them out? Obviously this has not been the case, even, within mainstream economics.[4] As Blaug has shown, this is the case with many of the "laws of economics" (Blaug 1985, 698-699). Moreover, how can one be sure that all assumptions are being tested? Despite the problems with logical positivism, the economics profession has clung to it as a methodology.

As Ramstad (2001) has noted, Commons's work is a type of economic holism. Commons did not attempt to isolate and analyze individual economic variables and actors. He felt that it was impossible to build a theory of economy using the same investigative tools the physical scientists used (and still use). Instead, Commons utilized a method of investigation that has come to be known as "pattern modeling," in which variables are considered as a function of their natural environment and of each other. Pattern modeling attempts not to isolate phenomena but rather to discern the significance of the interrelatedness of things. In this it is consistent with the goals of pragmatism. Stanfield explains,

> Pattern modeling is intent less upon reducing the variables and relationships than expanding upon them. It is an effort to bring into focus relationships or connections that are not evident in the conventional comprehension of the lived-world (1999, 236-237).

Pattern modeling is at odds with the theoretical constraints of logical positivism. It does not assume that there are any universal truths to be discerned from its studies, and it does not seek to make its theories testable. Rather, it is a methodology of science suited to the difficulties of human interaction. It is a method of investigation based upon reasonably sound human psychology.

Pragmatism as Method in Economics

As mentioned above, pragmatism, in essence, is a process of creating mental tools in order to discern good decisions and choices from poor ones. It is concerned with the development and recreation of the means-ends continuum, whereby current actions become the foundations for future actions. Choices that further this process are said to be instrumental (see Chapter 6). Pragmatism in general is an active philosophy that suggests that meaning is to be found through the decision-making skills of groups and individuals. Thus, a pragmatic "theory" of choice and action is a theory that explains a method of discerning good choices from bad choices; it has applications in policy-making as a method of investigation as well as an explanation of economic behavior.

The original pragmatism of Charles S. Peirce was meant to be a method of investigation -- a positive philosophy not directly pertaining to the social sciences. In

[4] As Blaug, 1985and 1997, has pointed out, the theory of demand is unable to be tested and unable to be falsified as stated. Specifically, how does one test all the demand conditions for varying prices at a fixed point in time?

John Dewey, pragmatism is a social process. Dewey, like Peirce, saw pragmatism as a method of choosing, a theory of action and decision. However, Dewey's subject matter, society, has purpose, and as such, the observer affects the observed and visa-versa. Dewey, writing on the method of the pragmatic philosophy stated,

> Although breathing is in fact a function that includes both air and the operations of the lungs, we may detach the latter for study, even though we cannot separate it in fact. So while we know, love, act for and against *things*, instead of experiencing ideas, emotions and mental intents, the attitudes themselves may be made a special object of attention, and thus come to form a distinctive subject-matter of reflective, although not of primary, experience.

He continues,

> We primarily observe things, not observations. But the act of observation may be inquired into and form a subject of study and become thereby a refined object...(Dewey 1971, 13-14).

From the above, we can see that pragmatism is a philosophy that stresses the interrelatedness of things in which emotions and intellect are present. Furthermore, Dewey's statement sheds light upon the importance of method to the pragmatist.

Because of its concept of an active, learning mind, a pragmatic theory of economy requires both historical and institutional analysis. If we are to consider the actions of individuals with purpose, our pragmatic theory of economy is forced to examine the effect of the economy on society and society upon economy, if such a differentiation can even be drawn. This type of analysis presents a difficulty, because it introduces a type of relativity whereby variables are only significantly understood in light of other variables that are also properly understood in light of the original variables -- difficult, to say the least. As a specific example, if value and choice are socially relevant, "truth" in an absolute sense of value or action becomes unknowable.

The constant shift and shuffle of society prevent the social scientist from isolating variables and proving their relationships. As far as the workings of society, there can be understanding, but never in an absolute sense. Gruchy, writing on the work of Commons, had this to say,

> The significance of the pragmatic approach to science can only be appreciated, Commons asserts, when a distinction is made between ultimate truth and pragmatic truth. With ultimate truth, whatever it may be, the pragmatist has no concern (Gruchy 1967, 158).

Commons realized that a pragmatic (or volitional, as Commons referred to it) economic theory could not be a theory in a purely scientific sense from the standpoint of logical positivism. That is because any pragmatic theory of action is not repeatable, due to the necessity of incorporating a specific historical antecedent. Rather, as Ramstad and others have noted, theory for the pragmatist takes the form of a basic set of specifications to guide the student or practitioner in his investigations (1986, 1067-1105).

Consequently, Commons was forced to reject the static theories of value that had prevailed in economics up to his time. Commons's theory of value and his larger theory of economy would be based upon the pragmatist's active mind, a mind that continues to develop with the ongoing life process while at the same time affecting the surrounding society.

It should be noted that the foregoing does not suggest that traditional economics lacks explanatory power, nor does it suggest that Commons himself held such a view. Commons seems to have held his predecessors in the highest regard, and only wished to build on what had already been done. As a pragmatist, he realized the significance of traditional economics but realized that its practical applications would be limited because it neglected the social aspects of the economy. As such, Commons was trying to explain phenomena and ask questions that would be of little interest to the orthodox economist. Methodologically, Commons's work is fundamentally different from more orthodox economic theory. This suggests that the work of Commons is best understood on its own terms rather than on those laid out by traditional economics.

Commons's argument with the classical school can be stated as a point of difference in a single assumption. Commons, and other institutionalists, believed that economic variables, devoid of their social surroundings, lose critical explanatory features. On the other hand, mainstream or traditional economic theory finds it an acceptable loss to separate economic variables from their environment.

In Commons, we can clearly see the expansion of traditional economic thought into something much wider. For example, his first book, *The Distribution of Wealth* (1893), was based primarily upon Menger's concept of human action, something Commons came to consider clashed with his other ideas. By the time he wrote *Institutional Economics* (1934), Commons considered Menger's ideas of diminishing utility and human action to be useful pedagogical tools, but felt that in practice, traditional ideas of human action and value lacked crucial understanding of the economic environment (Commons 1990, 718-722). Furthermore, Commons changes little of the traditional Marshallian supply-and-demand analysis to create his concept of scarcity, one of his five principles of human action and economy. However, again Commons would suggest that an understanding of his concept of scarcity alone does not convey a complete understanding of how the economy works.

The Ideal Type as Theory[5]

Commons's concept of "theory" owes much to Weber. His "ideal type" is a theoretical form different from that used in the natural sciences. From Weber,

> This procedure [the ideal type] can be indispensable for heuristic as well as expository purposes. The ideal typical concept will help to develop our skill in imputation in *research*: it *is* no 'hypothesis' but it offers guidance to the construction of hypothesis. It is not a description of reality but it aims to give unambiguous means for expression to such a description (Weber 1949, 90; italics in original).

Weber's development of the ideal type came from the need to develop a methodology that was capable of incorporating historical analysis. As mentioned above, in the case of the social sciences, Commons believed that variables necessarily become hopelessly embedded within the greater social process (Commons 1990, 722). In this he was in agreement with Weber. Weber's ideal type stems from the inability to develop "laws" from historical observation. Again from Weber, "only those aspects of phenomena which were involved in the 'laws' could be essential from the scientific point of view, and concrete 'individual' events could be considered 'types,' i.e., as representative illustrations of laws" (Weber 1949, 86). Weber was aware that this meant a shift from theorizing in the conventional sense. Weber justified this methodological shift as a requirement of social theory. According to Weber, social theory requires historical analysis, thus making "laws," the goals of conventional theorizing, impossible (Weber 1949, 86-87). Commons also was aware

[5] Dugger (1979) has suggested that Commons's theoretical method better fits the "real type" of the participant-observer method as opposed to Weber's "ideal type." Commons clearly understood his "principles" and "theories" to be abstractions from reality; thus, I refer to them as "ideal types" as Commons did. For an explanation see Commons 1990, 722-725, especially, 724: "Hence the economist cannot construct his ideal type without previous investigation."

of this and seemingly had little problem with it. In his eyes, it fit his concept of economics not as a set of universal truths, but, rather, as a method of investigation. As Commons puts it,

> It [Weber's ideal type] converts the whole process of economic theorizing from a "theory" in the older sense of the logical consistency of reality, to the mere methodology of constructing intellectual tools to be used in investigation. There is no longer a question of antagonism between theory and practice, for theory is only a tool for investigating practice, like a spade for digging up facts and converting them into an understandable system of agriculture. Indeed, a science is not a body of knowledge -- it is just a method of investigation, and its theory is its method (Commons 1990, 722).

Weber created, and Commons utilized, a theory unlike the type of theory used in the physical sciences. Weber's ideal type is a method of discerning truth through abstraction much like traditional theory. The difference is that Weber's ideal type is a broader term. The ideal type is an abstraction from reality that discards only irrelevant data. Thus, the ideal type does not necessarily isolate variables, nor does it suggest that isolation is always improper. The concept of the ideal type is no doubt familiar to many of those well read in the institutionalist economic tradition. The ideal type bears a significant resemblance to the pattern model mentioned above and utilized by many within that tradition.

In the physical sciences, where variables can reasonably be isolated from each other, an ideal type that does so is appropriate. That is, to compare the actions and behavior of an isolated atom independently from its environment is appropriate. The atom does not develop and change its behavior *permanently* upon interaction with its environment, nor does it necessarily change the environment itself. The atom is not cognitively interactive with its environment. Thus, it can be studied on its own without any scientific loss. This is not the case with human beings, however, which change and develop permanently with interaction with their environment. Human beings, unlike the atom, have purpose. As such, the nature of society and institutions become critical variables.

Commons believed that in the social sciences, the appropriate ideal type was both historical and institutional. He considered economy itself as an endogenous variable. Because of their general outlook, it was Commons's (and Weber's) opinion that the critical variables of economics and the broader social sciences could not reasonably be divorced from the social sector from which they derived.

As a theoretical point, the ideal type is not without its problems. Commons realized that the ideal type as a theoretical basis was likely to fall prey to institutional and personal bias because it necessarily forced the theoretician to become a social investigator (Commons 1974, 344-345; 1990, 728-730). He realized that individual theoreticians would be likely to model ideal types based upon their own personal outlook rather than the outlook of the characters in question. Because of this Commons, following Weber, stressed the importance of a *positive basis* for the ideal type rather than basing "ideal types" upon ideas of what ought to be (Weber 1949, 93; Commons 1990, 723). One must first observe to determine which variables are important and which are not.

It may help to remember that while the ideal type is not a theory in the traditional sense, it is still a theory -- that is, a method of investigation. Thus, Commons's ideal type is meant to provide a positive guidance for the investigator. This does not mean that the analysis or prescriptions of economists need be positive.

The purpose is to develop an ideal type that is flexible enough for the investigator to mold it to fit the particular circumstance but rigid enough for serious analysis.

Commons realized that economic investigators, so long as they remained outside the economic process, would find it impossible to keep their theories positive. Because of the economists' separation from the social processes of economy and production, the very questions they would choose to ask and analyze were very likely to be biased toward an ideal type that might be appropriate for the investigator but not for the subject matter. The economist's task must be to first develop a value system that is compatible with the subject matter of his investigation. The academic economist will have a different set of values than the factory worker or the capitalist. Because of this, the economist is likely to weigh the importance of economic variables incorrectly. The investigative process of the economist -- the very questions he chooses to analyze -- will necessarily reveal his thoughts and values. The investigator's pragmatic mind will irretrievably flaw his analysis.

Moreover, Commons understood that even among experienced investigators the critical variables or "ideal types" were unlikely to be the same. Because of this, Commons developed his basic principles of economy so that they would be flexible enough to compensate for different situations and different investigators while at the same time providing positive guidance for the practitioner. Commons's five basic principles of economy -- futurity, scarcity, efficiency, custom, and sovereignty -- become the basic tools or theories that economists could use to analyze transactions, Commons's basic unit of economy. In the next chapter, we will see that the flexibility of Commons's principles of economy will become their greatest weakness. While

Commons takes great care to define his principles of economy, the flexibility of his part-principles create ambiguities for the student of Commons and likely have contributed to the lack of interest in his work.

Toward a Theory of Economy

From Peirce and Dewey's pragmatic mind and Weber's ideal type, Commons developed not only his method but also his basic principles of economy. From their work, Commons developed a theory of economy that would fit his theory of human action. As he realized, any such theory would have to be evolutionary, historical, and institutional, at the same time more than a body of knowledge, but also a method of investigation.

Commons named his five basic principles of economics scarcity, efficiency, custom, sovereignty, and futurity. Combined, they comprise his theory of willingness, or human action. Their purpose is to guide the investigator in the analysis of the transaction, Commons's basic unit of economy. As Commons explains it,

> These five part-principles constitute, in their interdependence, the whole of the principle of Willingness. This, as concept, is the complex attributes of human beings. As principle, it is the expected repetition, with variability, of the total of all human acting and transacting within the limiting and complementary interdependence of the principles of Scarcity, Efficiency, Working rules, Sovereignty and Futurity (Commons 1990, 738).

We begin with the part-principle *scarcity*, which Commons defined as the ratio of the number of items that are desired to the number of the same item currently being produced (Commons 1990, 737). In a very loose sense, we can liken this idea to the modern economist's notions of supply and demand. Commons himself directly suggested the relationship of the part-principle of scarcity to the traditional theories of supply and demand (Commons 1990, 75). However, he believed that there were far too many relevant external forces to let his principle of scarcity go at that. It was in order to endogenize the relevant social variables that Commons created the principle of scarcity. Specifically, Commons wished to endogenize custom, production conditions, the legal environment, and expectations of performance.

Commons traced his concept of scarcity to Carl Menger. Speaking on the development of the part-principle of scarcity, Commons had this to say;

> In a money economy, as in Menger's commodity economy, Demand and Supply cannot be measured directly, but the effects of their variations are measured. This measurement of effects is Price, so that price is the measure of the variable relations of Scarcity, and is the pecuniary equivalent of his marginal utility (Commons 1990, 381).

Commons's concept of scarcity is a theoretical tool for analyzing the price system. Thus, it obviously bears resemblance to the omnipresent supply-and-demand model. However, according to Commons, the concept of price only has relevance in the money economy and does not convey value in any true sense. Commons suggests that money clouds the true nature of production and consumption (see Chapter 3). He states that this is because prices are the only truly observable measure of scarcity (Commons 1990, 262). But because money prices do not convey true values, the signals prices send are socially relative and not true signals of value. Commons explains,

> We find, on examination, that by nominal value what they really meant was scarcity-value, depending on the institution of private property whose measure is a unit of another institution of scarcity-value, money.... Each commodity, including money, has its own changing scarcity-value. Scarcity itself is a changing social relation

> between quantity wanted and the total quantity available in any or all bargaining transactions (Commons 1990, 261).

Note that in the above Commons refers to money as a commodity. This is an inconsistency in his analysis that will be returned to in the third chapter. For now, the above illustrates that Commons believed nominal prices represent scarcity-values that in turn are socially relative. Therefore, neither production nor consumption is necessarily geared toward its highest-valued use. Commons suggests that while supply and demand may make for tidy analysis, the theory's explanatory power is limited (Commons 1990, 261).

Thus, Commons's concept is much wider reaching and more flexible than the traditional theories of supply and demand. It does not require the traditional assumption of *ceterus paribus*, or "all things being equal," nor does it make the rather dubious assumption that money prices reflect the real prices of production and consumption. Rather than purporting to be an economic "law," Commons's principle of scarcity is a method of analyzing the current conditions of market redistribution of resources as a part of total human action. This last part is critical. As mentioned above, Commons saw each of his five basic principles of economy as the critical components of what he calls the whole-part relationship of willingness.

The whole-part relationship is Commons's way of endogenizing all relevant variables. In his system, human action cannot be understood without an understanding of all the parts in the whole-part relationship. In explaining to both his students and his readers the meaning of the whole-part relationship, Commons liked to relate one of his many automotive stories. He explained the whole-part relationship as functioning like the engine in his automobile -- a failure in any one of the systems of the engine would cause it to cease working. For instance, if there is a failure in an ignition wire, the engine stops. We cannot isolate the functions of the engine with regards to its operation; all its parts are dependent on each other for the proper functioning of the whole.

The same goes for the economy. According to Commons, we cannot understand scarcity as a human action without an understanding of the other four parts of the whole-part relationship. Understanding the principle of scarcity is useful and necessary for understanding the economy as a whole, but, like the ignition wire to the engine, it alone does not cause the economy to operate.

Each of the part-principles is really, then, not a theory in the strict sense, but rather an "ideal type" as outlined by Weber. Scarcity, for example, is an idealized conception of the market exchange process. Each part-principle is a useful tool in understanding, but cannot wholly convey truth. To understand human action we have to go further than just the principle of scarcity -- we have to understand the whole of willingness. In addition to scarcity, Commons developed the concepts of efficiency, custom, sovereignty and futurity.

He defined *efficiency* as the ratio of input to output (Commons 1990, 738). Commons also referred to efficiency as being a "technical social process" (Commons 1990, 270). Efficiency is measured by the ratio of use-value as output to man-hours as input, where use-value is the produced wealth, or increased power over nature, and man-hours are the average hourly wage of all labor engaged in production, transportation, and delivery (Commons 1990, 259). Thus, in Commons's terminology an increase in efficiency could result from either a reduction in inputs to produce a fixed total output or an increase in total output with a fixed quantity of inputs. Therefore, changes in efficiency occur irrespective of prices, prices being a residual effect of changes in efficiency. The term use-value is opposed to the term scarcity-value, by which Commons meant prices. Furthermore, Commons, borrowing from Marx, did not consider the contributions of selling, buying, or financing product to add to man-hours (Commons 1990, 284-285).

Commons's efficiency is his ideal type of the production process. We can see a loose similarity to the modern economic concept of the production function. However, efficiency does more than state the relationship of inputs to outputs because it is only a part of willingness, or total human action. Efficiency is the total social process of production. The nature of production is thus bound up not only with inputs and outputs but also with the values of the other four parts of the whole-part relationship. For example, changes in scarcity will change the nature of production and hence efficiency. Commons's notion of efficiency is not a static concept but rather a dynamic social process and a method of investigation. It is an excellent illustration of pragmatic economics in action.

Commons traced his concept of efficiency back to Ricardo and Marx. Commons considered Marx the first economist to have gotten production -- expressed as the concept of efficiency -- right (Commons 1990, 275). However, one should really not press Commons too far on this point. What Commons seems to mean is not Marx's concept of surplus value, or the labor theory of value. Rather, like Marx, he seems to be suggesting that the system of relative prices masks both the nature of production and of value (Marx 1905, 234). Commons seems to be in agreement with

Marx that it is not prices that determine the nature of production, but rather the existing state of technology. That is, the institution of money and money prices do not convey the true nature of production, but that production determines the quantity of money and prices. Moreover, prices fluctuate freely apart from production. From Marx,

> If the mass of commodities remain constant, the quantity of circulating money varies with the fluctuations in the price of those commodities. It increases and diminishes because the sum of the prices increases or diminishes in consequence of the change in price. ... A rise or fall in prices of a number of leading articles, is sufficient in one case increase, in another to diminish, the sum of the prices of all commodities, and therefore to put more or less money into circulation (Marx 1905, 134).

According to Commons, this is because money prices are socially determined, while the existing state of technology as well as the current social and legal environment, determine the mode of production. Thus, in Commons's system, prices become independent from production.

Commons felt that the Marxian theory of production -- that the mode of production is independent of the money economy -- when limited to a part-principle of economy remains a useful pedagogical tool. Like Commons's principle of scarcity, efficiency is to be understood as a tool or a method for the economist. It alone does not fully convey an understanding of the economy; rather, it is part of a method for understanding the economic process.

Commons describes the third of his principles of human action, *custom* or working rules as,

> The concept of Custom is that binding force which groups of individuals have over individual members; but the principle of working rules, guided by habitual assumptions, is the repetition, with

> variability, of the acts and transactions of individuals in so far as this binding force of the group continues to operate (Commons 1990, 737).

In Commons's principle of custom, we can see pragmatism directly applied to the economic problem. His custom is a wider application of his "working rules," or the traditional ways and means of the individual. As a part of the whole process of willingness, or human action, Commons states that "working rules" dictate the current state of economy. Commons's concept of "working rules" reconfirms his basic premise that economy is a socially created process. Because of this, production, exchange, and the legal system are all functions of past experience and knowledge. Custom is linked to Commons's other part-principles as a component of a larger social process. Thus, both law and the price system become historically significant and dependent.

This is no small statement -- the suggestion is that our current market system is not necessarily inherent or a natural state for humanity. As Commons puts it,

> Competition is not Nature's "struggle for existence" but is an artificial arrangement supported by the moral, economic, and physical sanctions of collective action. The theory of free competition developed by economists is not a tendency towards equilibrium of forces but is an ideal of public purpose adopted by the courts, to be attained by restraints upon the natural struggle for existence (Commons 1990, 713).

This position has been argued – perhaps more effectively -- since Commons's time in economic anthropology (Polanyi 1944 in Dalton 1968, 26-37). In his work we can see the direct link between pragmatism and its concept of the active, learning mind and a theory of economy. In other words, in Commons we find the first methodical answer to the question: "Why are institutions important?" If values are historically significant and the majority of individual behavior can be attributed to traditional ways and means, a study of the institutions of society becomes critical.

Sovereignty, Commons's fourth part-principle of willingness, is similar to his concept of custom in that it also refers to the repetition of action. However, sovereignty refers not to the accepted actions and ways of individuals and groups but rather to the actions of legal superiors to legal inferiors. For Commons, sovereignty refers to the controlled use of physical force as a binding economic constraint.

Up to this point, this study has analyzed Commons's later works: *Industrial Goodwill* (1919), *The Legal Foundations of Capitalism* (1924), *Myself* (1934), *Institutional Economics* (1934), and *The Economics of Collective Action* (1950). In these works, Commons had abandoned many of his early ideas. They represent Commons's mature writings, and as such will be the main focus of this study.

Commons originally developed his theory of sovereignty in a series of articles entitled *A Sociological View of Sovereignty* (SVoS) in which he developed his theories of institutions and institutional development. For the majority of his ideas, it is a mistake to suggest that the early works of Commons can be compared directly to his later works. In his early years, Commons advocated Ely's radical democratic forms of governance. As mentioned in the first chapter, Commons backed off from Ely 's more radical viewpoint later in life. Commons's concept of sovereignty, unlike many of his ideas, dates back to his early work. As such, a brief review of Commons's thought with regards to sovereignty is warranted.

As mentioned earlier, Gonce (1996) recognized the philosophical break in Commons's work. Commons made significant changes in his ideas around the turn of the century. It is arguable that SVoS marks the beginnings of his mature works. Within SVoS we find Commons's basic conception of institutions, institutional development sovereignty. Sovereignty, according to Commons, contains three conceptions: coercion, order, and right.

To understand Commons's part-principle of sovereignty we need to first understand his theory of institutional development. Commons's theory of institutions owes much to Veblen (1898), as Commons admitted (this issue is developed further in the sixth chapter) (Commons 1967, 13). Consistent with his theory of the individual, Commons's institutions are neither the sole development of individuals nor are they socially derived. Commons states,

> Institutions are not mechanical organizations imposed from without, but are definite modes according to which persons deal with one other.

He continues,

> An institution has first, a body of accepted beliefs, which color and shape the individual's desires from infancy; second, a group of material products, designed to satisfy these desires; third, an organization which sets the alignment of individuals toward one another (Commons 1967, 4).

In Commons's writings, individuals are capable of making decisions, but it is society that forms the tastes and preferences as well as providing the choices that are available to the individual. As we shall see more fully developed in Chapter 6, Commons's view is consistent with the concept of "bounded rationality" whereby economic agents make rational choices from limited information sets. In Commons, institutions develop as a response to the development of mankind. From Commons,

> Single passions and desires did not stand out alone in the mind of the hordes-man, because he had no institutions to develop them

> separately. His mind was homogeneous like his society. Religious, political, sexual, industrial activities were all concerned with the same small number of fellow-men; no definite times in the day or year were set apart for each .... But with the civilized man social institutions are both the condition and expression of self-consciousness (Commons 1967a, 5).

Thus, as mankind develops in his self-consciousness, his institutions develop to reflect his more advanced tastes and preferences. The development of these tastes and preferences come with the development of private property (Commons 1967, 10-12). Private property in turn develops out of human realization of the usefulness of things and their local scarcity that incites hoarding (Commons 1967, 7-10). Therefore, we can say that institutional development in Commons originates in human self-consciousness. This, in turn, leads to the development of private property and, in turn, forces the development of institutions that have the effect of reinforcing human self-consciousness. The development of an institutional structure makes the concept of sovereignty possible, as said structure defines the modes of conduct that individuals act within.

Thus, through the principle of willingness, social institutions provide individuals with expectations about the appropriateness of their actions. Sovereignty as a theoretical concept is both a binding constant and a positive endogenous variable contributing to the actions of the individual economic agent. In short, the actions of the state become Commons's part-principle of sovereignty, that being the exceptions of the rights and limitations of individuals and groups.

Finally, Commons's concept of *futurity*, like custom and sovereignty, involves the repetition of action. Futurity, as the name implies, is the expectation of future action and performance. Commons went so far as to equate futurity with pragmatism

(Commons 1990, 152). Futurity is the consideration of the practical effects that any given item will produce.

It is upon his concept of futurity that Commons bases both the ideas of intangible value and reasonable value. Both theories are based upon the idea that true value is to be found in the expected usefulness of an item. Commons placed his theory of price determination within his discussion of futurity. All three of these theories are discussed more fully in the third chapter. Commons did not believe that all choices are the result of expectations. Only choices that are critical or somehow extraordinary require the individual to make active choices. For the majority of choices, people rely on habitual patterns of behavior. Commons referred to these two modes of choice as routine and strategic transactions respectively.

Limiting and Complementary Factors

While the five aforementioned part-principles represent the constraints of human action, Commons's theory of limiting and complementary factors is his theory of human action. Commons's pragmatism led him to believe that it is the difficulties in everyday occurrences that prompt individuals to act. He referred to these difficulties as limiting factors. It is important to understand that Commons's theory is pragmatism applied as a theory of economic action. Moreover, as elaborated in the sixth chapter, it is very compatible with the theory applied by Veblen.

Specifically, limiting factors are restrictions that, if alleviated, would increase either efficiency or scarcity in one way or another. Upon the correction of the limiting factor, it becomes one of a host of complementary factors. These complementary factors refer to the traditional ways and means of the individual. As Commons explains it, "The limiting factor is the one whose control, in the right form, at the right place and time, will set complementary factors at work to bring the results intended" (Commons 1990 628). The limiting factor is a constantly changing variable that incites human action; it is the current problem that is in need of solving.

To explain this, Commons often used the analogy of a cantankerous automobile engine. The limiting factor may be found in the ignition, the fuel system, or the driver (Commons 1990, 89-90). Whatever the problem, the limiting factor is causing the system to fail; a correction of the limiting factor will cause the system to operate. Thus, in Commons's theory the part is unavoidably linked with the whole. The car will fail completely with a failure of any one of its individual components. Based in pragmatism, Commons's theory suggests that humans actively choose when confronted with new or unique problems. In the presence of normality, individual choice reverts to traditional ways. The interdependence of limiting and complementary factors leads Commons to suggest that the working of the economy is not the sum of its parts but the multiple of all its parts (Commons 1990, 629).

The concept of the limiting factor is Commons's prime mover of economy. The concept of the limiting factor is the method by which institutional change and economic action occurs. Commons went so far as to suggest the theory of limiting and complementary factors embodied the whole of political economy (Commons 1990, 634). This discussion will be taken up again in the fifth chapter. For now, we can say that Commons's position is that mankind shapes his surroundings by the process of artificial selection constrained by the five part-principles of willingness.

Summary

From the above, it should be clear that Commons utilized a philosophy of economic action perhaps not in conflict with that of mainstream economics, but certainly different from it. To understand Commons's economics, one first needs to realize that social and historical circumstances are an essential component of the analysis. Without such understanding, any potential answers his analysis may give become virtually meaningless.

In this chapter, this study has shown that Commons's theory of economy is based squarely upon the philosophy of human action known as pragmatism. Moreover, this chapter has attempted to show that Commons's theory of economy based upon this philosophy is not a "theory" in a sense traditionally employed by conventional economics. Rather, it is based upon Weber's concept of the ideal type, a method that Weber believed was a necessary course of action where historical analysis was concerned. Commons, who believed that historical analysis was necessary to understanding economics, employed Weber's method. This does not, suggest that his "theories" lack explanatory power, but rather that they require an understanding of "holistic" analysis. A system has to be understood as a complete entity rather than as the sum of its parts.

Furthermore, it is suggested here that Commons's theories were meant to be both an investigative method and a theoretical structure as typified by his five "part-principles" of economics. Each of these five principles will be discussed further in the next chapter, but for now they illustrate Commons's constraints upon individual action, constraints that may either bind or expand human action. They are drawn from Commons's view of pragmatism with its unique concept of an active learning mind producing an individual who is both a product of his culture and an active choice-maker.

Beyond being a method of investigation, Commons's five part-principles offer the individual the guidelines by which to act upon the limiting factors that occur in his day-to-day actions. The limiting factor is the impetus that causes the individual to act and to prompt change. In this way, the individual acts upon the community -- he has consequence -- in addition to simply being acted upon. Because the individual thus becomes a function of his environment, institutional analysis becomes not only desirable but also necessary. Commons's view of human action forces him to form a holistic theory of economic action.

Commons's adaptation of Weber's "ideal type," or the "pattern model" of the modern institutional economist, conveniently creates for Commons an avenue with which to analyze variables as a part of their environment. Commons's "pattern model," consisting of the five part-principles mentioned above, becomes the basis of Commons's economic thought.

Commons's five part-principles are interdependent and form a type of holistic economic thought whereby the economy, society, law, ethics, and expectations are inseparable. It is these five part-principles that form Commons's theory of willingness. He explains this as "This (Willingness), as concept, is the complex attributes of human beings" (Commons 1990, 738). However, Commons misleads the reader, as willingness is not an attribute of human beings but rather represents the forces that act upon and are acted upon by individual human action.

We have seen that Commons's theory of human action, upon which his theory of economy is based, is a reasonably complete theory of human action. It is based soundly upon his interpretation of pragmatic philosophy, from which he developed working principles of economics, thus making pragmatism a component of his economic theory. Commons's part-principles of economics, scarcity, efficiency, custom, sovereignty, and futurity, are not theories in the traditional sense. Rather, they represent a method of human action. For Commons, they are the critical factors that influence willingness.

In the next chapter, this study will show that Commons converted the theory of limiting and complementary factors into the theory of strategic and routine transactions. The strategic transaction, for Commons, is the theory of the limiting factor in action. Perhaps unnecessarily, Commons felt the need to differentiate between his theory in principle and in action. Additionally, we shall see that Commons utilizes the theory of strategic and routine transaction to explain the origins of value, the expansion of the market, production, and institutional development.

Chapter 3
Commons's Economic Theory

In this chapter, this study outlines the economic system of J.R. Commons. This is a difficult proposition, as anyone who has read Commons will attest. Throughout Commons's written works, he jumps from topic to topic with little to no concern for the reader's well-being, much less his understanding. Commons will define and re-define the same word several times, often in vague terms. This chapter attempts to present the basics of Commons's system in a manner comprehensible to the average reader schooled in the principles of economics. It is not the purpose here to analyze or criticize Commons's theoretical work but only to present it to the reader; analysis and criticism will follow in the fifth chapter.

Here this study links the part-principles of the last chapter to Commons's basic economic unit, the transaction. It will show that Commons's transaction is his theoretical basis for the socioeconomic relationships that occur in the economy. Moreover, this chapter will show that his transactions represent separate theoretical constructs designed as reference points from which to conduct analysis of given economic phenomena. That is, this chapter attempts to show that Commons gives his students not only a theory but also a way of doing economics.

Additionally, in this section, Commons's complex concept of *reasonable value* is explained. While not a critical component of Commons's system, it is perhaps his greatest and most original contribution to economic thought. Commons's conception of value was a product of his years of developing legislation for the state of Wisconsin where he learned to understand the economy as socially legislated process, a process of bargaining and compromise. It is perhaps the case that much might be cleared up if one were to add the word "socially" before "reasonable" to Commons's general theory of value as both socially derived and relevant, rather than utilitarian as in traditional economics.

This study will attempt to show that Commons's system is one that necessarily combines the principles of traditional economics with those of both law and ethics. Because of his view of human nature outlined in the last section, Commons's system of economy led him to a system not only of value but also of an economy that is both socially derived and socially relevant -- an economy that has been created, encouraged, and constrained in the public purpose.

Transactions

Commons's concept of the transaction, while a critical element in his economic system, was not developed until late in his career. As has been mentioned above, Commons's earlier work dealt mainly with historical studies and expositions of his economic investigation. It is not until his *Legal Foundations of Capitalism* in 1924 that Commons's theoretical system based upon his concept of the transaction seriously begins to take form.

As the title suggests, *Legal Foundations* deals primarily with the legal history of exchange, property, and ownership. However, it is here that Commons initially makes the distinction between the money economy and the production process. This was nothing new: the distinction had been made by Veblen, and by Marx before him. Commons, however, takes this distinction in a subtly different direction. In his earliest exposition of transactional analysis, *Legal Foundations*, Commons separates these two aspects of the economy into actions guided by authoritative and authorized transactions, respectively. Treading in waters originally forded by Marx, Commons provided a detailed explanation of how the money economy, guided by authorized transactions and typified by the operations of the market, is a relatively recent offshoot of the wider production process. According to Commons, the market economy as we know it is not the result of the "spontaneous outcome of individuals' propensity to truck, barter and exchange," to paraphrase the famous passage from Smith, but rather it is, as Karl Polanyi later stated "an instituted process" (1957 in Dalton 1968, 139-174). However, unlike Marx and Veblen, Commons painstakingly traces the historical legal steps taken in the creation of the current capitalist system from the time of the Norman Conquest in 1066 to the time of publication (1924) as proof of his thesis.

Despite his lengthy discussion, the transaction or transactional analysis was not Commons's primary purpose in *Legal Foundations*. Rather, he was looking to develop his theory of value, namely, his "reasonable" or "volitional" theory of value (to be discussed in depth later,) leaving his authoritative and authorized transactions largely unexamined. It would not be until *Institutional Economics*, published when Commons was seventy-two years old, that we find the fully developed theory of the transaction.

In *Institutional Economics,* Commons's theory of the transaction is for the first time fully developed. Commons describes his "transaction" as having developed from the earlier concept of exchange as typified by Marshall's equilibrium of supply and demand (Commons 1990, 55-56). It is Commons's claim that the neglect of the details of the exchange process by Marshall and his predecessors comes from a misunderstanding of the terms "ownership" and "wealth" in modern society. This neglect, according to Commons, stems from the misunderstanding of economy as solely as a set of man-to-nature relationship rather than its more correct characterization as a set of man-to-man relationship.

Commons traces the confusion of economists back to the meaning of property, which traditionally referred to "corporeal" property and to the assumption that possession equals ownership. As stated above, Commons felt that the basis of ownership lay in the principle of scarcity. That is, to own something is, in part, the ability to withhold its use from some other. This jibes with Commons's theory of economy based not in competition, as has been the case with traditional economics, but rather in monopoly.

The second privilege of ownership is the good's "use-value," as Commons termed it. Use value is the value that the owner of the good in question derives from its use. Therefore, according to Commons, ownership bestows both a scarcity value in terms of the owner's ability to withhold the good from others and also a use value in terms of the good's usefulness (Commons 1990, 252-253). It was Commons's opinion that the scarcity value of ownership did not provide any sort of "wealth" either to the owner or to society in general; it is, however, a saleable asset. This discrepancy, according to Commons, creates a problem: While use values create wealth and "true" value, it is scarcity values that dictate the level of production through prices. Thus, Commons, like Marx, saw the money economy as clouding the true nature of the production process. Commons argued that it is only a good that has scarcity value that will be produced, for without scarcity value the good will have a market price of zero. As such, there would be no desire or need to own such a good. We can see this phenomenon in the modern concept of the "public good" that is observed to have value but no price -- clean air is an example.

Again, it is not the scarcity value of the good that creates wealth in any true sense, it is the usefulness of a good that creates wealth. Commons's opinion is that it is the building or managerial process that creates wealth rather than the exchange or bargaining process. The scarcity value of ownership, Commons thought, was best defined as an asset, in that it has a positive economic value and can be sold, traded, or held.

In making this distinction, Commons separates the economy's "wealth-producing" function into the concept of the managerial transaction and the money or scarcity value of "assets" into the concept of the bargaining transaction. From the last chapter, we know it is through the occurrence of Commons's strategic transactions that value is in either sense created. In Commons's terminology, the strategic transaction is a transaction that occurs in the correction of a perceived limiting factor. The strategic managerial transaction creates use value by increasing the efficiency of the production process by either expanding output or lowering costs. On the other hand, the strategic bargaining transaction creates scarcity value by bestowing upon its owner the right to withhold its use from others who would wish to use it

Commons saw the exchange process as involving not a harmony of interests but rather a conflict of interests as well as a set of mutually dependent interests. A conflict of interests is created because if one man can own something, another cannot own the same thing. However, the actual process of exchange brings with it mutually dependant interests, as all involved parties have an incentive to resolve the transaction. When a sovereign who is a social representative grants property rights, the exchange process takes on a social significance. This is because the right to ownership is constrained by the public purpose (by "public purpose" Commons means, in this case, the expectation of order). More than a static concept, the transaction and the legal concept of ownership contain an expectation of future performance and future transactions. That is, current transactions set precedent for future transactions as well as defining the level of performance that can be expected.

Thus, according to Commons, the basic unit of economy, his transaction, must incorporate 1) a conflict of interest, 2) a consideration of the mutually dependent interests, and 3) expectation of order. With these considerations in mind, Commons developed his theory of the transaction that became the basic unit of analysis in his economic thought.

In *Legal Foundations,* Commons described the transaction as being "the physical dimensions of the will in action at a moving point in time…" (Commons 1974, 80). Ten years later, Commons would define the transaction as,

> they [transactions] are the alienation and acquisition, between individuals, of the *rights* of future ownership of physical things, as

determined by the collective working rules of society (Commons 1990, 58; italics in original).

Commons's transaction is a difficult concept to grasp. It is neither a solely static nor a solely dynamic concept. It is neither an individualistic theory nor is it purely environmentally or socially defined. Commons's transaction is, in short, the individual will acting within the legal and social confines of society. Thus, we may say that Commons's transaction is the physical manifestation of human interaction.

Commons's transaction is a social process, including not only buyers and sellers but also an arbitrating and defining authority. According to Commons, transactions only have significance when legal right is transferred. It is not the exchange of physical property that gives meaning to the transaction; rather, it is the legal transfer of ownership of the physical property. For example, when purchasing a car, the transfer of the keys to the vehicle is not itself the transaction. Were you to drive the car away at this point, you would soon find yourself in trouble with the law. Without the legal right of ownership in the form of a title, no real change in ownership has occurred and, as such, no transaction has occurred. Exchange in our economy, according to Commons, is a legally regulated process in which only socially approved exchange is allowed to occur.

Commons's theory of the transaction developed over his later years. In *Institutional Economics,* the fully developed transaction employs five economic agents: two buyers, two sellers, and an arbitrator. As Commons explains,

> A transaction, then, involving a minimum of five persons, and not an isolated individual, nor even only two individuals, is the ultimate unit of economics, ethics and law. It is the ultimate but complex relationship, the social electrolysis, that makes possible the choice of opportunities, the exercise of power and the association of men into

> families, clans, nations, business, unions, and other going concerns. The social unit is not an individual seeking his own pleasure: it is five individuals doing something to each other within the limits of working rules laid down by those who determine how disputes shall be decided (Commons 1974, 68-69).

Commons's transaction, unlike more orthodox theories of exchange, includes a legal interpretation of economic action. Additionally, his transaction is in a very real sense a *social process,* as it occurs within the confines of the laws of society and does not occur at a fixed point in time. Furthermore, Commons's legal theory of the transaction includes the expectations and legal recourse of exchange. As Commons explains, the terms of the transaction define what participants may, must, can, and cannot do (Commons 1974, 68).

The transaction is an exchange, but it is also much more than an exchange. As Commons notes, in modern society exchange only has significance when it has legal backing. Thus, Commons does not deny the validity of traditional market analysis, but only that it fails to capture critical elements of the exchange as a socially defined and delineated process. The transaction is more than a simple exchange -- it is a legally and socially defined contract.

When the exchange of physical goods is tantamount to ownership, then Commons suggests that the social institutions that guide exchange may be assumed away. That is, when property rights are well defined and information is present, accessible, and able to be processed, the social aspects of exchange may be assumed away. Thus, we surmise that in nations such as the United States, where the legal environment as well as the working rules of society are well defined, it may be appropriate - in Commons's mind - for some transactions to be analyzed in the traditional theory of exchange as typified by mainstream economics. This would seem to suggest that Commons felt that traditional economics represents a special case in institutional economics. Whatever the case, Commons's transaction is significantly differentiated from that of orthodox economics.

Commons divided his basic concept of the transaction into three types, each of which represented different legal-economic relationships that occur within the economy. The first of these, the *bargaining transaction,* refers to exchanges that occur between legal equals, the defining part-principle of which is scarcity. The second, the *managerial transaction,* refers to the exchange process between an individual legal superior and a legal inferior. The defining part-principle of the managerial transaction is efficiency. And finally, Commons's third transaction type, the *rationing transaction,* like the managerial transaction, involves the actions between legal superiors and inferiors. The rationing transaction, however, differs from the managerial transaction in that it involves groups of individuals. The rationing transaction distributes wealth and benefits from the legal dictates of legal superiors to legal inferiors (Commons 1990, 54-68). It would appear that the guiding part-principle of the rationing transaction is sovereignty, although Commons neglects to mention it.

No one of these transaction types can be wholly understood without understanding the others. Each is a theoretical construct used as a basic point of analysis. Continuing in his holistic vein, Commons felt that all three transaction types are inseparable components of any given concern. A consideration of only one transaction type at the cost of the others will only give a partial explanation of the given economic phenomenon. The sum interaction of these three transaction types forms the basis for Commons's construct of organizations, the going concern.

Bargaining Transactions

The first of Commons's transaction types, the bargaining transaction, will perhaps be the most familiar to those trained in traditional economics. Commons defined the bargaining transaction as "these negotiations and intended alienation and acquisition of legal ownership in consideration of payment or performance" (Commons 1990, 61). As mentioned above, the bargaining transaction occurs between legal equals, and can be roughly described as the legal exchange of goods or services between two individuals. However, the bargaining transaction involves more than just these two people; the transaction also involves the best competition of both the buyer and seller. Thus, as mentioned above, the bargaining transaction involves at the very least four economic parties. In either the case of the buyer or the seller, the transaction involves not only the transactor but also his best alternative choice.

Commons's modification of the economic principle of opportunity cost is not without purpose. The concept of opportunity cost was in Commons's time, and is still today, a critical element of mainstream economic thought. This principle states that with every action there remains a corresponding action and value that has not been taken. The value of the action not taken is called the opportunity cost of the action taken. The traditional theory of opportunity cost involves not a finite number of choices, as in Commons's theory, but rather an infinite number of possible choices. Commons's suggestion is that transactions in the real world do not exhibit an infinite number of choices, but rather a finite number of choices. Thus, the value of the choice forgone becomes a much more practical and identifiable matter than in the traditional theory of opportunity cost.

The bargaining transaction, as suggested above, is the utilization of the part-principle of scarcity occurring as a limiting factor of the economy and guided by the other four part-principles. As such, Commons's does not lay out any specific "law" that motivates the transaction. In Commons system the motivators of transactions may be either socially positive or negative, an issue that is returned to in Chapter 4. Rather, Commons explains the bargaining transaction by outlining a series of considerations that must be given to such a transaction. Commons's methods are directly linked to his guiding part-principle of scarcity that examines the ratio of unique goods being produced and at the same time being demanded.

Ownership is the key that links the bargaining transaction to the principle of scarcity. It was Commons's belief that it is legal ownership that creates a scarcity of goods and services. According to Commons, once a thing becomes owned it can be withheld from someone who does not own it. The principle of withholding is a primary benefit to the owner; its ability to be withheld from others is what makes it an asset. By "asset," Commons means that it is a good or service that has a positive economic value. This is opposed to wealth that has value but not necessarily a positive value. Modern economists make this same differentiation using the terms "economic goods" versus "goods." We may thus surmise that for Commons, the bargaining transaction is the legal transfer of wealth between two parties that are equal in the eyes of the law. The bargaining transaction occurs to the end of eliminating a limiting factor of action.

To clarify, consider the following example. For reason unknown, the price of labor has risen, causing current production practices to become inefficient. The current labor usage is therefore a hindrance to efficient production, or a limiting factor. This in turn prompts a strategic transaction - i.e., a market action of the firm - to procure a different quantity of labor. The development of the wage contract is between legal equals, and thus is of the bargaining type. Both parties then contract based upon future serviceability. The contract itself is then subject to approval or rejection by the wider socioeconomic process, thus to legal procedure and social custom.

As mentioned above, Commons's purpose in differentiating the bargaining transaction from the managerial is to isolate the process of exchange with the production processes and the underlying conditions of demand. Neither of these is a part of the bargaining transaction, which analyzes solely the conditions of the exchange relationship. Each transaction type has its correlative in value. The bargaining transaction occurs as a function of the generation of scarcity value by the holders of commodities, while the process of managerial transactions, correcting for limiting factors, creates use values.

As a method of political economy, Commons explains the economist's considerations of the bargaining transaction as having four basic points. The first issue of the bargaining transaction is the condition of equal opportunity. By this, Commons meant: "Do all pertinent individuals have the opportunity to purchase at the same price or are different prices offered to different groups?" Modern economists refer to this phenomenon as third degree price discrimination, whereby different groups of people are offered different prices based upon different demand elasticities. However, unlike the orthodoxy, the supposed losses in economic efficiency due to price discrimination were not Commons's primary concern. Rather, Commons focused on the degree of economic power, specifically how said power had been gained. That is, Commons sought to ask if certain economic actors were able to unreasonably influence prices based upon a significant degree of monopoly power over the buyer. Commons, unlike the orthodoxy of economic thought, starts with the assumption that monopoly power is universally present. The question for the economist then becomes: "Has the monopoly power been generated and utilized in a socially acceptable way?" Commons suggested that it was a matter for the courts to determine whether the price discrimination was reasonable or not.

The second of Commons's considerations with regards to the bargaining transaction was the issue of fair versus unfair competition. Namely, are either the buyers or the sellers using unfair methods of competition; if so, are the restrictions reasonable? Commons suggests that the primary consideration here is the "goodwill" that the firm has built up. By "goodwill," Commons refers to the intangible assets of the firm. For example, has the reputation of the firm allowed it to price in a manner that restricts competition? Do the employees of the firm have specific knowledge of the production process that causes the firm to be able to underprice other firms? On the other side, is one buyer able to gain knowledge that the other is not, thereby lowering his personal costs? That is, given the assumption of monopoly power, is this power being used in a way that falls within the boundaries set by society? Again, for Commons this is a matter for the courts to decide because the courts have, to some degree, built up the precedence of what society and the law considers "reasonable" as opposed to what it considers "unreasonable."

The third aspect of Commons's bargaining transaction is the consideration of bargaining power. Namely, were both buyer and seller able to compete in a reasonable fashion? Did both the buyer and the seller have equal opportunity of choice, or was trade restricted in some fashion? Lastly, did the buyers and sellers have sufficient understanding of the expected performance of the transaction? Once again, Commons defers to the courts to decide what is "reasonable" and what is not.

The last of Commons's considerations is to investigate if due process of law has occurred with regards to the transaction. In other words, has the ownership of the good in question been legally transferred to the buyer? Has the transaction occurred under conditions of coercion or duress, or has the transaction occurred voluntarily? Thus, Commons was analyzing the social environment of the exchange as a function of the exchange: Did the exchange take place in a fashion that is socially reasonable? Were the terms of trade consistent with the prices and values of society? Thus, the bargaining transaction is a construction made up of economists, the courts, and society. It is the economist's role to advise the court and society of the nature of the transaction that has taken place -- i.e., what are the conditions of the market power that the transactors have brought with them to the exchange?

The bargaining transaction is, then, the examination process for the part-principle of scarcity. Moreover, it is the socioeconomic examination of the exchange process. Commons's bargaining transaction is, in part, the investigation of the exchange process as an embedded feature of the larger social process. When combined with its correlatives, the managerial and rationing transactions, the transaction types form the basis for Commons's unit of economic action or the "going concern."

Managerial Transactions

The second of Commons's transaction types, the managerial transaction, while never defined explicitly by Commons, can be described as a transaction type involving both a legal superior and a legal inferior, where the former defines to the latter the parameters of what the latter must do. In short, it is a description of the managerial process. While the bargaining transaction distributes commodities among the populace, the managerial transaction explains the productive capacity of the economy. According to Commons, an increase in the efficiency of an economy's managerial transactions increases the productive capacity of the economy.

As previously mentioned, Commons made the distinction between the bargaining and managerial transaction to make the distinction between the productive and market, or exchange, capacities of the economy. Commons made the distinction in order to clarify these two conflicting aspects of economy. An increase in efficiency, or the productive capacity of the economy, tends to increase the supply of any given commodity and thus lowers its price. On the other hand, the bargaining process is a withholding of supply that tends to increase the good's price, all other things being equal.

Again, the reasonable conditions in which the managerial transaction is to occur are a matter for the courts. However, unlike the bargaining transaction, in the case of the managerial transaction, it is not only between persuasion and coercion that the court has to decide, but also between degrees of coercion. Since the managerial transaction involves a legal superior and a legal inferior, the relationship is, to some degree, intrinsically coercive and a constraint upon individual liberty. Therefore, the primary social consideration of Commons's managerial transaction is to determine whether the transaction has represented a reasonable constraint on the individual's liberty. At the same time, the primary economic concern of the managerial transaction is to model the production process.

Commons noted that the relationship of the managerial transaction was totally unlike that of the bargaining transaction but at the same time hopelessly intertwined with it. This point is best exemplified, according to Commons, by the labor contract (Commons 1990, 65). In bargaining a wage, labor and management are legal equals; that is, neither party can legally command action of the other. However, upon successful completion of the bargain and entering into the labor contract, the relationship becomes one of legal superior to legal inferior. The buyer of labor can now legally command action of the seller. Although the action of labor can be bought while the laborer cannot, what becomes problematic is that the two are physically inseparable. Because of this the labor contract, Commons notes, is unique. Ownership of labor would be tantamount to slavery -- currently illegal -- and as such, the managerial relationship becomes a matter of degree rather than a question of ownership, as is the case in the bargaining process. As Commons explains,

> The employee or agent, indeed, is not permitted to sell his physical body, which would carry with it all his liberty, but he is permitted to sell his willingness to obey commands within certain limits (Commons 1974, 314).

The managerial relationship is one that has developed alongside the growth of capitalism. In all of Commons's mature works, he carefully develops his views of the managerial institution of capitalism. As the managerial relationship evolved, so also did its regulation develop. Commons explains how in earlier stages of economy there was no such relationship. In *Legal Foundations* he says,

> In the agricultural stage the relation of owner to slave or serf conformed to the notion of property in that it was the exclusive holding and domination over a physical object for one's own use. The slave or serf was a thing, without liberty to choose opportunities, and the relation was that of owner to thing owned. In proportion as freedom of choice was recognized and protected by law the relationship was evolved through intermediate stages until it reached its modern dimensions of master and servant, employer and employee, principal and agent. The outcome consists, not in the elimination of command and obedience, but in the liberty of bargaining as to the terms or limits within which obedience shall be rendered (Commons 1974, 314).

The failure of the economics profession to separate transactions of the managerial type from those of the bargaining type is due, according to Commons, to improperly defining the meaning of wealth. Specifically, the misunderstanding arose, according to Commons, with a confusion of wealth and assets. As stated above, Commons's term "asset" refers to economic goods, while "wealth" refers to all goods. Thus, it is the production of wealth that creates true or use value, while assets only represent saleable wealth and do not produce any additional value. Commons suggested that wealth typically was defined as anything that has material and is owned (Commons 1990, 252). This, he believes, had led to a misunderstanding of the true meaning of wealth.

Rationing Transactions

Finally, we come to Commons's third transaction type -- the rationing transaction. Like the managerial transaction, the rationing transaction involves a legal superior and a legal inferior. However, in the case of the rationing transaction, the parties are not individuals but rather interested groups of individuals. Commons defined the rationing transaction as "the process of exercising jurisdiction" (Commons 1990, 754). He goes on to describe the rationing transaction as "it [the rationing transaction] is the process of reaching voluntary agreements of partnership among equals in the sharing of the benefits and burdens of a joint enterprise" (Commons 1990, 755). We may suggest that the rationing transaction can best be described as the collective allocative actions of a group of individuals. This group delegates rights and duties to another group of individuals. Either both or one side of the transaction may be collectively organized. In short, the rationing transaction is the process of collective bargaining; it is the allocative process of institutions.

Rationing, in Commons's scheme, occurs when individual actions become frustrated. Individuals seeking to make correct personal limiting factors often face pre-existing power structures that frustrate their ability to act as they would. Individuals will then seek to organize so as to ration their economic output. An example of such action would be an existing labor force unable to attain higher wages. These individuals organize into a union so as to ration their output while at the same time becoming a force to be reckoned with. Thus, the limiting factor (the wage rate) is corrected not through individual action but rather through collective action. Likewise the wage transaction has shifted from the bargaining form to the rationing form.

As described in the above paragraphs, the rationing process is essentially democratic. However, Commons was aware that rationing is often undemocratic (Commons 1990, 756). Commons sought to reform the rationing process to increase the general level of democratic participation while at the same time retaining the economic efficiency of dictatorship (Commons 1990, 758-760). Commons believed that pure democracy without arbitration "wasted, delayed, and weakened" human effort (Commons 1990, 756). Rationing that occurs under dictatorship requires no such waste and therefore is more efficient, economically. Dictatorship, however, is socially undesirable. As such, Commons sought to reform the rationing process through "judicial decision" (Commons 1990, 759). Such a situation was desirable according to Commons because – when organized properly – it combined the coordination of a command process with the socially desirable democratic recourse.[6]

Unlike Commons's other two transaction types, the rationing transaction is not part of the grand dichotomy between the productive or managerial economy and the scarcity of the bargaining economy. The rationing transaction occurs in the action of all social organizations; it is the process of institutionalized social provisioning. In the rationing transaction we see Commons's consideration of the process that

[6] Commons sought to reform the legislative process to encourage democratic participation in the legislative process. Specifically, Commons called for the incorporation of all relevant parties to any given transaction to have legal recourse to judicial decision making. This issue is discussed further in Chapters 4 and 5.

collective bargaining plays in allocating the spoils of economic activity. This redistributive effort, when combined with the other two transaction types, combines to form the basis of economic institutions.

Reciprocity and Commons's "Goodwill"

While Commons never refers to reciprocity as a transaction type, it is clearly a critical component of his system of economy. Commons suggests that his term "goodwill" and reciprocity are one in the same. As Commons puts it, "goodwill is reciprocity. It is not government at all, but mutual concession" (Commons 1969, 19). Commons's meaning of "reciprocity" seems to be a process of "give and take" whereby individuals reach agreements through a process of bargained concessions. Commons realized that many of the economy's intangible assets were the result of reciprocal arrangements. In fact, Commons clearly saw such arrangements as critical to the continued functioning of any given concern. Thus, we have given it a place here among the other theoretical components of Commons's system.

Commons used the term "goodwill" to refer to the day-to-day reciprocal arrangements through which the firm is able to support its continued existence -- specifically, the reputation, trade names, trademarks, and continued labor and capital agreements and understandings. Commons's goodwill stems from his understanding of the labor contract and its legal ramifications as well as the specific embedded intangible assets of the firm. As we have seen above, to work a laborer against his will would be an unreasonable restraint of his will (see bargaining transactions). As such, any labor contact is binding only so long as it is a "reasonable" restraint of individual liberty. Commons realized that the laborer can therefore terminate the contract at any given time. At the very least, the laborer is free to leave at the end of the day and never come back. Similarly, the employer is able, in most cases, to terminate employment with little to no notice if he so desires. Thus, the labor contract is, in most cases, not a contract in the usual sense of a legally binding agreement with an expectation of performance, but is a reciprocal arrangement.

In Commons's system this arrangement could either be one of coercion or of "goodwill." In the former, the laborer agrees to the contract out of a fear of starvation or personal loss. The laborer is thus coerced into working and continues to do so not out of any desire to see good work done, but only to put bread on the table. It was Commons's opinion that employers, if so educated, would come to see the arrangement of "goodwill" to be more productive in the long run. As Commons states,

> But they [employers] learned that it was worthwhile to be protected against themselves; that they needed to make it impossible to violate or overlook the rights of the employees. Especially they learned to approve of checks calculated to restrain their agents from arbitrary and unjust acts toward fellow–employees. In short, what they think they have learned is that, by admitting labor into the councils and authority of the company, they are winning industrial peace and the goodwill of labor (Commons 1969, 109).

Commons here uses the term "goodwill" of labor to mean the intangible knowledge of the labor process embedded within labor. However, it is unfair to suggest that this is all that Commons meant by the term. Goodwill is the total embedded intangible assets of the firm, both labor and capital. Restraints of trade that are the result of a firm's "goodwill" are thus reasonable restraints. For example, a firm may legally and reasonably, in the opinions of Commons and of the courts, restrict licensing of its trade name. Such agreements allow the firm to retain the intangible asset of its good name and reputation.

Institutions

At this juncture, it may be useful to review what has been presented thus far. In the last chapter we outlined Commons's theory of human action, culminating in the principle of willingness. This willingness, or action, is constrained by five basic interdependent principles. These five principles of sovereignty, scarcity, efficiency, custom, and futurity in turn combine to form the external constraints of human action. Within these constraints, action is motivated by the theory of limiting factors. It was Commons's opinion that individuals are constantly seeking out the "limiting" factors in their day-to-day interactions. It is the search to refine and correct these limiting factors that causes individuals to refine their environment.

In this chapter we have seen that these human actions are revealed in the three transactional forms discussed above. Commons's three transaction types, the bargaining, managerial and rationing transaction, are the three ways in which economic actors interact and manipulate the system that we call economy. The culmination of these transaction types is what Commons referred to as the institution that both affects individual behavior and is affected by that same behavior.

The sum of Commons's three transaction types is the basis for his concept of the "going concern" that he also refers to as an institution. This does not mean that a going concern is the same as an institution but rather that going concerns are a type of institution. Commons once defined his institution as "collective action in control of individual action" (Commons 1990 69). On another occasion, Commons explained that institutions have a threefold effect upon individual human participants. First, the institution has an accepted set of beliefs that shape individuals' tastes and preferences. Second, the institution produces for the individual means by which to satisfy these desires. And third, the institution creates a set of general rules that suggests how individuals interact with each other (Commons 1967, 4). When combined with Commons's theory of human action, we can easily see why Commons suggested that human actions within institutionalized society really become transactions, actions between individuals (Commons 1990, 73). As such, the concept of the institution is the culmination of Commons's theory of economy.

Commons's concept of institutions was a long time in development. Its development traces back farther than any of the other basic concepts of economy reviewed here. It is in his *Sociological View of Sovereignty* (1899-1900) that we find Commons's original development of the concept of the institution. Within it, he developed a general theory of the institution that is at the same time, an agent of restraint and of expansion of human action. Commons theory of institutional development is typified by his theory of the state, from which basic principles all other institutions develop.

As mentioned above, in Commons's system, social technological advancement occurs with the advancement of private property. The same is true of his theory of the state (see the above section on bargaining transactions). Thus, the original impetus for the development of institutions is coercive, as it derives in turn from the development of private property. Simply put, the state, from which other institutions develop, originally occurs in Commons's theory in order to protect a generated economic surplus -- to protect and monopolize society's private property.

Commons believed that the human realization that the necessities of life are scarce caused primitive man to hoard that which was useful. As a result, Commons theorized, the institution of private property was established. This hoarding, in turn, eventually creates an economic surplus. The resulting generation of economic surplus gives rise to an initially coercive state that exists to maintain the aforementioned surplus. This early form of the state, in Commons's opinion, was not a valid one (Commons 1967, 14-15). His reasoning is that a solely coercive state is not really a state at all, but rather private property. Commons believed that it was only through the eventual clamoring of the wealthier classes, bolstered by the principle of private property, that a primitive society develops a shared sovereignty. It is this shared form of control from which the first legitimate state as an institution of collective action arises. The state then takes on the role of safeguarding the community as well as being an institution designed to protect private property. Similarly, Commons traces the development of the institutions of the family and the church from their originally coercive structure to their modern form of collective action containing both aspects of welfare and warfare (Commons 1967, 62-94).

We may loosely correlate Commons's general theory of economic institutions with that outlined recently by Stanfield (1991), whereby institutions, and in particular the state, have the dual effect of protecting economic surplus while at the same time providing for society's welfare. As such, society's institutions not only restrain individual economic action but also liberate human action by providing and maintaining the community's economic surplus. Commons's institution not only constrains but also enhances or expands the individual's capabilities. As Commons puts it, "The head of a great corporation gives orders which execute his will at the ends of the earth" (Commons 1990, 73). Through the institution of the corporation, its executives are able to exert a far greater power and influence than they would without the institution.

Commons's theory provides us with a theory of institutions that explains them as being both coercive and persuasive, both constraining and liberating, and a result of both individual and collective action. The economic institution is, in Commons's view, the nexus from which transactions of all types occur. The economic institution, derived from the originally coercive notion of private property, which bestows upon its owner both the above-mentioned scarcity value and a use value (see managerial transactions). From the productive use value, "true" value is created in the sense that it expands the abilities of the community through increased efficiency. This increased efficiency in turn leads to an increasingly shared sovereignty as the plutocracy clamors for additional power.

Through the individual's search for the limiting factor in any given circumstance, the institution constantly revises itself, both constraining and freeing the individual to act. Of Commons' many definitions of the institution, perhaps the best is the one found toward the beginning of *Institutional Economics*, namely, that an institution is the "collective action in restraint, liberation and expansion of individual action" (Commons 1990, 73).

Reasonable Value

Perhaps the most misunderstood and underutilized of Commons's theories is his theory of *reasonable value*. This theory is arguably his greatest contribution to economics. Perhaps better than any other, reasonable value conveys to the careful student of Commons the significance of property and exchange in legal and historical context. However, the neglect of Commons's reasonable value really is not surprising given the roundabout way in which he explains it. Much of the misunderstanding likely stems from the many definitions of reasonable value that Commons gives throughout his works. A complete reading will yield at the very least four: a socially determined price, a highest or best obtainable value, a socially desirable practice, and a basis for institutional reform. All four are actually different aspects of one theory.

One should be careful not confuse Commons's use of the word "reasonable" with the terms "reason" or "rational." As mentioned above, Commons personally saw mankind as being largely irrational and tradition bound, engaging in reasoned decision-making only when necessary. At the same time, he paints a theoretical picture that is largely rational. Thus, Commons's view on rationality is not entirely clear. Whatever the case, Commons felt that society contained with it the potential for reasonableness or mutually agreeable arrangements even if individual or even social decisions often were not. That is, it would appear that it is the rationality of systems that imposes a form of rationality upon individuals.[7]

Commons's theory of reasonable value was the product of many years in observation of the legislative process. He had worked for the LaFollette administration drafting legislation for the state of Wisconsin during the early years of the twentieth century, and he came to understand how the courts worked and how their actions changed and guided the actions of society (see Chapter 1). Specifically, Commons came to understand that economic legislation was much more likely to pass if it was written in such a way that it coincided with preexisting statutes. The experience impressed upon him the importance of the legal structure in guiding the economic process.

Beyond his observation of the legislative process, Commons was also an astute student of history, particularly the history of law. Virtually the whole of Commons's *Legal Foundations* (1924) is a study of the nature and causes of the changes in the legal atmosphere from the feudal era to Commons's time that shaped our modern economic environment. As mentioned above, *Legal Foundations* endeavors to explain the current market economy as an instituted process, fulfilling what Commons liked to refer to as the "public purpose" (see Chapter 1). According to Commons, the current market system of the United States was instituted in order to suit the desired public purpose.

To take a step back, the idea of "public purpose" is the heart of Commons's concept of reasonable value. According to Commons, this principle of "reasonableness" runs through all transactions. As we have already discussed, Commons's transaction is a social process involving not only its direct market participants but also a sovereign power that bestows upon the transaction social acceptance of the individual's ownership in the form of a property right.

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[7] The informed reader will no doubt note the link to the recent investigations of economists in the newer institutional vein into the concept of "organic rationality." While not an issue investigated in

Commons, being the student of law that he was, understood the concept of right in the modern United States as being largely a derivative of the will of society. Commons claimed to have seen the change from the older conception of natural law (the notion of the God-given right of property) to a more modern version. This newer version follows from the reasoning that in a state of nature man has no rights, it is only the sovereign power that can grant the individual "right." In the case of the modern United States, the sovereign of course is the people. Consequently, "right" and its correlative "duty" are liberties granted through the will of society. Liberties are granted so long as they are seen as conforming to what may be described as the public purpose. Thus, we can see the importance of Commons's principle of sovereignty. In *Legal Foundations*, Commons traced the development of the individual's "right" to act as he would in society limited by that same society -- that is, so long as the individual's actions fit the public purpose. What Commons hoped to offer to the economic community was an alternative to the Natural Law theories (in which property is an extension of man's interaction with nature) to an understanding of private property that was not God-given but rather a liberty granted by society.

Commons understood that so far as the United States was concerned, the decisions of the Supreme Court determine at any given time just what is the public purpose and what is not. It is for this reason that Commons always linked ethics, law, psychology, and economics (Ramstad 2001, 1-30). As the final determinant of value in society in the Supreme Court, such rulings are necessarily linked to the ethics and psychology of the current justices. Thus, when Chamberlain refers to the Supreme Court of the United States as Commons's *deus ex machina*, he was more than a little

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this study, it is perhaps an area for future research.

right, as it is the justices who make the final decisions on the economy (Chamberlain 1963, 85).

Despite this, Commons did not see the Supreme Court as a sort of universal arbiter of the truth. Commons realized that it was public opinion and custom that was the true determinant of what was reasonable and what was not -- the Supreme Court is the vehicle that gives public opinion voice. As such, reasonableness is truly a socially determined process. Commons's concept of reasonable is neither inherently conservative, as some have suggested, nor radical. Some definitions are in order here. The term "conservative" is used to denote theories based upon preserving existing hierarchies and practices, while "radical" refers to theories that wish to significantly restructure or recreate current hierarchies and practices (Clark 1991, 71-86). Reasonable, in Commons's mind, refers to the range of economic outcomes that are socially acceptable. The economist's role, according to Commons, is to provide society and the courts with an understanding of what is economically possible based upon the best existing technologies and practices.

Summary

In summary, Commons's primary purpose was to explain the economy as a socially instituted process, administered in the public purpose. That is, the economy is not a self-regulated mechanism but rather a constantly recreated, socially regulated process. Due to his experience with the court system and judicial rulings on the economy, Commons came to understand how the decisions of the court created and constrained our economic system. Commons saw the court system as the final arbitrator in the conflicts between men and as a proxy for the value structure of society as a whole. In creating a system of economy interested in the relations between individuals, Commons turned to the historical decisions of the court to understand how the social process of economy came to be in the West.

In this chapter, our purpose has been to outline the economic theory of J.R. Commons. From the above, we can see that Commons's system of economy, while riddled with obscure and poorly defined terminology, is a unique and useful theory of economy. First, Commons's "transactional" analysis provides the student of economics with a method of practicing or doing institutional economics. Commons's economics provides not only significant insight into the working of the economy but also gives economists a method for using these insights in the process of serious analysis and discovery. For example, Commons's transactional analysis provides a better, more realistic model of exchange when compared with a traditional supply/demand model. Where the traditional model can, in the presence of very constricting assumptions, predict the movement of prices, the Commons model gives the economist the tools to explain why economic changes occur, the social and economic conditions which led to those changes, and what is likely to happen to prices.

Second, Commons's reasonable value provides the student and practitioner of economics a picture of the economy as an ongoing social process. Reasonable value is a method for studying the ways in which societies institute their economies, and how the norms and ethics of the community guide and shape the process of creating material well-being. Beyond this, Commons's theory provides a positive format from which reform should occur. As we investigate in depth later, Commons's value system suggests that the words "better" or "progress" really do have meaning, and that certain procedures are better than others.

Despite the insights of Commons's work, much of its significance is difficult to determine when only the theory is looked at. For example, when dealing with Commons's reasonable value, one is forced to ask, "reasonable to whom?" Commons's apparent answer, "to society," is really a non-answer: it provides no real direction or guidance. Specifically, Commons's apparent answer to this question gives no reason or basis upon which reform is to occur. This does not jibe with Commons's activist life. Only when Commons's theories are linked with both his philosophies of action and his real life work can the reader discern the true significance of Commons's work. Toward this end, in the next chapter we look closely at the method of a few of Commons's reforms to give the reader a complete picture of Commons's method of economics.

Chapter 4
The Applied Reform Method of John R. Commons

As mentioned in the introduction, Commons's economic theories are best understood in light of his applied work. As stated in the above section on methodology, the study of economic ideas is essentially a hermeneutic process. Therefore, to more correctly interpret the economic theory of a past era one should consider the historical circumstances of the era, and, if possible, consider the direct applications of any given theory. Toward this end, this chapter considers some of Commons's reform efforts in an endeavor to discover how he applied his ideas.

This chapter will first demonstrate the method and reasoning of three of Commons's most significant social actions: the creation of the Wisconsin Industrial Committee, Wisconsin Unemployment Insurance, and the American Association for Labor Legislation. Having reviewed Commons's applied methods, this chapter outlines the implicit cause of institutional change in Commons's thought, specifically the role of individual decision-making. The combination of Commons's reform method and his conception of institutional change reveals his conception of progress.

The intention is to show that Commons had a distinct idea of the meaning of "reasonable." First, what Commons's meant by "reasonable" is a circumstance that reflects the best possible practices given the existing technological state. These "best possible practices" may be described as an accommodation between "ideal" and "real." Commons's applied method reveals his understanding that values should be based not upon social custom or other conservative policies but rather upon the real circumstances of society pragmatically investigated and discovered. Second, his reform method strives for maximum democratic participation in the economic decision-making process. Moreover, we will see that Commons's economist is a provider of information to those in power, a pragmatic investigator of economic truths.

It is within four of Commons's more neglected works that we find the specifics of his reform method: *Labor and Administration* (1913), *Principles of Labor Legislation* (1916) co-authored with John Andrews, *Industrial Goodwill* (1919), and *Industrial Government* (1921). These books, written during Commons's most productive years represent the immediate finding of his investigations into economic practices and detail his efforts for the reform of those practices. Of the aforementioned books, both *Labor and Administration* and *Industrial Goodwill* are collections of articles published by Commons dating back to the turn of the century, *while Principles of Labor Legislation* is a history of the letter and the intent of labor legislation, and *Industrial Goodwill* is a series of studies done by Commons's students on "progressive" concerns.

The three examples of Commons's work reviewed in this chapter are not meant as a complete presentation of his practical work, nor could this presentation even be considered to cover the highlights of Commons's work. Rather, these three specific pieces of work are studied to illustrate his reform method. The first of these, the Wisconsin Industrial Commission (WIC), is perhaps the best example of Commons's reform method in action. It is also chronologically the first of the three examples given, occurring during Commons's work with the LaFollette administration in Wisconsin. The second example, the American Association for Labor Legislation, is given as a another example of Commons's method in action. Beyond this, the AALL deserves recognition for the roles played by this organization in the development of unemployment insurance and social security. Finally, the Wisconsin Unemployment Insurance Act is discussed because Commons saw it as his greatest achievement and because of its significant effect on the national unemployment act. First, Commons's general approach to "doing" economics, "utilitarian idealism," is reviewed.

Utilitarian Idealism

Commons's applied reform method attempted to incorporate what he referred to as "scientific reasoning" into economic analysis. What Commons meant by this was that economics ought to incorporate the principles of human aesthetics, ethics, and "pure science" or abstract mathematics into economics (Commons 1964b, 1). Commons called the approach of this type of work as *utilitarian idealism*. Meaning that the economist ought to strive for ideals, but also be tempered by the needs and actualities of reality. In discussing the role of the University of Wisconsin in ongoing reform efforts Commons explains his concept of utilitarian idealism.

> Wisconsin is not an accident – it is as inevitable as democracy. It makes a science and an art out of what to the Greeks was degrading toil. It should make an ethics of service to others out of science, art, wealth, and toil. It has not yet finished its work – it is really only

> feeling its way in response to the demands of democracy. It has not yet given a conclusive answer to the idealists, nor enlisted them all in its errand. It has challenged them to help out. The methods of applied science, now inaugurated in agriculture, engineering and business need to be extended to sociology, law, philosophy, ethics, history and literature, where idealists prevail. ...This is utilitarian idealism (Commons 1964b, 6).

We can see in the above quote that Commons desire to apply his theories pragmatically -- to apply knowledge and reason to the problems of the community. Note that Commons does not make a plea to use science or "scientific reasoning" in discovering the needs of the economy but rather the purpose of Commons's economic theory was to find the needs of the community. Commons therefore did not see economy as an end in itself but rather a means to an end. Moreover, by scientific reasoning Commons did not mean that economic theory ought to isolate itself from practice; indeed, he saw economic theory as inseparable from practice (Commons 1923, 113).

Commons's utilitarian idealism is an attempt to combine theory, "idealism," with practice, "utilitarianism" (Commons 1964b, 3). Commons saw this as a twofold process of reform toward both work and education. From Commons,

> To combine idealism and utilitarianism, our modern worker asks that we combine leisure and work in the same person. This means shorter hours of work and more opportunities for education. This is the first great problem of modern democracy, -- the industrial problem, -- how to get a fair living by reasonable hours of work, leaving enough leisure for both childhood and manhood.
>
> The second problem is education, -- the use of leisure. Leisure is an opportunity. It may be used or abused. What kind of education is called for? It is that which will develop the idealism of work – now instinctive but too often suppressed (Commons 1964b, 4).

From the above, we can see Commons's preference to place human development above the needs of the economy. Throughout

Commons's applied work, one finds a continued dedication to human participation and development and the use of science or technology to achieve these goals.

The Wisconsin Industrial Commission

The story of the Wisconsin Industrial Commission starts with the election of Bob LaFollette as governor of the state of Wisconsin in 1904. LaFollette, perhaps the most famous progressive politician of the progressive era, sought to create a stronger link between the state government and the University of Wisconsin. In 1905, LaFollette went to Commons, by then with the University of Wisconsin economics department, with the request that he draft for the state a civil service law (Commons 1964a 100). LaFollette had heard of Commons's work in Washington years before, when LaFollette was a senator for the state. LaFollette first and foremost wished the new law to require that *all* civil servants be required to take competency tests. As Commons states,

> All existing employees of the state, except the heads of departments and elected officials, were to take the same civil service examinations as others, to determine whether they were competent to carry on efficiently the work for which they had been appointed (Commons 1964a, 101).

LaFollette's primary purpose in developing a Civil Service Law was to stamp out regional and departmental "bosses." Like many Wisconsin initiatives, the civil service law became the basis for national law – in this case the National Civil Service Law, enacted several years later. Commons saw the law as the cornerstone for all future progressive reforms. Without the civil service law, Commons felt the progressive reforms mentioned below would have never survived.

Commons's work on the civil service law led to more work with the LaFollette administration, including the creation of the Wisconsin Railroad Rate Commission Law and public utility law among others. The Wisconsin Railroad Rate Commission Law of 1905 gave the commission the power to require rail rates to be "reasonable." If consumers deemed existing rates unreasonable, the commission would investigate. If the rates were found to be truly unreasonable, then railways would be given a reasonable rate determined by the commission (Harter 1962, 92). In determining the rate, the commission would allow both producers and consumers to plead their case; the burden of proof was on the plaintiff. After hearing the opinions and evidence of the concerned parties, the commission set the rate. If after the law is enacted, producers deem the law to be unreasonable, they may appeal to the court. However, during the appeal, no new evidence may be given that was not presented to the committee (Commons 1964a, 384). If new evidence is presented, the whole case is sent back to committee.

Two years after the railroad commission was created, Commons drafted the Wisconsin Public Utility Law of 1907. Prior to the 1907 law, public utilities had been regulated thorough the granting of charters (Harter 1962, 93). The charters were maintained through a command and control system. Consequently, adjustments to policy took time and incurred significant cost. In times of increasing costs, utilities -- unable to raise prices -- eventually resorted to subterfuge (Harter 1962, 94). As a result, the utilities would argue for higher prices in times when increases were not needed to safeguard against potential future cost increases.

Commons's utility law utilized his committee concept, soliciting information from consumers and producers to determine rates that were to all involved parties "reasonable." Using the structure of the railroad commission, the utilities commission would create standards valid in a court of law as fact.

Commons's committee form eliminated the problems of reasonable regulation that had plagued earlier reforms. The court now held the conclusion of the committee to be reasonable. Prior to this, individual safety investigators, for instance, had been charged with determining what is a reasonable degree of safety without outside input. The investigator would have to provide sufficient evidence why such reforms were necessary and reasonable (Commons 1964a, 386-394).

The success of Commons's work for the LaFollette administration led to the creation of the Wisconsin Industrial Commission (WIC). The basic agenda of the WIC was worker's compensation and safety. The WIC again utilized Commons's commission structure to determine the safety reforms that were reasonable. Like the other commissions, the WIC was charged with the investigation and determination of reasonable practices. As Commons put it,

> To the Industrial Commission is assigned the duty of investigating and ascertaining what safety devices and safeguards, what means, methods and procedures, are best adapted to render the factory safe. Having ascertained what they are, the commission issues an order prescribing that they shall be installed for each factory or class of factories. This, then, is the lawful order which all are required to observe (Commons 1964a, 386-387).

In its day, the WIC was highly successful. The WIC and Commons were able to reform safety laws, create workmen's compensation laws, child labor laws, and minimum wage laws for women (Landreth and Colander 1994, 345). According to Commons, the success of the WIC was due to its methods; the practices of the commission generated goodwill among both consumers and producers. Where prior command and control systems had generated a feeling of resentment, he felt his system allowed all parties to have a voice in regulation. Commons felt that his commission form created a fourth branch of government, one that was more accessible to the general public, one that created a form of proportional representation.

The American Association for Labor Legislation

John B. Andrews was one of Commons's first Ph.D. students, recruited by Commons in 1905 from Dartmouth College (Commons 1964a, 134). Andrews started as a labor economist working with Commons on his *History of Labour in the United States*. A few years later, in 1913, Andrew co-authored *Principles of Labor Legislation* with Commons. Of the two, the first was, to date, the authoritative history of labor. The latter book outlines in detail the laws regarding all aspects of public and private labor. Within these books we find not the letter of the law but rather its purpose and intent, giving it a continued relevance.

Andrews' greatest achievement, though, was the continued development of the American Association for Labor Legislation (AALL). In 1906, Ely and others had founded the AALL. Although Commons did not wish it, he was elected president of the new association. Commons immediately made Andrews his executive secretary in order to, as he said, "do all the work" (Commons 1964a, 138). During this time, Andrews also worked for the Wisconsin Department of Labor investigating matters of worker safety.

Like the WIC, the AALL very much typifies Commons's approach to the commission format. Commons had long advocated the democratic approach to commissions. The AALL, in determining socially "reasonable" terms for worker safety, utilized the opinions of all involved parties. Personally investigating circumstances, the AALL sought to find the best labor practices, and to make these practices law. To this end, the AALL was, for a time, very successful. Under the leadership of John Andrews, the AALL was the major influence on federal labor legislation from 1910 until the Second World War (Chase 1991, 800).

It would not be too much of a stretch to say that Commons and his students have had a significant effect upon the way we live our lives today. Many of the major reforms of the twentieth century bear Commons's stamp. From unemployment insurance to Social Security to a modern civil service to citizen input in legislative commissions, the ideas of Commons can be seen. The paradox is that while his practical work shaped the world in which we live, his theoretical ideas, which shaped these reforms, gather dust on the shelves, ignored by virtually everyone.

In order to provide the public with a voice, Commons advocated the use of regulatory commissions. It was Commons's belief that such commissions, if designed properly, could be an accessible point of entry for the populace to participate in the democratic process. In short, the commission could make the democratic process more reasonable by giving voice to the parties most closely involved in the process. As mentioned above, Commons felt that the decisions-makers of the democratic process often lacked critical information about the best possible arrangements that could currently be reached (see Chapter 1). Instead, the court was often forced to fall back upon conventional knowledge. It was Commons's observation that the majority of "errors" made by the court were due to lack of information. He saw the role of the regulatory commission as a provider of information upward to the court, which had the secondary benefit of further sharing sovereignty.

More than any other, Commons's regulatory commission structure was drawn from his knowledge of what worked and what did not work in practice. As has already been noted, Commons observed that for actions to be deemed reasonable by the courts they had to meet legal precedent. That is, the actions of the regulatory commission or economist had to be deemed constitutional. To this end, Commons suggested that regulatory laws should be written with a great deal of latitude. Specific laws, according to Commons, are less flexible and therefore more likely to violate existing law. Moreover, the suggested laws of the commission should regulate to the best *existing* practice. This was for three reasons: the first was that Commons felt it was not the job of government or the outside observer to recommend what is reasonable and what is not. It was his opinion that this type of regulation defeated the whole purpose of the commission -- to provide a voice for those actually engaged in the process being investigated. The second reason was that Commons observed that such "outsider" regulations were often deemed to be unconstitutional and failed to stand up in court. Third, Commons felt that government investment into discovering better business practices was an unwarranted risk of taxpayer money. He believed it was better to conduct research and development in the private sector, where the risks are born by willing participants.

The commission, then, has a very delicate and crucial task, and Commons made every attempt to ensure that the commission would neither be captured -- in the economic sense -- by any party or parties, or that its decisions or recommendations would be ignored by the higher courts. Commons suggested that the appropriate executive -- the mayor, governor, or executive branch of the national government -- appoint commissioners. These appointed commissioners should be educated in the areas of law, investigation, and regulatory execution. Second, they should be required to pass relevant civil service examinations. It is the duty of the commissioners to discover what is reasonable; to uncover the facts and conditions that yield the greatest practical welfare. They are then to suggest law that will enforce for all participating parties those practices and policies that are reasonable (Commons 1964a, 383).

In Commons's commission structure, the commissioners are free to send out investigators either publicly or in secret. They must make themselves available and give due weight to the opinions of all pertinent participants. Once the commission has uncovered all of the relevant facts, it reports on those conditions that are "reasonable" and law is drafted. However, at any later date any of the pertinent parties may object and sue to modify the ruling (Commons 1964a, 384-385). In this way, Commons hoped that the decisions of the commission would be open to scrutiny and unlikely to be captured by the interests of capital.

Again, we must stress that Commons's commissioners do not recommend to any interested party. This is of the utmost significance. It was perhaps one of Commons's greatest concerns that those closest to any given situation should have the greatest say in its process, not only for reasons of equity but also because the participants would likely have the best and most complete information.

The majority of commissions, according to Commons, were organized around a chief with several deputies. It was the job of these deputies to ensure compliance with existing regulatory law. In theory, these deputies had equal authority and were to be enforcing a universal law. In practice, Commons observed that different deputies enforced the law differently. Moreover, because industry often has little to no input in this type of regulation, an adversarial atmosphere is created. This system kept the decision-making divorced from those who were closest to the process. Additionally, this type of system lacked the leeway necessary to meet individual circumstances and consequently its ruling would be less likely to stand up in court. Finally, such a system would be far more likely to be captured, due to lack of normal input from producers.

The Wisconsin Unemployment Insurance Act of 1932

Originally drafted by Commons and his students in 1921, the law failed to pass the legislature every year until 1931 (Commons and Andrews 1967, 298). Harold Groves, was, in 1931, a Wisconsin assemblyman and a former student of Commons's. As mentioned in a preceding section, Commons saw the success of this legislation as the greatest achievement of his life. The Wisconsin law, the first of its kind in the

United States, became the basis for most other state laws and for federal unemployment compensation legislation.

Commons and his students modeled the Wisconsin law on previous accident compensation laws. The Wisconsin Law was based upon two basic principles: first, the employer ought to bear the responsibility for the unemployment that they create through job firings; and second, that legislation should focus on preventing of the problem. Toward this end, the Wisconsin system, unlike the current national system, first required only employers to contribute to the fund. Second, the Wisconsin law included provisions through which employers and industries that had fewer numbers of hirings and firings in any given year would be required to contribute less to their unemployment funds when compared to industries that had large employee turnover.

The specifics of the Wisconsin law were fairly different from unemployment insurance today. The first aspect of the Wisconsin plan, as mentioned above, required only employers to contribute to the program (Commons and Andrews 1967, 303). The rationale for this was twofold. First, it is employers, not employees, who bear the responsibility for unemployment. Unemployment was treated as a hazard of employment. Second, it was the opinion of legislators that employees bore the most significant brunt of unemployment and should not be required to pay into insurance to protect themselves from unemployment. A second aspect of the Wisconsin plan was that insurance funds were not pooled; each employer paid benefits that could be paid out only within that firm (Commons and Andrews 1967, 308). This had proved to be more popular with employers than a pooling program, and it was thus used to sell the program to these same employers. A third aspect of the Wisconsin law was its merit system for employers (Commons and Andrews 1967, 307). The Wisconsin law made provision for different rates of contribution based upon a firm's previous employee hiring and firing, specifically between 0 and 4 percent. Finally, the Wisconsin Law incorporated a payment system that was set up in such a way that employers had incentives to reduce unemployment and to create their own private compensation programs. As Harter summarizes,

> The Groves Act provided for a two-percent payroll tax to be paid by the employers, unless they created individual programs that provided workers with comparable benefits. Although the employers' contributions would go into a central fund, each employer would have a separate account. When an employer had paid fifty-five dollars per employee his contribution would be reduced to one percent until the account reached seventy-five dollars per employee. As long as the employer's account remained above seventy-five dollars he was excused from all further contributions. If the benefits lowered the level of an employer's account too much the scale of benefits was to be reduced and even eliminated if necessary (1962, 122-123).

It was Commons's and the Wisconsin legislator's hope that such a merit system would incite employers to consider the costs of unemployment more seriously and create incentives for a more stable labor market (Schlabach 1969, 87; Harter 1962, 123). Indeed, it was not Commons's desire to create a comprehensive social insurance program, nor did he believe such a system to be desirable. In fact, Commons's preventive program came into conflict with those who wished to provide widespread social insurance. Advocates of social insurance believed that Commons's plan, the primary purpose of which was to reduce fluctuations in the economy, did not address the fundamental instabilities of the capitalist economy. While Commons's system hoped to place the costs of unemployment on the employer, others were more skeptical that individual employers could do much to mitigate unemployment in the event of an economic downturn. As such, opponents, while they may have agreed with Commons's proposal to internalize the social costs of unemployment within the firm, saw the economic problem as being something larger than individual firms. Other opponents objected to Commons's use of individualized accounts for employers. They suggested that a pooling of funds would allow for greater benefits to be distributed. Commons was aware of the benefits of pooling, but believed that the "sale ability" benefits of the individualized plan outweighed the costs. That is, Commons believed that his plan was more politically feasible. He had hoped that most firms would choose to be self-insured and thus reduce the costs to the government while at the same time making the program more appealing to employers.

Institutional Change

The above begs the question of how institutional change occurs in Commons's system. Institutional change in Commons's system is the result of individual action, the result of individual perceptions of the limiting factors that occur in the day-to-day economy. The individual's correction of these limiting factors produces changes in the institutional structure and in economic values. This does not mean that the resulting institutional changes are not necessarily progressive, "optimal" in an economic sense, or even reasonable.

To clarify this statement requires a review of Commons's theory of transaction. We may safely say that in the case of the bargaining transaction, scarcity-value is created, while the managerial transaction creates use-value. It is the resulting increase in use-values due to economic activity that, with a democratic institutional structure, spread the control of society's resources.[8] We can safely say that Commons saw increased productivity as a factor in economic growth. However, this does not mean to suggest that Commons saw such growth as reasonable, nor does this suggest that use-values are inherently "good." What this study suggests is that Commons was recognizing that economic growth does not occur from increases in exchange or prices, but rather from the productive capacity of the economy. That is, the productive capacity of the economy is measured in use-values rather than exchange values. However, Commons clearly did not wish to suggest that use-values were natural or that that they were good, but rather that transactions of this type generated growth in the economy as measured by its productive capacity.

Commons also considered the meaningful role played by the exchange process in institutional change. Specifically, in his studies of law and history, Commons noticed that a spread of sovereign control through a general reduction in the coercive elements in existing institutions is also the result of the increase in scarcity-values. In Commons's eyes, it was the clamoring of the plutocracy that unintentionally earned freedom for the masses. The more diverse scarcity values are -- the better enforced are property rights -- the more economic power the plutocracy is able to gain. As such, the plutocracy has a vested interest in the development and enforcement of property rights. The spread of control thus benefits all members of society as political involvement becomes more accessible, diverse, and representative. Thus, we can see that significant institutional change is due to the exchange process.

[8] Commons frequently cited the cases of the United States and India as case studies in the expansion of sovereignty with gains in economic surplus.

To equate Commons's idea of "reasonable" to institutional change resulting from either transaction type alone is a mistake. In both transaction types we see that institutional change occurs in ways that can be safely said to both benefit and harm the community.

In Commons's system, both the aforementioned institutional changes that result in the growth of use-values and the development of scarcity-values create the foundation for economic progress. However, progress, as Commons understood it, is not necessarily the outcome of economic activity. To fully understand progress in Commons's system requires an analysis of his personal method. It is this more complete idea of "progress" that may be equated with "reasonable" in Commons's system. That is, reforms that are "reasonable" are also "progressive." However, to understand either "progress" or even "reasonable" requires some analysis.

Reform and Institutional Design

From the last chapter, the reader has been shown the objective method of Commons's reform action -- specifically, the objective method of attempting to incorporate pragmatic investigative methods in determining the best or most desirable practices. By evaluating Commons's reform method, we can see that he clearly thought that progressive reform or legal decisions occurred when they were based upon the best available knowledge of technical and social circumstances. For Commons, reform and change is better when it is based not upon traditional values or because "that's the way it is," but rather upon specific knowledge of processes that consider both the economic efficiency of a given practice and the costs and benefits of reform upon humanity.

Taking the Wisconsin Industrial Commission, which is perhaps the best example of Commons's work, we recall that the purpose of this agency was to develop an investigative team to aid the legislative process. It is important to remember that Commons's WIC did not make legislative decisions. Moreover, the suggestions of the commission were not without an explicit democratic check on their activities -- employees, employers, and legislators were all subject to review from other groups party to the transaction. From this, we can safely state that Commons's reform method stressed not only the importance of informed decision-making but also of democratic participation. Moreover, it is not a stretch to suggest then that reform based upon these principles is in fact "reasonable."

For support of this statement we need look no further than a surprisingly neglected passage in Commons's *Institutional Economics*. In referring to the investigative activities of the WIC and the democratic checks and balances levied upon that agency, he stated the following:

> While these investigations and findings [of the committee] are not "scientific" in the sense of the physical sciences, they are "reasonable" in the sense of the political and economic sciences, because they are based on three circumstances, not found in the physical sciences, of conflict of interests, mutual dependence, and the rules of order deemed necessary to keep industry going with due regard to public and private interests. They can be changed from time to time when new facts emerge from the technological, political, economic, and ethical changes. These call for changing meanings of Reasonable Value (1990, 719).

In the above quote, Commons's reference to conflict of interest, mutual dependence, and rules of order refers to the psychological conditions of the transaction; more specifically, it refers to the pragmatic individual, with significant antecedents and consequences. We can see the same approach in Commons's development of the AALL and the Wisconsin Unemployment Insurance Law. In all the examples given in this study, "reasonable" is determined by educated investigation of existing practices, choosing the best practices and reporting them as "reasonable." Such practices are then subject to democratic review.

It is easy to confuse Commons's reasonable value with a modern conception of "just price." To do so is to significantly oversimplify Commons's method. While Commons's reform method does result in prices and practices that may be deemed "just," or as appealing to the main body of the community, it is not the result but Commons's method that is critical. One may reach "just" prices or practices by any number of draconian methods, including totalitarian decree. Commons's method in determining prices and practices that are "reasonable" or "just" is very specific, attempting to employ the best technology and information as well as to incorporate the greatest level of democratic participation.

Progress

Progress in a wider sociological sense is not a defined part of Commons's theoretical system. However, from the above we can safely say that his reform does imply a particular method of progressive action. Moreover, a close reading of Commons's written work reveals an implied notion of "better." Progress in

Commons's eyes occurs as institutional forms lose their coercive element and become based upon persuasive lines. For example, Commons referred to the creation of national unemployment insurance as the greatest achievement of his life. Knowing Commons's system and purpose, we can see why this would be so. Such a law partially reduces the coercive element of the institution of labor, making it a more democratic and liberating institution. This is the key to understanding Commons's conception of progress.

Reading Commons, however, one does not come away with such a message, More often than not, Commons avoids personal valuation, pawning such issues off onto nebulous concepts such as "the court" or "society." As such, the casual reader of Commons can easily come away with the idea that reasonable decisions are those that are socially acceptable. This is the most obvious of Commons's messages and is perhaps the one given the most press. An example may be taken from his *Legal Foundations*:

> The value principle, looked upon, not as a quality intrinsic in commodities nor in the relation of man to nature, but as a social principle of inducement and an individual principle of anticipation, is none other than the expected power of persuasion or coercion over others which induces performance on the economic side, and gives rise to the claims of rights and liberties on the property side (1974, 382).

The above statement lends itself very well to the argument that Commons's theory does not contain any personal normative statements about the meaning of progress. Moreover, as mentioned above, similar statements can be found throughout his work. This study suggests that experiences in Commons's life had caused him to be wary of normative prescriptions. His experience with the religious establishment (covered in Chapter 1) likely made him very cautious of prescribed methods of reform. To find Commons's conception of progress, one has to dig deeply, but it certainly exists. To understand Commons as simply recommending reform on the basis of social consensus is to miss the most important aspects of his work.

Buried within Commons's method we find several implicit statements about what he believed to be progressive. For example, in the above discussion of Commons's bargaining transaction we pointed out the several aspects of economic activity the investigator was to pursue. From this, it would again seem that Commons's conception of value is simply a modern conception of a socially desirable practice, not necessarily "good" or "bad." However, this study suggests that this was not Commons's conception of "reasonable." It is the opinion of this study that Commons's whole theory of economy is based around the idea that economists, and thus economics, ought to ascertain the *purpose* of economic activity. Moreover, the individual ought to attempt to ascertain if that activity is "good" or "bad." Commons's theory of economy asks the economist to ask the question of whether economic activity is "good" for society. Commons states,

> Thus a volitional or economic theory starts with the *purpose* for which the artificial mechanism in question was designed, fashioned and remodeled, and inquires, first, whether that purpose is useful or useless, legitimate or illegitimate, ethical or unethical, right or wrong (1974, 377; italics in original).

The above reference to the "artificial mechanism" refers to a given economic practice. These practices are "artificial mechanisms" because they derive from deliberate human action. From the above we can clearly see that Commons assigned to the individual investigator a degree of normative latitude. This has been noticed by

Ramstad, who has made note of the existential nature of his work (1987, 661-671). However, this study suggests that implicit within Commons's work is an explanation or conception of progress.

As we saw in the last section, Commons's reform method had two distinct purposes. The first attempted to increase democratic participation in the economic process, specifically by ensuring recourse to any party of the transaction. The second aim of Commons's reform method was to increase the efficiency of the legislative process. This is accomplished by developing legal authorities' access to specific information. From this, we can develop some ideas about Commons's conception of progress. As Commons himself was aware, the questions we choose to ask and the activities we choose to investigate reveal our value conceptions. Likewise, Commons's choices reveal much. The fact that he sought to create avenues for increased democratic participation suggests that, to Commons, choices that are the result of consensus are "better" than those that are decided by decree. This also follows from Commons's clear preference for transactions that are persuasive rather than coercive in nature. We may safely suggest that reforms or institutional changes that increase individual voice in the economic process may be defined as being progressive, while those that reduce individual voice are regressive. By the same reasoning, we may suggest that reforms based upon technological fact are "better" than those based upon tradition, common practice, or common knowledge. Progress occurs when law or the norms of society are based not upon values that may be described as "ceremonial," but rather on the real and current conditions of the state of technology.

Beyond this, we can draw some further conclusions about what Commons meant when he referred to "reasonable values." Commons's choice of the "best" practices of industry as representing those that are reasonable reveals much. "Best," to Commons, does not mean the least expensive or the most economically efficient in narrow terms. What Commons means by "best" are those practices that are incorporated into the production process considering not only narrow costs, but total social costs. Practices that consider not only the needs of economy but also of humanity are "better" or more progressive when considered next to those that do not. In conclusion, this study suggests that Commons, while reluctant to reveal to the reader any specific conception of progress, does in fact do so. Through his investigative method, Commons reveals a distinct conception of "better," or progress. His conception of progress may roughly be summarized as reform that rejects naturalistic interpretations of law and economy and embraces pragmatic, participatory investigation and understanding.

Summary

It is hoped that this chapter has summarized the salient points of Commons's reform method. In turn, his reform method points to a specific conception of progress. This method may be summarized as an attempt to, first, create legal meanings of value that reflect, as accurately as possible, the best existing practices of production. Moreover, Commons wished to see government committees, responsible to the people, that would investigate and determine exactly what those best practices are. This type of work can be seen in the WIC and the AALL. These associations were set up as "think tanks" that could provide information to legislators about the current goings-on of the economy. Second, Commons's reforms attempted to create legislation that set up economic incentives to solve social problems. This aspect of Commons's work can clearly be seen in the Wisconsin Unemployment Compensation Law. As has been mentioned above, Commons knew that legislation and reforms were much more likely to succeed if they had the backing of a percentage of the business community. From this chapter, we can roughly surmise Commons's reform method, and hence his conception of progress, as an attempt to include the input of the greatest number of people and experts possible to create a workable legislative solution.

Commons's role as an economic reformer was to investigate and report on the best production practices currently available. In doing so he managed to combine concepts of social efficiency with the efficiency of the individual firm. In often-ingenious ways, Commons was able to craft legislation that would convince the business community that the efficiency of their firm could be increased while at the same time increasing social efficiency. In doing so, he created a significant body of legislation that formed the basis for much of the social legislation that we often take for granted today.

In this chapter, this study has attempted to examine the practical meaning of Commons's system. It is the opinion of this study that any economic theory professing to be an "institutional" one needs to ask the question, "institutional reform for what?" In this chapter this study, has chosen to analyze Commons's system with regards to its reform method. This work has attempted to show that reform in

Commons's system is originally the result of individual action, specifically through the correction of limiting factors. One result of this individual action is the current institutional structure of the state, including the legal system. In turn, it is the general consensus generated by this state and legal system that determines values and activities that are "reasonable" in terms of the legal system. Also in this chapter this study has attempted to show that Commons did not believe that all values that have been deemed reasonable are necessarily the best choices. Commons explained this shortcoming as a result of limited and incomplete information. As such, the real significance of Commons's system is in his investigative commissions as providers of information. The design of Commons's commissions reveals to the reader his conception of "good" or "progressive." This study has attempted to argue that the implicit conception of progress in Commons's system is two-fold. First, progress occurs with increased democratic participation; and, second, reform occurs as a result of pragmatic investigation rather than as a result of customary procedure.

Chapter 5
Commons and the Original Institutional Economics

This chapter will discuss the place of Commons's economic thought within the school of economic thought commonly referred to as "Institutional Economics." Within this, this chapter will attempt to resolve the conflict of Commons's "reasonable value" with the accepted method of value in that school of thought, namely, "instrumental value." To this end, a brief study is made of the critical tenets of institutional economics. This will require a brief overview of the intellectual antecedents of each theory. To that end, the works of Commons will be compared with those of the acknowledged founder of institutional economics, Thorstein Veblen, the often-cited Clarence Ayres, and some of the school's more modern practitioners

This chapter attempts to show that Commons's value theory is wholly consistent with the general "institutional" school of thought, both the writings of the older school as well as the newer school. As mentioned in the introduction, it has been suggested that Commons's value conception is wholly incompatible with the value tradition within the institutionalist tradition.

The Original Institutional Economics[9]

Original Institutional Economics (OIE) integrated an unusual body of thought from thinkers as divergent as Karl Marx, Max Weber, Herbert Spencer, Charles Peirce, Richard Ely, and the German historicists. Of course, that list names only a few of the authors who had an influence on the OIE. While often alluded to as an inconsequential cul-de-sac in the history of economic thought, the institutional school was, from the turn of the last century through the onset of the Second World War, the fiercest competition to the mainstream neo-classical paradigm (Yonay 1998, 3-4).

Economics today is generally defined as the "study of how scarce resources are used to satisfy unlimited wants." Readers of any modern textbook on economics will today find this program of study wholly embedded within the mindset of modern economics. This has not always been the case. Earlier schools of economic thought had addressed wider issues of economizing behavior. The institutional school was the last of this earlier breed. The institutionalists sought to explain the economy as an ongoing process of social provisioning. More than anything else, members of this school desired to uncover the social processes that had created the current market system. Members of the OIE wished to determine the institutional structures that lead to either economic development or economic stagnation.

Despite the above-mentioned achievements of this school, institutional economics had always had to fight the claim that it is really not a "school" of economic thought, but rather a loose collaboration of authors and ideas mainly united in their dislike of the economics orthodoxy (see Anderson 1919, 4-6; Burns 1931, 80-

[9] Both Stanfield (1999) and Miller (2002) are excellent papers on the meaning and focus of original institutional economics. The interested reader should also consult Gruchy 1967 and 1987, Hamilton

87; Harris 1932, 721-749; Holman 1932, 10-17; Scott 1933, 274-277; Harris 1948, 78; Roll 1953, 454; and Blaug 1985, 708-709). While it is true that the institutionalists sought to significantly reform, if not replace, then-current economic thought, it was more than mere criticism. While not as formalized as the more orthodox tradition, it can be argued that the institutional economists built a unique and complete system of economic thought.

The school of economic thought known today as institutional economics has its roots in the writings of Thorstein Veblen and other works dating to the final years of the nineteenth century. Veblen's writings suggested, among other things, that economics, because it dealt with the interactions of man, ought to be an evolutionary science that analyzed the economy as an ongoing instituted process (Veblen 1948, 215-240). This was in sharp contrast to the prevailing static marginal analysis of the time. Today, along with Veblen, John R. Commons and Wesley Clair Mitchell are also considered to be early influences and founders of institutional economics. Despite his status as one of the founding fathers of institutional economics, Commons's work remains relatively neglected when compared with the work of Veblen. It seems likely that one reason for the neglect of Commons's work is the supposed conflicting nature of the two authors' conceptions of value. It is for this reason that we will first make an investigation into what constitutes institutional economics today, with a specific focus on the value problem. Despite being the prevailing school of thought during the interwar years, the institutional school has for the most part languished in obscurity since then (Yonay 1998, 3-5). Much of the school's neglect is often blamed upon its supposed lack of focus and direction. While

1919, and Dorfman 1963.

it is not true that the institutional school lacked focus, one can sympathize with this position. Unlike the theory of orthodox economics, institutionalism requires careful reading and rereading to discern its message and focus.

The recent work of Stanfield (1999) has done much to clarify what institutional economics is and how it differs from more traditional economic analysis. Stanfield's thesis is that institutional economics and traditional microeconomics are in fact two separate disciplines studying different subject matter. As such, comparisons between the two are prone to miscommunication and misunderstanding. As Stanfield points out, the two schools of thought have differing conceptions of the economy "Conventionally economics defines the economy as choices made in the face of scarcity. ...[Original institutional economics] defines the economy as an instituted process for provisioning society" (1999, 232).

While conventional economics is concerned chiefly with price theory and all its ramifications, institutional economics is concerned with the ways and means with which the economy is instituted toward the public purpose. This does not mean that traditional price theory does not convey any insights to the policy-maker or student of economics, nor does it mean that institutional economics is somehow superior to traditional economics. What it does mean is that the two schools of thought take different views of their respective subject matter and that they are concerned with different problems. Consequently, the subject matter investigated and deemed significant between the two will often be conflicted. In short, institutional economics may be summarized as having the five following core beliefs,

> (1) Group behavior, not price, should be central in economic thinking;
> (2) more attention should be given to uniformities of custom, habit,

> and law as modes of organizing economic life; (3) individuals are influenced by motives that cannot be quantitatively measured; (4) economic behavior is constantly changing; therefore, economic generalizations should specify limits of culture and time to which they apply; (5) it is the task of the economist to study the sources of the conflict of interests in the existing social structure as an integral factor rather than as something diverging from a hypothetical norm (Atkins 1932, 111).

This older list is used in lieu of a more recent one because all the modern lists have been designed with the purpose of including Commons's work into the institutionalist school (Ramstad 1995, 996). The above may be said to constitute the paradigm of the OIE paradigm here used in Kuhnian sense. That is the OIE first attracted a devoted following of practitioners, and second, its defining characteristics were open-ended enough for its practitioners to engage in internal conflict resolution (Kuhn 1996, 10).

The list given here was not designed with any such purpose in mind. The first point in the above quotation should not be taken to mean that only collective organizations have any influence, but merely that they ought to be significant in economic analysis. The OIE strives to understand human action as resulting from social circumstances as well as from individual motivators. These agents have meaningful effects upon their surrounding social environment. OIE endeavors to comprehend the social and individual forces that induce action. To this end, OIE endogenizes both values and technology. Seen as exogenous in orthodox economics, the forces that shape human action -- the aforementioned value and technology -- are *the* questions that make up the OIE research agenda. Technology for the OIE represents more than the artifacts of science but rather both the artifact and the knowledge of the artifact's use. Technology is the knowing and doing process so thoroughly examined by John Dewey. With regards to this, a sixth condition should be added to the above-mentioned five; that institutional economics maintains a commitment to a conception of progress embodied in institutional change that encourages personal development and participation.

To Veblen, and the majority of the OIE, technology is the impetus for institutional change. As conventional ways of doing and knowing become obsolete, individuals are forced to change the existing institutional structure. Conventional habits are disrupted and new patterns are created. Veblen states,

> Social structure changes, develops, adapts itself to an altered situation, only through a change in the habits of thought… of the individuals that make up the community. The evolution of society is substantially a process of mental adaptation on the part of individuals under the stress of circumstances that no longer tolerate habits of thought formed under and conforming to a different set of circumstances in the past (Veblen 1899, 192).

Veblen goes on to state that the aforementioned "stresses" come from "advance in technological methods, in population, or in industrial organization" (Veblen 1899, 195). In Veblen's system, the current institutional state is in a continuous period of "catch-up" with the current state of economic affairs. Moreover, we can see that the technological process is quite widely defined.

The understanding of the technological process is of tremendous scope. Since technology is a dynamic process, the concept of resources also becomes dynamic and unfixed within the OIE program. Resources are not something that simply are; rather, they only come to have value when they become a useful part of the ongoing economic process. For example, gasoline only has value due to its ability to produce torque through controlled combustion. In the absence of the internal combustion engine, gasoline is no longer a resource, just as whale oil is no longer considered a prime resource.

In this light we can see that scarcity, for the OIE, is also a socially created institution in two ways. In the first, scarcity is the result of the withholding of resources through the institution of private property. In the second, scarcity is a function of the current technological state of man-made institution. The former and the latter are both affected by and affect human action.

Like technology, value is treated by the OIE as an endogenous variable. Like the technological process, values are seen as flowing both to and from individuals and society. Veblen suggested that all values derive from the conflicting tendencies of mankind toward creative and destructive ends. Clarence Ayres clarified this position further by suggesting that we like what we know (Ayres 1978, 53-70). Ayres believed values to be socially derived -- to find what we may call true values, we need to determine whether these values derive from destructive or productive tendencies. Thus, a significant part of the OIE research agenda is the modification of social and economic institutions toward more humane goals. As a whole, the focus of study for institutional economics is the process of social provisioning. To this end, it is concerned primarily with the development of institutional forms that lead to efficient and socially agreeable production and distribution of said produced resources.

Despite Commons's reputable status as a founder of the institutional school of thought, his work is infrequently utilized not only within the orthodoxy of economic thought but even within the modern literature of institutional economics. Thus, there appears to be an inconsistency. While Commons is widely recognized as a founder of the institutionalist school of economic thought, his influence within that school appears to be only as a token figurehead. Moreover, when Commons is utilized it is frequently in name only.

Some Explanations from the Literature for Commons's Absence

Few authors have attempted to explain the aforementioned inconsistency with regards to Commons's work. Among the few authors who do comment upon this apparent discrepancy, there is no consensus. The casual reader has to do little more than glance at the secondary literature to become confused about what it was Commons was trying to say. In fact, the problem is so pervasive that the few authors who have taken it upon themselves to evaluate Commons's work have left behind them almost as many opinions as there are studies.

Almost universally, the secondary literature places a large portion of the blame for the confusion upon the vagaries and difficulties of Commons's original material. Beyond this, we find that various authors place the remainder of the blame upon everything from Commons's use of difficult terminology to the cantankerous nature of the early institutionalist school in general.

Harter (1962) and Blaug (1985) have suggested that the difficulty with Commons is primarily his use of a terminology that is not familiar to the economics profession – specifically, his use of legal terminology. Mitchell, reviewing Commons's *Legal Foundations*, stated the following on Commons's cross-disciplinary approach:

> all books which lie on the borderlands cover some territory that is strange to most of their readers. Economists will find the legal distinctions difficult, lawyers will be puzzled by the economic theory, few historians have patience with any sustained analysis, and I fear many reformers will find everything strange except a few wrong-headed legal decisions that they know only too well (Mitchell 1924, 242).

Mitchell seems to be saying that when reading Commons, economists easily misread and hence misunderstand his view. The obvious concern is that, when faced with a difficult passage, the reader may simply "give up" Blaug, on the other hand, points to the difficulty in understanding Commons's fundamental terminology of the "working rule" and the "going concern." Blaug suggests that the fundamentals of Commons's work are so vague and ill defined that the reader can draw any number of conclusions about their meaning. Hence, Commons's work contains little explanatory power.

On the other hand, Ramstad (1987) has suggested that Commons's work is difficult for the economics profession to understand, and hence is little utilized, due in part to his theory's existentialist nature. That is, to utilize Commons's theories, the individual theoretician must take responsibility for his or her actions, must mix the normative with the positive. Ramstad's opinion is based upon his notion that Commons's work lacks an internally complete logical theoretical framework. By internally complete is meant that it is Ramstad's idea that while Commons's work does contain valid theory, it is not a theory that stands complete upon its own.

Rather, according to Ramstad, Commons's system is based in part upon direct investigation. This, according to Ramstad, reduces the economist to an investigator armed with a toolbox of economic principles; how those principles are applied depends upon the economist. Ramstad does not seem to be saying that there is no valid theory in Commons's economics, but rather that his theories can yield no answers, but only provide appropriate questions. Thus, there are no theoretical answers to any given problem, only a group of economic principles to be given consideration. It is this, Ramstad suggests that Commons's theories are not meant to be an answer unto themselves, but to be a means to an answer. To attempt to provide an explanation or understanding of Commons's work is difficult at best, since it contains only questions and no answers. As we shall see, there is a great deal of truth in this explanation.

Finally, Williamson (1990) suggests that the difficulties in interpreting Commons's works are due, in large part, to the continued insistence of the OIE's focus upon their methodological differences with the mainstream of economic thought. Rather than focusing upon the operations of institutions, the older institutionalists focused their economics upon methodological differences and hence incompatibilities with the focus of modern institutional economics and the economics orthodoxy. Williamson seems to be suggesting that the difficulties with Commons's work lie in the focus of many authors upon *how* Commons did economics rather than *what* Commons did as an economist. This apparently causes authors to focus not upon the questions that Commons asked, but rather upon a system of economic thought.

Beyond the argument of the difficulty of Commons's work, we find a debate upon the meaning and therefore the place of Commons's writings. Whalen (1989) has gone so far as to suggest that there are six "schools" of thought on the meaning and therefore place of Commons's work. This work, however, proposes that there are in fact four strains of thought regarding Commons's thought.

Of the four strains acknowledged in this study, the first is that Commons's theories are poorly thought out and not really theories at all. This strain suggests that Commons's work is largely unintelligible and ill defined. Specifically worth mentioning here is David Seckler's *Thorstein Veblen and the Institutionalists*, in which Seckler refers to Commons as a "muddy thinker" with "muddled, naïve, unsophisticated, and inherently uninteresting thoughts" (1975, 122). Commons's theories, according to Seckler, are "poorly wrought and somewhat lackadaisical classifications and sub-classifications of phenomena as they appear to him from a dimly-held and mainly intuitive conception impossible to define" (1975, 124). Seckler continues "[Commons's theories are] hardly an institutional theory at all" (1975 126). We may also place Blaug (1985) in this strain because he abandons Commons's work due to the difficulty of understanding his basic terminology. This viewpoint boils down to the sentiment "Commons is too hard to understand," which cannot be tested and thus is dismissed by this study.

A second strain suggests that Commons does contain a theoretical framework but that only Commons himself could understand it (Witte 1957, 12; and Harter 1962, 206). This viewpoint is held by many of Commons's students, including Edwin Witte. This fact is not surprising – Commons's classes focused upon applied issues and dealt little with theoretical aspects of economy. As Harter puts it,

> Among his students who rose to prominence were many who frankly admitted that they did not understand Commons' theoretical structure in institutional economics. The emphasis on public policy and practical economic problems was enough for them (1962, 206).

Edwin Witte's biographer Theron Schlabach (1969) backs this point of view by observing that the then Ph.D. graduate of the University of Wisconsin Department of Econmics -- where Commons taught -- could leave with less theoretical education than the average undergraduate.

While there may be some truth to the suggestion that Commons's thought is prohibitively personal, it hardly bears investigation, for there is no reason to investigate something that can only be understood by one individual. The present study will not investigate that line of thought. Moreover, on the evidence of this study alone, this criticism of Commons's is not valid. While Commons's work is difficult to comprehend, it is not impossible.

The third strain of thought suggests that Commons never developed a complete theoretical framework, but rather that he was a "concept builder" who only developed theories in areas of personal interest (Chamberlain 1963, 75; Rutherford 1983, 563). This seems to be the general consensus of modern authors writing in the OIE tradition.[10] Instead of developing a new theoretical structure, Commons is seen as building upon existing economic theory in directions that matched his observations of the economy. This strain generally suggests that Commons revised economic theory where it did not jibe with his personal observations, creating in his wake a sort of institutional economics. Thus, Commons's economics is seen as a patchwork of economic ideas that may or may not conflict with each other. Members of this school generally feel that Commons's writings, while they do contain an important body of thought, cannot be understood as a theoretically complete body of work.

Chamberlain, Rutherford, Whalen, and perhaps Ramstad are the most obvious adherents to this strain of thought. However, the works of Atkinson, Chasse, Gonce, Reed, Samuels, and Whalen, while they never venture an opinion, seem to be likely candidates for this strain given their "pick and choose" approach to Commons's work.[11]

Ironically, it is Gruchy (1987) who best explains this strain of thought with regards to institutional economics in general. The word ironic is used because Gruchy has been a vocal critic to such approaches to OIE. In an attempt to define institutional economics, Gruchy also mentions that some authors have felt that this school may be able to enhance mainstream economic thought. Specifically, they believe that institutionalism provides a theory explaining "how we got there" (and perhaps, though it is not clear, "where we are going in the very long run"), while microeconomics and macroeconomics provide the tools for the present (Gruchy 1987, 36).

Gruchy however, dismisses this idea by suggesting that it is methodologically impossible to integrate dynamic institutional economics or economics as process with static orthodox economics. In closing, of the four strains of thought presented here, only the final two will be seriously investigated by this study. The former two, as they contain untestable hypotheses, will be dismissed.

As has been mentioned above, Commons's place as an economist is debated within the institutionalist camp. While this debate has recently become much more

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[10] For evidence of this see the recent commentary on Commons's work in the *Journal of Economic Issues* where the majority of the work in the OIE tradition is published.

[11] By "pick and choose" I mean policy analysis rather than theoretical analysis. Thus, there is no immediate necessity to suggest a complete theoretical framework.

heated, it can be traced back as far as a 1936 article by Atkins and Robinson, who suggest that Commons's work is not compatible with the then-new work of Clarence Ayres. The foundation of the argument is that Commons, unlike Ayres, underappreciates the role of non-legal institutions in shaping individual action. However, this criticism falls short given Commons's elaboration of the principles of scarcity, efficiency, custom, futurity, and sovereignty, each of which contributes to individual action in Commons's scheme (see Chapter 2). Aside from arguments about the place of the institutional school in general, comments about the place of Commons within this group disappear until recently.

Ramstad (1995) makes the argument that Commons's writings are incompatible with the majority of OIE literature. It is for this reason, Ramstad suggests, that Commons is rarely cited even among institutionalist writers. He suggests, first, that institutionalist economists may be turned off by the latent conservatism within Commons's writings and embedded within his notion of reasonable value. Second, Ramstad mentions the supposed naïvete noted by Seckler -- that Commons's writings may appear to strive toward unattainable goals, specifically the equal participation of labor and capital in the bargaining process. Seckler saw this as a naïve and unattainable goal due to the inherent power of capital to subjugate labor and the democratic process. This study acknowledges that this is more than a possibility. Third, and most significantly, Ramstad argues that Commons's theory of value is incompatible with the ceremonial/instrumental framework utilized by the Veblen–Ayres School. This view is in part supported by the writings of Commons himself, stating in *Institutional Economics*, "This view may or may not fit others people's ideas of institutional economics" (Commons 1990, 1). From this, it would seem apparent that Commons was not trying to fit into any preconceived idea of what economics was about, but rather was trying to develop a body of thought unique to him.

On the other hand, Atkinson and Reed (1990) propose that Commons's notion of reasonable value is not incompatible with the ceremonial/instrumental dichotomy. These authors point out that both Veblen and Commons were attempting to include intangible property in economic thought. Atkinson and Reed suggest that Commons was aware of and accepted Veblen's dichotomy of pecuniary and technological functions, but because Commons's basic unit of analysis is the transaction, these functions are embedded within his three transaction types, the bargaining, managerial, and rationing transaction -- specifically, the pecuniary function in the bargaining and managerial transactions and the technological within the rationing transactions. Atkinson and Reed submit that the confusion arises from a misunderstanding of the dichotomy. They point out that Veblen's original dichotomy was between industrial and pecuniary behavior that later became technology and institutions. A misunderstanding of the words "technology" and "institutions" is, according to Atkinson and Reed, the source of the confusion. As Atkinson and Reed put it,

> It has not always been clear, for example, whether technology is made up of tools alone, or of tools *and* skills and therefore behavior. Another difficulty that has emerged with the change in the dichotomy lies in the declaration of whether institutions are structures or behavior or both (1990, 1098).

Thus it would seem that, according to Atkinson and Reed, there is no apparent discrepancy between Veblen and Commons, but rather with more recent interpretations of Veblen and Commons. Atkinson and Reed's argument, however, suggests that Commons's writings are potentially incompatible with more modern institutionalist writings. Atkinson and Reed do not address all the problems with regards to Commons and the OIE outlined by Ramstad. Moreover, it is not entirely clear how the claims of Atkinson and Reed refute Ramstad's basic argument. As it is not the purpose here to clarify their argument, this study assumes the reasonable value-instrumental value debate to be currently unresolved.

Some Criticisms of Commons's System

Commons's analysis, although it contains perhaps the best theory of economic institutional change to date, a cautious and sound reform method, and a practical guide to economics, has its flaws. First and foremost, Commons had the good fortune of working in an era open to progressive reforms. The then governor of Wisconsin, "Fighting" Bob LaFollette, was perhaps one of the most progressive individuals of the progressive era. It is clear from reading Commons's work how one gathers and encourages the sort of political and social atmosphere he apparently took for granted. Despite comments to the contrary by Rorty (1982), Diggins (1994) has convincingly shown the pragmatic philosophy has generally underappreciated the role of power in society. While Commons observed problems in the democratic system, it seems possible that he placed too much faith in that system's ability to represent the choice of the people.

Moreover, it is not clear why the current plutocracy would wish to further encourage the widening of sovereignty through progressive reforms. Although

Commons suggests that such reform happens unintentionally, the observations of the author suggest that the plutocracy would ensure legislation to limit the spread of economic power. How, then, does one initiate progressive reform designed to give participants a wider say in their ongoing concerns? In Commons we find the answer in reforms initiated in order to generate greater democratic participation. However, Commons's solutions lack discrete proposals. As mentioned above, Commons was aware that a democracy was only as good as its citizens and actively fought for better education of the nation's people. Commons stated this quite succinctly when he said,

> Two things, therefore, are necessary for a democratic government such as the American people have set before themselves: equal opportunity before the law, and equal ability of classes and races to use those opportunities. If the first is lacking, we have oligarchy; if the second is lacking, we have oligarchy disguised as democracy (Commons 1920, 3).

In his 1907 book, *Races and Immigration in America*, Commons voiced concerns that, at that time, an increasing percentage of the country's citizens were ill-equipped educationally to participate usefully in the democratic process. Commons went so far as to blame many of the political problems of the late nineteenth century on the mismanagement of emancipation and suffrage for former slaves. Commons felt that the newly freed slaves were mentally unable to usefully participate in the democratic process that had led to many of the economic problems facing the South. Similarly, he felt that many of the then-recent immigrants to the United States came from areas of the world that did not cultivate the spirit of democracy. Commons saw the United States as increasingly being populated by people who did not understand the duties of democracy. This, however, does not seem to have dampened his faith in the potential of the democratic system.

Commons gave little mention of possible reforms to alleviate this problem other than to suggest, first, that the citizenry be educated in the democratic process; second, that the United States put caps on annual immigration; and finally, that policy should discourage early marriages. Early marriages, Commons felt, led to increased likelihood of poverty and a continuance of poor education (Commons 1920, 1-22, 198-238). Thus, while Commons seems to have been aware of the problems associated with democracy, he seems to have had no better suggestion than a few policies aimed at increased voter participation. Moreover, he neglected to give any real reason why or how such reforms to the democratic process would take place. Again, we return to Commons's apparent neglect of the given political climate. Despite his above-mentioned harsh words concerning human nature, it seems that Commons placed an undue faith in humanity.

It seems likely that if Commons were alive today, he would approve our modifications to the immigration process. Today, all immigrants, before they are naturalized, must so through testing to prove they understand the democratic process. They must demonstrate that they know who their elected officials are and who make the choices that govern their lives; they are taught to understand the duties of a citizen of democracy.

On the other hand, Commons would likely disparage the current state of national education, where many high school students cannot name the three branches of the national government, let alone tell you what each branch does. Commons would surely say that such a populace bodes poorly for the future of our nation and will likely be lead by a corrupt system of oligarchs.

It seems that much of the problem stems from the implicit optimism in Commons's theory of strategic transactions whereby individuals are seen as having a builder's ideology. Despite Commons's harsh words regarding human nature, he fails to develop an explicit theory of destructive human action. Instead, Commons leaves it to the citizens, economists, and the courts to identify and sanction behavior that does not fit the desirable outcomes outlined in Chapter 4.

As a case in point to demonstrate Commons's tendency toward optimism, Commons seemed to believe that educated employers would find it in their interest to enact progressive reforms. This would occur, according to Commons, for many of the same reasons Henry Ford instituted the $5 per day wage -- to reduce turnover and to ensure a well-trained and loyal workforce. In doing so, Commons makes a few mistakes. First, he again seems to place an undue amount of faith in the businessman to develop an accurate and rational measurement of costs. That is, Commons seems to think that the business community, when made aware of cost-saving alternates, will always take advantage of them (see Commons 1921, 21-35). Second, Commons assumes that workers are firm-specific assets. That is, he assumes that a significant portion of the firm's imbedded intangible capital resides in the worker. In such cases, both parties have an incentive to maintain the labor contract, and Commons's assumption holds true. However, Commons neglected to foresee the modern workforce -- best typified by the fast-food industry -- of workers who have virtually no training and no skills, a workforce that is purposefully disposable, with little corporate culture and little in the way of what Commons would call "working rules."

[12] While Commons seems to have been aware of this problem, he never addressed it directly, only touching on it and then moving on to other areas. From Commons, "On the whole we have seen enough, in these establishments and others, to be convinced that management can provide security of the job if security is deemed important enough" (1921, 270). Thus, despite being aware of the problem, Commons does not offer any solutions. Moreover, Commons could never have foreseen the recent growth in the high school workforce that works to maintain not their livelihood but their lifestyle. In labor situations such as these, the employer has little incentive to reduce labor turnover.

Commons seemed to believe that all parties would wish these reforms, as they would lead to greater efficiency through greater access to up-to-date information. This would certainly be true if individuals thought they would gain more by allowing such access. However, if there is no perceptible gain, individuals might very well fight such reforms with the understanding that the current institutional arrangement yields a profit, so why change it? In fact, recent political reforms would seem to suggest that this is the case. Thus, while Commons chastised Veblen for being cynical, it may well be the case that Commons – at least in his theory of human action -- underestimated human invidiousness. This is surprising, since it is obvious from his ideas about human nature and the importance of a well-educated citizenry that Commons understood the deficiencies of humanity.

Following from the above, one can criticize the supposed conservative stream that runs through Commons's thought. By "conservative" is meant an ideology that is

[12] For an excellent, yet scathing, study into the labor practices and production methods of the fast-food industry see Schlosser (2001)

dedicated to preserving the existing order and its hierarchy. We would suggest that this really is not the case. Commons often stated that his system strove to work within the existing order. Moreover, Commons's reform method never attempts to develop entirely new policies or rules of action. Commons, instead, focused on the general adoption of what he perceived to be the "best" practices. As mentioned above, Commons perhaps placed an undue amount of faith in the possibility of progressive governments. However, he was not unaware of problems in the democratic system, nor did he necessarily believe that the existing leaders *ought* to remain leaders. Without a doubt, the Supreme Court for Commons is the final arbiter of law and hence economic organization. However, Commons was careful to point out that the Supreme Court is subject to the goodwill of the people. As this study has attempted to show, individual problem-resolution is at the heart of Commons's system. Thus we briefly review his theory of human action and his theory of the state.

Commons, as a student of law, was well versed in the legal concept of force and its economic correlative, power. He knew from his extensive experience with the United States court system that it would act in the interest of the largest vested power. Commons understood that the court would naturally function first of all as a protector of the most powerful economic interests. As such, the "public purpose" was likely not to be in the best interests of the whole community, but rather of its ruling class. For Commons, the sovereignty of the individual is a critical element of the just society.

As we saw in the second chapter, Commons's theory of human action is a volitional one. Individuals have -- to some extent -- free will. They are capable of assimilating data from their environment in order to make decisions that will guide them in their everyday lives toward some purposeful future of their own making. Commons's concept of limiting and complementary factors gives the economic agent purpose. In seeking out the limiting factor of any given set of transactions, we can see that individuals thus constantly seek out directions from which to improve their situation.

As such, individuals are equipped with the volitional tools required for participation in the democratic process. Individuals therefore posses the tools with which to make educated choices about their best means of representation. It merely remains for the social policy maker to facilitate individual decision-making skills in the form of education and to open avenues for the citizenry to access the democratic process as well as to ensure a well-educated populous.

Commons's conception of the institution suggests that such devices have the partial purpose of expanding the capabilities of human action -- the state is no exception to this generalization. In Commons we see that the state arises in order to both counter and monopolize the coercive forces of society. It becomes the centralizing force by which the economy is formed and regulated. As such, the economy and its corresponding price system is a function of the monopolized institution of the state and its guiding and protective hand. When combined with Commons's volitional theory of human action, the state naturally becomes an avenue for the expansion of human action. This positive progression is likely to occur naturally as citizens gradually discern good choices from bad ones. This, however, does not suggest that economic reform is unnecessary. In fact, it implies quite the opposite. The economist's role in part is to guide institutions -- specifically those of the state -- toward increased levels of access for the citizenry, as well as to reduce the naturally coercive nature of managerial and rationing transactions.

Thus, from Commons's theory of human action we can see that his concept of progress derives originally from the volitional choices of individual human action and not really from the Supreme Court as suggested by Chamberlain (Chamberlain 1963, 85). When it can be assumed that the latter derives its power from the former, it becomes clear that the court is a valid proxy for the volitionally determined values of the citizenry. Commons knew that it was not the Supreme Court but social custom that determined what was reasonable in the long run. As such, decisions that were not truly in the public purpose would eventually be overturned. Such examples of Supreme Court error can be seen in the recent case of use of marijuana for medical purposes. Despite the ruling of the court, local and state governments have enacted legislation and programs in violation of the ruling. Such actions aptly fit Commons's explanation of the executive power of the public purpose as the will of the populace.

To understand Commons's system as wholly derived from the decisions of the Supreme Court or even the law of the land is to oversimplify. Commons was not the naïve Midwesterner that some have suggested he was. While it has been suggested that Commons attached a sort of divinity to the highest court of the land, this is simply not true. He knew that the Supreme Court was likely to make mistakes and was not likely to act on behalf of all individuals equally. This is not to say that the court would deliberately act out of hostility or neglect for some, but rather that the court would be unlikely to have access to accurate information -- or more correctly, that accurate information would not have access to them. Because the court is made up of legal specialists and not omnipotent gods, Commons knew that any information that the court possessed would likely be conventional knowledge and out of date. For this reason, Commons sought the development of legislative commissions that would investigate the facts of the economy and could provide that information to the courts.

Commons's theory of reasonable value is, in part, the democratic bargaining process by which society hammers out the role of the economy as a function of the public purpose. Reasonable value, however, is not reason, any more than man is a creature of reason. That which is deemed "reasonable" by the courts is not necessarily that which is best in any sense, economic or otherwise -- especially if the sovereign process is limited to a few individuals. Thus, reasonable value as determined by the court only contains as much reason as the sovereign power possesses. It may change or even reverse itself over time; and what is "reasonable" to one may not be "reasonable" to another. In practice then, reasonable is a socially determined process. This is why the critical element in Commons's system is the unwritten understanding that there are ways to make reasonable practices *more* reasonable (see the above section on progress).

Commons failed to investigate the question of whether a democratic state can remain democratic within the property relations of the capitalist system. This question remains open for discussion but is beyond the scope of this study (Tilman 1987, 1379-1401). As mentioned above, the assumption of a progressive regime may be the critical failure of Commons's system. The study suggests that this failure results from his underestimation of the invidious tendencies of humanity. While Commons saw humanity as flawed and sinful, he seems to have felt that people were basically good.

On the other hand, Veblen, as we shall see, saw within people the potential for good as well as for evil. In fact, the proclivities of individuals toward either end formed the whole basis of his analysis.

All this, however, leaves us with the question of whether Commons's work can be considered to fall within the institutional school of thought. In the above section on the OIE, six characteristics were give that may be said to define institutional economics as a unique school of economic thought. It therefore follows that Commons's work should be tested against these on each point.

The first point mentioned above, that group behavior, not price, should be central to economic thinking is certainly true for his thought. While Commons's theories are based upon the volition of individual economic agents, his theory of transactions -- which are the central unit of analysis – involve human interaction, and as such involve group behavior. Prices, on the other hand, are determined by, rather than the determinant of, production. Prices, in Commons's system, are historical accident, the result of economic bargaining power.

On the second and third points, "more attention should be given to uniformities of custom, habit, and law as modes of organizing economic life" and "individuals are influenced by motives that cannot be quantitatively measured," again, Commons's theories fit. As mentioned above, Commons sought to understand how his part-principles of scarcity, efficiency, custom, sovereignty, and futurity shaped and influenced individual action. These part-principles in total constituted his concept of willingness or the socio-historical antecedent from which individual action occurs. Moreover, while the certainty of the wording of the third point is perhaps overstated, it is unlikely that anyone will ever come up with an adequate quantitative measure of custom.

The fourth point, "economic behavior is constantly changing; therefore, economic generalizations should specify limits of culture and time to which they apply," is somewhat more problematic. While Commons was clear in stating that his theories were not scientific "laws" that were universally applicable, he did not specify a "best if used by" date for his ideas. However, this is most likely not the intention of Atkins in writing the above statement. It seems more likely that this statement, along with the third, was an attempt to define institutional economics as a substantative field of study as opposed to the formalistic path taken by the economics orthodoxy. In this, Commons's work also fits.

The fifth point, "it is the task of the economist to study the sources of the conflict of interests in the existing social structure as an integral factor rather than as something diverging from a hypothetical norm," it is certainly true that Commons took conflict of interests, and its corresponding concept of market power, to heart. Indeed, the dominant purpose of Commons's transactional theory is to understand that human interactions, and hence economic interactions, can generally be regarded as containing conflict of interest. This, of course, separates Commons's ideas from the economic orthodoxy which look at perfect competition -- while not the norm – as a benchmark of economic behavior.

Thus, on the first five points, Commons's work seems to easily fit within the defined confines of institutional economics. However, with the exception mentioned above this has never really been in question. The final test as to whether Commons's value conception, reasonable value, is compatible with the Veblen/Ayres instrumental value on the other hand has been a matter of some debate within recent years and as such deserves a section of its own.

Reasonable Value and Instrumental Value

Much has been made of the supposed incompatibility of value systems within the body of thought collectively known as "institutional economics." The case for incompatibility revolves around the argument that Commons's theory of reasonable value is incompatible with the Veblen-Dewey-Ayres conception of instrumental value. While it is true that there are minor differences between the two systems, the systems are not irreconcilable. Although they do not address the value problem from a common perspective or purpose, they represent a convergence of thought rather than a divergence. The misunderstanding stems from the differing perspectives of the different authors. This study believes that the majority of the confusion arises from the fact that the two *do not attempt* to address the same value issues or questions. Consequently, authors who try to directly compare reasonable value with instrumental value are doomed to find incompatibilities. Commons's reasonable value is not meant to address the same issues as the Ayres/Veblen instrumental value; instead, the systems are similar methods of valuation from significantly different perspectives with different purposes. Despite this, a point-by-point comparison of the underlying intentions of these two theories will show that they are in fact surprisingly similar. To this end, an investigation is made of the salient points of both the value systems of Veblen and Aryes. These are then compared with Commons's system.

Veblen also noticed that societies -- particularly his own -- tended to be characterized by the conflicting tendencies of production and exchange. Veblen referred to these as "industrial" and "pecuniary," respectively. However, whereas Commons was interested in the shaping of the public purpose, Veblen was concerned with the workings and development of the capitalist system. Moreover, Veblen and Commons were two very different men who led very different lives. Thus it comes as no surprise that the two developed two seemingly different theories of value. What is surprising is that the two theories are so similar and that so many scholars would make so much of their very minor differences.

As has been documented thoroughly elsewhere, Veblen's system of economy was based around conflicting modes of thought and their manifestations (Dorfman 1945; Ayres 1963; and Seligman 1971). Veblen believed that, embedded within the action of individuals, two conflicting modes of thought operated. Within the actions of mankind, he proposed, we can discern both an "industrious" instinct and a "predatory" instinct. From Breit and Randsom, "The [industrious] aspect was closely related to those activities in which problems were solved through the use of tools, modern science, and matter-of-fact thinking" (1971, 38). Conversely, the predatory, or ceremonial, aspects of behavior are those that are "authoritarian, taboo-ridden, [and] emotion-fraught" (1971, 38).

According to Veblen, in the modern capitalist economy these tendencies are revealed in the separation of industrious or productive actions such as work from those that are destructive or rehabilitating to this process such as ownership and advertising.

Veblen (and Commons) liked to point out that a primary purpose of the modern corporation is to withhold goods and services from those who need them -- that is, to artificially curtail the production of goods and services so as to keep their prices high (Veblen 1904, 8-10; Commons 1911, 463-472). This process is thus a dehabilitating factor in the total productive capacity of the economy. Veblen made the distinction between industry and business and between industrious and pecuniary; the former two created value and increased efficiency while the latter reduced it. Veblen's primary purpose in making this distinction was to show the rampant waste that occurred in the capitalistic process rather than to explicitly develop a theory of economic value. His distinction between industrial and pecuniary is not an easily observable difference. That is, the withholding of production need not necessarily be a bad thing. From Veblen,

> All this does not imply that there is anything discreditable or immoral about the habitual use of strikes and lockouts. They are part of the ordinary conduct of industry under the existing system, and necessarily so. So long as the system remains unchanged these measures are a necessary and legitimate part of it (Veblen 1948, 434).

Veblen's aspects of economic activity are psychological rather than physical and not wholly separable from each other. All physical aspects of economy contain motivations that are both pecuniary and industrious -- it is not a matter of black and white, but rather of degree. This misunderstanding of the distinction made by Veblen was both clarified and muddled years later when Clarence Ayres took the Veblenian dichotomy and turned it into a theory of value.

Aryes attempted to show that the majority of revealed individual values are illusionary. That is, consumer tastes and preferences do not reveal "true" value. Thus, the majority of economic or price values that any given society produced would be little more than historical accidents. This does not mean that the price system does not convey useful signals, nor would Ayres suggest such a thing. However, the signals that prices fail to explain do not convey the means by which the economy is instituted, or any true idea of value. Rather, actions, activities, and commodities that have value in the Ayresian sense are those that are instrumental. By "instrumental," Ayres hoped to clarify the aspects of economic activity that Veblen saw as industrious and contributing to the life process (Ayres 1978, 29). We may summarize Ayres's instrumentalism as pertaining to those activities that involve a use of reasoned, non-invidious thinking.

Thus, where Veblen and Ayres sought to develop a theory of social activity with their dichotomy, Commons sought to explain the growth of economy. In developing their value conceptions, Veblen and Commons had very different aims. Thus, when Commons criticizes Veblen for his failure to develop a reasonable theory of value, he is really talking past him. Commons, like Veblen, believed that all individuals had within them "industrial" and "pecuniary" motives, although he suggested that these drives were customary rather than instinctual -- that is, learned rather than tropismatic.

From the above discussion, it seems very likely that the primary confusion between the works of Veblen and Commons comes from the work of Commons. In *Institutional Economics*, Commons chastised Veblen's failure to arrive at a theory of reasonable value. He should have said that Veblen had failed to come to a theory of value in Commons's terms. Commons blamed Veblen's pessimistic view of economic activity. He felt that Veblen's theories dismissed the monetary aspects of economy as being wholly wasteful and conspicuous. As is later shown in this chapter, this is not the case.

In fact, Veblen is frequently cited as having stated that he had no theory of value. This is because the instrumental method of value is not a theory of value in the same way that Commons's reasonable value is a theory of value. Instrumental value in a basic sense is best explained in the writings of Ayres. From Ayres, instrumental value is not a method by which prices are determined, nor is it a policy-making tool in any sort of finite or discrete sense. Rather, "instrumental" refers to the educated decision-making process of individuals. Choices are instrumental when they are properly informed and noninvidious. This does not mean that instrumental value provides a general policy rule; such decisions need to be made pragmatically. Many of the more recent writings attempting to clarify the issue of instrumental value have done little to alleviate the confusion of the theory's purpose. Claims that instrumental value proves some sort of general policy-making tool are not only incorrect but have led to misunderstanding of both Veblen's and Ayres's work.

Herein lies the error that many have made with regards to comparing the works of Commons and Veblen. Many commentators on Veblen's work have suggested that he saw "pecuniary" activities -- the practice of withholding goods and service from others -- and "industrial" activities -- the production of useful goods and services -- as aspects of economy that are destructive and productive, respectively. The study does not refute this conclusion. However, possible misapplication of Veblen's dichotomy has led to much confusion between the work of Commons and of

Veblen. Moreover, as has been shown above, Veblen's pecuniary and industrial do not necessarily correspond to "good" and "bad" respectively. Additionally, it is important to point out that Commons's managerial transactions and bargaining transactions and Veblen's pecuniary and industrial activities are not theoretically equal units. Veblen's distinction was based on the psychological motivator of action, while Commons's are based upon legal relationships. To compare Commons's dichotomy of bargaining transactions versus managerial transactions with Veblen's pecuniary versus industrial is in fact comparing apples and oranges -- *the former is a theory of human interaction while the latter is a theory of human action.* When one compares the actual value criteria of Veblen and Commons, one finds that they are remarkably similar. Both authors regard choices based upon observation, factual evidence, and democratic procedure as "better" than those based upon self-aggrandizement, ceremony or tradition, and limited information.

At this point, it may be useful to review Commons's theory of institutional change. In his introduction to the formidable *History of Labour in the United States*, Commons explains the cause of economic growth and development to be partially the result of the expansion of markets (2000, 3-8). It is, in part, the quest for profitable ventures that drives this expansion. According to Commons, the mere "instinct" of workmanship is not enough to ensure economic growth; it is also the entrepreneur of capitalism that is a significant driving force behind economic growth. Thus, it is the quest for scarcity value in bargaining transactions that, in part, fuels the fire of the production process. As Commons puts it, "The foreman or laborer does not find the materials and labor ready at hand, furnished by nature. He finds them held by owners of materials and owners of labor-power" (Commons 1990, 672-673).

Thus, Commons did not see the bargaining process not as something to be minimized or eliminated in the economic process. He knew that transactions of both types not only imposed limits upon society but also were capable of liberating individual action.[13] In order to avoid excess, Commons saw the necessity to regulate transactions of the managerial type as well as the bargaining type. His understanding of productive human motivation caused him to misinterpret Veblen's work.

What Commons neglects when he dismisses Veblen's "instinct" of workmanship is that his concept of the limiting factor is essentially the same thing. Granted, Commons's human action, motivated by his concept of the limiting factor, is a theory of action that can be either reasonable or unreasonable, whereas Veblen's theory applies to a specific mode of action. However, as has been noted by Bush, (1987 and 1994) and Ramstad, (1986) both Veblen's and Commons's theories derive from the basic concept of the pragmatic individual derived from the writings of Peirce. Commons and Veblen are working from the same basic framework of the human will in action. However, where Veblen's purpose is to identify the positive and negative aspects of human action, Commons's purpose is simply to identify the basic motivator of action.

As we have seen above, Commons's theory is a general theory of human action and does not differentiate "good" actions from those that are "bad." In

[13] As an interesting note, the reader should be aware that both Chamberlain (1973) and Frederick (1995) – the latter a student of Ayres -- have done studies on the instrumental aspects of "business" behavior. These works point out that the supposedly "negative" aspects of business behavior and the "positive" aspects of industrial behavior are not so clear cut.

Commons's system we only see such a differentiation being made implicitly. Perhaps because of his background, Commons is wary of making normative prescriptions. However, as this study has attempted to show, Commons's slant can be deduced. For actions in Commons's system to be deemed truly "reasonable" in a normative sense, they must correspond to certain modes of thought that may be roughly equated with Veblen's "instinct" of workmanship. From Commons's personal choices in action we can see that for him, choices that are based, first, upon the "best" practices pragmatically investigated and, second, upon alternatives reached by the greatest amount of participation possible, are better than those that are reached through other methods.

As has been mentioned, Commons saw the economy as an administered process, both created and guided by society for its own public purpose. To this end, the society sets the "rules" -- hopefully based upon pragmatic investigation -- for what may or may not be done in the economic process based upon what is and what is not in the "public purpose." As mentioned above, such "rules," or modes of operation, when based upon pragmatic investigation, may be defined as being "reasonable."

As mentioned above, another major problem is that the current literature compares Commons and Veblen on their own terms rather than delving into the meaning of what has been said. On first observation it appears that Veblen's dichotomy is a discussion of the same subject matter as Commons's bargaining and managerial transactions. To some extent, this is true -- both represent the divergent economic practices of management and industry. However, within Veblen's work there is an implicit concept of value that is not present in Commons's transactions.

As we have seen, the Veblen-Ayres theory of value suggests that true values lie neither in the price interaction of the market nor the subjective preferences of individuals, but rather in the decision-making tools of individuals. As such, instrumental value is not a theory of choice -- it is a theory of action. Commons's reasonable value, on the other hand, is a theory of price as well as a theory of economic interaction. To try to compare the two directly is bound to lead to some confusion. To find instrumental value in Commons, we must look further toward his theory of human action, to his theory of limiting and complementary factors. This theory, as we now know, is the seeking-out by individuals of the factors that impede progress towards a desired end. Thus, the limiting factor of Commons's system is a reasoned and educated choice -- as such, it contains the ability to be instrumental. Commons's reforms are designed to make individual choices more "reasonable" and thus instrumental.

The desired ends of individuals can either be realized through bargaining or managerial transactions. These desired ends might either be deemed "reasonable" or "unreasonable" depending upon the given public purpose. In Commons's system, choices that are the best existing practices ought to be deemed reasonable. Commons knew that many choices deemed reasonable by society are not what the OIE would refer to as "instrumental." As we have seen above, he advocated for the use of best existing practices to be deemed reasonable. While we can see that Commons's reasonable value is not universally instrumental in the Ayresian sense, his human agents acting upon "limiting factors" through the channels of society have the potential to act in a way that would be described as instrumental. What is most important is that in his work, Commons took action to see that those ends that may be described as being instrumental are those that are adapted as reasonable.

The difference between the so-called Commons and Veblen-Aryes "branches" of the OIE is really a difference of emphasis and variables. Commons sought to reform existing economic institutions, particularly the producing aspects, toward more socially desirable ends. Particularly, Commons sought to make the producing aspects of the process of social provisioning more humane or reasonable. On the other hand, the Veblen-Ayres "branch" of OIE concentrated more heavily upon social criticism than on the processes of production. This "branch" has focused on the destructive aspects of the values of commercial society. Where Commons focused on the productive institutions of economy, the majority of the OIE has focused upon the consumer side. More than anything else, Commons sought to make the process of work more humane. His declaration that the passing of workers unemployment compensation legislation in 1932 was the greatest achievement of his life is testament to this.

It is the opinion of this study that the lack of social criticism in Commons's work is the main reason why the majority of those engaged in the OIE today neglect his work. The aspects of economy that he focused on are simply not of interest to the majority of those engaged in original institutional economics. As Stanfield and Stanfield (2000) have shown, a significant number of those engaged in the OIE literature for the last several decades have been schooled most thoroughly in the

Ayrsian branch of institutional economics rather than the so-called "Wisconsin school" of Commons. This branch has focused primarily on social criticism while the "Wisconsin School" has not. Commons's students for the most part went on to serve in government positions. As Harter has noted, even when Commons's students did teach, they rarely taught his theory of economy; instead, they focused on practical applications (1962, 253).

The position of this study is that the works of all the OIE authors outlined above represent aspects of the same theory of economy. While it is certainly true that the legal structure of society does not jibe with Veblen and Ayres's concept of "technology," it is certain that Commons's reform method attempted to base the legal regulatory system not upon custom but rather upon the pre-existing technological structure. Thus we can see that both theories have 1) compatible theories of human action and human knowing based upon the pragmatic philosophy of Peirce and Dewey; and 2) similar theories of institutions and institutional change: the impetus to change induced by changing technology in Veblen and the strategic transaction of Commons's individual agent. Both contain, to some degree, a theory in which individual agents who are a product of current institutional arrangements are induced to act and change those arrangements. This is much more explicit in Commons's system than in that of Veblen, which has led some commentators to suggest that Commons's theory is better than Veblen's (Bazolli 2000, 64-82). Finally, all three authors have compatible theories of value.

Of course the economic theories of Veblen, Commons, and Ayres are not *completely* compatible. Specifically noteworthy is the difference in the role of the individual agent in each system. However, their theories do not conflict with each other. As has been noted by both Stanfield (1999) and Gruchy (1987), the current state of institutional economics suffers from a lack of formalization. As a school of thought that has languished in infancy for the last hundred years, we must be willing to make some allowances for it. Despite its staying power, institutional economics has not had the human capital to compete with the orthodoxy of economic thought; as such, its development has been slow. This study suggests that the OIE would benefit from some degree of increased formalization. This should not be taken as acceptance of the extreme formalization of neoclassical microeconomic theory. However, more concrete theoretical statements are certainly needed. It is the hope of this study that this work will provide some of the raw material for such future works. The recent interest by those outside the field of OIE in concerns that have historically been discussed almost wholly within it should be taken advantage of.

Summary

This chapter has shown 1) that Commons's economic theory is compatible with the theories of other authors in the OIE tradition; and 2) that the value conceptions typically referred to as "instrumental value" and "reasonable value" are, in their correct applications, two explanations of the same value criterion. Specifically, this chapter has shown that reasonable value and instrumental value are not variables that can be equated to one another -- reasonable value does not equal instrumental value. The reason for this is that Commons and Veblen had different purposes in designing their value theories. To understand the true meaning of

Commons's and Veblen's theories, this study suggests that one has to understand the personal value conception of each author. One has to consider not simply each author's value conceptions but each one's entire economic method. When one considers the value conceptions of Veblen and Commons, this study maintains that the two theories are demonstrated to be the same. Specifically, the personal value conceptions of both authors are derived from the pragmatism of Peirce. Also in this chapter this work has attempted to show that while Commons's system did an excellent job in reforming the U.S. economy in the early years of the twentieth century, it has some rather fundamental flaws -- most specifically, Commons's optimistic faith in the plutocracy and government to initiate progressive reforms.

Whatever the failures of Commons's system, it should be clear that his thought represents a complete theory of economy. Within Commons's thought, all aspects of economic activity are explained. While Commons's theory does not address the issues traditionally covered by economics, this does not mean that significant insights are not revealed. In Commons, we find a theory that explains economy as a purposeful, socially driven process. Commons's economics stresses the importance of a well-regulated economy with well-enforced property rights, equal access to both information and the governing process, and social support of the bargaining process.

Also this study attempts to show that, despite their age, Commons's ideas are highly relevant today. Specifically, his suggestions regarding increased public access to governance structures could lead to better regulatory agencies and less ambivalence from the general public toward such regulation. Commons's regulatory reform should be seen as a viable alternative to the modern-day "deregulate it" attitude. Such reforms would create a truly cooperative role in determining what is good and reasonable for society.

An example of the relevance of his ideas is Commons's contention that monopoly, not perfect competition, is the norm for economic organization. The traditional idea that monopoly is bad because it lacks allocative and technological efficiency leaves out critical variables -- namely, did the monopoly reach its current status through efficiency or through unreasonable withholding or abuse? These questions have been addressed within the NIE but are not yet part of the general economic discourse.

Chapter 6
Commons and the New Institutional Economics[14]

The primary purpose of this final chapter is to reveal the relevance of Commons's work and the work of the original institutional economics (OIE) to the body of economic thought generally referred to as new institutional economics (NIE). Further, because to date, scholarly exchange between the OIE and those within the NIE has been limited, a secondary purpose of this chapter is to point out aspects of each school that could add to the ideas of the other (see Chapter 5).

Hardly a "new" school, the NIE has developed over the last fifty years. Generally tracing its origins back to Ronald Coase's 1930s work on the theory of the firm, the NIE's economic theory derives predominantly from the concept of transaction costs. Borrowing from Coase, in the NIE, economic institutions develop in response to the costly aspects of transacting. More specifically, in the presence of market failures, economic institutions develop to mitigate these failures.

Recently, the NIE has become significantly more influential in economic circles. Douglass North's recent Nobel Prize is testament to the recently expanded influence of the newer institutional school. Exponents of institutional economics in

[14] For works comparing the OIE and the NIE the reader should consult Dugger 1983 and 1995, Groenewegen and Nagelkerke 1995, Jacoby 1990, and Rutherford 1995 and 1996.

general should realize that the NIE provides a credible voice for many of the issues addressed in the earlier institutional school.

Commons, the NIE has sought to understand the role that property rights, specific assets, and information play in the economic process. Unlike Commons and the OIE, the new school has remained on friendly terms with the economics orthodoxy. However, as this chapter will attempt to show, it is likely that value issues that the NIE will eventually have to address will likely move that school into conflict with the orthodoxy, much as happened with the OIE.

The work of John R. Commons is occasionally mentioned within the literature of those who have come to be associated with the "newer" institutionalist school of economic thought. While Commons's work is not fundamentally different from the rest of the OIE (see Chapter 5), his work is more often cited than other OIE authors in the NIE literature. Both Oliver Williamson and Douglass North, two of the preeminent authors within this school, list Commons's works as influences on their work. North (1990) has praised Commons's analysis of institutional change and structure, while Williamson has stated that Commons's use of the transaction as the basic point of analysis is helpful in examining certain economics issues (Williamson 1986, xi.). This study will make a brief examination of the NIE with an eye toward its relevance to Commons's work.

The New Institutional Economics

On the surface, the NIE would seem to be a very different school of thought from that of the OIE. The NIE employs a different theory of human nature and human action. When compared to the OIE, the NIE sees the role of institutions and institutional development differently, and the two have different research agendas. However, when one scratches the surface, there are many similarities between the two not obvious at the first look.

The NIE literature appears to be one in conflict. Within the recent literature, some writers in the NIE tradition seem to be embracing many of the ideas of the OIE (Mouhammed 1999, 630-647; Knight 2001, 28-48; Wolfstetter 2001, 53-55; North 2001, 3-8; Nee 2000, 64-88; Williamson 1975, 3, 1986, xi), while others seem dedicated to the neo-classical model (Brauninger 2000, 646-660; Guth and Ockenfels 2000, 335-347; Kim and Lee 2001, 499-519). Any attempt to present a NIE paradigm of beliefs is nearly impossible. Therefore, this study takes the approach of the last chapter and considers primarily the work of the school's acknowledged founders -- Douglass North and Oliver Williamson.

Douglass North is perhaps the most recognized proponent of the NIE. As mentioned above, he was the first Nobel Prize winner to write on the topic of institutions. In the last twenty years, North's work has slowly moved away from its more orthodox outlook, and the rest of the school has followed. A brief review of North's institutional theory therefore is warranted. North defines institutions in a fashion similar to that given by members of the OIE, particularly Commons. From North,

> Institutions are the humanly devised constrains that structure political, economic and social interaction. They consist of both informal (sanctions, taboos, customs, traditions, and codes of conduct), and formal rules (constitutions, laws, property rights) (North 1991, 97).

As North explains, institutions determine the choices available to the economic agent. They evolve incrementally as changes in relative prices cause individuals to chafe under current institutional structure and force modifications. North's use of the term "relative prices" should not be taken too literally. Changes in relative prices may occur for a number of reasons both directly or indirectly related to the market. The resulting institutional change, in North's system, may or may not lead to long-term economic growth. Change may also lead to undesirable results. To explain, clarification is called for.

In the above definition, North's description of institutions as constraints is misleading. Elsewhere, North suggests that many economic and social institutions lead to increasing returns with regard to output. Through lowered information costs, learning curves, and so forth, additional units of input can lead to proportionally greater amounts of output. Thus, institutions must not only constrain human action but also expand it -- by North's own explanation. However, according to North, due to market failures -- imperfect information, poorly defined property rights, and the like, as well as learning effects -- there can be no assurance that institutional change at any given time will necessarily lead to those changes capturing any significant gains from trade.

Because North's institutions often lead to increasing returns, future institutional change often becomes "locked" into existing technological paths. That is, institutional structures are "path dependent," whereby the state of existing production can determine the future paths of production. Although not an example of North's, the United States interstate system is a case in point. The existence of the highway system has decreased the cost effectiveness of other forms of transport, including light rail. Thus, we find ourselves trapped into a technology that is perhaps less than desirable given current problems of urban sprawl.

Path dependence can lead to outcomes that are socially and economically desirable or undesirable, although we should note that North himself focuses almost solely on the economic outcomes. Thus, we find North admitting that economic growth owes much to the existence of institutions that are conducive to economic growth – i.e., institutions matter. As such, North concedes that in the presence of positive transaction costs, central authorities have a role to play in providing the incentives for progressive institutional development (North 1990, 48, 2000, 7).

Like North's institutional analysis, the work of Williamson is based upon the transaction. Williamson, like North, sees institutions as cost-reducing, socially devised constraints. Williamson has focused on the area of NIE that he referred to as transaction cost economics (TCE). To see the connection between Commons's work and Williamson's, we only need look at Williamson's basic tenets of TCE. Williamson states,

> 1) The transaction is the basic unit of analysis.
> 2) Any problem that can be posed directly or indirectly as a contracting problem is usefully investigated in transaction cost economizing terms.
> 3) Transaction cost economies are realized by assigning transactions (which differ in their attributes) to governance structures (which are the organizational frameworks within which the integrity of a contractual relation is decided) in a discriminating way. Accordingly:
>   a) The defining attributes of transactions need to be identified.
>   b) The incentive and adaptive attributes of alternative governance structures need to be described.
> 4) Although marginal analysis is sometime employed, implementing transaction cost economics mainly involves a comparative institutional assessment of discrete institutional alternatives – of which classical market contracting is located at one extreme; centralized, hierarchical

organization is located at the other; and mixed modes of firm and market organization are located in between.

5) Any attempt to deal seriously with the study of economic organization must come to terms with the combined ramifications of bounded rationality and opportunism in conjunction with a condition of asset specificity (Williamson 1975, 41).

Williamson himself is aware of the link between his work and Commons, being the first in the NIE tradition to acknowledge Commons's work. This link between the two is especially clear in the above quote. Specifically noteworthy is Williamson's first point, "the transaction is the basic unit of analysis," which is very similar to Commons's basic unit, "I made the transaction the ultimate unit of economic investigation, a unit of transfer of legal control" (Commons 1990, 4). Noteworthy also is the fourth point, which suggests a comparative approach to economics institutions, also an approach that Ramstad (1987 and 1995) has suggested Commons utilized.

Specifically, within Commons's work, Williamson considers his concept of futurity to be an important antecedent to his own transaction cost economics. Williamson sees Commons's futurity as being concerned with the "similarity of repetition, with variability, of transactions and their valuations, performed in the moving present with reference to future action" (Williamson 1975, 3). According to Williamson, futurity is concerned with recurrent contracting, uncertainty, and the successive adaptations of the bargaining process (Williamson 1975, 3). These, again according to Williamson, are the key components of his transaction cost economics.

TCE, according to Williamson, is the economics of internal organization and is perhaps one of the most active aspects of the NIE. TCE is concerned first and foremost about the economic considerations that cause transactions to shift both to and from the market. TCE asks the question: If markets are efficient, then why do large firms exist? In response, TCE suggests that in the presence of various market failures, it becomes cheaper to circumvent markets and organized exchange within a hierarchy. TCE suggests that in the presence of significant information costs and asset specificity, it often becomes more efficient to produce within hierarchies rather than engaging the market.

Unlike the neoclassical mainstream, Williamson's TCE is based upon the assumptions of bounded rationality and opportunistic behavior. As first pointed out by Simon (1959), bounded rationality refers to a state of rationality wherein individuals intend to act rationally but are limited in their ability to do so. In Williamson's terms,

> Bounded rationality involves neuropsychological limits on the one hand and language limits on the other. The physical limits take the form of rate and storage limits on the powers of individuals to receive, store, retrieve, and process information without error. ...Language limits refer to the inability of individuals to articulate their knowledge or feelings by the use of words, numbers or graphics in ways that permit them to be understood by others (Williamson 1975, 21-22).

Bounded rationality, according to Williamson, occurs for two reasons: First, because the mind is a scarce resource; and second, because verbal and written language is an imperfect vehicle for the dissemination of information. As such, individuals economize on information, gathering it only when there are perceptible gains. Further, parities will often be forced to join in participation and take part in learning by doing.

The second assumption, opportunism, is assumed because it "must be." Williamson does not mean to suggest that all people are opportunistic at all times.

Rather, it is his belief that contracting needs to be designed to accommodate opportunistic behavior. Williamson defines opportunism as "self-interest seeking with guile" (1986, 47). He goes on to explain,

> More generally, opportunism refers to the incomplete or distorted disclosure of information, especially to calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse. It is responsible for real contrived conditions of information asymmetry, which vastly complicate problems of economic organization (Williamson 1986, 47-48).

Williamson states that with bounded rationality alone, without the assumption of opportunism, contracting would be much less costly and market transaction types would be more prevalent than is actually observed. The huge increase in hierarchical contracting relationships suggests that if opportunism is not the norm, it is a significant concern in economic transactions. The firm, then is seen as "organizing transactions so as to economize on bounded rationality while simultaneously safeguarding against the hazards of opportunism" (Williamson 1986, 32).

Borrowing from Commons, Williamson goes on to clarify the aspects of his transaction. He states that these are characterized by degrees of asset specificity, uncertainty, and frequency. The first of these, according to Williamson, is the key unique factor of TCE. Asset specificity refers to production-specific assets both tangible and intangible. Specificities cause transactions to become "locked in" to certain modes of production. That is, when specificities are present, firms have incentives to continue with certain forms of production or contracting even if those methods lack static efficiency.

Game Theory in the NIE – A Point of Comparison

The NIE's use of game theory provides them a valuable analytical tool and demonstrates yet another link with Commons's work. Game theory contains the potential to formalize some aspects of Commons's agency theory. Recall from Chapter 2 that Commons utilized a pragmatic agency theory that he referred to as strategic and routine transactions. Commons felt that individuals generally reacted according to general knowledge or communal folkways (routine transactions); however, in the presence of new, or unusual, or problematic phenomena the individual attempts to correct or analyze the problem (strategic transactions). At first the link between Commons's theory and game theory may seem unclear, but game theory offers an alternative to the universally maximizing behavior found within orthodox microeconomic theory.

Game theory may be generally described as "a collection of tools for predicting outcomes for a group of interacting agents, where an action of a single agent directly affects the payoffs of other participating agents" (Shy 1995 11). Within the NIE literature, game theory is most commonly utilized to analyze business organization and employee behavior. It has also been used to explain the behavior of labor unions and other economic entities. However, despite its widespread use within the NIE, it has remained largely ignored by scholars within the OIE. It seems likely that this is because of its requirement of rational economic agents. This is a problem because irrational action is an essential component of institutional theory. However, as alluded to elsewhere, the rationality problem may be blown out of proportion. For example, socially destructive behavior *can* be modeled using game theory, and *can* be presented as rational so long as the transactor's perceived payoffs are defined. Moreover, the transactors need not know the payoffs. Thus, the rationality question becomes a moot point, given that almost any type of behavior can be presented as rational in economic modeling. The lack of use of game theory in the OIE may also be due to the fact that the majority of studies utilizing this theory attempt to justify traditional economic beliefs. However, there is nothing in game theory that requires such an approach. Consider the following one-shot game, where the numbers on the left refer to perceived payoffs to player A and numbers on the right refer to perceived payoffs to player B.

	B Left	B Right
A Top	10,20	20,10
A Bottom	5,15	10,10

We can see that in the above game, so long as player A believes his perceptions about the payoffs are correct, he will always choose the "top" option. Similarly, B will always choose the "left" option. In choosing each option, the rationality of each agent is not critical, but rather, their perceptions are. If the perception of payoffs change, then so do the choices. It therefore becomes relevant to ask the question of how individual perceptions are formed.

As far as this study is concerned, the majority of the usefulness of game theory lies in the fact that it studies agents in their economic interactions. That is, the essential unit of analysis is the transaction, just as it is in Commons's work. Thus, Commons's transactional forms can in many cases be analyzed as repeated games. Adding to this, Commons's pragmatic agent can be represented in game theoretic terms. While it is not the purpose of this study to analyze game theoretic models within Commons's transactional framework one example is warranted.

Take for example, the case of the individual consumer faced with the choice of whether to purchase a "new" and "improved" fabric softener instead of the tried-and-true choice. This scenario can be modeled using Bayesian Decision Theory. The results of the Bayesian decision problem is expressed as a decision function and not as a particular action. The decision function depends upon the information that the agent receives (Eichberger 1993, 130).

In terms of Commons's system, the consumer is faced with a possible limiting factor: Will the new product increase the efficiency of his washing? Should the consumer modify his choice, or should he stick to the tried and true? This of course will depend upon the expected payout of the choice. If the consumer can reasonably expect *or* be convinced that the new product will increase efficiency, then his normal action will change and he will consume the new product. If the new product delivers the increased efficiency, it will become a complementary factor and a consumption norm. If the new product does not increase efficiency, it will be dismissed and the consumer will revert to the habitual mode of consumption.

Of course, this model contains at least two implicit assumptions. First, it assumes that the information that the consumer receives about the product is accurate. Second, it assumes that the consumer's actions are rational – although this is not necessarily a problem. Finally, it assumes that the cost of action is relatively low. For example, our model cannot address the following questions: How likely is it that the fabric softener will destroy the wash? Is the product available in a size that makes brand-switching possible? And finally, why do we want the softener in the first place?

Despite the problems of the model, it suggests many interesting questions about the nature of transactions. First, this type of modeling.points to the importance of the consumer's expectation of performance (futurity in Commons's terms): What is the appropriate payoff for the new product? Moreover, this type of modeling forces the economist to ask where expectations come from. Is consumer sovereignty a legitimate assumption, or are expectations and hence payoffs manipulated by sellers?

Of course, where choice is relatively cheap, sovereignty is of little matter. A product that fails to produce will quickly be eliminated. However, when choice is costly, sovereignty matters a great deal, while at the same time there is more incentive on the side of the seller to manipulate the claims of the product. In these cases, there would be a role for government or a central authority to provide information, or in extreme cases, legislation.

Models of this sort add nothing new to the work of the OIE, but they could go a long way to formalizing many of the issues long championed by that group. Scholars in the NIE have already done much of the work. Consider the following from a recent article by Andy Clark,

> Much work in economics, the social sciences, and elsewhere takes as a starting point a somewhat unrealistic conception of rationality -- a conception that ignores or downplays both the temporal and the situated aspects of human reason. Biological reason, I shall argue, is

> better conceived as an iterated process of adaptive response made under time pressure and exquisitely keyed to a variety of external structures and circumstances (Clark 1997, 269).

This is the essence of the Bayesian process described above. Clark's study goes on to outline a theory of human behavior that is constantly revising its expectations and hence actions subject to external influences. These actions then revise the external structure in which the individual interacts. Thus, without acknowledging it, he is building upon the tradition of the original institutional economics. For this study, the most important issue is that much of Commons's work can be integrated into modern economic methods with positive benefits to both bodies of thought. While Bayesian game theory adds little to the quality of Commons's work, it does perhaps provide it with superior rhetorical tools.

Commons and the NIE Tradition – An Analysis

Ironically, Commons's focus is also perhaps the reason why his work is more appealing to those involved in the NIE than in the OIE. As seen in the last section, the NIE has focused upon the costs of transacting resulting from market failures. Therefore, the research agenda of the NIE is more in line with the investigations of Commons than current research agenda of those in the OIE tradition. Where the NIE focuses on transacting, the OIE currently focuses primarily on social criticism. This difference is due primarily to the fact that the NIE has been able to ignore the value implications of their theories. Because of this, they have been able to remain on friendly terms with those within the more orthodox economic tradition. However this is not likely to last, as the concept of path dependence points to the endogeneity of wants – a cornerstone of the OIE and an impossibility to the orthodox theory. This in turn will eventually force the NIE to develop a theory of value separate from the orthodox approach. While this theory of value may not be the same as that embraced by the OIE, it will -- if the practitioners of NIE wish to remain logically consistent -- certainly differ from the utilitarian value theory utilized by orthodox economics. This issue is addressed in greater depth in the next section.

Let us for now attempt to make a point-by-point comparison between the OIE and the NIE. In the last chapter, six basic tenets of OIE were listed. From the above, first, group behavior, not price, should be central in economic thinking; second, more attention should be given to uniformities of custom, habit, and law as modes of organizing economic life; third, individuals are influenced by motives that cannot be quantitatively measured; fourth, economic behavior is constantly changing; therefore, economic generalizations should specify the limits of culture and time to which they apply; fifth, it is the task of the economist to study the sources of the conflict of interests in the existing social structure as an integral factor rather than as something diverging from a hypothetical norm; sixth, it should incorporate a pragmatic value conception.

With regards to the first point, the NIE would seem to fit. Williamson's statement quoted above with regards to the transaction being the focus of economic analysis suggests that group behavior is a focus of analysis; however, a good deal of the recent work in the NIE is focused on price determination (Emmon and Schmid 2002; Kim and Lee 2001; Guth and Ockenfels 2000; Brauninger 2000). This seems to reinforce the above statement that the NIE is not as well defined as the OIE.

Concerning the second point, certainly North's work gives attention to the role of custom, habit and law as do the recent works by Knight (2001) and Nee (2000), but again, a good deal of the NIE literature does not. On the third point, the NIE does *not* seem to fit. Almost without exception the work in the NIE considers relative prices to be the prime movers of human action. Indeed, as mentioned above, relative prices are seen within the NIE as being determinant not only of human action but also of institutional structure. Therefore, while path dependence may have the effect of getting prices "wrong" in the sense that they result in less-than-optimal outcomes, the primary policy implication for the NIE is to get the prices right. Thus, the NIE economist would likely answer the question "institutional change for what?" with the answer, "to get prices right."

On the fourth point, the NIE does to some extent shy away from the idea of economic laws. Consider the following from North, "But it is important that we understand that even if we did have it [policy] right for one economy, it would not necessarily be right for another economy and even if we have it right today, it would not necessarily be right tomorrow" (2001, 6). Again, this does not keep other NIE economists from suggesting that the general institutional goal is to get the prices right. On the fifth point, the NIE for the most part does seem to be in line with the principles of the OIE. The majority of work in the NIE starts not with perfect competition as an assumed norm; instead, it – like the OIE – assume a conflict of interests. Indeed, the foundational works of both Williamson and North consider the role of economic power in determining the pre-existing institutional structure and economic outcomes. On the sixth and final point, it may safely stated that the NIE does not – with exceptionally few flirtations – employ a value conception anything like that in the OIE. This, is the focus of the next section, and is discussed in depth there. In total then, NIE share several points of similarity and difference with the OIE.

Despite the differences between the NIE and the OIE there are significant points of similarity. Perhaps more importantly, many of the tools developed by the NIE provide useful insights into Commons's work. Williamson's concept of asset specificity explains some of the weakest points in Commons's theories. Moreover, Williamson's use of asset specificity as a theoretical construct supports North's path dependence. It follows from North and Williamson that industries with productive-specific assets are much more likely to remain path dependent when compared to other, more flexible industries. Moreover, such industries are likely to organize along hierarchical lines rather than engaging in the market. As Williamson points out, as specificities rise, or if information becomes poor or difficult or costly to convey, the costs of transacting rise and production is more likely to occur within the firm. With relation to Commons, asset specificity explicitly explains why transactions switch from the bargaining type to the managerial type, a point mentioned but not elaborated upon in Commons's original work.

We can also apply the concept of asset specificity to the labor contract. From Williamson we can see that if labor is embedded with significant production-specific assets, the firm then has an incentive to maintain the labor contract. On the other hand, for labor that has very little embedded specific capital, the labor contract becomes very tenuous because the firm has little incentive to maintain the contract.

In the third and fourth chapters, we saw that Commons expected educated firms to realize that many reforms such as worker safety, unemployment insurance, and health insurance would lead to greater productivity and lower costs. Using Williamson's TCE to analyze this statement, we can suggest that Commons assumed that embedded within the average worker was a significant amount of value to the firm -- in many cases, a fatal assumption. We may further say that the embedded values are, in fact, the "working rules" of the firm. Again, Commons could not foresee the modern fast food industry and modern retail in general, industries that have gone to great expense to completely eliminate such embedded assets. In this respect, TCE has given us a great tool in analyzing the reasons and causes of the conditions of labor.

Additionally, the NIE has formalized and clarified some of the OIE normative prescriptions. As seen above, Williamson's specificity suggests that certain labor markets are more likely to resolve in more socially desirable ends than are others. Unfortunately, TCE theory suggests that those most unable to help themselves are those who will be most likely to need help. Low paid retail labor is also the labor with the fewest embedded assets, and such workers will be the least likely to have job security, receive benefits, or organize unions. This is a problem that the NIE -- as of yet -- has failed to address. It is likely the case that this is because the NIE, to date, lacks a theory of value; it still suggests that institutional reform occurs and ought to occur as a market cost -- and price -- minimization.

Value Conceptions in the NIE

What is not present in North -- or any of the NIE authors -- is a theory of value other than the utilitarian theory utilized by the mainstream of thought. There is one notable exception. Consider the following from Knight, speaking on the appropriate role of the state, "The free and equal participation condition is fundamental to arguments about the beneficial role of institutional mechanism in solving collective problems in society" (2001 158). This work by Knight is a plea to incorporate pragmatic reasoning into the NIE toolbox. This one article alone, however, does not come close to a consensus on the value question.

This is surprising, because both North's path dependence and Williamson's asset specificities suggest that existing prices are historically relevant. Thus, if the current state of economy is to some extent a function of past technological and social development, and if individuals are only limited in their rationality, then the values of consumers and the output of suppliers is by definition not optimal. Moreover, in North's system, the ability of some institutional structures to capture the gains from trade while others fail means that it is unlikely that the current distribution of resources is optimized. In short, the works of the NIE suggest that the economy is historically relevant.

All this begs the question: If we cannot be sure that market prices lead to optimal or even desirable results, then why should institutional reform be conducted toward market optimization? As we saw above, the NIE explanation for institutional change is individual economic optimization -- the economic man analogy. However, if individual choices are flawed, then institutional structure is flawed. The idea that individuals can make inefficient decisions nullifies the traditional utilitarian theory of value. As such, there is clearly a role for institutional reform in the NIE system other than getting the prices right. Without any workable value conception, the NIE is hopelessly set-adrift. Clearly, the NIE's lack of a workable value theory significantly restricts its ability to yield any meaningful insights about the nature of social provisioning or economy. An incorporation of a value theory similar to Commons's reasonable value would significantly enhance the findings of the NIE.

An understanding of the reasons and causes for why the economy has reached its current state as a function of the public purpose would enable the practitioner to make suggestions about alternative institutional arrangements that might yield greater benefits to the public than the current process does. Moreover, the implicit understanding is that public purpose is more closely reached when democratic participation is developed and when information and technology are efficiently conveyed to legislative authorities. For example, an understanding of the above-mentioned labor problems combined with a theory of value could allow the economist to make policy recommendations and institutional reform to correct undesirable outcomes. Such recommendations might include tax incentives that cause employers to bear the cost of unemployment resulting from a volatile labor market -- such as Commons's unemployment insurance law. Other prescriptions that might follow could include the review of institutional structures to ensure their efficiency with regard to the public purpose. An example here might include a review of the labor and marketing practices of industries, as well as the corresponding legal structure, to ensure that a majority of the public understands the practices of said industries. A third prescription might include the application of economic principles of efficiency to legal and democratic systems.

Summary

This chapter has addressed two issues. First it has shown the significant overlap between Commons's work and the work of the NIE -- specifically, the role that information failures, property rights, and limited or bounded rationality play in shaping the economy. Second, this chapter has shown the role that each theory has in explaining the deficiencies of the other. The combination of the two theories has the potential to yield a powerful analytical tool for analyzing economic activity and guiding economic reform. Most specifically, I hope to have shown that Commons's work would benefit from the TCE framework, while the work of the NIE requires the incorporation of a Commonsesque theory of value.

On the other hand, the economics profession has always been wary of such normative prescriptions. This, of course, is due to the implicit assumption within orthodox economics that market outcomes are "good" in that they represent optimal price and distributive outcomes. This, of course, follows from the mystical and archaic concept of "economic man" as a self-interested utility maximizer. For the NIE to develop a theory of value will require a rethinking of its concept of human action perhaps along the lines outlined in the second chapter of this study.

In conclusion, this study has attempted to convey that both schools of institutional thought would benefit from cross-pollination. Specifically, the OIE could benefit from the NIE's formalized ideas on OIE concepts. On the other hand, the NIE would gain a degree of clarity and a stronger basis for policy prescription by adapting a theory of value such as the "reasonable" theory of value professed by Commons.

Summary and Conclusions

This study has attempted to resolve three issues. The first of these -- addressed in the first four chapters -- is the meaning and significance of the economic thought of John R. Commons. Commons's economic system as explained above may be quickly summarized as follows. Society and its respective institutions act on the individual in a host of ways. Specifically, Commons listed five -- scarcity, efficiency, custom, sovereignty, and futurity. These institutions have the effect of both constricting and expanding human action. Individual action occurs either through passive thought in the form of complementary transactions or through active thought in the form of strategic transactions. These transactions may be said to fall into three types: bargaining transactions – a rough approximation of the market process; managerial transactions -- hierarchical relationships in which one individual commands another; and rationing transactions that involve the rationing of economic output through collective organization. Through their interactions, individuals shape and form the surrounding institutional environment. At the same time, these actions are subject to a social valuation process whereby certain actions are deemed appropriate and others inappropriate. Actions then are to some extent adjusted through the process of collective action to meet the desires of the wider community. Commons referred to this process of social valuation as the determination of reasonable value. It is therefore the case that Commons saw the market not as a natural outgrowth but rather as a deliberately created and re-created process.

Commons's focus on transactions, rather than prices, yields a system of market interaction that incorporates legal and social considerations where the orthodoxy does not. Moreover, Commons's differentiation of different transaction types "demystifies" the economy by separating the productive capacity of the social order from market interactions. Commons's theory convincingly reveals prices as being historical accidents, wholly separate from economic production. Such distinctions make it possible to refute the generally presented argument that market-determined prices are somehow "optimal" in a distributional sense. This distinction, of course, was not new with Commons, being derived in turn from Marx. However, Commons's argument presents a more socially acceptable argument given the current political climate and the strong emotions that surrounds Marx's work.

In the presentation of Commons's work, this study has shown his theory to be an application of the pragmatic philosophy. Pragmatism is more than an influence to Commons's economics -- it *is* in many senses his economics. Pragmatism in Commons's work is characterized in his theory of limiting and complementary factors or the individual's perceptions of critical and non-critical economic variables. Commons's market participants are more than the simple automata of traditional or mainstream economic thought -- they are socially engaged, learning, and developing, individuals that respond to, while at the same time recreating, their social environment. As is shown in the fourth chapter, the rationality of Commons's economic agent is unclear. That is, while Commons openly stated that human being were largely "stupid and irrational," his theory of limiting and complementary factors suggests an individual that acts toward the realization of perceived goals -- thus suggesting rational action. Therefore, future work based upon Commons's work would do well to consider developing a theory of irrational transactions or some such consideration.

In the first four chapters of this work this study has also shown that Commons's transactional structure provides the economist not only with a taxonomic reference of economic interaction but a method of doing economics. Commons's transactions provide the economist with the tools to determine the intent of economic interaction -- that is, to determine if a given transaction serves the public purpose or is reasonable. This study has shown that Commons's application of his economic theory reveals the specific characteristics that define outcomes as being reasonable or unreasonable. That is, Commons's personal value conception is clearly tied up in his theory of reasonable value.

Commons's conception of value, reasonable value, is both a positive and normative conception of value; it is a theory of value that is at the same time social and individual. Commons gives us a vision of prices as both socially constrained and constructed phenomena -- they are constantly redefined in a social context, and subject to social approval. Beyond this, Commons's theory of value is a theory of publicly administered prices. It is also a method of economic reform embodying an objective value criterion. It is suggested here suggested that this value criterion, the source of much debate, is often missed in Commons's work because for the most part it is only given implicitly. His personal history perhaps caused Commons to shy away from normative prescriptions, but they remain in his work none the less. Using the pragmatic method, we can see from Commons's applied work that he considered certain types of reform as being "better" than others are. Commons's applied reform method reveals a general normative prescription that the utilization of knowledge and technology, as well as increased economic participation in economic decision-making, is "better" or more reasonable, than to do otherwise. These "reasonable," or desirable, actions may be described as "instrumental," in the sense that Dewey used the word -- that is, they further the human means-ends continuum.

Commons's economic system, however, is far from flawless. In an attempt to shed some light of the weaknesses of Commons's work this study has also addressed the most significant criticisms of Commons in the literature and has made some criticisms of its own. Perhaps most important is Commons's unfailing faith in his fellow man. Despite his harsh words on human nature, like the pragmatic philosophy that his work was based on, Commons presents a theory that is ever hopeful -- a strategy that served him well in real life, but is perhaps the weakest point in his economic theory. In the opinion of this study, Commons's failure in this respect leads him to overestimate the potential avenues for progressive reform. Specifically, Commons's failure to realize producers' ability to eliminate employee owned human capital in any appreciable sense, thus turning people into cogs of machinery is cited. Witness here the fast food industry with its completely replaceable and instantly interchangeable human capital.

Also, Commons's apparent complete lack of ability to deal with the subversion of the democratic process through disinterested and ill-educated voters weakens his economic theories. However, in all due fairness, this is perhaps asking too much from a pragmatic theory of economy. Commons's theory is limited to the theory of psychology from which it is derived – one that is now over one hundred years old. An area of future research might include a rethink of Commons's work along the lines of more modern psychological and philosophical reasoning. Rethinking Commons's ideas using modern cognitive psychology and Rorty's brand of pragmatism would likely yield significant insights. However, one should note that whatever the weakness of the pragmatic philosophy, it did not weaken Commons's personal ability to initiate reform; indeed, as has been shown above, Commons was extremely successful in this aspect. Thus, "grounding" Commons's theories in a more modern philosophy or psychology would not necessarily make them "better" in terms of being able to initiate reform but merely make them more theoretically consistent.

Beyond the meaning of Commons's work, this study has attempted to reconcile the supposedly competing value theories in original institutional economics -- namely the Veblen/Ayres "instrumental value" -- and Commons's "reasonable value." In the above chapter, it has been shown that the apparent differences between the two lie not in different conceptions of value but rather in misplaced semantics. While it is not clear in Commons's work if economic actions result from learned or tropismatic behavior, both theories involve a value theory based in psychological motivators. Both theories regard motivators that are based upon destruction, coercion, or simply poor information as being "worse" than those that are based upon investigation, democratic participation, and concern for the life process.

This study has shown that much of the confusion about the two theories comes from Commons's own misguided criticism of Veblen. The word misguided is used because the two conceptions of value do not try to address the same issues. Indeed, reasonable value is not instrumental value. However, the concept of reasonable value as a social process is imbued with instrumental value when Commons's theory is considered as a whole. One has to consider the works of Commons, Veblen, and Ayres in total to understand that they all hope to achieve the same goals. Those goals are; first, the reconstruction of the economic agent from the "economic man" to the pragmatic individual. The goal here is to strip economics of its naturalistic basis and replace it with a picture of economy as an administered process in the public purpose. Second, all the above-mentioned authors attempted to provide a value criterion compatible with the needs of a democratic society. Namely, that policy and action ought to best utilize existing technology and knowledge -- through democratic principles -- while at the same time either removing or sanctioning those institutions and transactions that prove to be socially regressive.

This is not to say that all the works of the "founders" of institutional thought contain like ideas. Perhaps the greatest of their differences is that Veblen believed that capitalism was untenable and required radical action. Commons and Ayres, on the other hand, were both liberal reformers attempting to work within the capitalist system. Perhaps work remains to be done in reconciling the work of Veblen with that of Commons and Ayres. Future studies may focus on the realistic possibility of reform within capitalistic societies. As mentioned above, it is likely that Commons was overly optimistic about the possibilities for reform.

Finally, this study has shown the relevance of Commons's work to the developing school of thought collectively referred to as new institutional economics. The aim in this endeavor has been twofold. First, it has been shown that the work of the certain aspects of the NIE sheds a good deal of light upon many of the issues addressed by Commons. Specifically, some of the theories of the NIE explain some of the deficiencies in Commons's theories. Most particularly, the NIE focus on the economics of transaction costs makes explicit aspects of economic interaction neglected by Commons.

For example, Commons neglected the modern producer's ability to minimize or eliminate employee-owned human asset specificity through technology. Commons assumed that employee were generally imbued with assets that were valuable to the firm. Thus, firms would have an incentive to retain employees and for the employees to not be damaged by the labor process. This in turn caused Commons to suggest that employers would be open to progressive labor reform as a cost-reducing measure. The transaction cost literature suggests that this is not the case when human asset specificity is low. Thus, future research might consider an application of transaction cost theory to both Commons's theory of labor and his theory of governance. Research in these areas could greatly clarify aspects of Commons's work.

Additionally, this study has suggested that the NIE would benefit from a value theory like that revealed in Commons's work. Such a theory of value, when combined with the recent additions of the NIE to the economic canon, offer a theory of economy that would provide not only an analytical tool but also a normative barometer from which public policy could be guided. The implicit prescription of

Commons's reasonable value is that the economist has a role to play in guiding public policy, encouraging action that will more efficiently move the economy in directions that are more suited to the public purpose. This, of course, would require the economics profession to realize the place of institutions, their origins and development. Economics would be forced to analyze the economy not as a mechanistic series of optimizing exchanges but rather as a social process designed to provide the populous with the goods and services needed to sustain its development.

In conclusion, this study has shown: First, the scope, method, and significance of Commons's economic thought. Specifically, Commons's work has been explained in a clear and concise framework based upon pragmatic philosophy. Second, it has addressed and resolved the supposed conflict between reasonable value and instrumental value, placing Commons's work squarely in line with the rest of the OIE tradition. This study first attempted to show that when Commons's applied reform method is examined, the meaning of his work becomes clear. Commons clearly used Deweyian instrumental reasoning to advocate policy. This rather unconventional approach to method is an outgrowth, again, of the pragmatic philosophy, which strives not to explain but rather to understand. As such, understanding is to be found not only in words but also in action and experience. Finally, this study has attempted to show the significant linkages between Commons's work, the OIE, and the work of those engaged in the NIE tradition.

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