March 25, 2026

Dear Political Economy program committee:

At the fall meeting I talked with Francesco about a book I have been working on that is just about to come out. It is about the political economy origins of modern democratic capitalisms. The opening, introductory chapter follows.

Francesco suggested that I submit a proposal to the Summer Institute for a session where I describe the book, so it would be a different session that a paper presentation, but could fall within the usual time constraints. Martin Fizbein has read earlier versions of the manuscript and would be a good discussant. I can make a copy of the manuscript available to anyone who is interested.

Thanks for your consideration.

Best, John Wallis

March 25, 2026

Dear DAE Program Committee:

The DAE has been hearing and seeing bits and pieces of the book I have been working on over the years, as well as work with Naomi Lamoreaux.

The book is finally finished and I would like to present the whole package to the DAE this summer. The opening chapter of the book follows. I would present the three main parts of the book in a regular session.

Best, John Wallis

Chapter 1: *Leviathan Denied*

In the 19th century a handful of countries around the world began to *develop*. Societies first appeared that were capable of sustained economic growth over long periods of time, who implemented political systems that selected leaders by elections in which large portions of the population participated, and citizens enjoyed a wide range of political, civil, and personal rights and security. The societies were all capitalisms in the sense that individuals were free to use their resources in whatever way they thought best, within the existing rules. The societies did not all begin growing at the same time, some were large and some were small, some developed modern manufacturing industries and some remained largely agrarian, yet all of them experimented with some forms of democracy at some point. In the crisis years of World War I, the 1920s, and the Great Depression of the 1930s, some of the countries maintained and consolidated their democracies. Others, lost their democracies, fell into different forms of autocracy, and ultimately initiated the conflicts that led to World War II. By the late 20th century all of the countries had recovered their democracies and enjoyed material standards of living not only well above the rest of the world, but unprecedented in human history. Although the details of their political and economic systems varied widely, they were all developed by the criteria above.

Over the last two centuries people have tried to explain the rise of modern developed societies. One aspect of development is technological change, which has transformed the way people interact with the physical world. The other aspect of development is institutional change, changes in the way people organize their societies, their organizations, and live their lives. I will

not attempt to weigh the relative importance of technology and institutions, both are important.[1] This book examines the role that institutions played in the appearance of developed societies and in their continued existence, as well as how we think about institutions, their place in societies, and their place in theories about societies. It focuses on institutions as agreed upon rules that result from a collective decision process within organizations, whether the organizations are private or public. This is a much different, and more limited, definition of institutions that the study of institutions usually uses.

The institutional literatures are sub-fields within the academic disciplines of economics, political science, sociology, and anthropology in the social sciences as well as in philosophy, law, and history. They all talk to one another and are closely intertwined. While some of the divisions within the literatures are very deep, they share a number of common ideas and ways of framing basic problems in understanding how societies work. They are all concerned with the role that rules play in creating and sustaining social order. Social order is an outcome, not a value. People may, however, value peace and stability over violence and disorder. There is little doubt that how people think about the sources of social order leads them to pursue institutional arrangements they hope will strengthen and secure social order.

Political, economic, and social development is largely the result of increases in social order. The next chapter will show that, in economic terms, increasing stability by reducing the rate and frequency with which economies shrink, is a much more important source of long term

[1]The last two Nobel prizes in economics were given in 2024 to Acemoglu, Johnson,and Robinson for their work on the role of institutions in development and in 2025 to Aghion, Howitt, and Mokyr for their work on the role of technology in development.

economic growth than increasing the rate in which economies grow when they grow. Likewise, developed societies exhibit much lower rates of political instability than other societies.

For that reason, and for others as well, all the institutional literatures are concerned with stability in human relationships. The concern is manifest in trying to better understand how people coordinate with each other. While people coordinate in many ways, the formation of organizations that adopt rules to govern the relationships between their members and to increase the value of those relationships by rules that enhance coordination is central to the process of development. More developed societies are better organized, better coordinated, and as a result, more stable. The core idea in this book is that organizations use agreed upon rules to enhance coordination within organizations, and to do so organizations form organizations of organizations to help make those rules better at coordinating, both within and between organizations. The appearance of developed societies in the 19th century was the result of changes in the way those societies used agreed upon rules to enhance coordination and stability.

The institutional literatures all share a common approach to how rules enhance coordination: they are followed. If I believe that you will follow the rules and you believe that I will follow the rules, then in situations where the rules apply you and I are better able to predict how we will behave and therefore can therefore coordinate more effectively. Rule following is at the center of institutional literature's idea about how rules affect coordination. The political economy of institutional development is largely about how societies form governments that can effectively create rules that both the citizens and the government will follow, what is often called credible commitment.

But yet, when the sociologists who study organizations began making serious empirical investigations into how organizations used rules, they surprisingly found that many organizations devote resources to creating rules that members of the organization do not follow. The "assumption [that people follow rules] is based on the view that organizations function according to their formal blueprints: coordination is routine, rules and procedures are followed, and actual activities conform to the prescriptions of formal structure. But much of the empirical research on organizations casts doubt on this assumption." (Meyer and Rowan, 1977, pp. 342-3) The institutional literatures did not completely ignore that many rules were not followed. Organizational sociologists developed some imaginative and creative ideas about the purpose of rules that are not followed, notably in Meyer and Rowan (1977), Dimaggio and Powell (1983), and Powell and Dimaggio (1991). But most of the institutional literatures focus on how societies manage to get people to follow rules, rather than wondering at all about why so many rules could be enforced, but were not followed. That organizations created rules and methods of enforcement, and then let people ignore the rules was simply not an interesting question to ask if the concern was the increase in social order caused by rule following. But it is an interesting question to ask if we want to know how rules actually work.

Organizations adopt agreed upon rules to increase the value of relationships within the organization. They do not adopt rules because following them is, in itself, of value. An example may help. My wife and I were both initially married to and divorced from other people. She had two daughters and I had two sons. When we married and the six of us moved in together, lots of adjustments had to be made. My wife suggested to me that our youngest son, then nine years old,

be responsible for taking out the garbage. I looked into the future and realized that our nine year old would not reliably take out the garbage, even when asked, and that I would be caught in the middle between my wife and my son over taking out the garbage. I suggested that I would take out the garbage whenever she asked me to. We agreed. It was an *agreed upon rule*. It was not a norm of behavior, we had no idea how other people took out their garbage, and it wasn't a pattern that had become a habit over time.

Our garbage rule is enforced, but not followed. I take out the garbage whenever I am asked, usually right away. If you sat by our garbage cans and recorded who took the garbage out, however, you could not infer what our rule was. A half full garbage can bothers my wife more than it bother me, and she often takes out the garbage. Our garbage rule is a *default rule*: it is a rule that can be enforced but is not always followed. It enhances coordination in our organized relationship even though it is not followed. The garbage rules creates an *outside option*. It gives my wife the option of asking me to take the garbage out, and when asked, I take it out. Our garbage rule is not a norm of behavior, there is no pattern to who takes out the garbage, and it is not based on our beliefs about how other people take out the garbage.

In all of the institutional literatures, rules enhance coordination because if people follow the rules then it is easier for people to expect how each other will behave. Yet, the garbage rule enhances coordination without being followed. Throughout the book I will give examples of default rules that are not followed in various settings. For example, it is extremely common that firms write contracts with each other containing many explicit rules. But then the firms put the

contracts in a drawer and their behavior does not follow the rules they agreed to.[2] What matters is not the terms of the agreement but maintaining the relationship between the people who made the agreement.

While the institutional literatures are aware that rules are often agreed to and then not followed, they have not systematically developed insights into how those rules work to support coordination. More relevant for this book, the parts of the institutional literatures who argue that institutions play a central role in the process of social development have ignored altogether rules that are agreed to, can be enforced, but are not followed. If rules that are not followed are important "rules of the game," then attempts to explain the emergence of modern developed societies as the result of institutional changes are bound to be incomplete. We have ignored important aspects of how rules actually work. Existing explanations stress the importance of and include only rules that are followed. Because rule following is associated with enforcement, particularly coercive enforcement, the role of institutions in the development process centers on how can governments be structured that create and enforce the right kind of rules. That is a natural question to ask, but it is not the most productive question to ask.

Two centuries before modern economic and political development began, Thomas Hobbes laid out what he thought was the best form of government in *Leviathan*. Hobbes argued that the most effective way for societies to get out of the state of nature, the war of all against all, was for all the people in a community to agree that they would obey the rules laid down by the Leviathan. In return, the Leviathan would create and enforce rules that would insure PEACE. If

[2]See Hamilton and Bozovic (2016) and Macaulay (1963) for examples and the literature.

Leviathan failed to provide PEACE, the people had no obligation to obey his rules. In Hobbes's logic, the Leviathan had strong incentives to make and enforce rules that led to PEACE. His logic was brilliant, in many ways centuries ahead of his time. It was not until powerful nation states began to dominate the world's economy and polity in the 18th and 19th centuries that political and social theories began to seriously consider Hobbes and his ideas about social order and the ability of societies to limit violence.

Like many before him, Hobbes's understanding was that the source of social order was the creation of rules to govern relationships between people. Those rules must be followed in order for people to expect that others would follow the rules, the expectations that sustained social order. In order to credibly be followed, however, the rules needed to be backed by coercive power, where coercion is the threat of violence. Hobbes's logic effectively explained how the coercive authority could be incentivized to create and sustain rules that would insure PEACE. People would obey the Leviathan's rules, including orders to punish rule breakers, as long as Leviathan and the rules resulted in PEACE. Hobbes logically spelled out how violence could be sufficiently organized and then used to create a sustainable social order. It required rules and laws, and much of Hobbes's thinking concerned the nature of rules.

With the appearance of modern societies characterized by steady and sustained economic growth, selection of leaders by elections, and constitutional governments Hobbes's ideas became much more relevant. His growing influence was not because single actor powerful Leviathan states were appearing. Hobbes offered two crucial insights. First, Hobbes offered a clear logical explanation for why a powerful state would be willing to obey its own rules. Second, Hobbes

explained how violence was organized. If coordination between people required rules that were followed, and rule following required a state with coercive power, then how the state organized violence would surely affect how the state used the threat of violence – coercion – to insure that rules were followed.

The connection between coercive power, the organization of violence by the state, the enforcement of rules, and the degree of coordination possible under those rules did not begin with Hobbes. He was hardly alone among political theorists in asserting that rule following was necessary to support social order. Republican theorists, from Aristotle through Polybius, Machiavelli, and Harrington were just as concerned about rules and social order, but they argued that mixed and balanced government was the key to social order by providing the best protections of their freedoms and liberties. Republican ideas play as large a role in this book as Hobbessian ideas. Republican ideas about constitutions and mixed and balanced government had much greater effect on the institutional changes in the structures of government in the 19th century than Hobbes, as we will see.

Hobbes, however, had an outsized effect on the way social theorists attempted to explain the increase in social order in the developed societies of the 20th and 21st centuries. Not all the ideas originated with Hobbes, but he put them in a very attractive package for theorists who wanted to build logical models of societies. Hobbes reaches three conclusions about the best form of government. They are:

1) Social order requires rule following,

2) Rule following requires credible enforcement which depends on a credible threat to use

violence to enforce the rules. Powerful individuals and organizations agree to abide by the rules the Leviathan establishes because that is the only way for them to avoid the state of nature; and

3) The Leviathan must be a single decision maker, even if Leviathan is an organization the Leviathan must be a "single actor."

After WWII, when social scientists, historians, philosophers, and legal scholars began trying to explain how developed societies first appeared and how they worked, Hobbes offered an attractive model. People didn't follow Hobbes because they thought Hobbes was right about a government that everyone obeyed,[3] they followed Hobbes because he had a coherent logic that gave them a conceptual framework to think about how powerful nation states could manage to protect, rather than exploit, the civil, political, and economic rights of their citizens. Hobbes claimed that he was first political scientist. Geometry, not physics or chemistry, was his model science. Euclid derived his geometry logically from a few simple assumptions. That was precisely what Hobbes did with politics and the state. The models of states and societies that built on Hobbes shared three characteristics:

1) The State was a single actor. There is only one source of agreed upon rules.

2) Social order depends on rule following.

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[3]"... Hobbes wrote Leviathan, which many readers today read as a defense of absolute monarchy, but which was a defense not of monarchy but of absolute authority in whatever person or persons it was vested. Hobbes certainly thought that monarchy was the best form of government, but he did not think that it was possible to demonstrate it. What he thought he had demonstrated was that political authority must be absolute." (Ryan, *On Politics,* 2012, p. 415) Few who drew on Hobbes in the 20th century thought the best government would be absolute.

3) Rule following required a rule enforcer who possessed sufficient capacity for violence to discipline everyone in the society.

Many theories of development used this framework as a starting point. The Pluralist political scientists Robert Dahl, David Truman, Seymour Martin Lipset, Stein Rokkan, and many others as well post-pluralists like Margaret Levi and Theda Skocpol. The economists and economic historians, Douglas North, Robert Paul Thomas, David Landes, Daron Acemoglu and James Robinson, and Yoram Barzel. Sociologists Charles Tilly, Anthony Giddens, and Margaret Archer as well as the earlier work of Max Weber, Emile Durkheim, and Karl Marx. In law H.L.A. Hart and many others. In anthropology Robert Bates. The list could go on for pages. I draw on all of these literatures throughout the book.

This book is titled *Leviathan Denied.* Not because Hobbes is wrong, he is brilliant. But because Hobbes's 17th century ideas flavored the kind of ideas that developed in the 20th century to explain the emergence of modern developed societies. Hobbes could not have imagined, much less observed, modern developed societies. Yet, the way Hobbes set up the problem of rules and social order has had an enormous effect on 20th and 21st century thought. Those ideas ignore rules that are not followed as an important element of institutions.

Hobbes claimed he was a political scientist because of his logic. This book argues in much the same way. Using a definition and two simple assumptions, it provides an alternative way of explaining why modern developed societies emerged, why the have survived (to date), and why so few other societies have made the development transition. Like *Leviathan* it is purely a logical argument. Unlike *Leviathan* it also tests the implications of the logic by

explaining/testing how and where democratic capitalisms emerge in the late 19th and early 20th century, why some of those nascent democracies lost them between 1920 and 1940, and why so few additional developed societies have emerged since. After the next chapter on stability and expectations, the book develops the argument in three parts: concepts, history, and implication

1.2 *Concepts: Rules and Organizations*

Rather than beginning with the relationship between rules and organizations at the level of whole societies, the framework begins with rules and organizations at the level of a single organization with a definition and two assumptions.

The definition: organizations are groups of people who adopt rules to govern relationships between their members.

The first assumption: rules are adopted to increase the value of relationships between the members of the organization.

Organizations encompass the gamut from families, to firms, to universities, to businesses, to states and nations. They are all forms of interactions between people in which rules play a role. The assumption is that rules enhance, rather than "maximize," the value of relationships, because there can be many people in an organization and how we should weight their different values is too difficult a problem to solve. Rules increase the value of relationships between people by enhancing their ability to coordinate. In this book all "rules" are agreed-upon-rules within organizations, a very important distinction. Norms of behavior are not rules in this book.

The second assumption: any individual who is not better off from belonging to an

organizations, i.e., gets a rent from belonging, will leave the organization. The second assumption is the *participation constraint*. This assumption amounts to assuming people are rational, but it is better to be explicit about the constraint because it plays a central role in the theory.

If rules are adopted to increase the value of relationships, then no one can believe that a rule will be followed in all circumstances. Every rule, if followed, will in some circumstances reduce the value of relationships within the organization. When those circumstances arise, the organization will ignore, change, or repeal the rule. This is the *fundamental tension*. Relationships always dominate rules. W can never expect that any rule will always be enforced regardless of circumstances, that would be an irrational expectation.

Given that rules enhance coordination because people form expectations based on the rule (the logic of rule following in the institutional literatures), rules that people know will not be followed in all circumstances are not as effective at coordinating people. If people are at all rational and forward looking, they know that not all rules will always be followed. How do organizations attempt to mitigate the fundamental tension?

The answer is that organizations reach agreements with other organizations to create and enforce rules for each other. In very general terms, if the relationships in one organization are insulated from relationships in a second organization, then having the second organization enforce rules for the first organization may mitigate the fundamental tension. When I was younger I worked construction jobs. I belonged to the Laborer's and Hod Carrier's Union and usually worked as a carpenter's helper. The Laborer's Union and the Carpenter's Union reached

an agreement with the construction firms to enforce specific rules. One was that carpenters could drive nails, laborers could not.

In practice, however, laborers often drove nails. Although the rule was clear and everyone understood the rule, the union nail rule, like the garbage rule my wife and I adopted, was a default rule. Every laborer/carpenter pair was different. They were heterogenous. Because the nail rule is a default rule, the construction firms and laborer/carpenter pairs could use the nail rule to enhance relationships, but they did not have to follow the rule in practice. Only if a dispute arises and is taken to the unions, is the external rule enforced. This gives the firms and pairs a much greater degree of flexibility to organize their work. Rather than always following the rule, they use the rule as an *outside option*. The logic of how these external rules work is explored in Part One.

The nail rule coordinates best if it is an impersonal rule. That is, even though carpenters and laborers have different identities under the rule, if the rule applies in the same way to all carpenters and laborers then the carpenters, laborers, and construction firms know how the rule will be applied. The nail rule will be more effective if the personal identities of the carpenters and laborers do not affect how the rule is applied. Impersonal rules apply in the same way to large groups of individuals. Identity rules, in contrast, apply differently depending on the identities of the parties to whom the rule applies. People cannot know how an identity rules will be applied in the abstract, because until the identities of the parties to the dispute are known, how the rule will be applied cannot be anticipated.

Together the firms, the workers, and the unions make up an organization of organizations.

In Part One, I call an organization of organizations a *rosette* (it looks like a rosette in the figures). Within a rosette, the rules are much more effective at coordinating between members, and between organizations, if the rules are impersonal. External impersonal default rules are more effective coordinating rules than internal prescriptive identity rules. Part One derives and explains the economic advantages of impersonal rules, even though those rules are not necessarily followed. Societies did not structure governments that were able to create impersonal rules for a wide variety of purposes until the middle of the 19th century.

The logic of a rosette can be used to explain how violence can be organized, but in a very different way than Hobbes. Powerful organizations, the ones with the potential to be violent, form agreements that create rents for the members of the agreement. Typically the agreed upon rules are identity rules that vary from individual to individual. The special treatment the rules create is the source of the rents that each member of the organization enjoys. The rents help hold the organization together. This is the "logic of the natural state" in *Violence and Social Orders,* the book I wrote in 2009 with Douglass North and Barry Weingast.

The title of this book is *Leviathan Denied* for three reasons.

1) Governments and states are never single organizations, they are always organizations of organizations.

2) While rule following is important, there are many rules that can be enforced but are not followed. Within organizations of organizations rules are often more effective if they are impersonal default rules. By their very nature, these rules are not coercively enforced, yet they play a critical role in the maintenance of social order.

3) Agreed upon rules are always the creation of organizations, and the rule environment, which contains the collection of all the rules in a society, is never under the domain of one government organization. If institutions are the "rules of the game," then we must understand how organizations create and utilize rules to enhance coordination, throughout a society. Modern development is the result of changing the way the rules interact with each other throughout societies, not just the rules the state enforces.

These reasons are not just different from Hobbes, they are aspects of rules and organizations that the institutional literatures, all the authors I mentioned earlier, including North, Wallis, and Weingast, have overlooked. Part One explains why moving to impersonal default rules could make economies much more productive and so explain the onset of modern growth. But how does a political system manage to credibly create and enforce impersonal rules?

1.3 *History: Impersonal Rules and Consolidated Party Systems*

In most societies governments create and enforce identity rules. Even in early 19th century Britain and in the American states, 75% of all laws passed by Parliament and state legislatures named specific individuals, specific organizations, or specific localities to whom the law applied.[4] These societies had identity rule legal regimes. Even if the laws were perfectly enforced, most of the laws applied to specific individuals. Most individuals, as a result, did not have access to the rules. In *Violence and Social Orders*, North, Wallis, and Weingast laid out the

[4]See Hoppit (2017) for Parliament and Lamoreaux and Wallis (2021) for the American states.

logic of how an identity rule regime could limit violence by reaching agreements between powerful organizations and individuals that, by treating each organization differently, created rents for those individuals and organizations that they would lose if they did not abide by the agreement. The stability of the agreements was always fragile, because the agreements depended on rents, which can never be fixed. They called this the "logic of the natural state," because essentially all large human societies before 1800 were organized this way. Natural states are identity rule societies in which access to agreed upon rules is limited to elites. I use the terms natural states, identity rule regimes, and limited access orders interchangeably throughout the book.

In contrast to identity rule societies, in the 19th century governments in a few societies began limiting identity rules and increasingly created impersonal rules that, in principle, applied equally to all citizens. In these societies all citizens had access to the impersonal rules. They were "open access societies" with impersonal rule regimes. Open access orders and impersonal rule regimes are terms I use interchangeably throughout the book.

The rise of modern developed societies involved the transition from identity rule societies to impersonal rule societies, from natural states to open access social orders. Unfortunately, the contribution of *Violence and Social Orders* (*VSO*) was to lay out the logic of the natural state and explain why natural states did not develop. Their political arrangements manipulated economic interests to maintain a fragile political stability. It was the best natural states could do. But *VSO* did not explain why or how the transition from natural states to open access orders occurred, nor did it explain how open access orders sustained impersonal rules.

When the Pluralist political scientists began to ask why democracies in a small number of democracies had survived in the early 20th century, there were only a small number of democracies to examine. Most societies remained identity rule natural states without elections to select leaders. A basic limited definition of democracy is a society that uses elections to select leaders. All of the democracies existing at the end of WWII went far beyond basic democracies. They were actually impersonal rule open access societies. The Pluralists could see and document that all of the democracies in existence had developed party systems in which a small number of "major" parties managed to compete in elections repeatedly.[5] The major parties accommodated each other, they did not attempt to eliminate their opponents when they won elections. The major parties that arose by 1920 dominated politics in the developed countries through most of the 20th century. These were "plural" societies where groups with competing interest somehow managed to live together without falling into internal violence.

The Pluralists saw that the stable sustainable democracies all had *consolidated* party systems, where a small number of major parties competed in and won election after election, despite the fact that the rules governing elections allowed anyone to form a party and compete. The Pluralists, however, had trouble explaining where these consolidated party systems came from. And here, again, the inability of institutional theories to account for rules that are not followed comes into play. As E. E. Schattschneider, Giovanni Sartori, and the party system

[5]As I was writing this on March 25, 2026, word came from elections in Denmark in which the Social Democratic Party received 22% of the vote. The *Economist* magazine reported that this was the lowest vote total that the party had received since 1903. A major party indeed. *Economist* online daily "The World in Brief," March 25, 2026.

theorists who followed acknowledged, political parties were "alegal." There were relatively few agreed upon rules governing political parties. How could these critical political organizations form without rules to structure them?

Not only are rules that are not followed an important part of institutions, so are rules who affect behavior in ways that have apparently nothing to do with the form of the rule. This is a case where a pattern of behavior emerges that depends of the existence of agreed upon rules that have no apparent connection with the pattern, at least in the sense that the form of the rule specifically addresses the behavior in the pattern. The emergence of consolidated party system appears to be an instance of this kind of rule based behavior. It is a special case of rules that are enforced but not followed.

In a consolidated democracy there are not many rules about political parties. The reason seems to be that a party that wins and election could use those kind of rules to harass, suppress, or eliminate its competitors. Instead, the parties gradually, and somewhat randomly, adopted a suite agreed upon rules that

1) give the party (or coalition in a proportional representation system) that wins the election gets control of the government under constitutional limits.

2) elections are free and open, voters are not coerced and enjoy privacy and safety when they vote, and any group can form a party to run in elections.

3) all of the major parties agree to pass impersonal legislation when in power.

The logic of the three elements is straightforward. Parties that win elections get significant benefits from doing so if they get control of the government. If parties are subject to

periodic elections, then their time horizons will include the possibility that they will lose elections. If the parties all agree to create and enforce impersonal rules that apply equally to all the parties, then it will be difficult for the party in power to harass, suppress, or eliminate its competitors. If the expected future gains of winning elections are high enough, then all parties can find it in their interest to support agreements that limited laws to impersonal rules, because that guarantee their survival into the future.

The three democratic elements must be present before a consolidated party systems with a few durable major parties (depending on the electoral system) that compete in elections repeatedly through time emerges historically. Elements 1) and 2) are readily documented in the Pluralist literature. While there is no general histories of impersonal rules, we can use the number of corporations per million residents as a proxy for impersonal rules, element 3). The adoption of impersonal rules for forming corporations is an important aspect of business history, and we can document the number of corporations in 1910 from Les Hannah's census of corporations.

After laying out the conceptual framework, case studies of individual countries are presented in Chapters 14 through 17. Chapter 18, documents the presence of absence of the three democratic elements. All the societies with all three elements developed consolidate party systems, those without the three elements did not. Moreover, only the consolidated democracies survived into the 1920s and 1930s.

Consolidated party systems are remarkably free of explicit rules governing political parties, but that does not mean that consolidated party systems are independent of agreed upon

rules. Historically and in today's world, consolidated party systems only appear in a society where the agreed upon rules regarding elections, constitutional structures, and impersonal rules are present. Modern development only occurs when the political system has been stabilized by a system of durable parties, when impersonal rules make agreed upon rules more effective at supporting heterogeneous behavior throughout the society, and political dynamics incentivize consolidated parties to sustain impersonal rules.

1.4 *Implications: Institutions and the ontology of social facts*

The last part of the book considers implications of the logic developed in Part One and the history in Part Two. The first chapters examine existing theories of the transition to modern developed societies: Tilly, Olson, Acemoglu and Robinson, and North, Wallis and Weingast, as well as a deeper review of Hobbes. These are largely single actor theories in which the rules are created and enforced by a single agent in interaction with a larger society. Ideas about liberty and freedom in the work of Hayek is reexamined in light of the ability of default rules to expand liberty and freedom rather than restrict it. North and Greif's economic histories are reinterpreted to include the extent to which adopting impersonal rules make existing relationships more valuable, rather than new institutions enabling growth by expanding markets. Finally, the organizational sociology's view of rules that are not followed as myths that confer legitimacy on organizations is reassessed. None of these important works and ideas are displaced, but all of them look different when viewed from the perspective of rules, organizations, and rosettes.

The remaining chapters address the basic idea of the institutional literatures that

institutions are humanly devised constraints and are comprised both of agreed upon rules and norms of behavior. Rather than the formal/informal distinction, these chapters suggest that the fundamental distinction is between rules that are "agreed to" through a collective decision process and constraints that are "not agreed to," but result from the interaction of individuals and the patterns of behavior they exhibit. The definition of institutions used throughout the book is "agreed upon rules." Norms are not agreed upon, and are therefore a different type of constraint than agreed upon rules.

We cannot have a consistent theory of institutions, how they arise and how they work, if we are forced to explain both rules that are agreed to and rules that simply appear because of patterns of behavior. The two are fundamentally different social processes. Emile Durkheim introduced the concept of "social facts." Social facts are all the aspects of the world that exist only because of the interaction of people. Durkheim equated social facts with institutions, but I suggest that we use social facts as the inclusive umbrella definition of social behavior. Institutions as agreed upon rules and organizations are an element, a specific type of social fact. Social facts then include norms, values, and beliefs. Importantly, social facts also include relative prices. Relative prices have never been included as institutions, but they are clearly social facts. Relative prices only exist because people exchange goods and services.

These ideas are then used to conclude and review why modern democratic capitalisms with consolidated political party systems and open economies both developed and have been sustained for almost two centuries. The conclusion are different than the existing explanations that rely on elections, representation, and secure property rights. Instead of those being the

conditions under which modern development occurs, elections, representation, and secure property rights are *outcomes of changing institutions*. The changes in institutions as agreed upon rules are immediately observable in rules governing elections constitutional structures, and impersonal rules.

Table 1.1

Countries Considered in this book

Norway
Netherlands
UK
Sweden
Denmark
Finland
Belgium
France

United States
Canada
New Zealand
Australia

Germany
Spain
Italy
Austria
Portugal