

# Pitfalls to Avoid when Measuring the Institutional Environment

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# Starting observation

- Difficulties and mistakes in measurement
- Magic of numbers
- Rent seeking in consulting and intl aid
- Are leading to:
  - ◆ Dubious “best practice” standards
  - ◆ Mistaken policies—observed: IDB, SNLE

# We should measure value not only costs

- Institutions include providers of services that reduce transaction and enforcement costs, both private and public. Examples:
- Land registers →
  - ◆ Mortgages: number, interest rate spread
- Companies registers →
  - ◆ Other firms (legal representative)
  - ◆ Courts → all contractual parties of registering firm

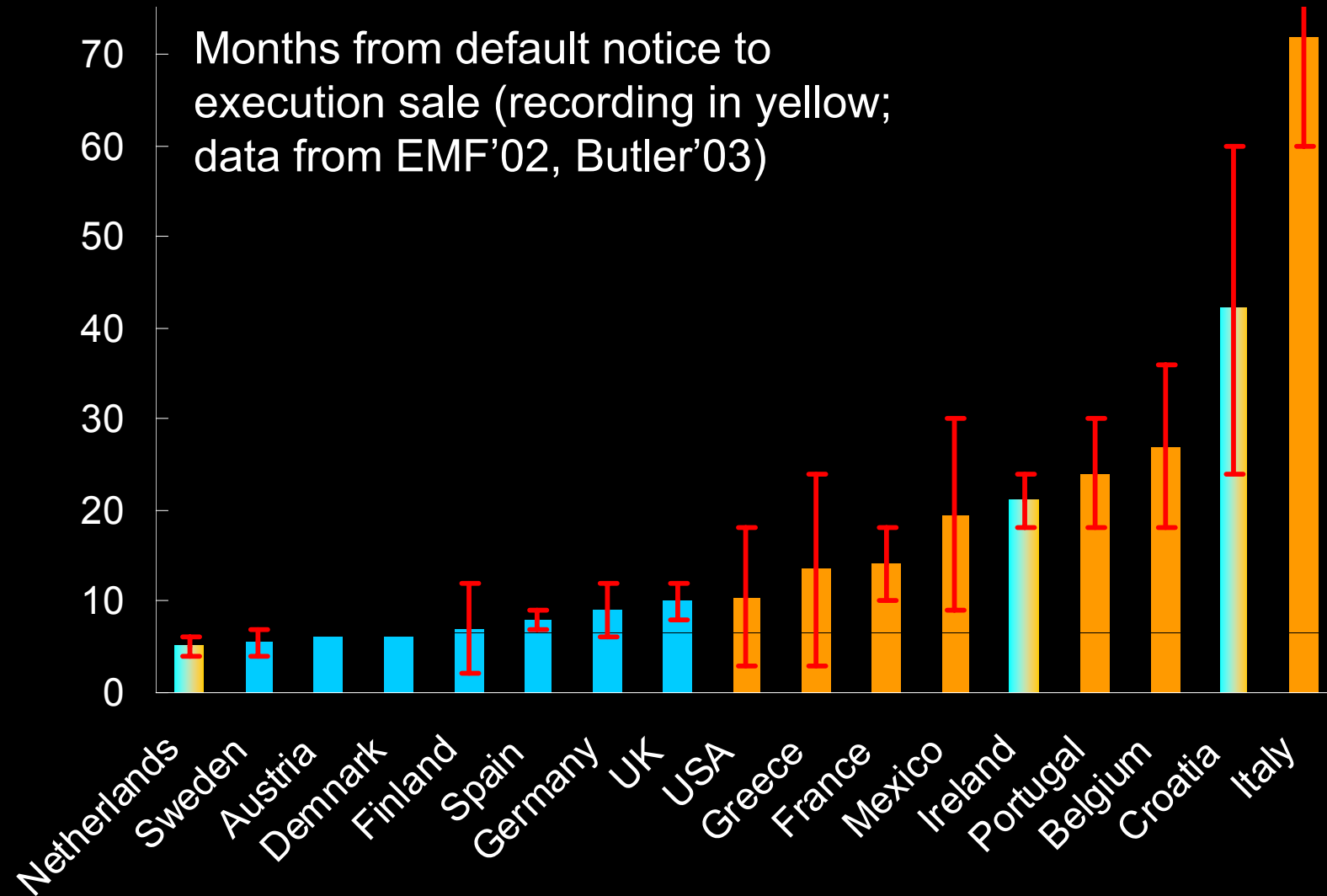
# Evaluating value requires broader concept of user

- Firms are not the only—not even the main—users
- Examples:
  - ◆ Courts do not only affect litigants but also produce precedents and have systemic effects on all firms
  - ◆ Companies registers, no only firms when registering but their future customers and creditors
  - ◆ Land registers equally affect future buyers & creditors

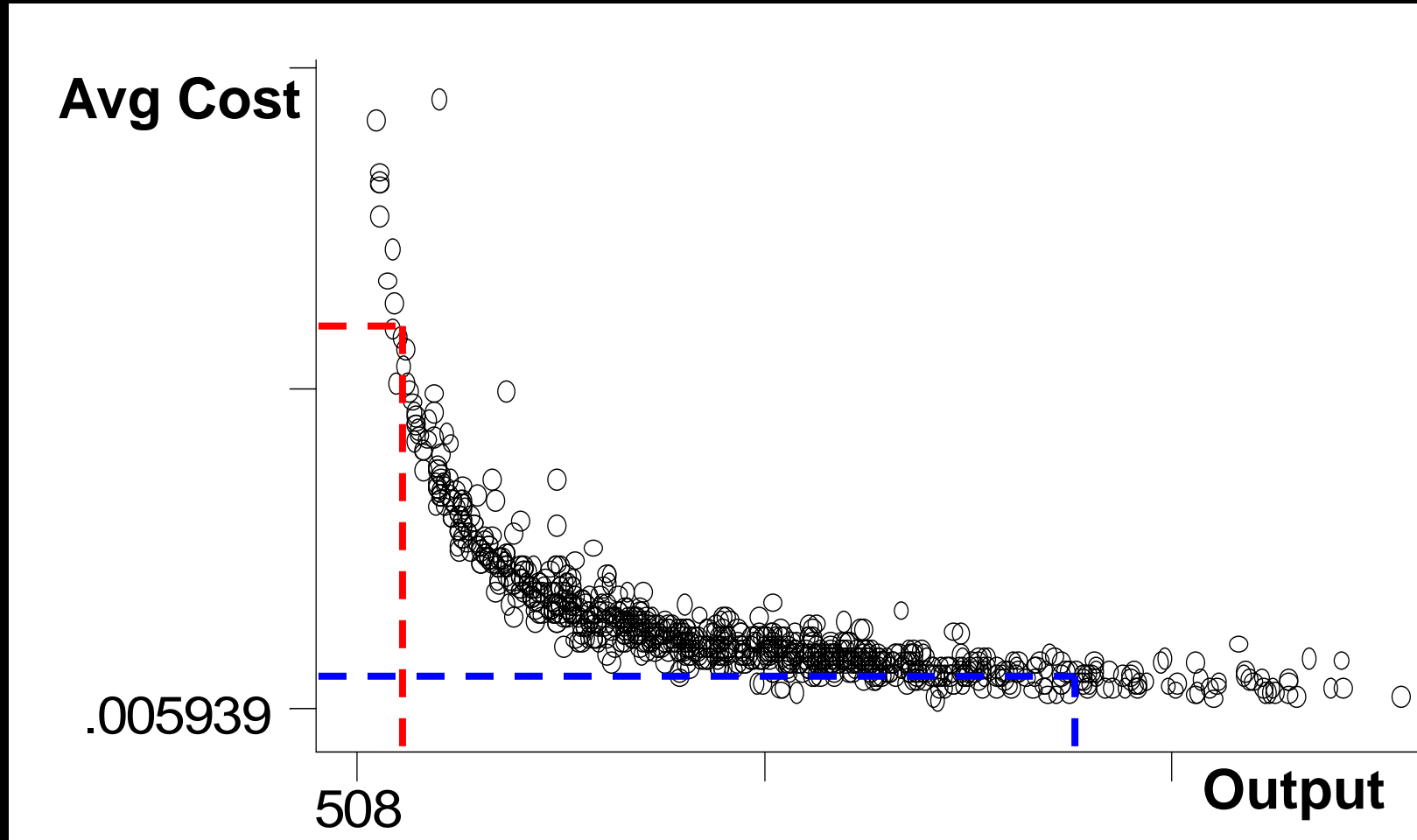
# We should measure all costs not only those incurred ex ante

- Avoids silly “simplification” policies: e.g., new firm registration in Colombia & Spain
- In general, it avoids bias against legal systems relying more heavily on ex ante control
- Example:
  - ◆ Substitution b/w ex ante & ex post costs in mortgage foreclosure →

# Example: Substitution b/w ex ante & ex post costs in mortgage foreclosure



Be aware that average costs are affected by economies to scale



(especially when measuring only the vertical axis)

# Policy consequences of emphasizing average costs

- Capital intensive reforms, disregarding
  - ◆ demand
  - ◆ fixed costs
  - ◆ sustainability
- Example:
  - ◆ Peru titling effort spent a fortune to get very little effect when compared to less formal titling



# Consider standard transactions and procedures instead of the mandatory set of procedures

- Two reasons:
  - ◆ No difference b/w procedures being publicly mandated or privately imposed by professional monopolies (e.g., lawyers in MA vs notaries in F)
  - ◆ Likely to be the minimum cost as driven by free choice
- Consequence:
  - ◆ Consider *facilitators* if chosen by parties in the standard set of procedures
  - ◆ Will help to avoid creating new public facilitating bureaucracies (e.g., one-stop shops)

# Overall guideline: treat rent seeking as the price of specialization

- Considering costs as the only objective is sensible only if institutions are fully explained by rent seeking

But

- Rent seeking, transaction costs, agency costs or whatever you can call them are simply the price of specialization

## A last word of caution

- It is perhaps true that if we cannot measure it we cannot fix it but, at least we leave as it is, while
- if we measure it badly, *we risk making things worse*

Thanks