Edward Peter Stringham, *Private Governance: Creating Order in Economic and Social Life*  

As a competitor in junior tennis tournaments, I recall the surprise many expressed upon learning that most matches have no third-party oversight. This lack of enforcement notwithstanding, participants contest thousands of matches annually—most without a dispute.

In Edward Stringham’s thoroughly-documented book, *Private Governance: Creating Order in Economic and Social Life*, he explains the shock I described above: private governance works so seamlessly that most people—even professional economists—overlook it, all the while attributing social order to formal law. This “legal centralist” perspective, though all-to-pervasive, is reduced to tatters by the final pages of Stringham’s book.

Part one of *Private Governance* argues that individuals form clubs to provide governance, part two examines “privately governed markets,” (p. 37), and part three concludes with
additional insights about the market for governance, the relationship between market and state, and the promise of future research.

As Stringham notes in part one, economists are correct to recognize the widespread potential for conflict; they are incorrect, however, to assume a third-party monopolist (i.e. government) must intervene for cooperation to emerge. The greater the gains to be had from cooperating, the greater the incentive for exchange partners to innovate solutions to governance problems. One way that individuals supply governance is by forming “clubs” with rules that govern member behavior. These groups punish deviant members by excluding them from access to club benefits. Unlike government, club participation is voluntary; furthermore, club members can use economic calculation to compare the benefits of an additional rule with its attendant costs.

After laying the theoretical foundation, Stringham illuminates several painstakingly-researched examples of club governance. He explains the emergence of the world’s first stock market in the Netherlands, the origins of the New York and London stock exchanges, as well as London’s Alternative Investment Market. These financial markets developed in the absence of state enforcement, instead relying on reputational mechanisms and exclusion of fraudsters. In fact, once off the ground, they were often forced to contend with ignorant and heavy-handed government regulators.

In chapter 7, Stringham shows how PayPal—on the verge of extinction due to fraudulent transactions—tackled their governance crisis without waiting for the help of slow-moving government. In fact, at the time of PayPal’s problems, there were already extensive (and ineffectual) cyberscrime laws on the books. PayPal’s leadership solved their problems by implementing algorithms to detect fraud ex ante rather than waiting for government to rectify their issues ex post. In the next chapter, Stringham addresses the private police that have patrolled San Francisco since the Gold Rush. As he documents, even when local government began supplying a tax-funded police force, many residents voiced their preference for their voluntary counterparts.

In a chapter that promises to make Neoclassical economists uncomfortable, Stringham draws on moral philosophy and psychology to argue that one of the most powerful—and overlooked—mechanisms of private governance is self-governance. Whether because of Adam Smith’s “impartial spectator” or due to cultural norms such as religion, evidence indicates that many individuals cooperate even in the absence of external constraints.
Finally, Stringham tackles two hard cases. The first challenge consists of markets “requiring” third-party adjudication, such as seafaring merchants who repeatedly came to one another’s aid prior to contractual negotiations. Voluntary solutions enable disputants to select private adjudicators skilled in the relevant area of commerce; by contrast, one-size-fits-all government regulators often demonstrate a knowledge-base bordering on cluelessness.

The second hard case stems from the most complex markets: are private arrangements sufficient to handle the messy world of mortgage-backed securities and credit default swaps? In fact, Stringham shows that private governance is up to the task by not only highlighting innovative private arrangements, but also dispelling popular financial myths in the process.

As Stringham emphasizes in his concluding chapters, not only does private governance work, but the best-case scenario for government is matching the performance of markets (thereby crowding out private solutions); in many cases, however, government imposes a litany of new compliance costs that dwarf any attendant benefits.

One small criticism of Stringham’s book is that it might have been more comprehensive. While he draws upon the world of finance for several of his chapters, he alludes to the fact that private governance is everywhere. It would be nice to see an expanded version of this book that includes more far-ranging examples, specifically some drawn from modern life (the chapter on PayPal is great, so it would be instructive to see other cases of private “cyber-governance.”)

Stringham ends by urging economists to recognize that the “unseen beauty that underpins markets” (p. 226) also grounds markets for governance. Even if private governance was responsible only for the examples he describes, “its accomplishments should still be considered among the greatest achieved by humanity,” (p. 228). The prospect of future research in private governance, though, is limitless says Stringham, and so he concludes with an optimistic call for others to join him in exploring how cooperative interaction is solving our biggest problems. One can only hope that many heed the call.