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Preventing Economists' Capture[1]

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When economists talk about regulatory capture, we do not imply that regulators are corrupt or lack integrity. In fact, if regulatory capture were due solely to illegal behavior, it would be simpler to fight. Regulatory capture is so pervasive precisely because it is driven by standard economic incentives, which push even the most well-intentioned regulators to cater to the interests of the regulated. These incentives are built into their positions. Regulators depend on the regulated for much of the information they need to do their job properly, and this dependency encourages regulators to cater to the regulated. The regulated are also perhaps the primary audience of the regulators, as taxpayers and citizens more generally have much less incentive to monitor regulation, and generally remain ignorant. Hence the regulators will tend to perform their job with the regulated, rather than the public, in mind, further encouraging the regulators to cater to the interests of the regulated. Finally, career incentives play a big role. The regulators' human capital is highly industry-specific, and many of the best jobs available to them exist within the industries they regulate. Thus, the desire to preserve future career options makes it difficult for the regulator not to cater to the regulated.

If these are significant reasons regulators are captured, it is not clear why economists should not be similarly susceptible to capture. First, although not all data that economists use are proprietary, access to proprietary (that is, industry controlled) data provides a unique advantage in a highly competitive academic market. To obtain those data, academic economists generally

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[2] University of Chicago, National Bureau of Economic Research, and Centre for Economic Policy Research.

have to maintain a reputation for treating their sources favorably. Therefore, there are incentives similar to those of regulators to cater to the industry or the political authority that controls the data. Second, outside of academia, the natural audience of economists' work consists of business people and government officials who would apply some of that knowledge. A piece of research, and the person who did it, will gain credibility by winning popularity and support among business people or the government. Even if no researcher purposefully caters to business or the government, this selection will tend to promote researchers who cater to business or the government. Finally, academic human capital is highly specific. Opportunities in consulting and other high-pay, high-status careers outside of academia are not equally distributed; economists who cater to business interests would seem to have a more lucrative set of opportunities.

Another more subtle source of bias arises from the publication process. In economics, authors cannot submit a paper to multiple journals contemporaneously, and manuscripts are subjected to many lengthy revisions. This extenuating process maximizes the power of the editor vis-à-vis the author. Thus, the capture of even a few editors can have magnified effects throughout the profession.

In sum, if economists face incentives very similar to those facing regulators, why shouldn't they be similarly susceptible to capture? In this chapter, I develop these arguments and provide some evidence consistent with the hypothesis that capture of economists by business interests exists, and is pervasive.

As with regulators, economists' capture is far from complete. There are numerous examples of academics at odds with industry wants, and even entire theories at odds with industry interests. For example, the Efficient Market theory is not very congenial to the finance industry.

What are some of the factors that limit capture in academia? One factor that can reduce capture is access to data that are independent from industry. Macroeconomists who rely on government-provided data or financial economists who rely on publicly available stock price data are less likely to be captured than researchers doing field experiments who have to obtain confidential data from companies. A second factor is the ability to speak to a broader audience. Economists who write for the larger public, such as Joseph Stiglitz and Paul Krugman, operate under fewer of the pressures that can lead economists to be captured by business. They might even suffer the opposite pressure: the high demand for economists who criticize business may risk introducing an antibusiness bias into some of these economists' work. Finally, some economists may be less attractive to an industry for reasons

unrelated to their work itself, which in turn reduces for these economists the attractiveness of catering to that industry. For example, all other things being equal, an economist with a thick foreign accent might be less likely to be asked to be an expert witness or to find a job in a domestic industry, except in very quantitative (and generally not very lucrative) positions. We would expect such economists to be less likely to cater to business interests.

To help prevent capture, I propose several remedies. First, a reform of the publication process, allowing multiple contemporaneous submissions and restricting the outside activities of editors. Second, a data policy for field experiments and proprietary datasets that minimizes the ability of companies to influence the published results of this research. Third, a mechanism of shaming academic economists who take unjustifiable positions in the media or in expert testimony. Although academic writings are scrutinized during expert testimonies, expert testimonies are not scrutinized by the academic community. It is time for this to start.

Ultimately, the best way for economists to reduce and prevent capture is to promote awareness among ourselves that the risk of capture exists. Until we admit that we *can be* captured by vested interests in much the same ways that regulators can, we cannot hope to prevent capture. For this reason, the key first step is to start talking about this problem.

The rest of this chapter proceeds as follows. The first section reviews the forces that the literature has identified as leading to regulatory capture. The second section applies the same logic to economists, and also provides some empirical evidence in the context of the debate on executive compensations. The third section presents some mechanisms through which capture can be reduced.

THE FORCES THAT LEAD TO REGULATORY CAPTURE

Starting with Olson[3] and Stigler,[4] the economic literature on regulatory capture begins from two premises: regulators' opinions can be influenced, and not all groups have equal opportunities in influencing them. In this section I review the main reasons for regulatory capture as identified in this literature. This section does not claim any originality, but it is designed to set the stage for my analysis of how these same forces can theoretically lead to capture among economists.

[3] Mancur Olson, *The Logic of Collective Action* (Cambridge, MA: Harvard University Press, 1965).

[4] George Stigler, "Theory of Economic Regulation," *Bell Journal of Economics* 2 (1971): 3–21.

From bribes to threats, there are plenty of illegal ways to influence regulators.[5] I purposefully ignore these channels – not because they are unimportant – but because they are less interesting if we want to study how to prevent capture in the United States. Illegal methods are rare here and are easier to fight; admitting for a few exceptions, it is generally sufficient to enforce the law.

When we restrict our attention to legal means, there are three main channels through which regulators' opinions can be influenced: career concerns, information, and environmental pressure. I deal with each of these in turn.

Career Concerns

Outside interests can influence the career of a regulator by offering (implicitly or explicitly) better paid jobs to regulators outside of the regulatory arena. This channel only works when the typical wage prevailing in the outside organization is significantly higher than the one prevailing in the regulatory arena. This is not always the case. For example, nongovernmental organizations (NGOs) do not pay large salaries, preventing them from using this channel to influence the regulators.

This form of regulatory capture does not require an explicit quid pro quo between regulators and regulated, such as a job offer in exchange for a favorable decision. It can take a much more legitimate form, which can be quite pervasive. Industry players may hire former regulators because of the valuable skills they have accumulated as regulators. Given these skills, however, the industry employer will prefer former regulators whose record indicates they appreciate the employer's interests, and are more sympathetic to them. It is hard to imagine, for example, that an investment bank would hire a regulator who has expressed very negative views of the economic function of derivatives. Given these concerns, some regulators will try to signal their pro-industry view with decisions that favor the regulated.

Even if a regulator is not interested in getting a job outside of the regulatory arena, outside interests can affect her career inside the regulatory world. A key assumption in the economic theory of regulation is that large and dispersed constituencies remain poorly informed about regulatory issues. Because each individual is affected so little by regulatory decisions, it is not in his interest to invest in acquiring information on these issues. This rational ignorance theory[6] asserts that large and dispersed constituencies

[5] Ernesto Dal Bó and Rafael Di Tella, "Capture by Threat," *Journal of Political Economy* 111 (2003): 1123–54.

[6] Anthony Downs, *An Economic Theory of Democracy* (New York: Harper & Brothers, 1957).

are far less likely to follow regulatory decisions and thus do not provide much feedback on their actions. As a result, the main parties that provide outside feedback about the performance of a regulator are vested interests. This asymmetry of monitoring gives the vested interests greater influence. They can, for example, potentially undermine the career of a regulator by spreading false rumors about her level of competence.

If, as advanced by Hilton,[7] the main goal of a regulator is to avoid "squawking," or political complaints by the regulated firms, then regulators would as a rule be highly amenable to industry preferences. Yet a smart politician might read "squawking" by industry insiders as a sign of a regulator's effectiveness, and would therefore reward the regulator for doing precisely the opposite of what Hilton's model predicts. A more sophisticated model is provided by Leaver.[8] Leaver's model starts from the premise that regulators make mistakes. Regulators know, however, that when they make a mistake against the vested interests in their industry, these mistakes will be exposed as such and will have an impact on their reputation. By contrast, when regulators make mistakes that favor the industry, these mistakes will not be so easily exposed. Therefore, the model predicts that, when in doubt, regulators would rather err in favor of the regulated, rather than against them.

Furthermore, regulators may want to hedge against potential mistakes by routinely being more favorable to the industry they regulate. The industry will be less likely to expose a regulator's mistakes if the regulator has a reputation for being an industry ally.

Information

Regulators often require access to industry-specific information to do their job properly, and without this information they risk making embarrassing mistakes. Much of this information is possessed by the regulated firms. In the absence of an explicit disclosure requirement, the regulator must bargain with the regulated industry to obtain that information. This creates an easy opportunity for firms to "trade" information in exchange for favorable treatment. This quid pro quo is generally implicit. Regulators try to establish a cooperative environment with the regulated firms; to support this cooperation, regulators need to make certain concessions, and in turn

[7] George W. Hilton, "The Basic Behavior of Regulatory Commissions," *American Economic Review* 62 (1972): 47–54.

[8] Clare Leaver, "Bureaucratic Minimal Squawk Behavior: Theory and Evidence from Regulatory Agencies," *American Economic Review* 99 (2009): 572–607.

they expect the industry to cooperate by disclosing information. Both sides operate under the merely implicit threat of withdrawal from this cooperation.

An historical example of this kind of implicit bargain is provided by Mahony.[9] In drafting the 1933 and 1934 legislation, the Roosevelt administration needed a great deal of information in a short period of time. The traditional investment banks, already well connected politically, offered to provide this information. In exchange, Mahoney writes, the banks acquired some ability to influence legislation and were left largely untouched by the Pecora Committee investigations.

Environmental Pressure

Regulators do not operate in a vacuum. They generally possess industry-specific human capital, which has been accumulated through formal training and years of work in a specific industry. This specialized human capital tends to generate an interest in supporting activities that value this human capital. A person who specialized in derivative trading, for instance, is more likely than most to be impressed with the importance and value of derivatives, just as a nuclear engineer is more likely to think nuclear power is the energy source of the future. If most of the regulators were picked from among nuclear engineers, we might expect the country to more widely embrace nuclear energy. The example of France seems to demonstrate such an effect. As a result of complicated cultural reasons, an unusually large portion of the political and bureaucratic elite in France is trained in engineering at the Ecole Politechnique – and France derives more of its energy from nuclear power than any other nation.

Compounding the problem is the fact that regulators frequently rely on their network of trusted friends to gather information "from the outside." If everyone in that network is drawn from the same milieu, the information and ideas that flow to policymakers will be severely limited. A revealing anecdote comes from a Bush Treasury official, who noted that in the heat of the financial crisis, every time there was a phone call from Manhattan's 212 area code, the message was the same: "Buy the toxic assets." Such uniformity of advice makes it difficult for even the most intelligent or well-meaning policymakers not to be influenced.

[9] Paul G. Mahony, "The Political Economy of the Securities Act of 1933," *Journal of Legal Studies* 30 (2001): 1–31.

Asymmetries

All these potential sources of biases would not be very problematic if all the interests had equal ability to lobby and influence the regulators. The economic literature on regulatory capture relies on a fundamental asymmetry in the influence of various groups, because in a perfectly competitive world, competition among conflicting interests will lead to the efficient outcome.[10] The source of this imbalance of power has to be found in the small size (both in relative and in absolute terms) of many players. As Olson[11] argued, relatively small players capture a small fraction of the benefits of lobbying, whereas they have to pay the full cost. In a world in which coordination is costly, they will have fewer incentives to lobby than the large players, who internalize a significant fraction of the benefits of lobbying without having to pay any coordination costs. Besides the dispersion issue, a limited size is by itself an obstacle to lobbying. Lobbying has some fixed costs, which cannot be amortized if the market size is too small, even if the market is controlled by a monopolist. As a result, lobbying disproportionately increases along with the size of firms.[12]

Besides size, profitability is an important determinant of lobbying intensity. More profitable companies can afford to pay more to lobby, and they have more to protect. For example, public notaries in Italy (and in all French law countries) are limited in quantity and earn substantial rents. As a result, they have organized a powerful lobbying effort to justify the rationale of their position.[13] You do not see any similar effort in the United States, however, where public notaries are clerks and earn no rent.

HOW THESE FORCES CAPTURE ECONOMISTS

Now that I have reviewed the forces that can capture regulators, I can present and test the hypothesis that these forces can capture the economic profession as well. Because economic academic research spans many different fields, a generic captor does not exist. Both the captors and the degree of capture

[10] Gary Becker, "A Theory of Competition Among Pressure Groups for Political Influence," *Quarterly Journal of Finance* 98 (3) (1983): 371–400.

[11] Olson, *The Logic of Collective Action*.

[12] Deniz Igan, Prachi Mishra, and Thierry Tressel, "A Fistful of Dollars: Lobbying and the Financial Crisis," Working Paper 17076, National Bureau of Economic Research, May 2011.

[13] See, for example, XLI Congresso Nazionale del Notariato, "Civil law-Common law. Sviluppo Economico e certezza giuridica nel confront tra sistemi diversi," Pesaro, 2005.

vary across topics. To situate my ideas, I frame most of the examples in terms of the debate on executive compensation. I do not use this example because it is an example of uniform capture; to the contrary, many economists have written about the distortions in executive compensation caused by corporate governance problems.[14] I do not mean to suggest, therefore, that the profession is fully "captured," any more than I mean to suggest that all regulators are captured. What makes this topic particularly suitable is precisely the fact that the profession is not entirely aligned on one answer and that, at least in theory, you could argue successfully on both sides of the debate. One could argue that the market for executives is a competitive one, in which they get paid what their marginal productivity is, or one could argue that the market is distorted by corporate governance problems. It is precisely this variety that allows me to better identify the subtle biases that are present in the profession.

Career Concerns

As with regulators, vested interests can influence economists' careers along two dimensions. They can provide opportunities for employment (either full time or part time) outside of academia, and they can influence the career of a researcher inside academia.

Career Outside of Academia

Let us start with the easier channel: employment opportunities outside academia. Firms can hire academic economists for top-level positions, as a board member, or as a consultant. Regardless of the job they are hired for, it does not help to have taken a critical position on the level of executive compensation. One reason is that such a position might signal an antibusiness bias, which would be detrimental in any business job. It is also counterproductive if the economist ends up in the top position, because it might negatively affect his own compensation. Finally, it makes him less appealing to other CEOs who might want to have him on their board, because his presence on their board might spell trouble for them. For these reasons, if economists are interested in future outside appointments, they have incentives to take the position that the high level of executive compensation is justified.

[14] For example, Marianne Bertrand and Sendhil Mullainathan, "Are CEOs Rewarded for Luck? The Ones Without Principles Are," *Quarterly Journal of Economics* 116 (2001): 901–32.

Most economists, however, do not leave academia and are not appointed to any board. At most, they work as expert witnesses for various firms. Because there is not much litigation on this issue, it is not ideal to discuss the potential biases that arise from this activity (or from the desire to qualify for this activity). In addition, most economists will argue that the adversarial nature of the litigation process is the best guarantee that it will not lead to biases. For every plaintiff, there is a defendant, and thus expert witness positions should be able to offer an opportunity for everybody, on both sides of every issue.

Unfortunately, this is true only in principle. In most cases there is quite an imbalance between plaintiff and defendant. More often than not, plaintiffs are operating on a contingency basis, bearing the cost of all expenses. As a result, plaintiffs tend to be much more cautious than defendants in spending large amounts of money on expert witnesses. By construction, defendants are well endowed (if they were not, the plaintiff would not file suit against them). They tend to have a lot to lose and are therefore more willing to spend large sums of money to protect their interests in court. For this reason, consulting opportunities are not equally distributed across both sides of the same topic. It pays more to develop a reputation for being an apologist of powerful interests than to support plaintiffs' cases against those interests.

Furthermore, lawyers like consistency from the expert they use, because this minimizes the chances of a damaging cross-examination. Thus academics who want to play actively in this market have an interest in sticking to a very clear position in all their writing, including their academic writing, which is often read by the opposing counsel. This is the opposite of what the academic pursuit of truth would require.

Publish or Perish

A more challenging task is to establish a link between outside pressures and success in academic careers. An academic career is mostly determined by a person's ability to publish in peer reviewed journals and to have her articles cited.

Unlike in the law arena, in which top journals are edited by students, in economics and finance, major journals are peer reviewed. Hence the ability to publish is mostly determined by editors and referees. Editors have probably the greatest power in deciding whether to publish a paper or not. They choose the referees, who are generally very predictable in their taste, and reserve the right to overrule them. I am very confident that editors receive no form of direct pressure to publish articles that reflect more

pro–business interests. Yet this does not mean that the publication process is free from biases and that academic careers are completely free of any outside influence.

The lack of bias in the publication process depends crucially on the lack of bias of the editors of major journals. Because there are multiple outlets, an author can shop around. Unlike in law, however, the search process is impaired by the prohibition on submitting the same paper to multiple outlets contemporaneously. Combined with the relatively long review time and the multiple rounds required, this process gives quite a bit of power to the editor to massage papers in the direction he or she prefers. If an assistant professor who is going up for review soon is asked at the last round of a long review process to modify slightly his conclusions to make them more palatable to a certain audience, would he refuse? It is easy to see why he might not. Such a compromise not only biases the conclusions of one paper, but also risks generating a perception that to publish in that journal one has to reach the "right conclusions." Hence researchers who want to publish in that journal may start tilting their conclusions in the "right" direction. In equilibrium, the editor does not have to exercise any arm twisting, because all the distortion takes place before the first submission, and is done voluntarily by the researchers to reduce the risk of seeing their paper rejected.

Even if impaired by the restriction on contemporaneous submission, competition across journals helps to reduce idiosyncratic biases among editors. It cannot help, however, when this bias is generalized among editors. Suppose, for instance, that all editors sit (or want to sit) on corporate boards. They might then all be biased in favor of papers that justify large compensation to executives and board members. Similarly, imagine a hypothetical paper showing that expert witnesses are for sale and bias their opinions for money. If most of the editors of the major journals do a significant amount of expert witness consulting, do you expect that they will be absolutely neutral in judging the paper?

An Empirical Analysis

All the analysis presented so far has been in the way of hypothesis. To test whether there is any bias of this nature in the publication process, I looked at publications in the area of executive compensation. One of the main problems in doing such an analysis is selecting the appropriate sample. On the one hand, to choose a sample that is not affected by the potential biases of editors, I cannot choose just published papers. On the other hand, if I do not have any measure of quality, the analysis is meaningless. For this

Table 6.1. *Variables' description*

Positive on level	Dummy equal to 1 if the paper supports current levels of compensation or it suggests to increase them, buying the optimal-contracting argument over the rent-seeking argument
Negative on level	Dummy equal to 1 if the paper proposes that the current levels of compensation are excessive and/or supports the rent-seeking argument
Greater slope	Dummy equal to 1 if the paper supports a higher weight given to the performance-based compensation
Smaller slope	Dummy equal to 1 if the paper supports a higher weight given to the performance-based compensation
Economic journal	Dummy equal to 1 if the paper is published in JPE, QJE, or AER
Financial journal	Dummy equal to 1 if the paper is published in the JF, JFE, or RFS
Managerial review	Dummy equal to 1 if the paper is published in a managerial review
Law review	Dummy equal to 1 if the paper is published in a law review
No business school	Dummy equal to 1 if no author is affiliated with a business school
Bebchuk dummy	Dummy equal to 1 if the author is Bebchuk
Citations in Google Scholar	Number of citations in Google Scholar as of 5/2/2011 – 5/5/2011
Downloads from SSRN	Number of downloads in SSRN as of 5/2/2011 – 5/5/2011

reason, I start from a sample of the 150 most downloaded papers from the Social Science Research Network (SSRN) before 2008 using the search key "executive compensation." SSRN downloads have the advantage of not being affected by editors. However, for published papers, they are highly correlated with citations and thus are a (noisy) proxy of quality. I chose pre-2008 articles to exclude the financial crisis and to give sufficient time for the papers to be published.

After dropping a few survey papers, I read all the abstracts and classified them on the basis of the conclusions I could draw from their results. I labeled as "positive on level" the papers that find that the current level of compensation is justified or even too low. For example, if an abstract concludes that "the evidence supports the optimal-contracting argument over the rent-seeking argument," (see Table 6.1). I classified the paper as positive on level. I labeled an article as "'negative on level" if it argues that the current level of CEOs' salaries is too high. For example, a paper that "explains how managerial influence might lead to substantially inefficient

Table 6.2. *Summary statistics*

Variable	Obs	Mean	Std. Dev.	Min	Max
Positive on level	144	0.146	0.354	0	1
Negative on level	144	0.208	0.408	0	1
Greater slope	144	0.125	0.332	0	1
Smaller slope	144	0.104	0.307	0	1
Economic journal	144	0.021	0.143	0	1
Financial journal	144	0.111	0.315	0	1
Managerial review	144	0.028	0.165	0	1
Law review	144	0.118	0.324	0	1
No business school	144	0.424	0.496	0	1
Bebchuk dummy	144	0.069	0.255	0	1
Citations in Google Scholar	141	83.021	144.535	0	793
Downloads from SSRN	144	1374.986	1061.984	580	7594

The sample is composed of the 150 most downloaded papers posted on SSRN as of 5/2/2011 – 5/5/2011 obtained using "executive compensation" as keywords. Variable definition is reported in Table 6.1.

arrangements that produce weak or even perverse incentives" is classified as negative. Overall, 15% of the papers fall in the first category and 21% in the second, whereas the rest are neutral (see Table 6.2). I did the same regarding the desired level of pay for performance sensitivity: 12% of the papers argue that the sensitivity should be higher, while 10% argue that the sensitivity should be lower. I consider a paper positive on the level of compensation and/or on the level of sensitivity as a more probusiness paper, whereas I consider one that advocates a lower level of compensation and/or a lower level of sensitivity as a more antibusiness paper.

In Table 6.3, I compare the probusiness and antibusiness biases of major outlets. Articles published in major economic journals (e.g., *Journal of Political Economy*, *Quarterly Journal of Economics*, and *American Economic Review*) tend to have a clear probusiness bias with respect to the rest of the sample: they have significantly more conclusions that are positive on the level of compensation, significantly less that are negative on the level, and significantly less that are negative on the sensitivity. Managerial reviews tend to publish fewer articles concluding that compensation should be lower and fewer articles suggesting that sensitivity should be lower. The finance journals and law reviews do not exhibit any significant bias. One possible explanation is that law reviews are edited by students and finance journals have a much faster turnaround, which reduces the ability of an editor to manipulate the content.

Table 6.3. *Probusiness and not probusiness content in different journals*

VARIABLES	(1) Positive on level	(2) Negative on level	(3) Greater slope	(4) Smaller slope
Economic journals	0.551*	−0.183***	0.218	−0.106***
	(0.279)	(0.0386)	(0.279)	(0.0307)
Finance journals	0.0721	0.130	0.00962	−0.0433
	(0.104)	(0.124)	(0.0900)	(0.0688)
Managerial reviews	0.135	−0.183***	−0.115***	−0.106***
	(0.223)	(0.0386)	(0.0319)	(0.0307)
Law reviews	0.0611	0.170	0.0611	0.0707
	(0.0994)	(0.124)	(0.0994)	(0.0990)
Constant	0.115***	0.183***	0.115***	0.106***
	(0.0319)	(0.0386)	(0.0319)	(0.0307)
Observations	144	144	144	144
R-squared	0.056	0.038	0.016	0.014

The sample is composed of the 150 most downloaded papers posted on SSRN as of 5/2/2011 – 5/5/2011 obtained using "executive compensation" as keywords. Variable definition is reported in Table 6.1. OLS coefficients reported. Robust standard errors in parentheses. ***p < 0.01, **p < 0.05, *p < 0.1.

Even if editors can capture economic research, why should they? And in what direction? Is it true that industry contacts bias researchers in a particular direction? To test whether people who sit on corporate boards have a disproportionately pro-management attitude, I looked at a new survey created by the University of Chicago Initiative on Global Markets (IGM), of which I am a director. The IGM asks a panel of expert economists – "senior faculty at the most elite research universities in the United States," as we say on our Web site, chosen "to be geographically diverse, and to include Democrats, Republicans and Independents as well as older and younger scholars" – two policy-related questions each week. (Because I am one of those experts, I omit my own responses to avoid contaminating the results.) It turned out that experts who served on a corporate board were four times more likely than those who did not to disagree with the statement, "The typical chief executive officer of a publicly traded corporation in the U.S. is paid more than his or her marginal contribution to the firm's value." Experts who served on a corporate board were also four times more likely than those who did not to disagree with the statement, "Mandating that U.S. publicly listed corporations must allow shareholders to cast a non-binding vote on executive compensation was a good idea."

Clearly, this correlation does not prove causation. It is possible, for instance, that the people who sit on corporate boards understand these issues better and are therefore more likely to disagree with both statements.

Table 6.4. *Citations as a function of content*

VARIABLES	(1) Citations Google Scholar	(2) Citations Google Scholar	(3) Citations Google Scholar	(4) Citations Google Scholar
Downloads from SSRN	0.0759***	0.0783***	0.0743***	0.0786***
	(0.0173)	(0.0173)	(0.0178)	(0.0178)
Positive on level	78.07**			
	(35.82)			
Negative on level		13.97		
		(30.93)		
Greater slope			59.95	
			(45.73)	
Smaller slope				−41.24**
				(17.46)
Constant	−33.86*	−28.61	−27.69	−21.89
	(17.24)	(20.61)	(18.23)	(18.88)
Observations	141	141	141	141
R-squared	0.378	0.343	0.360	0.349

The sample is composed of the 150 most downloaded papers posted on SSRN as of 5/2/2011 – 5/5/2011 obtained using "executive compensation" as keywords. Time period: 1990–2007. The variable definition is reported in Table 6.1. OLS coefficients reported. Robust standard errors in parentheses. ***p < 0.01, **p < 0.05, *p < 0.1.

Since the survey asks respondents to state the confidence each one has in his own response, I can explore the validity of this hypothesis that people sitting on corporate boards know better. If this were the case, I would expect board members to exhibit greater confidence in their responses than the rest of the sample, but I find no evidence in favor of this hypothesis. Another possibility is that the direction of causality is reversed: it is not that joining corporate boards influences people's opinions, but that people with business-friendly views are likelier to be asked to join boards in the first place. Yet this would not absolve a regulator in an economist's eyes! If an economist were confronted with evidence that regulators with more pro-management beliefs had better career opportunities, she would conclude that, "on the margin," regulators had an incentive to tilt their beliefs in favor of management. Why should the conclusion be any different if the subject is an academic economist?

Academic success is not only driven by number of publications, but also by their impact. Therefore I want to see whether articles with more probusiness conclusions are more likely to be cited. Once again, I need to control for quality. As a measure of quality, I use the actual number of SSRN downloads because this number is not affected by editors' choices. Table 6.4

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reports the results. Controlling for SSRN downloads, articles that are positive on the level of compensation receive more cites (measured as Google cites, but the results are the same if I use SSRN cites). Similarly, articles that suggest that sensitivity of pay to performance should be lower receive fewer cites.

Overall, these results suggest that the optimal strategy for a junior faculty member who works on executive compensation and wants to maximize her chances to get tenure is to write articles that show that the level of compensation is appropriate and the sensitivity to performance should be increased.

Biases at the Promotion Level

Thus far, I have only looked at the impact that editors' biases can have on a professional career. Promotion to tenure, however, is not just determined by the number of top publications and their cite count. Other factors play a role. Harvard Business School, for example, explicitly mentions impact on the world of business as one of the criteria to grant tenure. Other schools are not so explicit, yet "intangibles" clearly play a role. To what extent does probusiness bias help in promotions above and beyond what it contributes to getting papers published?

One potential source of bias comes from the fact that universities are major fundraisers. Fortunately, in the United States (but not necessarily in other countries), there are Chinese Walls to protect academic integrity from being corrupted by money. Donations cannot have constraints that impinge on academic freedom. A donor, for example, cannot name the holder of the chair he/she donated, nor indicate preferences for who should hold it. Similarly, a grant cannot be given with restrictions on the type of conclusions that need to be reached. Similar restrictions, however, apply to Political Action Committees, whose contributions cannot be tied to a particular position of the politicians. Nevertheless, we do think that political donations affect the politicians who appoint the regulators and that career-driven regulators take this bias into consideration when they make decisions. Why should it not be the case that donations influence deans, who in turn can influence promotions? If this is the case, why wouldn't faculty internalize this bias in their writing? The important difference is that, once tenured, faculty members are not subjected to this pressure any more, whereas regulators continue to be.

Documenting this bias is a very difficult empirical task, beyond the scope of this chapter. Nevertheless, I would like to provide a small piece of evidence consistent with this bias. Fundraising considerations are probably stronger in business schools than in other parts of academia. Hence, if this bias

existed, it would be more pronounced among business school professors. Therefore, I can use the preceding sample of executive compensation articles to determine whether business school professors are more inclined to take pro-business positions in their articles. Because they are subjected to the same editors' biases, the difference between business school professors and other academics could be attributed either to business school promotions internalizing this bias, or to a pro-business selection bias among business schools.

Table 6.5 shows that when none of the authors of an article works at a business school, the article is significantly less likely to be positive on the level of executive compensation and significantly more likely to be negative. I find no effect on the pay-to-performance sensitivity.

Because Lucian Bebchuk, a law professor, has coauthored many articles that are critical of executive compensations and appear in the top 150 downloaded (7%), I want to make sure that the effect is not just a Bebchuk effect. To this purpose, in the second part of Table 6.5 I add a dummy equal to 1 if Bebchuk is a coauthor of the article. Not surprisingly, the Bebchuk dummy is highly significant with the expected sign. Although it reduces the significance of the non–business school dummy, it does not eliminate the effect.

This effect could just be a selection effect, if only probusiness people end up working in a business school. Once again, this is similar to the regulatory arena; more probusiness people end up in regulatory positions, because they have to work with business. Whether it is selection or actual distortion does not matter a great deal. Either way, industry can count on a faculty very attentive to its interest.

Economists Not Interested in Money

As I mentioned earlier, the biggest difference between academics and regulators is that academics have tenure. Thus the career concerns described thus far apply only before an academic has tenure. After earning tenure, academics might still have monetary considerations, but these may not be paramount. Although the idea of an economist not interested in money might sound like an oxymoron, such people do exist. Academics (even academic economists) are not motivated by money alone. In fact, one could argue that people who choose the academic career are selected among those who value other dimensions (like the ability to influence other people's ideas and fame) more than money. Yet this same exact counterargument applies to regulators. The choice of a regulatory career generally reflects an interest in the public good, more so than a career in business.

Table 6.5. *Content as a function of type of job of the authors*

VARIABLES	(1) Positive on level	(2) Negative on level	(3) Greater slope	(4) Smaller slope	(5) Positive on level	(6) Negative on level	(7) Greater slope	(8) Smaller slope
No business school	–0.111*	0.122*	0.0107	0.0468	–0.101*	0.0738	0.00443	0.0483
Author	(0.0561)	(0.0704)	(0.0565)	(0.0533)	(0.0566)	(0.0669)	(0.0552)	(0.0534)
Bebchuk dummy					–0.127***	0.614***	0.0793	–0.0188
					(0.0343)	(0.131)	(0.129)	(0.0980)
Constant	0.193***	0.157***	0.120***	0.0843***	0.197***	0.134***	0.118***	0.0850***
	(0.0436)	(0.0402)	(0.0360)	(0.0307)	(0.0441)	(0.0405)	(0.0368)	(0.0314)
Observations	144	144	144	144	144	144	144	144
R-squared	0.024	0.022	0.000	0.006	0.032	0.166	0.004	0.006

The sample is composed of the 150 most downloaded papers posted on SSRN as of 5/2/2011 – 5/5/2011 obtained using "executive compensation" as keywords. Variable definition is reported in Table 6.1. OLS coefficients reported. Robust standard errors in parentheses. ***p < 0.01, **p < 0.05, *p < 0.1.

As in the case of regulators, however, this argument does not exempt economists from the risk of capture. First of all, the fact that they have other motivations does not mean that money does not enter their utility function. *On the margin*, career concerns and monetary rewards should matter. Most importantly, even if economists are completely insensitive to monetary rewards and only motivated by fame and desire to influence the outside world, they can be captured by vested interests. It is enough for these interests to offer more influence and fame, which they can easily do.

Let's consider an example. Suppose that banks need to be regulated to curb the too-big-to-fail problem. Suppose there are two methods. One solves the problem completely, but it is very costly for banks. The other provides only a partial solution, but it is much less costly to banks. Which approach would an economist advocate who has no interest in money but is solely motivated by the desire to be famous? Obviously, the second one. By advocating the first one, she would be considered unrealistic. She would not be invited to major conferences sponsored by banks or by regulators who are in cahoots with banks, and her papers would probably be rejected from the major economic journal where economists who are more attuned with the industry needs will referee her paper and publish their "more realistic" schemes. When some version of the inferior scheme is approved, the academic economists first proposing it will receive fame and glory, whereas the advocate of the effective scheme will be ignored. When the scheme, many years later, will show its shortcomings, the fault will all be attributed to the politicians who implemented it wrongly. The academic supporters will still enjoy the reputation of "having done something."

In fact, these concerns start to be internalized in the economic discussion, in the form of political economy constraints. Academic analysis of policy issues is not satisfactory if it does not incorporate the political constraints imposed by lobbying. In other words, models that do not consider sufficiently the power of vested interests are not acceptable. In a Brookings Papers meeting, I was criticized for my political naiveté, because "to take public positions on important policy issues without knowledge of the political process is a big mistake,"[15] where "political process" should be read as political constraints imposed by lobbying.

Information Needs

A late colleague of mine used to say that because entomologists do not have to socialize with bugs, he did not have to socialize with business people.

[15] "Brookings Papers on Economic Activity," The Brookings Institute, Spring 2009, 76.

Entomologists, however, cannot socialize with bugs. If they could, are we sure they would not? The entomologists who socialize would be able to understand better the world of insects, collect better data, and, most likely, write better papers. I suspect that if socialization with bugs were possible, academic competition would lead entomologists to spend a lot of time with bugs. The real question is whether the bugs would want to socialize with entomologists. Bugs do not have much choice, but business people do. Why would business people spend some of their very valuable time with us? We would like to believe that it is because they learn a lot from us. It could be the other way around: we learn from them and they know it and take advantage of it to influence us.

Researchers need data. Often a proprietary dataset can make a researcher's career. What are the incentives for a business to share these data? Generally, the first concern is not to damage the business in any possible way. Thus any business protects itself with some right of refusal, in case the data amount to some evidence that could harm the business. Researchers, anticipating that the company that provided the data may prevent controversial evidence from being published, will prefer to focus on either noncontroversial topics or topics for which the results are likely to cast the company in good light. This implicit agreement is not unique to academic economists. Biographers know that to have access to confidential information about their subjects, which enhances the quality of their work, they must develop a reputation for slanting biographies positively. If a biographer writes a negative or critical biography, then future potential subjects will be more likely to refuse him or her access.

The easiest place to see the importance of this quid pro quo is with Harvard case studies. The most typical cases are field cases, based in part on private information provided by the company to the Harvard professor who is writing the case. The explicit quid pro quo is that field cases require approval by the company before release. As we described in Dyck and Zingales,[16] some companies actively manage their information release to shape the cases. Recalls HBS professor Louis Wells:

> I learned that Enron was upset with my public-source case on the conflict surrounding the company's investment in India. After the second time the case was taught, someone from the administration approached me, told me of the company's concerns, and asked if anything could be done about it. Another faculty member was, I was told, writing a field-based case on the same subject. It was suggested that I might

[16] Alexander Dyck and Luigi Zingales, "The Bubble and the Media," in *Corporate Governance and Capital Flows in a Global Economy*, eds. Peter Cornelius and Bruce Kogut (New York: Oxford University Press, 2003).

consider teaching the more rich field case, if it fit my teaching objectives. Meanwhile, I sent my public-source case to Enron for comment. In the end, I removed the public source case from the system and adopted a shortened version of the field case, which was indeed richer in information and enabled me to accomplish the original teaching objectives.[17]

Interestingly, the case in question – the shortened field case – was taught for many years at HBS, and it ended up provoking bitter complaints from Enron. The fact that the case continued to be taught despite these complaints suggests that a company's ability to manage the process only goes so far. Nevertheless, there's no denying that firms can potentially exert non-trivial influence over the cases that are written about them.

An implicit quid pro quo takes place even in academic research, and it is much more pernicious as the importance of field experiments increases, because the power of companies over researchers increases. A younger colleague, for example, was offered the opportunity to conduct a field study with a payday loan company. She was offered this option because she had written a paper with a very positive view of payday loans. Although the company had no say in the conclusions of the paper, they had to approve the study. Most importantly, if the study had found some embarrassing result and this result was properly emphasized in the paper resulting from this study, my colleague's chances to continue collaborating with the payday loan company (or for that matter, any payday loan company) would have been seriously in doubt. Nobody is doing anything improper; still, it is unlikely that any similar studies will cast payday loans in a negative light.

Environmental Pressure

Akerlof and Kranton[18] highlighted that people are not only motivated by monetary incentives. They can exert a great deal of effort when they identify with the values and the culture of an organization or a subgroup (see Kwak, Chapter 4). Thus capture can take place not just through monetary payoff, but also through the desire to belong to a certain group with which a person identifies. The more homogeneous business elites are, the more severe this problem is, because the pressure to conform becomes greater.

Many academic economists, and business professors in particular, have a form of admiration for and envy of successful business leaders. Just as military strategists who never fought a war seek credibility and support from

[17] Dyck and Zingales, "The Bubble and the Media."

[18] George Akerlof and Rachel Kranton, *Identity Economics* (Princeton: Princeton University Press, 2010).

generals who won important battles, academic economists seek validation from business leaders.

Asymmetries

As for regulators, all these potential biases would be irrelevant if all the interests involved had the same power to influence. Unfortunately, for economists this is very unlikely to be the case. To the extent that economists are influenced by potential future employment or board opportunities, bigger companies are disproportionately more powerful, because they can provide more prestigious positions and better paid ones (salaries are highly correlated with size). To the extent that economists are influenced by future consulting opportunities, bigger companies have disproportionately more difficult (and interesting) problems to resolve[19] and they can afford to pay more, because any solution can be applied on a much broader basis. The same is true if the attractive career prospects are in the expert witness business. Bigger companies have more at stake and are therefore willing to pay more to defend their interests. If a source of economists' capture derives from the information the industry has, bigger players have more and more valuable information and are better able to deliver it.

Thus, as is the case for regulators, the types of pressures economists receive are unbalanced.

PREVENTING ECONOMISTS' CAPTURE

Given the similarity of the mechanisms that lead regulators and economists to be captured, some general remedies can work for both. I briefly mention these, while focusing most of my attention on the mechanisms specific to the academic market.

General Measures

The Power of the Media

The reason why small vested interests dominate the political agenda is that it is frequently rational for the public at large not to become informed. When a new bankruptcy law is considered, most voters do not pay attention. The probability that it will affect them personally is very low. Hence it is not

[19] Luis Garicano, "Hierarchies and the Organization of Knowledge in Production," *Journal of Political Economy* 108 (2000): 874–904.

worth their time to become informed on what the issues are. If voters remain ignorant about their own interests, moreover, it does not pay for politicians to try to protect them.

The press, however, reduces the cost of getting informed by collecting, verifying, and summarizing the facts.[20] By repackaging information in a way that makes it entertaining, news media are also able to overcome the private cost that individuals face in learning the gathered information. Even if it is not in each individual's monetary interest to become informed, the utility benefit provided by the entertainment component can overcome the cost of the time spent in absorbing the information.

Making citizens informed not only changes the incentives of politicians, but could also change the behavior of the chief executive officers of the firms lobbying the regulators. Why did U.S. producers of canned tuna choose, at very significant cost, to change the way they fished for tuna to protect the dolphins? Why is Nike so careful in avoiding the use of child labor when it manufactures its products abroad? In both cases, intense media coverage compelled these companies to change course.[21]

Most CEOs care about their public image. At the very least, they would like to avoid being labeled "dolphin killer" or to be considered responsible for child exploitation. It tarnishes not only their image but the brand image of their company, which they spend so much money to create and maintain. For this reason, they are willing to pay attention to citizens' concerns, even if these concerns do not immediately affect the demand for their products. In the same way, they could be shamed if found to influence regulators or academics too much.

News media can also reduce the capture of economists. Academics, as a group, tend to be very sensitive to their public image. For those who are motivated by fame and impact, a negative public image is extremely costly. Thus media inquiries of the academic world, like the one done in the movie "*Inside Job*," can be extremely useful in curbing the potential effects of capture.

[20] Alexander Dyck, David Moss, and Luigi Zingales, "Media vs. Special Interests," Working Paper 14360, National Bureau of Economic Research, September 2008.

[21] On March 8, 1988, all the major U.S. networks broadcast a tape of a Panamanian tuna boat, the *Maria Luisa*, killing hundreds of dolphins while fishing for tuna. Building on public outrage, the Earth Island Institute, Greenpeace, and the Humane Society launched a boycott of tuna. Restaurant chains took tuna off the menu and school boards across the country stopped using tuna until it was "dolphin safe." On April 12, 1990, Heinz announced that it would only sell dolphin-safe tuna. Within hours the two other largest tuna producers made a similar commitment. A similar story applies to Nike after the June 1996 issue of *Life* magazine carried an article about the use of child labor in Pakistan to produce Nike's soccer balls.

Indirect Benefits of Antitrust Enforcement

As mentioned previously, that business interests can have an impact on academic research does not, in itself, present a problem; rather, the problem is that in this influence game the playing field is uneven and some interests are much more powerful than others. Disparities in power arise from disparities in size and concentration, two variables that antitrust policy can address. Strong antitrust enforcement has two indirect benefits. First, by reducing size and concentration, it can level the playing field in the influence game. Second, by breaking up monopolies it divides the homogeneity of interests, creating some competition among conflicting lobbies.

Specific Measures

Besides general measures, there are several remedies that can be applied specifically to the academic market.

Shaming Economists Without Principles

A very useful self-defense against lobbying pressure is adherence to principles. Principles force economists to be coherent through time and through situations. Although not all economists adhere to the same principles and we certainly cannot expect that they will, adherence to some set of shared principles, whatever they might be, would be useful. Judges, for example, motivate their decisions on the basis of legal principles and precedents. Although they have the flexibility to adapt these principles and precedents to particular circumstances, legal principles and precedents nevertheless limit the available options in any decision.

In the same way, if economists had to justify on the basis of principles and data all their major public policy statements as well as their expert testimony, they would be less malleable to industry pressure. This defense would be enhanced if they could be shamed by colleagues for violating these principles. For example, an economist who always opposes government intervention but makes an exception when the government bails out a certain industry in which he has a direct interest could be easily exposed to professional disapprobation and public ridicule.

Unfortunately, shaming is a public good, at least as far as shaming aimed at keeping people honest is concerned. When it involves politicians and celebrities, it can pay off commercially; the program "Keeping Them Honest," run by CNN, presents a case in point. When it comes to economists, however, this hardly seems a viable commercial enterprise. For this reason,

this "wall of shame" should be organized by a professional association or some public interest NGO.

Ideally, this "wall of shame" would also penalize economists who have compromised their principles for money or have made major mistakes. For example, in years past, many famous economists wrote papers commissioned by Fannie Mae and Freddie Mac. In some of these papers, they went so far as to say, "This analysis shows that, based on historical data, the probability of a shock as severe as embodied in the risk-based capital standard is substantially less than one in 500,000 – and may be smaller than one in three million."[22] Still, the authors do not seem to have suffered any consequences from these patently incorrect conclusions. In fact, one of these authors was promoted to director of the Office of Management and Budget and later hired as vice chairman of Global Banking at Citigroup.

Mandatory Disclosure of Expert Witnesses

To facilitate public shaming and to make the capture of economists more difficult, it will be useful to mandate the disclosure (possibly with a delay) of expert witness testimonies, even when a case settled. If economists know that their testimony will be read by colleagues and checked by students, the reputational cost of lying will increase. The possible delay will protect the expertise of the academic from being immediately diffused, but it will not undermine the reputational cost of defending positions most academics would consider untenable.

A Data Code

The beauty of empirical research is that you never know what you find. In fact, the surprising results are the most interesting ones. But some interesting results might reflect poorly on a company. And this is a risk companies do not want to face. Thus, when they disclose data, they generally disclose it with some strings attached. One common string is that they reserve the right to prevent publication of the research if the results are damaging to the company. Even if there is no explicit agreement of this type, the company and the researcher often have an implicit agreement to the same effect. Hoping to avoid having their work buried, researchers tend not to look where they may unearth potential problems. In effect, they only look for certain results.

[22] Joseph E. Stiglitz, Jonathan M. Orszag, and Peter R. Orszag, "Implications of the New Fannie Mae and Freddie Mac Risk-Based Capital Standard," in *Fannie Mae Papers*, 1 (2) (March 2002), 6.

If everybody understands this limitation and is able to place it in context, it will still be possible to draw appropriate inferences from the research. If I can only report when a coin flip yields a tail, others can easily infer when it yielded a head, as long as they know how many times I flipped the coin. On the other hand, if only tails are reported and published, but not how many coin flips have taken place, then readers will find it much more difficult to infer the proper picture of the underlying phenomenon – especially when some economists will dare to say that "tail" is an established fact because all the published papers agree that coin flips yield tails.

How can the profession avoid this severe distortion? One solution is to impose two disclosure requirements at the submission stage. The first is a disclosure of the type of agreement with the company that provided the data at the time the access, or the permission to conduct the field study, was granted. Although the disclosure of explicit agreements cannot prevent implicit agreements to the contrary, a proper formulation of the contract can make them more difficult.

The second disclosure is the number of related studies that were conducted and have not been published. This is tantamount to disclosing the total number of coin flips, so that other researchers can correctly infer how many times the coin came up "heads."

Another way to reduce this potential distortion is to increase the disclosure requirements and to create more public datasets. It is probably not a coincidence that the emergence of the Efficient Market theory in finance, which was strongly at odds with the interest of the financial industry, coincides with the creation of the Center of Research on Security Prices at the University of Chicago, which gave access to data to all researchers.[23]

A New Governance of the Publishing Market

In economic and financial journals, editors hold significant power vis-à-vis authors, especially untenured authors. A rejection of a paper after three rounds can easily make a difference between receiving a promotion and being passed over. Most editors do not abuse this power. Nevertheless, it creates a dangerous scope of abuses because editors are more likely to have interests outside of academia. Suppose I am advising Microsoft in its antitrust litigation – how likely am I to publish a paper that shows that Microsoft abuses its dominant position in the operating system market? One could argue that a smart researcher will know of this potential bias and

[23] As my initial footnote reveals, Center for Research on Security Prices funds my research; so I may be accused of a conflict of interest here.

submit the paper to another journal. Yet this information is not publicly disclosed, and only people "in the know" might find out.

Even if the editor is a very honest person and will give the paper a fair chance, he or she is likely to shape it in a way that downplays disturbing results. Editors' advice at the last round is rarely ignored by authors, especially young, untenured ones. For most it is just too costly and risky to start from scratch.

To eliminate this potential distorting power, I suggest a few reforms in the governance of the publication process. First, economic journals should open up to competition, as law journals do. It is ironic that the economics profession, which touts the benefits of competition, limits it when it comes to its own research submission process. Contemporaneous submissions will reduce the power of the editors, to the advantage of the authors. This is the reason why it is unlikely that this reform will start from the journals themselves.

The second element of the reform consists in allowing the authors to post their signed rejection letters. Journals insist that rejection letters are their sole property and they are sent to authors for their eyes only. Authors do not own the copyright. If rejection letters are kept confidential, then editors' reputations are unaffected, even when they make egregious rejection mistakes. If authors can post rejection letters, they can embarrass the editors when they make mistakes, especially when these mistakes seem to be driven by outside interests.

The last element of my reform will impose more rigid restrictions for editors. They should receive higher compensation from the journal, but commit not to do any other job outside of teaching. This restriction should hold not just for the period of their editorship, but also for two years after. Although imperfect, this revolving door policy can limit the most egregious cases of conflicts of interest.

The Importance of Being Nerds

In the 1950s and 1960s, Harvard Business School (HBS) was recruiting its faculty among the most talented, more analytical MBA students. Starting in the 1970s, the rise of big consulting companies and their competition for talents started to deprive HBS of its natural pool: analytical MBAs with high social skills. As a result, they started to recruit among PhDs from other institutions. There are generally two characteristics of PhDs: they are smart and they tend to have some social issues. They are smart, because otherwise they would never be permitted to enter a PhD program. They have social issues, because otherwise they would never *choose* to enter a PhD program:

smart and socially skillful people make much more money in the industry. When they ran out of talented American PhDs (because many moved to the industry), HBS and many other schools started recruiting foreigners.

There are several ways in which diversity in backgrounds and the presence of faculty with social handicaps help reduce the degree of capture. Social handicaps make a person less suitable to an industry job, reducing the value of what businesses have to offer down the line and thus reducing a possible channel of capture.

Similarly, diversity of backgrounds can be beneficial in several ways. First, diversity forces people to challenge the conventional wisdom and gives them a broader perspective, making social pressure and environmental capture less likely. Second, diversity implies that at least some faculty are not easily employable, reducing this channel of capture. Third, people with double nationality and backgrounds have two communities in which they can be captured. If the interests of these two communities are not perfectly aligned, then this multiple potential capture can generate competition, reducing the power of each individual captor.

In this respect, the internationalization of the academic market is very positive because it facilitates the debate among academic groups influenced by different interests. Once again, competition among these different groups leads to a more efficient outcome, in the spirit of Becker.[24]

Awareness

Shortly after the Greek debt crisis in May 2010, I spoke with a high-level official of the European Central Bank (ECB) who was in charge of monitoring the market. We discussed the potential cost of letting Greece fail. The crucial question was how the debt holders of other sovereign debt would have reacted to a default of Greece. I agreed that that was the crucial question, but I raised the doubt that some market makers had a vested interest in spreading the perception that the consequences would be disastrous, so that the ECB would intervene, reducing their losses. "I am aware of this bias," said the ECB official, "and every day when I talk to market participants I try to undo it. Whether I am successful in fully undoing this bias, it remains an open question."

Awareness of the risk of capture is the first line of defense. It might not be sufficient protection, but it is certainly a necessary one. Without this awareness, any other initiative is hopeless. Unfortunately, my experience talking with colleagues suggests that this sense of awareness is missing.

[24] Becker, "A Theory of Competition Among Pressure Groups for Political Influence."

There is a diffuse perception that we are different. Even though a simple application of economic principles, as I have done in this chapter, shows that we should be no different from regulators in our susceptibility to capture, we are unwilling to admit it. Until we are ready to do so, any other mechanism to prevent capture will be useless.

CONCLUSIONS

Most academic economists are very honest people who chose their career because they were motivated by noble goals, such as the quest for truth and "making the world a better place." The same, however, can be said for regulators. So why do academic economists think that regulators are generally captured, whereas they cannot stand even the thought that this might happen to one of them? How can it be that this time *we are different*?

The purpose of this chapter is to highlight parallels between the forces that we use to explain regulatory capture and the forces that can capture economists. Unless we economists are made of a different fabric from the regulators, I do not see why we should not be subjected to the same kind of pressures.

Based on the analysis of these forces, I discuss several mechanisms to help prevent (or reduce the effects of) capture: a reform of the publication process, an enhanced data disclosure, a stronger theoretical foundation, and a mechanism of peer pressure. Ultimately, however, the most important remedy is awareness of the problem – an awareness most economists still do not have.