

**Alternative Responses to the Orange County Bankruptcy:  
An Inquiry into the Images Underlying Theory**

Susan Hardie MacDonald

Dissertation submitted to the Faculty of the  
Virginia Polytechnic Institute and State University  
in partial fulfillment of the requirements for the degree of

Doctor of Philosophy  
in  
Public Administration and Public Policy

Orion F. White, Chair  
Joseph Rees  
Gary Wamsley  
Karen Hult  
Michael Harmon

August 18, 2000  
Blacksburg, Virginia

Keywords: Orange County bankruptcy, Civil society, Risk, Globalization

Copyright 2000: Susan Hardie MacDonald

Alternative Responses to the Orange County Bankruptcy:  
An Inquiry into the Images Underlying Theory

Susan Hardie MacDonald

(ABSTRACT)

The bankruptcy of the government of Orange County, California in 1994 is treated as a case study depicting a potentially critical problem emerging for democracies. The analysis links financial and fiduciary perspectives by re-examining the actions of Orange County officials and citizens through three separate analytical frames: the dynamics of economic globalization; citizen engagement through the channel of civil society; and the theory of risk—both its nature generally and its financial aspect specifically. The conclusion reached is that globalization has made contingency and uncertainty ubiquitous and this indicates that the practice of governance in its public administration dimension should include a return to pragmatic, process approaches to policy and implementation.

## Acknowledgements

Any student who has completed the myriad assignments required for a Ph.D. has many people to thank, but an adult student who has spent years away from the classroom can be especially sensitive to all of the people who have helped her along the way. This is especially true in my case. Space and time prevent me from mentioning each one individually; I shall merely express my gratitude at the outset to members of the Center for Public Administration & Policy, the College of Architecture and Urban Affairs, the Department of Political Science, and several administrative offices at Virginia Tech for intellectual, financial and moral support during my sojourn in Blacksburg. I am profoundly grateful to each.

I would like to recognize by name the members of my committee. Karen Hult was the first person with whom I spoke about the Orange County bankruptcy and over the past six years she has been generous with both her time and resources, sharing personal records from an earlier investigation with me, among other things. I would like to thank her not only for the many conversations and insights, but also for her patience and understanding as I applied various organization theories to the bankruptcy. I would also like to thank her for a meticulous reading of my text.

Gary Wamsley has helped me in numerous ways, but at least two stand out: he supported me financially with an assistantship coordinating the visits of student-professionals from the Netherlands School of Government and he gave me several opportunities to explain cash management principles and the vagaries of derivatives to unsuspecting students in his budgeting classes. Both experiences were rewarding and I am most grateful to him for the opportunities.

As director of the Center, Joe Rees not only allowed me to share his office for over a year, handling database assignments and learning web management skills, he also gave me the opportunity to witness departmental administration from within. His discretion and diplomacy were complemented by a keen sense of caring, and I am profoundly grateful for his collegueship and support. I am also thankful for numerous discussions about risk and helpful leads to the literature.

Michael Harmon has been helpful to me in numerous ways, but I would like especially to thank him for his personal kindness and support, and his discerning sense of responsibility. In that one of my reasons for pursuing the Orange County bankruptcy was an acute dissatisfaction with facile explanations that merely blamed Citron, I am most appreciative of Michael's critical account of responsibility.

Finally, I am profoundly grateful to Orion White for supervising my dissertation and for spending untold hours with me, discussing the role of money in American society; micro / macro forces and their interaction in social analysis; psychoanalysis and the work of Jacques Lacan, and many other things. I deeply regret deciding, in the end, not to use Lacan in my dissertation. I

found his treatment of the master signifier extremely helpful in coming to terms with the global economy, and I hope some day to pursue this in my writing. Above all, I wish to thank Orion for his engaging intellect and imagination as well as for his friendship.

Certainly those within the academy are most directly involved in a student's intellectual achievements and are most deserving of thanks, but often there are others who play important, albeit more indirect, roles. For me, it has been the nuclear family of my childhood. Their personal and financial support has been extraordinary. As important as their intended kindness, however, have been their unintended gifts. Throughout my life, my mother has provided strength when times were bleakest and this path toward the Ph.D. has been no exception. My father and brother have provided inspiration of a different sort. Both have certainly been supportive—one more with resources and innumerable insights into derivatives and other financial instruments, the other more with words. My father came of age during the depression and it instilled in him a keen sense of the value of money and an appreciation for economic rationality. Moreover, his determination and ingenuity in the face of adversity reinforced a belief in the individual. My twin brother, on the other hand, was disabled from birth with cerebral palsy. While he preceded me by over ten years with his doctorate, for him, it takes a village to survive every day. These contrasting views of the individual and community, then, were ones on which I was raised. This dissertation represents, in an oblique and undoubtedly inadequate way, my humble attempt to respond to their diverse perspectives. It is therefore to them that I dedicate this work.

To James – both of them.

## Table of Contents

<b>Chapter 1: The Bankruptcy as Democratic Conundrum .....</b>	<b>1</b>
<b>Chapter 2: Civil Society .....</b>	<b>15</b>
The Problem as Civil Society Theorists Envision It.....	18
Intellectual Heritage.....	22
Responses to the Problem.....	28
Problems with the Civil Society Literature.....	41
A Fourth Approach .....	50
Concluding Observations .....	54
<b>Chapter 3: The Bankruptcy and its Origins .....</b>	<b>57</b>
The Basics.....	58
The National Context.....	61
The California Context.....	65
More Change in the 1980s .....	67
The Seeds of the Bankruptcy Revisited.....	70
The Convergence.....	73
Table 3:1 California County Revenue Changes 1978-1994 .....	74
Table 3:2 OCIP Portfolio Statement for April 30, 1994.....	75
The Voters.....	81
The Investigations' Findings.....	83
Other Responses.....	89
Concluding Observations .....	90
<b>Chapter 4: Risk Management.....</b>	<b>94</b>
The Public Administration Context .....	95
Historical Origins .....	103
Applying Lessons to the Social Domain.....	107
From Probability to Correlation.....	110
Backlash .....	111
Probability and the Market.....	114
Risk and Culture.....	123
Table 4:1 Cultural Archetypes.....	125
Revisiting Risk and the Orange County Bankruptcy.....	131
<b>Chapter 5: Conclusion.....</b>	<b>136</b>

## Chapter I: The Bankruptcy as Democratic Conundrum

On December 2, 1994, the Board of Supervisors in Orange County, California announced losses of \$1.5 billion (later revised to \$1.7) from their investment fund of \$7.4 billion. Within days they filed for Chapter 9 protection from bankruptcy and their chief financial officer, Robert L. Citron, resigned. In the ensuing months, practitioners and scholars within the public administration community responded to the crisis in myriad ways. The county itself sued its principal financial advisor, Merrill Lynch, and two bond rating agencies for failing to apprise them of the county's true financial status. Both federal and state officials launched formal investigations into the causes of, and thus responsibility for, the bankruptcy, and state courts have tried and prosecuted both Citron and his assistant.

Among the federal agencies to investigate the bankruptcy, the Securities and Exchange Commission has been the most vigilant. Initially it inquired into Robert Citron's reelection five months earlier to determine whether Merrill Lynch, or any other financial advisor, had made illegal contributions or otherwise influenced the election inappropriately. Although it found no evidence of wrongdoing, the SEC did promulgate regulations prohibiting any securities dealer in the future from contributing to public campaigns within two years of doing business with that official. It followed this with investigations into the passage of California legislation that first eased investment constraints on counties and later made all financial reporting of these investments voluntary to determine whether private financial advisors in general, or Merrill Lynch in particular, had inappropriately influenced the legislative process. Then, in the wake of Orange County citizens' 1995 rejection of a short-term tax increase that would have guaranteed the full and timely repayment of bondholders' loans to the county (in effect disavowing any complicity in, or connection to, the county's investment strategy and its failure), the SEC urged all California counties to demonstrate citizen understanding and acceptance of future bond issues. SEC Chief Arthur Levitt accompanied this action with a recommendation to all public finance officers that they give serious consideration to applying strategies of risk management to their public invest-

ment practices, arguing that the Orange County bankruptcy, and its citizens' repudiation of their debt commitment, threatened the future viability of the entire municipal bond market.

By recommending evidence of citizen understanding of and support for future bonds, Levitt reinforced the principle that public debt remains, fundamentally, an obligation of citizens and that future public indebtedness must honor that commitment. This principle undergirds the conventional understanding that public bonds have lower yields than corporate bonds or stock, which is justified by government bonds' greater security. At the same time, Levitt appears to have recognized that public finance involves some level of risk and to be suggesting that if municipalities choose to take advantage of high yielding investment instruments, they should learn how better to manage that risk and involve citizens in accepting it. These companion messages of security and risk pose interesting dilemmas for the public finance administrator.

Public administration scholars have responded to the bankruptcy, and the events in its aftermath, either by focusing on the financial details of the county's investment strategy and the concomitant risks involved in derivatives purchasing, portfolio leveraging, and the changing nature of a deregulated financial market, or by concentrating on the normative aspects of public finance and the fiduciary role that public investors must also assume.

*These two principal approaches to the bankruptcy are, I will argue, necessary but not sufficient to uncover the important lessons the Orange County crisis may hold for the field of public administration.* There are at least two reasons this case deserves further and different consideration—one related to political crises in general, the other to changes in the global economy and the changing role of local government in the United States. First, as a crisis, the Orange County bankruptcy shares the attributes of political scandals more generally. As Theodore Lowi observed in his foreword to *The Politics of Scandal* (Markovits & Silverstein, 1988), such investigation is “comparable to [examining] cells under the microscope ... in other words, ... [it is] a useful exaggeration of reality.” So, Lowi went on to say, the analysis of scandals enables us to examine

the norms or standards of a political system by focusing on actions that offended our sensibilities or contradicted our expectations. As important as this point is, however, such analysis of public finance scandals merely returns us to the more conventional studies already mentioned, where *either* financial *or* fiduciary norms are given advantage. Such an approach, I believe, not only denies us the opportunity to explore the more interesting aspects of the bankruptcy, it also fails to assist the public administrator in understanding a complex future of which the Orange County case may be an important bellwether. In the future, as market values penetrate ever more deeply into public enterprises, the public administrator will be increasingly bedeviled by choices that are best described as zero sum. As long as the scholarly debate remains focused on financial practices on the one hand, and fiduciary norms on the other, the result will be that public administrators are obliged merely to choose between two sets of conflicting principles. Moreover, as long as the problem remains cast as a zero sum choice, its deeper, more structural dimensions will evade examination.

Bellone and Goerl address the public administrator's dichotomous choice in their article "Reconciling Public Entrepreneurship and Democracy" (Bellone & Goerl, 1992), but believe the choices may be reconciled. They compare the requirements of entrepreneurship with the ethical demands of public service across four dimensions: autonomy vs. accountability, vision vs. participation, secrecy vs. openness, and risk vs. stewardship. They conclude that it is possible for the public finance administrator to reconcile these conflicting pressures by encouraging greater citizen participation in administrative decisions. Implicit in this prescription, of course, is the idea that participation in and of itself will produce a deeper sense of citizen responsibility for, and acceptance of, governmental action. The importance of this conclusion will become apparent presently.

The second reason for giving additional attention to the bankruptcy involves two other, interrelated phenomena: the increasing globalization of the economy and the continued devolution of responsibilities to state and local governments. Although decentralization has been generally acknowledged and accepted in society, there has been relatively little attention given in the Public

Administration literature to the effects on public institutions of the shift toward a global economy—although recent articles by Baltodano (1997), Callender (1998), and Farazmand (1999) suggest such attention might be developing.

In political science, however, there has been no such deficit of scholarly attention to the effects of an increasingly global economy on domestic political institutions. This is due in part to the discipline's long-standing inclusion of international relations as one of its component fields and its more general concern with questions of political economy. These two interests converged in the early 1980s when research into international regimes emerged, and scholars began to study the effect of these regimes on the role of state actors. The work of scholars such as Robert Keohane (1984) and Stephen Krasner (1983) might be cited as early exemplars of this trend. What is important for the present study, however, are the conclusions of more recent political scientists in terms of global economic trends and their impact on domestic politics as well as democratic institutions.

Keohane and Milner (1996) argue that it is no longer possible to understand domestic politics apart from the broader, international circumstances and events that increasingly influence the political institutions and constrain the policy options of actors within nation-states. In fact, Garrett and Lange (1996), contributors to one of the chapters in Keohane and Milner's book, argue that state preferences, policies and institutions are more than interrelated. Indeed, they argue that domestic political responsiveness to social demands will vary in this global environment only to the extent that social forces are buttressed by the "strength of labor unions, the electoral rules, the number of veto players, and the extent of political independence of key bureaucracies such as central banks" (p. 6). Contributors to Keohane and Milner's work make no attempt to judge these international forces on normative grounds; rather, their stated initial premise is to view all political actors as rational. As such, the editors contend:

the debate in this volume is *not* between rationalistic and nonrationalistic approaches. It *is* about the relative importance of the constraints and incentives im-

posed by the world economy, on the one hand, and the constraints and incentives inherent in preexisting national institutions, on the other. It is also about how these international and domestic constraints interact. (p. 6)

This assumption of rationality is not present in John Dryzek's (1996a) work of the same year, although he does accept the "realist" conclusions of Keohane and others who contend that the nation-state is constrained in substantive and important ways by changes in the global economy. Specifically, Dryzek argues that whereas principles of free trade were once grounded in assumptions about state control of capital, globalization has combined with deregulation to produce more open markets in goods, services and capital simultaneously. Accordingly, virtually all states, be they developed or developing, have now adopted the twin objectives of competition for capital investment and discouragement of capital flight. This economic imperative has important consequences for democracy, and it is to this dilemma that Dryzek devotes most of his attention.

It is not necessary to go into the details of Dryzek's argument here. Suffice it to say that he does not restrict his discussion of democracy to state institutions. Rather, Dryzek identifies three domains where democratic activity may occur: within the state, apart from the state, and against the state. Within the state apparatus, however, which includes actors at all levels of government, he sees the greatest opportunity for citizen participation either in times of economic or military crises or, in more normal times, at the local level of government. Local governments, though, may be limited in their efforts to respond to their communities to the extent that capital requirements constrain their policy-making leeway. Meeting capital requirements through policy choices may take either or both of two forms: policies geared to attract capital irrespective of citizen preference, and policies grounded in economic logic premised on self-interest. If his argument is correct, and I have presented only a coarse sketch of it, citizen responsibility may prove a more intractable goal than Bellone and Goerl have suggested. In other words, government officials may seek citizen support to legitimize their efforts to attract capital, but as long as citizens remain no more than a means to securing economic ends, they are not likely to stand behind those

actions, especially if they are followed by unexpected consequences, any more than did the citizens of Orange County.

According to Dryzek, the difficulty is partly structural—insofar as nation-state imperatives get translated into state and local requirements through the adoption of professional norms or standards and the competition for scarce resources. At the same time, the democratic center of gravity is shifting away from the nation-state and being dissipated among actors in the international arena, on the one hand, and state and local governments, on the other. The problem, then, for the local public finance administrator becomes one of resolving the split between creating space for citizen discourse that goes beyond traditional notions of citizen participation by encouraging more thoughtful discussion, and taking into consideration the financial constraints imposed by a global economy.

Interest in citizen participation has grown in recent years, especially as evidence of citizen repudiation or general disavowal of public officials' actions has increased across the country. Arthur Levitt's concern with the Orange County voters' repudiation of their debt may be viewed as one more instance of this trend. The dilemma, simply put, is how it is possible in democratically governed communities across the nation for citizens to be as alienated from their government as they appeared to be in Orange County. Among the several scholars who are concerned with citizen alienation but who, like Dryzek, seek to encourage citizen participation--be it in officially sponsored activities or elsewhere--and promote what might generally be called "strong democracy" are Benjamin Barber (1984, 1995), Jean Bethke Elshtain (1994, 1995), and Michael Sandel (1996a, 1996b). Within Public Administration, one would include people like Camilla Stivers (King & Stivers, 1998; Stivers, 1990, 1994), Richard Box (1998) and, of course, contributors to the Refounding Project at Virginia Polytechnic Institute and State University (Wamsley et al., 1990; Wamsley & Wolf, 1996). These scholars are known by various labels, but generally fall into the category of people concerned with civil society or participatory democracy.

Viewed as a dilemma of democratic participation, further examination of the Orange County bankruptcy affords us the opportunity to begin understanding the tensions between entrepreneurial or market-based approaches to democratic governance, on the one hand, and more community involvement or civil society approaches, on the other—especially insofar as technical questions, such as those found in public finance and investment, are concerned. The debate surrounding entrepreneurial government is a relatively recent addition to the Public Administration literature, despite over a decade of public agency adoption of entrepreneurial practices. Still, this argument may be seen as part of a longer tradition of discussion regarding differences between public and private sector management. Much of that debate, however, has mirrored analyses of the Orange County bankruptcy, with some scholars focusing on the implementation of specific business practices while others emphasize the normative considerations implicit in the management of democratic institutions. A noteworthy exception is Alan Melchior's recent contribution in the *Handbook of Organization Theory and Management* (1998). Melchior does not see entrepreneurial government as a panacea to the problems facing public administrators, but he does credit proponents of this movement with changing the nature of the fundamental debate within Public Administration from that of the politics-administration dichotomy to what he has named the "capacity-control" debate. Here, "capacity" refers to the ability of government to become competitive and "control" refers to bureaucratic management. This characterization, however, not only biases the debate in favor of entrepreneurial government, principally by its selection of terminology; it ignores the Janus-faced nature of law more generally. As Habermas observed in *Between Facts and Norms* (1996), law is both a reflection of public preferences and a form of coercion, depending on the law in question and one's orientation to it. Melchior's reduction of all bureaucratic implementation to mere "control" is little more than a caricature of the process and the often subtle and complex problems faced by public administrators.

This dissertation is intended to contribute to both the entrepreneurial government and public-private management debates, although its concern is less with attempting to demonstrate the correctness of one position or the other than with exploring the orientation or attitudes of public administrators who are asked to enact either of these approaches. *Specifically, I hope to*

*join the issues of entrepreneurial government and citizen disaffection by focusing on the individual public administrator and her relationship to the community, her mode of establishing trust, and her understanding of citizenship as a component of democracy under both of these scenarios. To do so, I propose to examine the assumptions embedded in the theories of entrepreneurial government, especially as questions of risk are involved, and of civil society.*

In some respects, the questions involved here might be likened to those explored in Charles Taylor's *Sources of the Self* (1989) where he focused on "what it is good *to be*," rather than "what it is right *to do*" (p. 3, emphasis added). Admittedly, Taylor's effort entailed an extensive examination of similar assumptions in modern western moral philosophy and, while I may draw on some of his insights, it is not my intention to attempt a moral analysis. *Rather, my interest is in examining the underlying assumptions about the individual qua public administrator, his daily practices as a public servant and his relationship to those whom he serves, from the perspective of both the entrepreneurial or risk management model and that of participatory democracy.* To characterize this effort somewhat differently, I want to explore the images underlying the theories of risk and of democracy in much the way Reinhold Bendix (1956, 1974) did for human interaction when he compared nineteenth century management ideologies in England and Russia in the early stages of industrialization and those of the United States and East Germany during the years of advanced industrialization in order to "correct past distortions of both rationality and exploitation" (p. xxi). A third example, from yet another field, is Albert O. Hirschman's *Rival Views of Market Society* (1986). Here, Hirschman examined the underlying ideologies and views of human nature that informed the competing perspectives on the market--either as tamer of passions and intermediary of human connectedness, or as dominator and subjector of human labor. Both views contribute to the rich and varied history of economic thought. Significantly, Hirschman concluded that both perspectives are necessary, but added:

It is now becoming clear why, in spite of our lip service to the dialectic, we find it so hard to acknowledge that contradictory processes might actually be at work in society. It is not just a question of difficulty of perception, but one of considerable psychological resistance and reluctance: to accept that the *doux-commerce*

and the self-destruction theses ... might *both* be right makes it much more difficult for the social observer, critic, or “scientist” to impress the general public by proclaiming some inevitable outcome of current processes. (p. 139)

While the unearthing of fundamental assumptions may appear somewhat iconoclastic in Public Administration, my reasons are twofold. First, the field has accepted the use of images insofar as organizations are concerned. Works such as that by Gareth Morgan (1997) have received multiple printings and editions. Increasingly, we see scholars attempting to cope with the problem of the “hollow state,” contributing to works such as *New Paradigms for Government* (Ingraham, Romzek, & Associates, 1994), and using images as mediators of change. The popularity of these works is testimony to the fact that images matter; they help to shape who we are, what we believe is possible, and how we go about accomplishing our tasks. In other words, they are constitutive. At the same time, we either engage in debates about reinventing government, public entrepreneurship, and public accountability as if the people affected were disconnected from the actions prescribed, or we assume the basest human instincts and develop institutions to control, or at least contain, them. Stated differently, we often have difficulty making connections between the macro and micro levels of analysis. Economics has formally recognized this split by establishing macro and micro subfields in the discipline. As changes in macro politico-economic forces continue to impose themselves on the public sector and its administration, a better understanding of micro possibilities and orientations is necessary.

It is far beyond the ambition of this dissertation to fill that gap entirely. Nor do I intend to prove that citizen participation in municipal finance is possible, or demonstrate that global economic mandates affect all levels of government. Rather, my intention is more modest; it might even be described as pragmatic. *That is, I hope to excavate the competing theories of risk management and civil society for insights into the expectations and assumptions of human motivation and practice, especially where the public administrator is concerned. In other words, I want to join the arguments of entrepreneurial government and civil society at the level of the hypothetical individual administrator and his modes of interaction with, and relationship to, the community that he serves.*

Accordingly, the model of entrepreneurial government I hope to examine will have its roots in the debates, legislation and legal practices employed by Orange County prior to its bankruptcy filing as well as risk management strategies employed in the private sector. This is not to suggest that I will restrict my analysis to only those documents; rather, I intend to make extensive use of such materials in order to relate certain components of their discussion to more familiar theoretical themes. The comparative analysis with the civil society literature will, of necessity, be more removed from the bankruptcy. Here, I will concentrate on the literatures in public administration and political science whose principal concern is with countering citizen alienation with practices that might strengthen citizen involvement in public affairs.

Analysis of the relevant literatures suggests that the question of identity plays a central role in the debate over the role of the administrator in democratic governance. Sandel (1996b), for example, repeatedly refers to conflicting sources of identity as an explanation for public acquiescence to a minimalist, rights-based form of government. At the same time, he urges us to engage the identity conflict directly through discussion of these competing images, and their importance to us, as an initial step in developing a greater sense of community or common purpose. The importance of identity has also been recognized in the organization theory literature, especially in that branch of new institutionalism known as “cognitive isomorphism” (Scott, 1995). As Scott points out, scholars adopting this perspective accept the social construction of both individual and group actors and emphasize the importance of imitation in securing social acceptability. Indeed, organizational legitimacy, which Scott defines as “the degree of cultural support for an organization” (p. 46), is in this view secured “by adopting a common frame of reference or definition of the situation” (p. 47).

William Connolly (1991), however, reminds us of the downside of such conformity. That is, inherent in the idea of identification is the concept of non-identification or difference, and history, he notes, reveals a pattern not only of preference for that with which we identify, but a

“conversion of difference into otherness” as identities seek ineffably to protect themselves. After considerable analysis, he offers an approach for coping with this downside, a suggestion that he admits does little more than

signal a direction: to affirm the indispensability of identity while contending against the dogmatism of identity; to cultivate care for the agonism of life by disclosing contingent elements in any specific identity; to politicize the ambiguity in human being. (p. 159)

Yet he concedes that such an approach faces many obstacles, not the least of which is our propensity to respond to social fragmentation, individual alienation, threats of nuclear war or international economic instability, and limitations on democratic sovereignty from international economic competition in ways that are counterproductive. We have typically responded at two levels: first, in “fixing and consolidation of a set of contending identities, each of which takes itself to be the true identity deserving hegemony” and in the “universalization of the drive to affluence and mastery among states” (p. 172). Connolly’s first example might well describe Public Administration’s response to the Orange County bankruptcy, where financial considerations compete with fiduciary norms for dominance. More broadly, of course, this competition could be extended to the politics-administration dichotomy or even to ideological distinctions found in political debate more generally.

Connolly’s second example draws our attention to the global economy and its myriad requirements. These mandates, it appears, may be transferred from national governments to states and localities through devolution of tasks or transmission of professional standards. Yet national governments may also serve as shock absorbers, buffering smaller governments from the full impact of global forces. National governments may also cooperate with each other to moderate their responses to global economic forces. In either event, Connolly’s identification of our “drive to affluence and mastery” as one of several possible responses to global circumstances suggests that we examine this position more carefully.

Both examples, he cautions, only foster greater resistance and fragmentation, not greater harmony or common purpose. This situation is exacerbated by the globalization of contingency which, he explains, “puts the squeeze on the territorial ideal of democracy; it intensifies pressures to preserve the appearance of internal democracy by denying the significance of global issues that escape the terms of accountability in the territorial state”(p. 200-1). Like Dryzek (1996a), Connolly responds to this danger by urging us to consider alternate loci of democracy: Within the territorial state these efforts might take place apart from the state, but attention should also be given to forging alliances at the international level.

Connolly helps us appreciate the political dimensions of identity, and the relationship between individual and collective identity. Indeed, he characterizes this relationship as both “honorable and dangerous” and suggests:

When circumstances are favorable, the relation is one of patriotism chastened by skepticism of state authority; when they are unfavorable, the relation degenerates into either disaffection with the state or a nationalism in which the tribulations of the time are attributed to an evil “other” who must be neutralized. (p. 199)

If these options exhaust the possible relationships between citizens and their state, then we would most likely find ourselves at the turn of a new century in a relationship that has degenerated into disaffection. Proponents of entrepreneurial government, then, could be understood as advocating a model of government in business’s image in order to gain acceptance not only by that community, but also by a society that appears, at least, to have largely bought into this identity. Most proponents of civil society, on the other hand, recognize the malaise but are not so eager to recommend a material outcome. Rather, they urge citizens to engage more fully in discussion—not only of policy options, but also of the norms and values underlying the various policy proposals. Yet this recommendation assumes that discussion will, or at least can, lead us beyond the conventional stalemate. Certainly discussion will make us more aware of other positions and values, and if discussion is productive it might even dissuade us from exiling different

views into the Siberian plains of “otherness.” Whether it can move us beyond that stalemate is another matter.

Interest in discourse has permeated the public administration and political science literatures in recent years. The most influential proponent in the scholarly world is, undoubtedly, Jürgen Habermas (1987, 1996). His voluminous work on communicative rationality has influenced many scholarly traditions from political theory to policy implementation. Habermas emphasizes the sharing of norms in non-instrumental discourse, that is, discourse that is aimed not at winning a debate but at creating an intersubjective reality where different perspectives may be articulated and justified, if necessary, with the goal of enhancing mutual understanding. Creating the opportunity for such discussion and monitoring the exchange so that it does not degenerate into instrumental or manipulative discourse can, of course, present serious challenges, especially given the nature of modern society. Habermas contends that one of the principal reasons such discourse is uncommon today is that the “lifeworld” where such talk was commonplace two centuries ago has now been taken over by political and economic institutions that have instrumental objectives as their reason for being. It would thus appear that Habermas is arguing on behalf of “democracy apart from the state.” Yet in his later work, *Between Facts and Norms* (1996), he acknowledges that the complexity of many issues now in the public domain makes it virtually impossible for citizens to deal effectively with common problems independent of the state. Accordingly, he urges policy makers and implementers to create space for such normative discussions in their day-to-day activities.

Yet, it should be recalled that many of our democratic institutions were developed in the 17th and 18th centuries when assumptions about the individual were simplistic at best. Nevertheless, variations on these assumptions have continued to inform social analyses despite dramatic advances in psychoanalytic theory in the 20th century. I believe that some basic tenets of process theory can enlighten our understanding of human interaction in the public domain and move us beyond the present stalemate between entrepreneurial and fiduciary action as well as enhance the objectives of participatory democracy. In other words, I am suggesting that by

shifting the level of analysis away from system characteristics or norms to differences in assumptions about the individual, where perception and action originate, it will be possible to move beyond the zero sum choices that plague much of public administration theory and practice today.

The dissertation will proceed in three stages. I will begin with a review of the civil society literature with the hope of gaining insight into the complex phenomenon of citizen disengagement or disaffection in democratic societies. Here, various interpretations of civil society will be considered and the concept of social capital investigated. This will be followed by a re-examination of the Orange County bankruptcy, cast in the context of a changing local and global economy. This section will include not only a summary of the events leading up to bankruptcy, but a review of the major findings about the causes in its aftermath. The third leg of this analytic tripod will involve an excursion into the conceptual underpinnings of risk, especially as it pertains to public finance in general and the Orange County bankruptcy in particular. These three disparate threads will then be reassembled in the final, concluding chapter where I hope to draw lessons for the Public Administration community.

## Chapter 2: Civil Society

Interest in civil society has grown over the past eleven<sup>1</sup> years, among practitioners and scholars alike. Most trace its origins to 1989 and the nonviolent fall of the Berlin wall. Moreover, this interest crosses traditional boundaries—those of political party or ideology in the everyday realm of public affairs, as well as disciplinary boundaries within the academy.<sup>2</sup> Finally, interest in civil society has not been geographically contained. There is growing evidence among developed industrialized states, both in Western Europe<sup>3</sup> and the United States, as well as in developing and newly industrializing economies<sup>4</sup> that the concept is gaining currency. While interest may be widespread, there is less evidence of any consensus on what the term “civil society” means or how its introduction into the political sphere might help to ameliorate present conditions. As a concept, then, civil society may be considered polysemous—meaning different things to different people. Within the United States, for example, some argue that a move toward civil society provides the cure to an overreaching state, while others contend that it represents a return to family values and a long overdue attempt to repair innumerable tears in the social fabric wrought by identity politics and increasing social fragmentation.

<sup>1</sup>Mary Ann Glendon (1997) traces the origins of the debate to 1989 and the efforts of Lech Walesa, Vaclav Havel and others to bring down totalitarian regimes in Eastern Europe. At the same time, she recognizes that scholars had contributed to the topic prior to this. The editors of *Journal of Democracy*, for example, trace the “rediscovery of civil society” (July 1994) to the late 1970s in Poland. While I will give credit to some of this earlier literature, my focus will be on the more recent scholarship.

<sup>2</sup>Political science, sociology and law are the disciplines most frequently represented in this debate, but interest within the theological community is growing (Wuthnow, 1994; Bounds, 1977) and Glendon (1997) cites economics, complex systems theory, and philosophy as disciplines that could contribute to the discussion. Given the assumptions about human nature and the importance of the family in the general debate, psychology and anthropology might also be added.

<sup>3</sup>Examples of this scholarship include John Keane, *Democracy and Civil Society* (London: Verso, 1988); John Keane (ed.), *Civil Society and the State: New European Perspectives* (London: Verso, 1988), and Anthony Giddens “Post-traditional Civil Society and the Radical Center” in *New Perspectives Quarterly*, v. 15, no. 2 (Spring, 1998 pp. 14-20).

<sup>4</sup>The range here is broad, encompassing Eastern Europe, Africa, Latin America and China. Examples of scholarship mentioned by Christopher Beem (1996) include Eba Rana Bellin, *Civil Society Emergent: State and Social Classes in Tunisia* (Princeton: Princeton University Press, 1992); John W. Harberson, Donald Rothchild and Naomi Chazan, eds., *Civil Society and the State in Africa*, (Boulder: L. Rienner Publishers, 1994); Zbigniew Rau, ed., *The Reemergence of Civil Society in Eastern Europe and the Soviet Union*, (Boulder: Westview Press, 1991); and Yang Mayfair Mei-hui, *Gifts, Favors and Banquets: The Art of Social Relationships in China*, (Ithaca, NY: Cornell University Press, 1994). Also noteworthy is Wakeman Jr., Frederic, (1993) “The Civil Society and Public Sphere Debate” in *Modern China*, 19(2): 108-137.

At the same time, the concept is not without its critics. Their concerns often involve the term's imprecision and the effect that such ambiguity has on social science research. Here, the problem has less to do with the variable meanings that the term is often given than with corroborating or refuting the myriad claims implicit in its use. In other words, the concern is to advance understanding of social interaction by empirically testing hypotheses. For example, some civil society proponents argue that a renewed emphasis on voluntary organizations enhances social capital. However, critics counter that unless we have a precise understanding of what social capital means, and can identify measurable indicators of its presence, social scientists will be unable to discern whether increased voluntary activity is indeed related in any substantive way to greater social capital. Put differently, the writers are saying that without greater conceptual precision we will be left with only mediocre theory.

Although many of these perspectives vary considerably in intent, most share a belief that greater social cohesion can be achieved through discussion about, and increased inculcation of, common values. Typically, proponents hold out an ideal—be it of democracy or capitalism or a combination of the two—that is threatened by present conditions and argue that greater prevalence of certain specific values is necessary to achieve that ideal. These values may be nurtured through specified practices or realized through discussion, but the emphasis is on values. I do not intend to argue that values are unimportant. Clearly, they inform our actions in myriad ways much of the time. What I do contend, however, is that to the extent advances in civil society have a bearing on public sector activities *at the local level of government*, where citizens can act most directly to affect their lives, discussion of values will rarely produce the kind and extent of common ground needed to provide the social milieu or context that effective and responsible democratic institutions of government require. Fragmentation and diversity are rarely resolved by imposing one set of values over another. Moreover, embedded in the history of democracy, with its majorities and minorities, is the concept of difference. Negotiating differences without tyranny has been both the challenge and ideal at least since the nation's founding. That said, disagreement over core values need not preclude the possibility of creating social contexts in which

diverse people can come to common understandings about specific steps to be taken in the short-term. It is my intention in this dissertation to demonstrate why, in fact, such a pragmatic approach offers greater possibilities for democratic discourse in general, and public administration in particular.

Importantly, the move toward civil society is occurring at a time when other forms of public action are appearing less efficacious. The global economy is changing the roles played by national governments, making them partners in the economy more than providers of order and social services. Often, nation-states resolve disputes by participating in international regimes that, in turn, guide the actions of domestic players. One example that has received considerable attention recently is the World Trade Organization. Yet where nation-states were once the principal actors in such regimes, they may now represent only one among several participants. At the same time, much of the public activity that has taken place at the national level for most of this century is now migrating to states and local governments, or being contracted out to the private sector. Yet here, again, there is change. Increasingly, state and local leaders serve as coordinators of activity at the regional and neighborhood levels, rather than purely as providers of services to residents of their jurisdiction. Economic development, transportation, health services and corrections are typically regional activities, while education, welfare and other social services are increasingly the concern of local governments and neighborhoods. The move toward civil society can help public administrators, especially at the local level, navigate this new terrain, but the lessons will be short lived if all that that we learn is to repeat the “culture wars” that have been waged in the media and halls of power at the national level.

This chapter will proceed in several stages. First, I will summarize the civil society literature as it has evolved over the past ten years, although an emphasis will be placed on literature that has the greatest relevance to the Public Administration community in the United States. Included in this section is consideration of the myriad problems that the move toward civil society is intended to address. In other words, I will examine the varied forces that have motivated the growing interest in civil society. Because most civil society advocates make assumptions either

about the purposes a civil society is intended to serve or the nature of human beings in a modern state, the second section will trace, albeit somewhat cursorily, the evolution of the term in western political thought. The third and fourth sections constitute the heart of this chapter; they will document the contributions this turn toward civil society has made and then identify several problems which the topic, as presently constructed, has encountered. Many authors, for example, see civil society and its institutions as addressing problems that the state has, for whatever reason, been unable to resolve. Yet these same authors often disagree on whether civil society represents a carefully demarcated sector of society, independent of both the state and the market, and whose growth or diminution can be empirically tested and measured, or whether it serves a greater purpose as an intellectual concept or heuristic device whose boundaries will necessarily vary over both time and place. The chapter will conclude with some observations on the balance of the dissertation.

#### The Problem as Civil Society Theorists Envision It

The sources of concern vary widely, but most agree that our present practices of democratic governance are inadequate; indeed, they fall so far short of any ideal that the very concept of democracy is endangered. Some see the problem as an overbearing and overweening state (Crane, 1997; Newton, 1997). Among this group are those who cite the intervention of the national government into every aspect of our lives—from the products we buy to the roads on which we drive or the very air waves through which we communicate—and contend that a vital civil society is needed to resist further incursion of the state into our lives. They argue that a burgeoning welfare state stifles individual initiative and deprives productive members of their hard-earned money. Some look abroad and see the emerging democracies in Eastern Europe, or economic reforms in China, as a reminder of our own perennial quest for freedom. For these proponents, then, civil society represents an opportunity for citizens to solve problems on their own, independently of the state, and to do so voluntarily, absent the state's coercive influence.

A second group identifies problems with both the state and the market. On the one hand, they suggest that the state has increasingly exceeded its authority by interfering in debates more properly left to the people and their representatives where compromises can be negotiated. Often, the Supreme Court's decision on abortion is cited as evidence of this trend (Elshtain, 1995). On the other hand, the market's excessive concern with consumerism and the satisfaction of individual wants leads it to deny not only the desirability but the possibility of a common good (Bradley, 1995). Uniting both of these impulses is the perceived emphasis on individual rights to the exclusion of the social ties that bind us in community (Sandel, 1996a, 1996b). To analysts in this second group, then, unbridled liberalism has ensured our autonomy but left us bereft of social solidarity. Evidence of our waywardness can be found in our primary institutions: the traditional family is threatened by divorce; neighborhoods are either in decay or exist in name only; and religious participation—at least in mainline denominations—has been stagnant, if not in serious decline. Others cite growing childhood poverty, as more children are raised by single parents, and a growing disparity between rich and poor. These people argue that it is not only the greater disparity in wealth that is problematic, but our growing indifference to this widening gap (Dionne, 1996, 1997). Still others point to an increase in crime. While there is some indication that the crime rate has declined in recent years, the United States now has more people in prison than does mainland China. At the same time, the ability of people of faith to act on their beliefs is increasingly hampered by the state and its preoccupation with individual rights (DiJulio, 1997). School prayer is often cited as an example of such state interference. Moreover, these trends are occurring at a time when the United States is widely considered to be the most powerful democracy in the world and clearly the greatest economy.

Some of those who argue that our concern with individual rights is excessive point to a decline in volunteerism as indicative of our malaise. These people often cite Robert Putnam's "Bowling Alone" (Putnam, 1995a, 1995b), which documented changes in Americans' participation in voluntary associations, and its sequel "The Strange Disappearance of Civic America" (Putnam, 1996), which attributed much of this decline to the popularity of television. The concern here is not only that Americans spend more leisure time alone; it is that in the process we

lose our ability to relate effectively to other people—our discursive abilities atrophy, we become less tolerant of people who are different from us, and we become less trusting of others. In other words, the social capital that is required to hold any society together has eroded to such an extent that the very foundation on which democratic freedoms are based is threatened.

Additional evidence of this threat to democratic foundations can be seen in a growing tendency for political debate to be less concerned with reaching compromise than with positioning and power (Barber, 1995), (National Commission on Civic Renewal, Bennett, & Nunn, 1998). It can also be seen in a growth in cynicism in the United States and a preoccupation with questions of identity or “wants masquerading as rights” (Elshtain, 1995). Importantly, the problem is not only the behavior of other people (Dionne, 1996), but may be found in our own lives—in worries about the security of our jobs and the changing economic conditions presented by a new global economy, and in worries about our children and the environment in which they are being raised. Dionne also notes that while some look to technology to solve our problems, they ignore more fundamental issues that undergird the present dilemma, which include a “society built on purely individualistic values that steadily cut away the bonds of solidarity, morality, and trust” (Dionne, 1996, p. 29). A similar concern is voiced by Glendon (1997), who contends that we are losing the personal qualities and abilities to practice democracy as increasingly we participate with our money rather than with our energy and time. Such indirect participation only strengthens and reinforces the special interest lobbying of elites, rather than the democratic participatory practices of citizens.

A third group of practitioners and scholars recognizes the unintended consequences of an expanded welfare state, but regards the rational actor model of the market as equally, if not more, problematic. Opinions in this group vary, as do those in the other groups, but what unites these scholars is less a consensus on the problem than a prior commitment to an activist state. Moreover, while they appreciate the incongruity of this model in a global economy, they have yet to identify a viable alternative. Jean Cohen (J. L. Cohen, 1998), for example, agrees with those who

believe that fragmentation has strained the social fabric, but argues that it is the combination of increasing fragmentation and accelerated cultural, economic and technical change that is so destabilizing. This “condition of modernity” places an ever increasing burden on social institutions of all types to provide the means for social cohesion, and a parsimonious understanding of civil society, which excludes government, only exacerbates the problem. By restricting our understanding of civil society to the non-governmental sphere and, concomitantly, reducing government to its coercive aspect, we not only curtail opportunities for developing social trust, but we ignore the many discursive and trust-creating or enhancing arenas that may be provided by public institutions.

Dryzek (1996a, 1996b) casts the problem somewhat differently. He is more willing to accept a distinction between civil society and the state but sees civil society as expanding the range of possibilities for democratic action, rather than merely providing a public sphere empty of coercion. That said, Dryzek readily acknowledges that the state itself is restricted by certain “imperatives,” driven either by market forces or popular will, which preclude the possibility for some forms of political action. When this is the case, he suggests, those seeking to effect political or social change are more likely to find a voice within civil society. Examples include forms of protest that are “against the state” or in conflict with state interests, as well as groups whose financial circumstances are such that they have little chance of competing with wealthy lobbyists. The problem, then, that Dryzek sees civil society addressing is one of limited access to democratic institutions. This may take the form of exclusion from traditional sources of power, as in the corporatist states of Western Europe; token inclusion or co-option of groups common within more pluralist states in the Anglo-American tradition; or changing state imperatives in either situation.

A third perspective in this group is provided by Walzer (1991, 1994) who casts the problem in yet another light. On the one hand, he recognizes the difficulties that fragmentation presents for society, but regards individual “dissociation” (1994, p. 188) or the fragmentation and isolation of individuals within society as a more serious problem. To Walzer, our “radical” free-

dom not only fosters weak but rancorous associations at the same time that it promotes individual isolation and passivity. He notes that, historically, Western societies have sought one of four approaches to governing (Walzer, 1991), or achievement of the good life: through 1) republican political association, 2) socialist organization of the economy, 3) a free and open market, and 4) nationalism. The problem with these rival ideologies is that each represents a singular, mutually exclusive pursuit, and while each has merits on its own terms, each also has limitations. For Walzer, then, the problem is not only that we are fragmented, both individually and in terms of the myriad identities and groups that we form, but that traditional responses to social organization address only one aspect of our lives—to the exclusion of the other dimensions.

In sum, the problems to be addressed by civil society range from too much government to excessive liberalism, and then to an inadequate understanding of public life. With this range of perspectives on the nature of the problem, it should be no surprise that the range of solutions is equally diverse. Before turning to these solutions, however, it is helpful to review, at least briefly, the historical origins of the concept.

### Intellectual Heritage

In the United States, the idea of civil society has most often been traced to Alexis de Tocqueville who, in *Democracy in America* (Tocqueville, 1990), noted Americans' widespread participation in voluntary associations and the importance this participation played not only in nurturing a democratic disposition, but in forestalling the concentration of power in the institutions of central government (Elshtain, 1995), (Wolfe, 1989, 1997). In referring to Tocqueville, many scholars and political observers stress the importance of civil institutions at the nation's founding. Others cite the importance of more contemporary political theorists such as Hegel (Drydyk, 1991) or Gramsci (J. L. Cohen, 1998) in developing the concept of civil society. When referring to more recent scholars, authors often point to cultural changes since the nation's founding, the present condition of modernity, or simply the evolution of the term over time.

In exploring the rich history of the “idea of civil society,” Seligman (Seligman, 1992) draws our attention to an even longer and more profound intellectual tradition, which he grounds in the Scottish Enlightenment but traces as far back as the Stoics. Taylor (Taylor, 1990), by contrast, draws on social relationships in medieval Europe for insight into its origins, but credits Locke and Montesquieu with the more significant contributions. Because of the term’s historical grounding, it is helpful to review briefly some of the arguments presented by Seligman and others.

As noted, our understanding of civil society is most often traced to the 18<sup>th</sup> century and the principles guiding colonial settlers. To the Scottish Enlightenment philosophers, however, civil society was coterminous with the state; that is, thinkers like John Locke, Adam Ferguson, and Adam Smith did not distinguish between spheres of public action as we do today. They did, however, distinguish between public and private, but included civil society within the public sphere where men (women were typically excluded) pursued the common weal. Members of the Scottish Enlightenment also relied on principles, or laws of nature that transcended the public sphere, to guide human actions in this civil domain. At the same time, both Locke and Smith located moral conduct in the individual.

Seligman observes that these ideas were not original with the Scots. While he traces both the emergence of universal laws and the importance of the individual as an autonomous actor to the Stoics, he credits Aquinas with incorporating the Stoics’ universal laws into early Christian thought by subordinating them to divine will. At the same time, he argues that such subordination legitimized the state by making it part of God’s higher purposes, thus transforming the state into an expression of a higher moral order. In other words, the state became an instrument of divine will, a mediating institution between God and human beings, and an instrument in furthering moral order. Of course, events in the “real” world eventually undermined this harmonious vision. Religious wars not only raised questions, at least indirectly, about which truths were truly divine; they seriously challenged the authoritative role of intervening institutions—be they the monarchy

or the Pope. As importantly, philosophers and landed gentry alike began questioning the locus of sovereignty (once clearly the province of the King) as monarchs were made subject to their own laws and sovereignty gradually shifted to the people, at least propertied males, whose consent was now required for the monarch's actions to be legitimate. As royal authority was both challenged and constrained, the legal contract took on greater importance in securing social order.

Such was the political and religious context in which the philosophers of the Scottish Enlightenment found themselves when Hutcheson, Ferguson and Smith were writing. Seligman identifies four dichotomies facing these scholars: those between 1) individual and social, 2) public and private, 3) egoism and altruism, and 4) interests and passions. All four, he contends, were to be resolved in a new conception of civil society (Seligman, 1992, pp. 28-32). Central to this resolution was the concept of human nature, which for Smith and others was dualistic: sometimes egoistic, sometimes altruistic; sometimes governed by reason, sometimes by the passions. While they regarded the individual as ultimately free, possessed of basic rights and equal to others under God, they also believed humans were subordinate to God and therefore bounded in their freedom. In other words, freedom did not imply license. Importantly, while the Scots viewed human beings as autonomous in their rights, they also viewed humans as innately social, especially insofar as self-esteem was concerned. Indeed, it was this need for recognition and mutuality that made it possible for civil society to resolve the several dichotomies. Human beings might be egotistical, but their vanity caused them to seek the approval of others and, in seeking such approbation, they were moved to altruism. In this way, the social sphere became the source of morality; civil society tamed the ego and bent it toward higher purposes. Seligman reminds us that Smith's understanding of the Invisible Hand in the market worked in much the same way. Self-interested action, embedded as it was in a social context of moral sentiments, enabled both egoism and altruism to operate in tandem. Social or public forces thus abided in individual actions; the common good existed within private interests; and the universal resided within the particular. Appeals to an external code or source of morality were not required; human interaction in the public sphere (civil society) would resolve the dichotomies.

These ideas were made manifest in the American colonies. The earliest Puritan settlers established covenant communities consistent with their beliefs, where individuals were bound together by their love of God and, hence, their fellow human. Participation in the community was part of a divine calling, although this calling might be to either religious or secular pursuits. Secular institutions, while separate and distinct from the church, nevertheless operated within community norms. In this way, morality resided both within the individual and in the community. By the mid-seventeenth century, however, this moral cohesion had been weakened by additional settlers who brought with them newer ideas. Social fragmentation forced grace, and thus morality, to be “interiorized into individual conscience” (Seligman, 1992, p. 77).

In Seligman’s account, the cohesion made possible by civil society was disrupted not only in colonial practice but by theory as well. Such was the contribution of David Hume. Writing about the same time as Smith and others, Hume contended that moral sentiments had no basis in reason but involved only the passions. Reason, on the other hand, was concerned with universal truths. Put differently, moral sentiments occupied the territory of prescription, or the “ought” in society, while reason concerned itself with description, or *what is*, and the two realms were mutually exclusive. Accordingly, Hume argued that justice, based as it was on reason, was no more than human convention; thus, conceptions of justice necessarily varied across both time and space.

Immanuel Kant’s contribution to this debate is ambiguous in Seligman’s account. On the one hand, he describes Kant as “fighting an almost rear-guard action to salvage that connection between the workings of reason and the moral sphere that scientific thought (and the writings of Hume) were increasingly questioning” (Seligman, 1992, pp. 41-2). On the other hand, to the extent Kant succeeded in reconnecting morality and reason, he did so by distinguishing between the spheres in which these activities took place, that is, the public and private. For Kant, then, right, both in the sense of individual rights and in terms of justice, was secured by autonomous and equal individuals exercising the formal strictures of reason. This exercise took place in the public

realm, but “public,” here, is not coterminous with the state but, rather, involves the institutions of civil society as distinguished from the biological family. While Kant believed legitimate constitutional rule rested on the presupposition that the state’s laws “would be such that had all the (rational) citizenry debated them, they would have arrived at the same” (Seligman, 1992, p. 43), this hypothetical debate could produce only a just society, not an ethical one. Morality (ethical ends) was not the proper purview of the state, whose responsibility was to ensure citizen consent; rather, morality fell more appropriately to the purely private domain of individual affairs.

Hegel criticized Kant’s disjunction of the ethical and juridical and, in Seligman’s view, sought to reunify the two in his theoretical account of civil society. Hegel argued that the family had been the source of social solidarity and individual support under feudalism, but that this responsibility was assumed by civil society in modern times. What the family had provided through love, civil society now provided through property. Indeed, property served multiple purposes: It was the principal medium of exchange, a primary source of reciprocity, and an important form of recognition linking people in the now fully modern world. Because of the corporation’s critical role in the distribution of property, it played a vital role in Hegel’s theory, both representing the interests of its members and inculcating a sense of community among them. In this way, Hegel united particular interests and ethical norms of community within “civil society,” although this civil arena was no longer coterminous with the public sphere. At the same time, Hegel believed that individual freedom in its fullest sense could only be realized in the state, where the general will was pursued and particular interests were sublated. Nevertheless, the transformation of self-interest into common purpose was furthered by individuals’ participation in the corporation where they acquired social skills and a sense of community.

Jay Drydyk (1991) amends this characterization of Hegel. He understands Hegel to be critical of both modern liberalism and radical egalitarianism. Liberalism, in both its economic and political manifestations, involved the institutions of civil society dominating the political; radical egalitarianism, on the other hand, entailed political institutions dominating the civil. What was

needed, in Hegel's account, was a balance between the two where both sets of institutions served to reinforce and mutually support the other. At the same time, individuals participated in these spheres differently. In civil society, one's consciousness was that of a burgher, pursuing one's interests that were often material in nature; in the state, on the other hand, one's consciousness was that of citizen where the general will was pursued. Here, general will is understood as what one wishes *for all* or *on behalf of all*. The central distinction between special interests and general will is that of conditionality. Special interests are conditional; that is, they will serve certain groups at certain times. General interests, on the other hand, are unconditional; they are available to all, at all times. Apart from certain liberties or rights, which a community may deem imperative for all, the single ethical principle on which the state rests is that of non-exclusion. This did not mean that the state should redistribute wealth. In fact, Hegel opposed such programs for their breeding of dependency. But the principle of non-exclusion did preclude the imposition of one group's particular will on the whole as mere pretense of general will.

The twentieth century's contributions to the concept of civil society have been relatively limited. Jean Cohen (1998), however, credits European analysts of civil society, including Antonio Gramsci and Jürgen Habermas, with adding three components to our understanding. Gramsci believed civil society provided the institutions or collectivities through which group identities were formed and norms of behavior established. In this respect, it served both cultural and symbolic functions by providing meaning to participants in the associations. Second, civil society included not only formal institutions and voluntary associations, but also informal networks and social initiatives that help to change both the polity and civil society itself. Third, Habermas credited civil society with providing the space for discourse not only within the myriad collectivities that constitute civil society but among these groups as well. This discursive role represents for Cohen "the normative core of the idea of civil society and the heart of any conception of democracy" (1998 p.15).

Historically, then, the concept of civil society has incorporated several dimensions: that of both public and private space, the intersection of individual and social concerns, a source of

moral or ethical conduct, and a reconciler of interests and passions. Viewed by the Scottish Enlightenment as coterminous with the state, civil society was considered a locus for interaction that was inherently public. At the same time, participation in civil society carried a moral dimension, even though these moral sentiments were motivated by the human desire for approbation. Later, Hume disassociated morality from reason, regardless of the sphere in which the activity occurred, while Kant decoupled ethical affairs from the juridical. Hegel attempted to reconnect aspects of the ethical and juridical, but did so in part by segregating the spheres in which the two activities took place. Under Hegel, then, civil society became part of the purely private realm. For our purposes, what is important is the selective way in which aspects of the civil society concept continue to be embraced by contemporary social critics. Scholars who invoke Tocqueville and his Scottish Enlightenment forebears, for example, may stress the moral sentiment aspects of civil society but regard the sphere not only as private, but completely independent of the state. Those who invoke Hegel may emphasize the inculcation of community norms or values, but then associate this with public ends rather than purely private interests. Nevertheless, many of the themes presented here are repeated in the arguments of contemporary commentators. While the themes may be similar, many of the details are rearranged. There are many options and the following sections provide ample evidence.

### Responses to the Problem

In general terms, there are at least three views of civil society corresponding to the three types of problems identified with the present state of democracy: those concerned with individual freedom, those alarmed by what they see as an eroding social fabric, and those who want to foster democratic participation. Moreover, within each of these groups, one finds both academic and popular advocates as well as variations in emphasis. At the same time, while interest in civil society is broad and includes people from a range of political persuasions, it does not mirror the full political spectrum. First, some of those writing about civil society are critical of the ways in

which it has been presented. At the same time, most advocates hold a central position while those at either extreme being in the minority.

Those concerned most with state oppression look to civil society as a means by which citizens can address social problems independently of the state. Within the academic literature, Ernest Gellner's *Conditions of Liberty: Civil Society and its Rivals* (1994) perhaps best represents this view. Here, the institutions of civil society given greatest attention are those that accomplish both social and political ends. These would include churches, charities, and human care groups like Hospice—all of which provide necessary social services. They would also include associations involving leisure time, be they ones promoting sports like the National Rifle Association, or ones preserving nature like the Sierra Club. Less emphasized in this literature are associations like the family or even neighborhoods, which are deemed important to society but fall more logically into an informal, or personal, domain than civil society—understood in this view as a more formally structured sphere. Indeed, there is little that is voluntary about a family, given that one is usually born into it. Also given less attention in this perspective is the role that civil associations play in nurturing common values. Norms and values are not ignored here; indeed, they are accorded considerable weight. However, they are esteemed for their expressive qualities, rather than for any contribution they might make to holding a community together. Social capital is less of an issue than individual moral rectitude.

Civil associations, then, are important to these advocates for the opportunities they provide citizens to express themselves voluntarily and to participate in public life. For some, civil associations can also be important for the role they play in politics. Lobbying is required for many of these organizations, and the programs they sponsor, to survive. By participating in the association, either through one's labor or one's money, individuals express their voice in the political arena. The results of this political activity can be problematic for others who share this view of civil society, but who regard state intervention—be it indirect or benign—through voluntary association as an example of an overreaching state that both distorts the market and curtails

individual choice.<sup>5</sup> Crane (1997), for example, urges self-restraint instead of political advocacy as a means of curtailing the reach of the state. While differences exist among these advocates on the relationship of civil associations to the state, there is little ambiguity about the appropriate ways for association members to participate—economic participation is as important as physical participation or giving one’s time. Furthermore, one reads little concern about the role of the market in this literature. On the contrary, voluntary associations foster cooperation and reduce transaction costs among participants, thereby supporting the market value of efficiency. In sum, civil society provides a vital means through which Americans express themselves—be it their personal beliefs or their social preferences. As mediating institutions, then, civil associations promote individual freedom and create a buffer against the expanding reach of the coercive state.

By far the most numerous group of civil society advocates includes those who see problems with both the excessive reach of the liberal state and the atomistic emphasis of the market, geared as it is to individual consumption. Indeed, both state and market forces have served the cause of liberalism so well, in this view, that the foundations on which the liberal nation-state depends have begun to decay. These foundations include, but are not limited to, ethical and moral values, a sense of common purpose, a general sense of equality, and individual responsibility. For these proponents, then, civil society provides not only a middle ground or buffer between the state and the market, but a place where personal values can be developed and nurtured. Civil society includes not only churches and the other voluntary institutions mentioned above, but informal groupings like neighborhoods and families as well, for it is here that the “seeds of virtue” are planted and first nourished.

For this group, then, civil society is important not only because of the voluntary nature of its participants but because of the “habits of the heart” (Bellah, Madsen, Sullivan, Swidler, & Tipton, 1985) promoted by such participation. Participation in the myriad associations that lie

<sup>5</sup> This position is carefully described and critiqued in (J. Cohen & Rogers, 1992, pp. 397-406).

outside the dictates of both the economy and the state fosters the attitudes of mind necessary for tolerance in a pluralistic society, the ability of citizens to discuss differences, and the desire to reach compromise. At the same time, civil society is the place where values can be shared and character developed. Although these institutions are varied in purpose and orientation, they promote morality and the inculcation of norms.

This broad middle ground is perhaps best represented by the Council on Civil Society and by scholars like David Blankenhorn, John DiIulio, Don Eberly, Jean Bethke Elshtain, Mary Ann Glendon, and James Q. Wilson, who are associated with the Council and were among the twenty-four co-authors of its recent report *A Call to Civil Society* (Council on Civil Society & Elshtain, 1998). Their work, however, rests on some earlier scholarship and it is important to mention this first. As far back as 1977, Berger and Neuhaus<sup>6</sup> identified the importance of “mediating institutions” that engaged citizens in collective action independently of both the state and the market. Their thesis was based on a perception of Americans’ paradoxical desire for the services provided by a welfare state, on the one hand, and their simultaneous “animus against government, bureaucracy and bigness as such,” on the other (Berger & Neuhaus, 1996 p. 157). Rather than viewing this as an unresolvable contradiction, Berger and Neuhaus suggested that it would be possible to realize both aspirations through the nurturing of mediating institutions, defined as “those institutions standing between the individual in his private life and the large institutions of public life” (ibid., p. 158). They reasoned that human beings secure their identity and find meaning in their private lives, but modern society is organized into megastructures, be they government organizations, professional associations, or large corporations. While these megastructures serve a necessary function in society, they do little for the individual in terms of meaning-creation or social solidarity. In fact, Berger and Neuhaus argued, they serve to reinforce the tendency in modern, liberal thought toward abstraction and the pursuit of absolutes--including absolute rights. As a consequence, we live bifurcated, disconnected lives, often lacking in meaning and fulfillment. In

<sup>6</sup> Although first published in 1977, all references to this text will be to a twentieth anniversary reprint edition in which other essays as well as reflections by the authors are included: Berger, Peter and Richard John Neuhaus, *To Empower People: From State to Civil Society*, edited by Michael Novak, 2d edition, (Washington D.C.: AEI Press), 1996.

the process, we become alienated from the very megastructures we create. This is particularly problematic for democracy, they reasoned, which depends on public support for its very legitimacy.

Berger and Neuhaus identified four mediating structures—neighborhoods, the family, the church, and voluntary associations—which, properly supported by public policy, could serve to lessen this sense of disconnectedness and enhance the legitimacy of democratic institutions. They pointed out, however, that their proposal should not be confused with decentralization, another reform gaining currency at the time. The difference was more than one of control or accountability; it involved individual empowerment, or the ability of people to take control of their lives through action in their communities, regardless of their level of income.

Little attention was given to this argument in the 1970s, although the problems did nothing to abate. One of the scholars most responsible for drawing both popular and academic attention to the issue is Robert Putnam. Having completed a twenty-year study of Italy (Putnam, 1993) where he examined newly created regional governments and their impact on political efficacy and economic prosperity, Putnam turned his attention to the health of America's civil associations. He published his findings in 1995 in his now-famous article "Bowling Alone" (Putnam, 1995a, 1995b). Examining national survey data from several independent groups, Putnam found that since the 1960s not only had the number of Americans voting in elections declined, but that attendance at public meetings as well as participation in organized religion, labor unions, and parent-teacher associations had also declined<sup>7</sup>. Moreover, not only had participation declined, Americans' cynicism and distrust had risen. At the same time, he discovered quite by accident that more Americans were "bowling alone," that is, bowling on their own, apart from leagues. In fact, more Americans reported bowling in 1994 than voting in congressional elections. Moreover,

<sup>7</sup> Putnam amended some of these findings in his later work (Putnam, 2000).

the data suggested that this decline in participation and trust affected all groups, regardless of educational attainment.

At the same time, Putnam discovered that several forms of participation had indeed increased: participation in tertiary organizations like the Sierra Club, National Organization for Women, or the American Association of Retired Persons; personal support groups; and non-profit organizations. Yet participation in many of these organizations consisted of little more than paying dues rather than active engagement in common projects. The difference, he argued, was that many of these tertiary associations produced little or no social capital, which he defined as “features of social organization such as networks, norms, and social trust that facilitate coordination and cooperation for mutual benefit” (1995a, p. 4). Importantly, Putnam noted that it was this social capital that scholars in fields as diverse as education, urban poverty and drug abuse had found instrumental in various programs’ success. In other words, as in Italy, programs were most likely to succeed where the associations were horizontal and members of the community were civically engaged. Associations, as Alexis de Tocqueville had observed 160 years earlier, were important for democracy.

Putnam amended his argument the following year (1996). More extensive analysis of the data revealed that the level of civic participation did vary by respondents’ age, but not by traditional life cycles. Instead, the variation was more noticeable when broken down by generation, with those becoming adults after W.W.II being far less engaged in their communities and far more distrustful of institutions than those who had matured before the war. Earlier analyses had camouflaged this distinction, in part because of rising levels of education among the younger cohort. Putnam concluded that the principal culprit in this change was likely (though not yet definitively) technology: more specifically, the advent of television.

Putnam’s argument was not that technology was evil, merely that technological innovation might be accompanied by previously unrecognized costs. This observation was reformulated in another work published in 1995: *Seedbeds of Virtue* (Glendon & Blankenhorn, 1995).

Many of the contributors to this volume are associated with the Council on Civil Society and their findings lay the groundwork for many of the recommendations made in the Council's 1998 report. The underlying premise in *Seedbeds of Virtue* is that democracy is still an experiment that requires nurturing to survive. Just as the natural environment can be depleted unless proactive measures are taken to sustain and replenish it, so, too, can the social environment. Contributors to the volume hypothesized that the very freedoms we embrace so enthusiastically may serve to erode the base on which those freedoms rest. While the contributors examined this hypothesis from various perspectives, I shall focus on only two.

Of particular concern is the relationship between democracy and morality. James Q. Wilson opens his essay by asking whether liberal democratic regimes can “foster a shared culture that will restrain human appetites without relying on oppressive political force” (1995, p. 17). He responds by noting that, traditionally, the purpose or end of the *polis* was virtue or the good life. This changed, however, with the evolution of the liberal state where individual rights became the end and the state assumed the role of their protector and often arbiter, especially when understandings of those rights differed. Wilson traces this change to the Enlightenment—specifically to Hume, Smith and Kant, and their privileging of reason, especially scientific reason, over sentiment or affect. While he admits that the immediate benefits to society were substantial, this privileging of rationality eventually extracted costs. These costs were realized when the logic of certain ideas was taken to its extreme.

Wilson examines four cases: skeptical reason, individual rights, equality, and culture; I will summarize his argument for reason only. As we have seen, Hume distinguished descriptive concepts from prescriptive ones and attributed the former to reason, the latter to the passions. Wilson points out, however, that Hume made no judgment on the relative worth of the two activities; in other words, in Hume's account questions of morality, based as they were on sentiment, were not less important than questions of behavior or rational action. The distinction took a pathological turn in the 1920s, however, when logical positivists advanced the idea that ethical

norms were meaningless because they could not be verified empirically. In much the same way, Wilson argues, John Stuart Mill extended the concept of liberty so that it lost any connection to social obligation. Similarly, the meanings of equality and culture were extended so as to render all human practices completely relative. While the intellectual elite might embrace this high modern or postmodern condition, Wilson argues that “in our parochial lives we are only moderately touched by the modernist waves; the degree of change depends on our inner bearings, our social resources, and unpredictable circumstance” (Wilson, 1995, p. 30). Numerous civil society advocates share the view that the academy is out of step with everyday people and note that it is the pedestrian, middle class person to whom their literature is addressed. Beem (1996b), for example, made a special effort to distinguish the Council’s work from that of more traditional scholars, specifically noting the Council’s concern for the people who live in communities, as opposed to scholars in “ivory towers.”

The editors of *Seedbeds*, having posited the self-destructive potential of liberalism taken to its logical extreme, and the desire of everyday citizens for a greater sense of morality in their lives, turn to William Galston (1995) to consider the form this morality should take. Galston acknowledges Kant’s distinction between individual virtue and social justice, but links the importance of intelligence, public spiritedness and self-restraint to effective self-government. It is not that men must be angels, he observes, but that “the operation of liberal institutions is affected in important ways by the character of citizens (and leaders)” (ibid., 1995, p. 38). Galston distinguishes, then, between individual virtue as an instrument of the polity and virtue as a social good (or end) in itself. He then argues that both types of virtue are important in a liberal society, although the virtues deemed useful to the polity may differ from personal or private ones. Some virtues are required in every nation: the courage to go into combat in the state’s defense, the willingness to obey laws, and loyalty to core principles found in constitutions and other documents. While Galston recognizes that these virtues need not be absolute—that is, individual situations may require disobedience or resistance, and all members of the polity need not uphold them for the state to survive—they are virtues that, he contends, should be widely shared.

At the same time, Galston recognizes that liberal societies are sustained by both individualism and diversity. Individualism requires the virtue of independence, or the willingness to take responsibility for one's person and one's actions, and is nurtured by the family. Diversity, on the other hand, requires tolerance. By this, he does not mean license or absolute relativity. On the contrary, Galston argues that habits and customs should be compared and evaluated. Discussion of differences, however, requires openness to others' views and persuasion. Still, a liberal economy also requires virtues to sustain it. These include a commitment to the work ethic, aspiring toward a mean between "ascetic self-denial and untrammled self-indulgence" (ibid., p. 45) and adaptability—a virtue especially important in a changing global economy. A liberal polity requires respect for the rights of others, moderation in one's demands of the state, and sufficient self-discipline to accept personal sacrifices when they are necessary for the general or long-term good. Political leaders should possess the ability to accept and work with constraints, the judgment to promote common purpose, the strength to resist temptations of popularity, and the good sense to balance popular opinion and sound policy. Finally, citizens and leaders alike benefit from the virtues of "publicity," that is, openness in public affairs, and a "disposition to narrow the gap ... between principles and practices" (ibid., p. 48).

While his list of instrumental virtues is long, that of intrinsic virtues is more limited. These include rational self-direction, the capacity to act in accordance with one's sense of duty, and the capacity to develop one's own individuality. Development of all these virtues, he believes, begins with the family, although they are nurtured and reinforced in neighborhoods, associations, the workplace, and elsewhere. This brings us to the 1998 recommendations of the Council on Civil Society reported in *A Call to Civil Society* (1998). Here, the Council links a decline in shared values in the United States with a decline in social solidarity, in general, and the growth in income disparity, in particular. They understand that the domestic economy is affected by changes in the global market, but they attribute Americans' indifference to such changes, especially the increase in poverty, to greater fragmentation in society and erosion in values that bind us together.

Shared values are important for Council members not because they want to create a moral society, but because they want to create moral individuals. The Council emphasizes the importance of individual character and argue, like the Public Administration scholars David Hart and Dale Wright, that “the ‘civic good’ begins with the primacy of virtuous man” (1998, p. 416). Moreover, Council members contend, again like Hart and Wright, that academics have, by and large, forsworn the possibility of universal values, even though our democratic institutions depend on them for survival. As a consequence, they make their appeal to the average, middle class person for whom these values are still important.

These values include, but are not limited to, a sense of personal responsibility, respect for legitimate authority, and respect for others as human beings. Moreover, Council members argue that virtue takes “root in individuals essentially due to the influence of certain moral ideas about the human person and the nature of the good life” (Council on Civil Society & Elshain, 1998, p. 7) and that individuals are exposed to these ideas in association with other people. The report identifies twelve “seedbeds of civic virtue:” the family, neighborhoods, faith-based institutions, voluntary civic organizations, arts establishments, local government, primary and secondary educational institutions, higher education, economic institutions, the media, shared faith in common civic purpose (or belief in the common good), and a public moral philosophy. In other words, their seedbeds include physical institutions and personal relationships, formal organizations as well as belief systems, and private as well as public sector institutions. While the Council excludes most institutions of the state from its repertoire of civil institutions, it does list those units of local government that are accessible and participatory and education at all levels. It also relies heavily on the nation’s constitution, other founding documents, and America’s legal tradition to provide a common civic purpose.

Christopher Beem (1996a, 1996b) underscores the importance of these founding documents when he distinguishes among associations within civil society. He argues that unbridled association can foster prejudice and uncivic virtues, just as easily as civic virtues in as much as

militia units and gangs are as voluntary and participatory as Hospice or the Boy Scouts. Viewed in this light, pluralism's excesses can become far more deleterious to social order and democracy than the reaches of a federal state, as advocates such as Crane and Gellner suggest; in this event, only an appeal to common moral bonds can adequately counter such adverse consequences. Beem points out that both Abraham Lincoln and Martin Luther King, Jr., successfully appealed to Americans' common principles in their respective struggles against slavery and segregation and he sees a need to renew this appeal today. Specifically, Beem mentions the Declaration of Independence and the Preamble to the Constitution as embodying the principles that may provide the common bond now missing from our political discourse.

Another group holding the middle ground and reporting on civil society in 1998 is the National Commission on Civic Renewal, co-chaired by William Bennett and Senator Sam Nunn (National Commission on Civic Renewal et al., 1998). While the authors stress the importance of "trustworthy human qualities" (ibid., p. 4) to the effectiveness of democracy, and bemoan the passivity and often cynical resignation of many citizens to social problems, they also urge a more pragmatic, action-oriented approach to community problem-solving than the Council on Civil Society and similar advocates. As importantly, they recommend the forging of alliances among individuals, voluntary associations, private markets and public organizations to achieve common purpose (ibid., p. 8). While citizen discourse is encouraged, their emphasis is on concrete projects that address specific problems. Bennett and Nunn never use the words "social capital," but the effect of their recommendations is tantamount to developing positive, trusting, and constructive "relations between individuals and groups."

A third, and final, group of civil society scholars includes democratic institutions in their concepts of civil society and regards most public institutions, on balance, as a positive force in society. Jean Cohen (1998), for example, contends that by restricting our understanding of civil society to the non-governmental sphere and, concomitantly, reducing government to its coercive aspect, we not only curtail opportunities for developing social trust, but we ignore the many dis-

cursive and trust-creating or enhancing arenas that may be provided by civil and public institutions alike. Indeed, she agrees with Putnam that fostering voluntary cooperation through civil society has many advantages over state enforced means of securing the common good, but argues that too narrow a view of civil society limits both its theoretical and practical value. Rather, she maintains that the core normative component of civil associations is the space they afford members to discuss organizational questions openly and among equals.

Cohen also focuses on Putnam's use of social capital and distinguishes among *five* different aspects: "individual trust; general norms of reciprocity; belief in the legitimacy of institutional norms; confidence that these will motivate the action of institutional actors and ordinary citizens; and the transmission of cultural traditions, patterns, and values" (ibid., p. 17). She observes that while trust can reside only in individuals, institutional norms can be developed and maintained socially. More importantly, Cohen argues that understanding civil society as a response to dichotomous choices between the public and private sectors, individual rights and duties, or social custom and legal code miscasts the problem and leads to false policy choices. At the same time, members of public institutions who fail to appreciate the role they play in developing and nurturing social capital—in all of its manifestations—ignore a critical part of their mission. Moreover, understanding more about how these three spheres interact and how interaction among them can be improved should, she contends, be the concern of democratic theorists in the immediate future.

A different perspective within this third category is provided by Michael Walzer (1991, 1992, 1994, 1999). As noted above, Walzer recognizes the difficulties that fragmentation presents both for society and for democracy, but he regards individual "dissociation" (Walzer, 1994, p. 188) or the isolation of individuals within society as a more serious problem. Civil associations go part of the way to address this concern for they provide both the physical space for uncoerced association and a set of "relational networks—formed for the sake of family, faith, interest, and ideology" (Walzer, 1991, p. 293). In this capacity as both physical space and political concept, then, civil society can help bridge the gap that has emerged in democratic countries be-

tween our spheres of action and components of our lives. Historically, Walzer points out, western societies have historically pursued one of four possible approaches to governing: republican political association, socialist organization of the economy, free and open markets, and nationalism. The problem with these rival ideologies is that each represents a singular, mutually exclusive pursuit and while each has merits on its own terms, each also has serious limitations. At the same time, modern industrialized societies have evolved into complex amalgams of these ideologies with none preserving any one ideology in its pure form. For Walzer, then, our lives are fragmented at multiple levels and the traditional responses to social organization have reinforced this by addressing only one aspect of our lives—to the exclusion of the other dimensions. Bringing civil society, which exists *in* the state but is not *of* it, into the equation makes it possible for people to live in *all* of these dimensions. We may not inhabit all dimensions at a single time in our lives, but increasingly we will inhabit more than one dimension simultaneously.

Several years later, Walzer revised his assessment of civil society (1999), identifying three primary weaknesses with its institutions: inequality, fragmentation, and fitfulness. By inequality, he means that civil society does little to moderate the social forces of inequality, exacerbated by an expanding global economy; indeed, civil associations—even those with services for the poor—may often lend capacity to care givers and create dependents of those whom they serve, in much the same way that the welfare state often created dependents. Civil associations may also help to fragment society, organized as they often are to serve a particular set of interests. Finally, civil associations foster fitfulness, by which he means that they rely upon part-time, voluntary labor to meet broader social goals. Although virtually all associations have a paid, professional staff who maintain the organization institutionally, service delivery can be erratic. To address these concerns, Walzer suggests that the two dominant groups of Communitarians—those who favor common action via the state and those who prefer collective action through private association—help remedy the deficiencies in each other’s cause. That the non-profit sector can assist the state by assuming some social service responsibilities heretofore primarily lodged within the state has been amply demonstrated by the rise of the civil society movement

more generally. However, Walzer proposes several ways in which the state can also help support and ensure the viability and continuation of non-profit organizations, both through program legislation and tax relief.

To review, the problems addressed by civil society proponents range from too much government to excessive liberalism, and then to inadequate understanding of public life. That such a plethora of perspectives can exist is, at times, bewildering. Yet Taylor (1990) reminds us that these divergent views can be traced to Thomas Hobbes and Charles Louis Montesquieu. Hobbes, he suggests, understood sovereignty to lie with the king, and thus took a political view of society. Montesquieu, on the other hand, saw law as limiting monarchy, but understood the law as empty unless it was upheld by personal dignity and independent institutions, such as “parlements” and “estates.” Opposing views are thus part of our heritage.

#### Problems with the Civil Society Literature

Implicit in many of these accounts are critiques of alternative approaches to civil society. Jean Cohen, for example, takes exception to those who would preclude the state from any role in fostering or sustaining civil society. Few resemble Walzer, whose more catholic perspective envisions a civil society that expands the spheres of collective action, rather than placing one version of civil society in opposition to another and forcing a choice between them. However diverse and multifaceted this range of perspectives might be, it does not exhaust the commentary on civil society, for there are many concerns about the concept itself as well as critiques of the arguments made by its proponents. Much of the criticism has been directed at Robert Putnam, his analysis of political conditions in Italy, and the extension of lessons gleaned from that research to circumstances in the United States. This criticism takes several forms—some of it focusing on research methods, some on the diverse nature of associations or the definition of social capital, while others emphasize the causal relationship between social capital and effective democracy. This section will attempt to state these arguments thematically, drawing on the principal contributors to each. However, because so many criticisms target Putnam specifically, the

summary will mimic that pattern—even when it means including authors whose attacks do not cite Putnam directly.

To appreciate the criticisms, it is helpful to review briefly Putnam’s argument in *Making Democracy Work* (1993). As alluded to earlier, Italy created regional governments in 1970 and transferred numerous responsibilities from the national government to these smaller units. Recognizing the importance of such a transfer, Robert Putnam began immediately to collect data on the performance of these new administrative units. Because his interest was institutional, the data he collected attempted to measure the new agencies’ performance across time, using twelve indicators. These measures were grouped into three categories: policy processes, policy pronouncements, and policy implementation (ibid., pp. 65-82). As data collection progressed, however, he observed fewer changes in institutional performance across time than across space; specifically, he noticed distinct differences between the performance of regional governments in northern and southern Italy. This led him to add indicators of “civic community” to his data set. These included: vibrancy of associational life, newspaper readership, electoral turnout in referenda votes, and preference voting (a negative indicator). He also surveyed regional politicians, community leaders and the public to determine whether the perceptions of those involved matched the more objective indicators. He found not only that the perceptions corroborated his other findings but that where civic community was strong, other performance indicators were also strong. In his concluding chapter, Putnam contrasts his findings with arguments that stress the difficulty of collective action, like that of Mancur Olson (1982). These are found mostly in the economic literature but have been embraced in recent years by political economists and many political scientists more generally. Putnam’s point is that these theories “prove too much,” (Putnam, 1993, p. 165) because they make collective action appear all but impossible. His findings suggest that collective action is possible, given a supportive culture.

Putnam traced the roots of his findings to medieval Italy, where independent city-states, organized horizontally, had populated the north while external powers, organized hierarchically,

had colonized the south. He linked these findings by means of another concept, “social capital,” which he defined as “features of social organization, such as trust, norms, and networks, that can improve the efficiency of society by facilitating coordinated actions” (Putnam, 1993, p.167). In other words, he argued that political institutions are more effective when there already exists a predisposition to trust and cooperation within the surrounding community. In subsequent writing, Putnam applied this distinction between horizontal and hierarchical organizations to political structures in the United States.

Most of the criticism of Putnam’s argument comes not from economists, whose work he was amending, but from sociologists. The concept of social capital was developed by a sociologist, James Coleman (1988), and epistemological concerns—if not disciplinary rivalries—appear to motivate some of this criticism. Focusing more on Putnam’s observations about the United States than his study of Italy, Theda Skocpol (1996, 1997a, 1997b) and Charles Heying (1997) take issue with Putnam’s thesis that television has caused social capital to decline in the United States. They argue that shifting allegiances of elite leaders, whose communities increasingly consist of professional affiliations rather than neighborhoods, have more to do with declining social capital than television. Heying suggests that elite disengagement is more likely attributable to the global economy that draws corporations away from community-enriching activities toward other, more profitable pursuits. Skocpol, on the other hand, argues that many of the associations Putnam identifies as being in decline are ones traditionally supported by women—indeed, educated women who are now in the labor force rather than volunteering. As importantly, she notes that changes in electoral politics, including the decline in parties and the expansion of professionally managed interest groups, have also altered the nature of grassroots political participation and influenced patterns of civic association. Yet Putnam excludes interest groups and other associations that are more likely to receive professional support from his analysis because they are organized vertically, which, he contends, often fails to generate social capital.

W. Lance Bennett (1998) elaborates this theme of shifting associational allegiances by arguing that changing patterns of work and increased economic insecurity have encouraged many

people to pursue “lifestyle” or “identity” politics, which he suggests are “highly personal, leading to direct and even confrontational personal solutions over governmental ones”<sup>8</sup> and that, when successfully managed, tap into different forms of political organizations and expressions.

Debra Minkoff (1997) extends this argument by suggesting that national social movements provide a viable alternative to community-based, face-to-face organizations, especially for minority groups and the politically marginalized. Because of their appeal to many who might not otherwise be interested in collective action, as well as the grassroots base of many of these movements, Minkoff contends that these associations also contribute to social capital and should, therefore, be included in any tally. In addition to these national groups, Frank Riessman and Eric Banks (1996) include self-help groups, service organizations, community development organizations, neighborhood crime watch groups, and community organizing programs that have emerged in recent years and warrant inclusion in any inventory. Collectively, these scholars attack Putnam’s criteria for the associations he includes and, thus, his conclusion that the United States is experiencing a decline in social capital.

Nicholas Lemann (1996) examines the *logic* of Putnam’s civil society argument and comes to a similar conclusion. He sees Putnam’s return to medieval roots as part of an effort to locate *virtu civile*, understood in Machiavelli’s terms as an associational predisposition or “ingrained tendency to form small-scale associations that create a fertile ground for political and economic development, even if...the associations are not themselves political or economic” (ibid. p. 22). But, Lemann continues, if patterns of association are so deeply rooted in culture, then shifts in participation (such as the decline Putnam laments in the United States) must represent *mutations* in patterns of participation, rather than any overall disappearance. Lemann then offers alternatives for several of the associations Putnam found in decline. For example, soccer groups could substitute for little leagues and Pentecostal denominations are likely to replace mainstream relig-

<sup>8</sup> This appears on p. 4 of text downloaded from the internet in machine-readable form.

ious organizations. William Galston and Peter Levine (1997) take this a step further when they suggest that these newer forms of association might even be replacing traditional forms of political participation, especially among younger citizens. In fact, they speculate that increased interest in voluntary organizations is more likely to explain the decline in voter turnout than television.

The possibility that participation in voluntary associations could *reduce* political activity raises the complex issue of causal direction and the relationship between participation in voluntary associations and citizenship. Once again, opinions vary greatly. For many advocates, it is almost axiomatic that a strong civil society will promote democracy. Yet some scholars contend that causality works in both directions; that is, democratic institutions play as important a role in setting the conditions for a flourishing civil society as voluntary associations contribute to democracy. Skocpol (1997a, 1997b), for example, examines conditions in Tocqueville's America and shows how the U.S. Post Office provided the infrastructure necessary to make communication—and the foundations of civil society—across an expanding territory possible. Walzer (1992, pp.103-4; 1999), as we have seen, extends this argument by demonstrating ways in which civil society and its institutions *need the state*.

Keith Whittington (1998) returns to Tocqueville to suggest that Putnam and others have misinterpreted his argument. In the first place, Tocqueville was comparing 19<sup>th</sup> century America with feudal institutions in Europe and found governmental structures in the new country extremely weak. At the same time, he discovered greater equality among Americans than Europeans. The combination, Tocqueville feared, would lead to anarchy, although the plethora of voluntary associations he encountered provided promising counter-evidence. They served not only to channel citizens' efforts and needs, but helped to educate people of relatively equal abilities and means in the responsible ways of self-government. Whittington concludes that current interpretations of Tocqueville not only idealize the Frenchman's argument, they also overlook the negative aspects of voluntary association, which Tocqueville saw as potentially destructive of democ-

atic institutions, especially when they challenged the moral authority of the state (*ibid.*, pp. 22-25).

This tension between civil society and the state has practical dimensions as well. Pablo Eisenberg (1997) sees recent growth in the not-for-profit sector, now with over one million organizations, as surfacing some latent weaknesses that could result in public distrust of these organizations similar to that experienced by government. He identifies lack of public accountability and ethical problems, among others, and recommends greater government oversight—in lieu of self-regulation—to address these problems. John DiIulio (1997), on the other hand, cautions against government interference in civil associations, especially in the implementation of welfare reform legislation, which now grants considerable latitude to churches and other faith-based institutions receiving federal assistance to retain their denominational characteristics.

Brian O’Connell (1995, 1996) raises concerns about the effect of increased government contracting on voluntary institutions. He identifies three roles for voluntary associations: service delivery, issue advocacy, and individual empowerment. In the past several years, however, the service delivery function has received the greatest attention, especially as governments at all levels have experienced both financial cutbacks and pressure to transfer responsibility to the private sector. He fears that the independent nature of voluntary associations will be dwarfed by this increased service function, at the expense of the other two areas. Moreover, he cautions that government’s accountability for contracted services will be sacrificed, in part because of the two sectors’ differing missions. Government, he reminds us, has a responsibility to serve all citizens equally, whereas voluntary associations are, by their very nature, discriminatory.

Sheri Berman (1997) likens scholars who advance civil society to “mass society” theorists in the immediate post-WWII period because “both fail to recognize that civil society can often serve to weaken rather than strengthen a democratic regime” (p. 564). Democratic theorists, she suggests, could more profitably focus their attention on political institutions, rather than cultural

forces that tend to favor conformity. Berman contends that in a fragmented, complex society, civility and trust are more likely fostered by political institutions than by a strong civil society. In sum, the linkages between civil society and democracy are not as clear or straightforward as they might, at first, appear. Indeed, the conceptual lubricant, social capital, is similarly complex.

Michael Foley and Bob Edwards (1996, 1997), (Edwards & Foley, 1998) argue that the term is both over-simplified and neglects the contribution of James Coleman (Coleman, 1988), who distinguished among *human* capital, or personal qualities that reside within human beings; *cultural* capital, or the values that are shared among people; and *social* capital, or the “norms of reciprocity and trust” that “inhere in relations between individuals and groups, not individuals per se (Edwards & Foley, 1998, p. 129). In this view, social capital is not something people take with them across associations, but patterns of behavior that inhere in institutions. Indeed, people may participate very differently in church groups, for example, and in PTA organizations, even though they are members of both.

Andrew Greeley (1997) elaborates this point when he reminds us that Coleman introduced the term “social capital” in 1988 to provide a bridge between the disciplines of sociology and economics. Coleman, he argues, never intended for “social capital” to inhere in individuals; that is, it is not a personal attribute or even mode of behavior, as it has been used by the Council on Civil Society and others. Rather, social capital resides in social *structures*. It is, in Greeley’s words, a “powerful social resource in human relationships, effecting either human capital (as in the case of families and schools) or profit (as in the case of the diamond market or the Cairo marketplace)” (p. 589). Other examples range from fraternities or sororities in college to organized crime families, such as the Mafia, or drug gangs. Greeley identifies five features of social structures that may generate social capital. These include:

- 1 Obligations, expectations, and trustworthiness of structures;
- 2 Informational channels;
- 3 Norms and effective sanctions;
- 4 Closure of social networks, in which all actors interact; and
- 5 Multiplex relationships in which resources of one relationship can be appropriated for use in a second relationship (pp. 588-9).

To illustrate, Greeley examines data on volunteering where respondents were asked about their volunteer activity and, if they volunteered, how they first learned about the activity. He found that 52% of all respondents said they volunteered and, of those, 28% (the largest subset) volunteered through, or as a consequence of their affiliation with, a religious organization. While most of these volunteers participated in work that was also religious in nature, many contributed to secular activities, such as education or health care, even though they had been drawn to it by a faith-based institution. In this way, Greeley concludes, “the social capital generated by religious structures supports not only formally religious volunteering but ‘secular’ volunteering as well” (p. 592). Social capital, conceived in this way, could decline *if and only if* the volume of volunteer activity generated by religious institutions also declined or the religious structures themselves declined in number. Moreover, social capital itself must be neutral. It is a resource and, as such, can be measured empirically; but he stresses that it is *not* a dependent variable for it remains *independent of the ends* to which it is put.

Greeley stresses that religious organizations, diamond markets, and families of organized crime are all relational structures that produce social capital. The ends to which the social capital that each generates is put will vary considerably but that does not alter the production of this capital. Moreover, none may contribute in any meaningful way to democracy, although intuitively one would expect organized crime to be more destructive of democracy than the other examples. Determining this, however, in Coleman’s account, would have nothing to do with the groups’ illegal activity but everything to do with the families’ *structure* and whether it encouraged democratic participation—however that was defined.

Kenneth Newton (1997) conceives of social capital differently. He distinguishes among three components: norms and values, networks, and outputs. Norms and values, he suggests, are subjective phenomena that bear on interpersonal relationships and may be perceived differently by different groups of people. Communitarians, for example, would likely differ from libertari-

ans in their expectations of colleagues and associates, as well as institutions, since the two groups' understanding of concepts like freedom and democracy diverge. Nevertheless, common norms and values are important for achieving reciprocity or “fraternity”—in the sense used in the French Revolution.

Networks are patterns of association that help give rise to trust. This kind of capital is important to social science because they can be observed and measured. However, Newton doubts that such observation can produce causal inferences as networks develop trust at the same time that they draw upon trust for their sustenance. The third type of social capital involves outputs; these may be facilities, services, or groups. Examples might include neighborhood watch groups or service organizations like Hospice. In these instances, social capital is defined by its function. However, Newton cautions that the function should be stipulated as an hypothesis and then tested empirically, rather than assumed to be produced as part of its definition.

Dietlind Stolle and Thomas Roche (1998) distinguish between only two types of social capital: an immediate form they label “private or personalized civicism,” which refers to interpersonal relationships and the bonds of trust that may ensue, and a more abstract form they call “public civicism,” which refers to “values such as tolerance and cooperation toward citizens in general” (p. 48). While voluntary associations will tend to produce the first kind of social capital or interpersonal trust among its members, only a subset of these associations will actually produce the second kind of social capital, which is of greater benefit to democracy. Gangs, for example, may produce the former but not the latter. Stolle and Roche examine two general attributes of association: the ends or purposes they pursue, especially the degree to which their purposes involve public policy or are directed to community activities, and their level of inclusiveness. After surveying 43 different types of associations, they found that members differed significantly from nonmembers in their measures of social capital. Moreover, they found that members of political associations were more likely to volunteer generally than members of any other group, while members of cultural, community and economic groups were more likely to demonstrate trust and reciprocity than members of other groups—even those in political associations.

Still, trust and reciprocity were more generally apparent across all associations than tolerance, although trust and reciprocity declined as memberships became more homogeneous. They found, in other words, that type of association matters.

#### A Fourth Approach

It should be obvious by now that social capital is not only a complex concept but that however one defines it, associations vary in their generation of it. Viewed as a heuristic device, the definitional requirement becomes less acute. Putnam's use of the term, as a product of research, is more in this vein. However, his study was scientific: It tested the null hypothesis that institutional reform had no effect on policy or governance. In the process, he discovered that the effect of institutional reform varied by geographic region and that social capital was the principal distinguishing feature. Although Putnam adjusted his study to include several politically relevant indicators of social capital, his selection was less discriminating than it might have been. Sociologists who had spent far more time thinking about social capital later apprised him of this oversight. (Of course, Putnam compounded his problem by precipitously applying lessons in Italy to the United States.) While we now understand that any empirical investigation into the relationship between institutions and their membership is complex and must be carefully designed, this has shed light only obliquely on the conundrum posed by Orange County citizens and their response to the bankruptcy.

The problem, as I see it, is that throughout this discussion, scholarly emphasis has remained on social structures and institutions, with much less attention given to the individual participant and her role in the process. Personal values are accorded considerable weight, but more as a requirement of individuals for society than as something that individuals might seek out for themselves. This emphasis is curious, in that interest in civil society has been traced to the fall of the Berlin wall in 1989 (Glendon, 1997). Yet the East European movement has been invoked with little examination of what it entailed. Václav Havel's account in "The Power of the Power-

less” (Havel, 1985) suggests an approach that is more fertile. Havel characterized the problem facing East Europeans in the early 1980s as self-reinforcing, where the requirements of the system and people’s blind acceptance of these requirements served to bolster each other and perpetuate the system. Importantly, he distinguished between early forms of totalitarianism, which were tied to powerful rulers, and the present form, which he labeled “post-totalitarianism” (ibid., p. 27); in its existing guise oppression was institutionalized and individual freedom was subordinated to the “rules of the game” or conventions of the totalitarian state. Civil society, in Havel’s account, is that sphere of action, carved out by individuals who make an effort to “live within the truth” (ibid., p. 41). By this he meant that the individual takes action, however small, to “follow one’s own desire,” (ibid., p. 41) and take steps toward authentic existence. While he identified as many as four stages in this process, the first and most basic was existential—that is, it entailed self-confrontation by the individual about his existence in the world. This shift in the orientation of the individual vis à vis both himself and his relationships with others is pre-political—it is not initially about the system. Rather, it is about how the individual chooses to live in the world, given that this system is ever present. Such a statement is essential if political progress is to be made down the road.

Havel understands this re-orientation to be grounded in the question of one’s identity, but he does not see it as self-serving or self-interested. On the contrary, he regards this attention to identity as moral because this re-orientation is as much about relationships with others—being open to, and honest with, others as it is about openness and honesty with oneself. Civil society, in the sense that it lies outside the post-totalitarian regime, represents a separate sphere—but it is neither public nor private in the sense that Western proponents have used the term. Because civil society refers to the space one creates for authentic existence, it can be narrowly circumscribed and hidden or broadly defined and quite open.

As important as one’s existential posture is the form of action Havel describes. He cautions against focusing on ideology because he believes that it is this very commitment to ideology that has produced the present totalitarian system. Changing ideologies will only produce more of

the same, albeit of a different order. Rather than devote attention to ideas, Havel recommends that one's focus be on the concrete—on small discrete steps that can be taken to improve life as it is lived every day (ibid., p. 88). He understands that every society requires some organization to function, but he urges the structure to serve people, not the other way around (ibid., p. 69). Finally, in a statement unsettling for most Westerners, Havel compares the East and the West:

The post-totalitarian system is only one aspect—a particularly drastic aspect and this all the more revealing of its real origins—of this general inability of modern humanity to be the master of its own situation. The automatism of the post-totalitarian system is merely an extreme version of the global automatism of technological civilization. The human failure that it mirrors is only one variant of the general failure of modern humanity. (Havel, 1985, p. 90)

Automatism is not a response unique to totalitarian regimes; it is common in Western consumer societies as well. Moreover, Havel contends that this blind conformity to the “system,” whatever that “system” may be, simultaneously releases the participants from any responsibility either for the “system” or their actions in it.

Orion White grounds his work in process theory and the psychoanalytic writings of Jacques Lacan, but his understanding of civil society is remarkably similar to that of Václav Havel. First, White's view of civil society rests on the individual.<sup>9</sup> From this perspective, social fragmentation is not a problem to be corrected but a basic aspect of freedom that should be recognized and allowed to thrive. Indeed, problems arise when we try to reduce social fragmentation, force greater conformity, and impose order on human relationships. This does not mean that White advocates licentiousness or that he believes social interactions cannot be improved—neither is the case. It does mean that we have traditionally approached social change in the wrong way.

<sup>9</sup> This summary was culled from (White, 1998).

White would agree with Havel that individual identity is essential both to one's freedom and to a sense of responsibility; yet most of the time we suppress or ignore our desires in an effort to conform or be accepted by others. As a consequence, we not only fail to deal with who we are and live in our own space, we fail to appreciate differences in others. Being unable to exist satisfactorily in our own space, we develop "malformations" or pathologies in our social interactions. These are generally of three types: overgeneralization of problems, excessive deletion in our characterization of situations, and distortions—that is, assuming the role of victim, rescuer, or persecutor.

This becomes important in social interactions in general, and Public Administration in particular, when we try to forge consensus on an issue. Rather than understanding language as a form of self expression, we evaluate it on the degree to which it conforms to our own way of thinking. This is particularly problematic when we rely upon principles and other abstractions to convey meaning. As we have seen with the term "civil society," abstract concepts are often polysemous—they mean very different things to different people. Relying on abstractions, then, like values and norms, means that instead of collapsing the space between us and creating common ground, we are more likely to create greater distance. (This is essentially the difficulty White has with Habermas, who grounds his theory of communicative rationality in the exchange and explanation of norms.) To prevent this, White suggests a "process approach," drawing on the writings of Whitehead and James, where the focus is on a concrete situation or problem. By discussing the concrete situation, and allowing different perspectives to be aired, we have a better opportunity of creating, over time, a shared sense of meaning and forging common ground.

White also cautions against trying to identify permanent solutions to problems. Life, as Heraclitus understood, is like a river—one cannot step in the same waters twice. With change ever present, White suggests taking experimental, next steps toward change. Combining the adoption of an existential stance of difference toward others with a tentative approach toward altering situations in the concrete can, he contends, help groups create common meanings and move us closer to collapsing the chasm that separates us, rather than further dividing us. This

approach has been used successfully in organizational development, and he believes it can be expanded more generally in public organizations. Because the approach rests on an appreciation for the radical difference of human beings, and a non-ideological approach toward the concrete, it also fosters a sense of ownership of attempted solutions. Participants “buy in” to the solutions they create. At the same time, because it assumes an experimental posture, next steps that do not work out can be altered without tremendous personal investment being sacrificed. In other words, this approach enables us both to appreciate and respond to the ever-changing conditions of life while fostering a sense of responsibility towards one’s circumstances. It is this orientation toward others as different, and the locus of interaction in the concrete, that constitutes civil society.

### Concluding Observations

Increased interest in civil society has not been restricted to the academy; it is widely reflected in society at large. Lester Salamon and Helmut Anheier (1997) found that within the thirteen countries they surveyed, the non-profit sector provided five percent of all jobs and accounted for five percent of the gross domestic product. In the United States, it employed 6.5% of the labor force and accounted for 13% of all job growth in the past decade. Its relevance to Public Administration, however, goes beyond this economic and sociological impact. Increasingly, the public sector is expected to develop cooperative arrangements with non-profit, voluntary organizations to fulfill public goals. This is not only a consequence of reduced public budgets during much of the 1990s but also the recognition that voluntary organizations can provide some social services more effectively than public agencies alone. Moreover, it is not only citizens in local communities who often express an interest in these arrangements, but Congress and state legislatures as well. Welfare reform legislation, for example, not only provided numerous incentives for cross-sector cooperation, it incorporated severe sanctions for those recipients who failed to uphold certain community values. Drug abuse and child truancy, for example, can result in the suspension of adult benefits, while a drug conviction will permanently disqualify the of-

fender from welfare eligibility. It is therefore important for the Public Administration community to understand the networking arrangements in which it is expected to engage and the reasoning behind it.

Another insight the Public Administration community might glean from this discussion is the extent to which methodological issues can complicate epistemology. What we know and how we know it are intertwined. Given that Public Administration is an interdisciplinary field that draws on several established disciplines, the twists and turns in the civil society and social capital debate might provide insights into other controversies.

In this review, we have seen that many civil society advocates stress the normative aspects of civil association and encourage development of this sector because of the values it can engender. While these values are not mandated by law, the obligation to adhere to them—if not actually embrace them—is implicit. While this attempt to develop common purpose through the identification of abstract principles may be appealing, White and Havel show us that this approach to civil society is unlikely to succeed. In the first place, as we have seen with the concept of civil society itself, abstractions are likely to be polysemous and do as much to divide people at the same time that they create the illusion of agreement. Second, placing the emphasis on abstract principles takes attention away from concrete problems that can more successfully be addressed. This has been reinforced by experience. A multi-denominational group of churches, for example, found that it could get far more accomplished when participants focused on programs for the poor than when they discussed theological doctrine.<sup>10</sup> This was also the conclusion of a bipartisan commission on civil society (National Commission on Civic Renewal et al., 1998), although they also saw a role for values.

<sup>10</sup> “Call to Renewal” is an interdenominational program begun in 1997 to address myriad needs of the poor. The leadership has repeatedly stress the progress made among groups that had been at odds over theological issues once they set those issues aside and began concentrating on helping the poor.

I hope to show not only that this view of civil society is feasible, given the changing circumstances in public finance, but also that this approach more directly addresses the conundrum presented by the bankruptcy and citizen reaction in its aftermath. It is now time to review the circumstances leading up to the bankruptcy and the public finance context in which they occurred. This will be followed by an examination of entrepreneurial government and risk before returning to matters raised in this review of civil society.

### Chapter 3: The Bankruptcy and its Origins

The Orange County Board of Supervisors filed for Chapter 9 protection from bankruptcy on December 6, 1994, surprising not only county residents, but citizens of California, financial advisors, bond rating agencies, and the public administration community—professionals and lay persons alike. The details of financial mismanagement that led to the bankruptcy have been carefully reported elsewhere (Baldassare, 1998; Jorion, 1995); only the highlights will be recapitulated here. However, as Baldassare has pointed out, what was so surprising about Orange County's filing was not only its size—losses approximating \$1.7 billion or roughly 20% of the entire pool—but also that it was so unexpected.

Admittedly, residents had re-elected County Treasurer Robert Citron only six months earlier and the relative safety of the Orange County Investment Pool (OCIP) had been the central issue in that campaign. Nevertheless, Citron was re-elected by more than 60% of the population, suggesting that voters were either unimpressed by the arguments made by his opponent, John Moorlach, or they were too comfortable with the status quo (or financially naive) to take the warnings seriously. Still, many of those caught by surprise had been closely connected to Citron's investment strategy. The county's Board of Supervisors, with oversight responsibility for his operations, had formally recognized him the previous December for providing the financing that enabled the county to introduce an innovative gang control program. Merrill Lynch had underwritten a \$110 million bond issue as recently as October 1994 to which both Standard and Poor's Corporation and Moody's Investors Services had accorded the county the second highest rating, AA. The California legislature's special committee investigating the bankruptcy in its aftermath found all these groups to be more or less complicit in the failed strategy. It reported:

The collapse of the Orange County investment pool and the bankruptcy of Orange County was not simply a result of the miscalculations and errors of one individual, but rather is reflective of systemic problems and a breakdown of the established governmental process in Orange County (California. Legislature. Senate. Special Committee on Local Government Investments, 1995, p. 28).

It is difficult to imagine that any of those connected with the investment strategy would have perceived the county's bankruptcy as being in their self-interest.

This chapter will review the findings of the various investigations into the causes of the bankruptcy and the pressures that led county officials to embrace, explicitly or not, the treasurer's ill-fated strategy. In the process, I hope to link actions at the local level to changes in policy or thinking at the state and national levels—as well as to changes in the global economy—in an attempt to piece together how so many disparate groups might have ignored the warning signs that, in retrospect, were clearly evident. My purpose is not merely to repeat the findings of other scholars who have focused on either the politics or the investment strategy, but to demonstrate the linkages between these sectors and how the combination affects the practice of Public Administration. Finally, I hope to conclude with some observations about the ideas that guided public officials' conduct and their sense of public service.

### The Basics

At the time of the bankruptcy, there were 187 government units, in addition to Orange County, participating in the Orange County Investment Pool. Many of the participants were cities or towns located in the county; a few were towns outside the county's geographic limits that had asked to participate because of the county's record of high yields. All of the county's school districts were invested in OCIP because state law required them to do so. Finally, regional water, transportation and other special districts participated in the pool, although their involvement was voluntary. Apart from Citron's reputation as a successful investor, groups were drawn to the investment pool because it was large and represented a wealthy county. 1990 census data<sup>11</sup> report median family income in Orange County at \$48,439, fifth in the state of California behind Marin, Santa Clara, San Mateo, and Contra Costa counties. The average value of

<sup>11</sup> These data are taken from Section E of (CACI Marketing Systems, 1992).

owner occupied houses with mortgages was \$287,071 in 1990, sixth highest in California.<sup>12</sup> This was below the average value of \$387,384 in Marin County but above the state's average of \$239,101. Yet averages conceal the cumulative wealth of a county with 2.4 million people. Philippe Jorion estimated total real estate value in the county between \$100 and \$150 billion and ranked Orange County eighth highest in the world in gross domestic product—at \$74 billion—if Orange County were a country (1995, p. 2). The county's overall wealth and size of its investment pool were important because they gave OCIP access to a greater variety of financial instruments, lower rates by brokers and other financial advisors, and access to more expert and more timely information than many other local government investment pools (ibid., 1995, p. 19).

The county's treasurer, Robert Citron, had served in that capacity since 1970, having secured voters' confidence in six previous elections. He had also been recognized for his financial accomplishments, not only by the Board of Supervisors, as mentioned, but also by various groups including *City & State* (ibid., 1995, p. 8), which had ranked him among the nation's top five financial investors in 1988 and the American Society of Public Accountants, which had pronounced him an "outstanding public official" during the June 1994 election (ibid., 1995, p. 86). The pool itself had repeatedly outperformed the state of California's investment pool. Between the recession years of 1991 and 1993, OCIP produced returns between 8 and 9%, while the state of California generated returns in the range of 5 and 6%. The differential meant additional revenues to Orange County of approximately \$500 million for the two year period (ibid., 1995, p.8). The state's performance relative to Orange County had even been a campaign issue in 1990 when Tom Hayes, the incumbent state treasurer, lost his re-election bid to Kathleen Brown, who pointed to the state's lagging performance in her appeals to voters. Ironically, it was Tom Hayes whom Governor Pete Wilson later appointed to oversee the county's investments in the aftermath of the bankruptcy.

<sup>12</sup> These figures were taken from Section D of (CACI Marketing Systems, 1992).

Yet it was not mere status or greed that drew local governments to the pool; the economic need was palpable. Since 1978 when California voters passed Proposition 13, local governments had been forced to become more daring in securing revenue. Not only had local property taxes declined, but federal funds had also dwindled as revenue sharing monies dried up while increased health and welfare responsibilities devolved to states and local governments. Military base closings in the early 1990s only exacerbated the recession that had, by then, spread to California. Suffice it to say, for the time being, that astute cash management had become an economic necessity in California.

Two factors are generally credited with causing the bankruptcy: excessive use of derivatives and the leveraging of Orange County's financial portfolio. Although more will be said about both of these as the discussion proceeds, a few introductory remarks are helpful. Derivatives are often described as financial instruments, akin to bonds or stock, whose value is derived from an underlying stock, commodity or other asset. Frequently the value will be calculated by a formula, such as the difference between short and long-term interest rates or the exchange rate between two currencies. A former designer of derivatives explains them as follows:

A derivative is a financial instrument whose value is linked to, or derived from, some other security, such as a stock or bond. For example, you could buy IBM stock; alternatively, you could buy a "call option" on IBM stock, which gives you the right to buy IBM stock at a certain time and price. A call option is a derivative because the value of the call option is "derived" from the value of the underlying IBM stock. If the price of IBM stock goes up, the value of the call option goes up, and vice versa (Partnoy, 1997, p. 31).

To pursue this a bit further, if IBM stock were selling at \$50 per share and the call option stipulated that 100 shares could be purchased in three months at \$51 per share, the option itself (or contract) could be sold in the intervening months. Since an option does not have to be exercised, but merely gives its owner the right to enforce the terms specified if she chooses to do so at the time, it would not trade for the full value of the stock. Instead, a premium would be paid to the issuer. If IBM stock rose to \$55 per share in a month, the call option would be worth

more than its initial premium value; however, if the stock declined, the option would be worth less—even though the contract’s provisions remained the same. This kind of call option is a forward contract—a bet, if you will, on the future—and its value will fluctuate with the value of IBM stock until the date it comes due and the contract’s provisions are either exercised or allowed to expire.

Leveraging is a form of borrowing and involves the use of existing assets to purchase additional assets. The activity might be compared to taking out a home equity loan, which is normally obtained to make home improvements and the house itself used as collateral in the event the loan cannot be repaid. If the home equity loan were obtained, instead, to finance the purchase of a second house, and that house later sold at a profit, the loan could be repaid with interest and, assuming the profit exceeded interest payments, the original borrower would make money with relatively little effort. Essentially, Citron borrowed money against existing assets (usually government bonds) in order to purchase additional assets (again, government bonds). However, since public borrowing is restricted by the California constitution, he could not borrow money from a bank; he had to use more oblique means in order to achieve the same results. He did so by purchasing financial instruments known as *reverse repurchase agreements*. His strategy had apparently succeeded for a while. At the time of the bankruptcy Citron had leveraged almost \$7.5 billion in assets into a fund worth \$20 billion, in effect almost tripling the size of his investment pool. Looked at in this way, the \$1.64 billion loss represented only 7.5% of his investments. Still, it must be asked what a county treasurer was doing investing in derivatives and leveraging citizens’ assets by a factor of almost three.

### The National Context

Most accounts of the bankruptcy trace its origins to the passage of Proposition 13 in 1978. Certainly, the taxpayer revolt in California and its various permutations that manifested themselves throughout the country in the 1980s prompted many actors in the public arena to seek alternate sources of revenue. More shall be said about this presently. However, to appreciate the more subtle interaction of public administration and financial investment that underpinned

the bankruptcy, it is necessary first to recall the inflationary pressures of the late 1960s and the impact on the U.S. economy of the twin Arab oil embargoes in the 1970s.

Inflation had been building in the United States since the Vietnam War. The years preceding inflation might be viewed as ones of stability and conventional wisdom. The norms of public finance were essentially those inherited from the Depression where safety, liquidity and yield were valued—in that order. Safety meant ensuring that the value of the principal, or public investment, was maintained. In municipal finance, where taxpayer dollars were normally received on a semi-annual basis, this meant depositing funds for immediate use in a trusted local bank and investing the remainder in short-term U.S. Treasury or agency bills, notes or bonds.<sup>13</sup> Liquidity, which involves the conversion of financial instruments into cash, would also be served by this strategy as the market value of U.S. Treasury or agency financial instruments is readily discernable and investors are almost always available to buy them. Since yield was given third priority, the fact that the U.S. government's rate of return on borrowed funds was tied to the discount rate, and thus was invariably lower than the total return of most corporations, was of lesser concern.

Prolonged inflation had serious consequences for both the economy and the conventional wisdom of public finance. First, it put pressure on the U.S. dollar in international currency exchanges. Since the Bretton Woods agreement after WWII the United States had served as banker to the world. U.S. dollars were backed by gold and for many years gold sold at \$35 per ounce. Other countries' currencies might fluctuate, but they would do so principally in relation to the dollar. Domestic inflation, however, threatened this arrangement both because it meant more dollars were in circulation—at home and abroad, thus lowering their value—and because it was increasingly difficult for the United States to maintain sufficient gold reserves and uphold the

<sup>13</sup> Bills, notes and bonds are similar in that they all represent forms of public borrowing. The difference among them involves the length of time between issuance and repayment of principal. Bills are repaid within months; notes within one or more years but not more than ten; bonds within thirty years.

fixed exchange rate. In 1971, after discussions with our allies, President Richard Nixon suspended the Bretton Woods agreement and allowed the dollar to float against other currencies. This didn't solve the inflationary problems, but it did prevent an immediate run on gold reserves. More importantly, it introduced market forces into an area of finance that had previously been almost exclusively the prerogative of the state. According to Paul Volcker:

Even at the start in the early 1970s, there began to be just a germ of a vested private interest in instability in the exchange markets. Up to that time, all the big international commercial banks ran foreign exchange departments essentially as a service to their customers. There was not a lot of money to be made operating within the Bretton Woods margins of less than 1 percent, and with parity changes taking place only at long intervals. But when exchange rates were freed, bank traders soon found out they were very good at making money from the fluctuations.... By the start of the 1980s, these back room service departments had become important bank profit centers--\$50 million, \$100 million, even \$200 million a year, depending on the size of the bank.... (Volcker & Gyohten, 1992, pp. 230-2)

Volcker continues, speaking of conditions in 1985—prior to efforts by the G-5 nations to begin cooperating in setting currency exchange rates:

What seems to have happened as floating rates continued was that the market lost any real sense of what exchange rates were appropriate and sustainable over time; as economists put it, there was no “anchor” to tether the expectations of the traders and to induce them to operate against a trend before it went too far. All of that matters because a nation's exchange rate is the single most important price in its economy; it will influence the entire range of individual prices, imports and exports, and even the level of economic activity (Volcker & Gyohten, 1992, pp. 230-2).

In the early 1970s, the combination of forces—floating the dollar and continued inflation—added to market uncertainty. This uncertainty was particularly acute in commodities trading. Mark J. Powers and Mark G. Castelino, writing about financial futures, attribute the institutionalization of futures trading and the formation of the International Monetary Market in 1972 to these companion forces (1991, p. 11). Prior to this, futures contracts had been exclu-

sively private agreements between business associates; there was no common or public venue for this exchange. As such, the volume of futures trading was quite limited. The formation of a formal market, however, not only made it easier for futures to be sold, it institutionalized a business practice and spawned a new set of financial instruments known as derivatives.

At their most basic, futures contracts enabled commodity traders to reduce the risk of doing business by isolating some of its components. In agriculture, for example, interest rate risk could be partitioned from the traditional uncertainty of climate risk by purchasing financial instruments that anticipated unfavorable interest rate conditions and thus allowed the trader to hedge against them. Just as the call option on IBM stock noted earlier anticipated a certain direction in the value of IBM stock, so too would interest rate futures anticipate a direction in the price of money.

At the same time, the oil embargoes complicated our understanding of safety, among other things. OPEC's oil restrictions tripled the price of crude oil and, concomitantly, the cost of every product and service dependent on it. Moreover, this increase affected the value of other items not directly dependent on oil. When inflation is low, perhaps 3% per annum, Treasury bonds paying 5% will still yield a net "profit" of 2%. In this instance, a one-year Treasury note worth \$100,000 will yield a total of \$105,000 one-year hence, but the same bond is worth the equivalent of only \$101,850 if inflation is running at 3%. However, when inflation reaches double digits, as it did after each embargo, a 5% yield will translate into a net loss of principal. To illustrate, if a municipality received \$100,000 on January 1 and inflation was running at 12%, these funds would be worth only \$88,000 a year later if nothing else were done with them. However, if inflation were at 12% and the funds invested in a one-year Treasury note yielding 5%, the municipality would have the equivalent of only \$92,400 ( $\$100,000 + 5\%$  less 12% inflation) one year later. In other words, when the rate of inflation exceeds the interest rate, the value of principal declines and the fiduciary responsibility to preserve the value of taxpayer funds is undermined.

## The California Context

Double-digit inflation produced two general responses in the seventies. For those with financial assets, it prompted the search for higher yielding investments; for those without, it encouraged borrowing. The economy in California was strong and officials were primarily concerned with losing the value of their assets through inflation. Indeed, it was concern for the safety of principal that led the California Bureau of Audit to recommend to the legislature in 1975 that state and local agencies be allowed to invest in two financial instruments theretofore prohibited—security loans and reverse repurchase agreements. The Auditor General defined a security loan as a “written contract whereby a legal owner...agrees to lend to a ‘borrower’ specific marketable corporate or government securities for an indefinite period” (California. Office of the Auditor General., 1975, p. 2). In this instance, the California agency could “lend” a stockbroker or financial institution a one-year Treasury note worth \$100,000 and receive cash or a promissory note in excess of the current market value of that note. In addition, the agency would continue to receive regular interest payments or dividends although, in the case of corporate stock, it would forfeit any voting privileges that stock ownership had conferred.

Reverse repurchase agreements resembled security loans except that the contract was verbal instead of written and a date of repurchase was specified. Normally, a financial institution would be willing to purchase the note from a public agency because it had another client who wanted to buy the note when none was readily available on the market. The financial institution could make up its loss to the public agency through the fees it charged the other buyer.

In its report, the Auditor General estimated that California state and local agencies held more than \$7.8 billion in government securities and corporate stock at the time, and that in any single day as much as \$175 million worth of assets could be temporarily transferred to financial institutions, providing an additional net income to California agencies of \$3 million per year (ibid., 1975, p. 8). The report also noted that economic conditions, interest rates, and market fluctuations would determine the exact additional net revenue that would be realized, although

there was no mention of the possibility that these conditions could produce a loss. The Auditor General did, however, caution that the California constitution prohibited use of reverse repurchase agreements for the purpose of borrowing money; he did not suggest ways in which the temporary cash received might appropriately be used. Since Citron used reverse repurchase agreements to leverage his investment pool, this question of “appropriate use” of borrowed funds did become germane. The only risks anticipated in the 1975 report, however, were those associated with the soundness of the financial institution temporarily borrowing the public assets.

While state officials responded to inflation by introducing measures to preserve their assets, California citizens responded differently. Proposition 13 was in part a response to the inflationary spiral that swept the country during the seventies. As costs increased, tax rates often followed suit. Impetus for California’s tax proposition originated in Orange County where Howard Jarvis had been a long-time resident. A conservative, opposed in general to government spending, Jarvis had also recently retired and was trying to cope with spiraling costs on a fixed income. He had been politically active in the past, but not particularly effective. His efforts that year to reduce property taxes struck a responsive chord with Californians.

Proposition 13 accomplished several things. First, it stipulated that all properties that had not been sold in the past two years (i.e., 1976-78) would have their assessed value returned to 1975/76 levels. (Properties that had been sold would be valued at their market rate.) Second, it set a ceiling both for property taxes and for increases in the assessment of property values. It set tax rates at 1% of the property’s value and limited annual increases in assessments to 2%. Finally, it required that 2/3 of the state legislature or local voters, whichever was appropriate for the tax measure at issue, would be required to amend tax initiatives in the future. In combination, this meant that local governments would be severely restrained in their efforts to raise revenue. Some have described the proposition as a fiscal straitjacket. Its impact has been broad and deep, more so possibly than even its creators might have imagined.

In general, Proposition 13 forced officials to look to nontraditional sources for revenue. One of these was greater development, and its effect upon patterns of land use has been substantial as local governments sought to balance their budgets by promoting new construction. New construction not only added to the existing property base, it also carried special fees that lay outside the parameters of Proposition 13. This had the unfortunate effect, however, of encouraging cities and counties within the same geographic region to bid against each other for the most profitable development. This “fiscalization of land use,” as the legislature has described it (California Legislature. Assembly. Local Government Committee, 1994) has become the subject of repeated hearings and investigations over the past ten years, prompted by a concern that California is advantaging retail business over other forms of economic growth that might prove a longer term benefit to the state. It has also discouraged regional development efforts and may even have contributed to the fragmentation in local politics which Baldassare identified as one of three critical factors in the Orange County bankruptcy (1998, pp. 46-50).

Fragmentation in the political—as opposed to social—context refers to divided responsibility, as when two or more government units share responsibility for delivering a given service, and divided accountability, as when members of the same office are accountable to different groups. More directly related to the investment pool, this curtailment of property tax revenues also helps to explain the widespread interest in Orange County’s investment strategy. Many of the governmental units investing in the pool were there voluntarily, as has been noted. Some participants even borrowed money to enhance their investment possibilities. That so many groups were counting on him to finance public operations may have increased the pressure on Citron to produce high returns.

#### More Change in the 1980s

The political economy witnessed more change in the 1980s. In August 1979, President Jimmy Carter appointed and the U.S. Senate confirmed Paul Volcker as Chairman of the Board of Governors of the Federal Reserve System (the Fed) and Volcker moved quickly to slay the dragon of inflation. While Congress controls fiscal policy through its taxing and spending

authority, the Fed holds the reins of monetary policy. These include setting the discount rate, or the interest charged to the largest commercial banks, determining the amount of reserves member banks must retain, and selling government securities. Traditionally, the Federal Reserve had relied on the discount rate (which regulates the cost of borrowing money) to manage inflation, but Volcker believed that the “markets had developed a high degree of cynicism about the willingness of...the Federal Reserve...to stand firm” (Volcker & Gyohten, 1992, pp. 165-6). Accordingly, he shifted the emphasis in Federal Reserve policy from the price of money to its supply.

This is neither to suggest that the Fed ignored the discount rate altogether, nor that interest rates were unaffected by this new emphasis on bank reserves. As it turned out, both rates had to be adjusted several times and emergency credit measures finally announced by President Jimmy Carter before consumers adjusted their spending patterns and the market’s habit of price escalation was broken. By February 1980 inflation had reached a rate of 14.9 percent (ibid., 1992, p. 171) although it leveled somewhat thereafter to produce an annual rate of 13.5 percent.<sup>14</sup> By 1983, however, the Fed’s policies had strong-armed inflation down to 3.2 percent, albeit at the expense of the economy. In 1980, civilian unemployment stood at 7.1 percent; two years later it had climbed to 9.6 percent.<sup>15</sup> Meanwhile, the discount rate rose from 13.35 percent in 1980 to 16.39 in 1981 before declining to 9.09 percent in 1983.<sup>16</sup> At the same time, public bonds were becoming more attractive as an investment, for their yields (averaging 8.86 percent in 1983<sup>17</sup>) exceeded inflation then by more than 5.5 percent. The effect on Orange County and other government units in California was to encourage the judicious purchase of federal bonds and thus mitigate, for awhile at least, the impact Proposition 13 had on public finances.

Although well understood, it is helpful to take note of several other changes taking place in the 1980s. First, as has been alluded to already, the decade was witness to the extension of the

<sup>14</sup> U.S. Bureau of the Census. *Statistical Abstract of the United States*, 1995, p. 492

<sup>15</sup> Ibid., p. 399.

<sup>16</sup> Ibid., p. 529.

<sup>17</sup> This was the rate for one-year Treasury bills. (U.S. Statistical Abstract, 1995, p. 529)

tax revolt across the states and to the national government. The Reagan Revolution will be remembered for at least two achievements: the fall of communism and the devolution of federal responsibilities to the states. Conservatives might have been more successful in their desire to streamline and reduce government had Democrats not controlled Congress for most of those years. The net effect, however, of this disjunction in policy priorities was the retention of federal legislation reflecting many liberal priorities and, at the same time, the reduction of taxes restricting the ability of the national government to finance these programs. These opposing objectives were accomplished largely by amassing the largest federal debt in history and devolving many responsibilities to state and local governments. By the end of the decade localities were reeling under the combined pressures of increased responsibilities and fewer dollars to accomplish them.

Yet, the 1980s were also the decade in which the global economy came to the fore. The twin oil crises and the breakdown of the Bretton Woods Agreement had taught Americans that the world was clearly interdependent and that if they wanted to maintain their standard of living, they would need to take into consideration what was happening beyond U.S. borders. As importantly, the rise of Germany and Japan as economic powers—not as large as the United States but clearly strong enough financially to challenge U.S. leadership—meant that Americans could no longer take their economic dominance for granted. However, while the United States might no longer be able to serve as anchor for the world economic system, it was not yet prepared to become merely one player among many. As an organizing political principle, then, the global economy enabled policymakers to justify both the economic downturn in the early 1980s and the more enduring resistance to government involvement in business and other affairs throughout the decade. Downsizing and other business efforts to streamline operations and reduce costs were all part of America's efforts to compete with the Newly Industrializing Countries, found especially in Asia, that were beginning to dominate the automobile, electronics and computer industries in this new global economy. Deregulation and devolution were twin efforts to reduce national government burdens on business, thus arguably enhancing the efficiency of both sectors, and to bring collective decision making closer to the people.

## The Seeds of the Bankruptcy Revisited

Having reviewed the political-economic context, it is now possible to return to the bankruptcy and its more proximate causes. As has been noted, Proposition 13 severely restricted the revenue possibilities of California local governments by establishing a ceiling for property tax assessments and limiting the rate of future increases in both the assessed property value and the rate of taxation. As importantly, however, it also brought state decision-makers into the local tax process for the first time. As the Legislative Analyst's Office reported:

... Proposition 13 transferred the authority to allocate property taxes from local government to the state. To implement this new responsibility, the Legislature developed a property tax allocation system (AB 8...1979) that largely prorates property taxes among local governments within a county in a manner very similar to how property taxes were allocated before Proposition 13. That is, if a county or city got a very small share of countywide property taxes before Proposition 13, it tends to get a very small share today. (California. Legislature. Joint Legislative Budget Committee. Legislative Analyst, 1998)

Counties in California serve dual functions both as administrative arms of the state and service providers for county residents. As such, local officials must strive to please two masters. In their first role, they provide jails, health, welfare, and court services; in the latter, they provide libraries, parks and sheriff protection to citizens not otherwise served by a city (California. Legislature. Assembly. Committee on Local Government, 1990). Unfortunately, the source of funding for these services does not always match the political authority to which officials are responsible because the vast majority of county revenues, regardless of their use, are allocated by the state legislature. Moreover, the state's formula for distributing revenues is complex and varies significantly by county. For example, in a 1998 report the Legislative Analyst noted that as recently as 1996/97 the spread in per capita county support ranged from approximately \$160 to \$1,897, with a statewide average of \$233. That year, Orange County ranked third from the bottom, receiving only about \$175 per person (California. Legislature. Joint Legislative Budget Committee. Legislative Analyst, 1998).

Orange County officials had complained repeatedly about their state allocation, but to little avail. Again, the Legislative Analyst explained that the state controls five types of general-purpose county revenue: property taxes, two types of sales tax, vehicle license fees and, at the time, trial court subventions. Variations in county allocations are attributed to three factors: county taxes in 1977/78 when Proposition 13 was passed, property development—especially retail trade—in the county proper as opposed to development within cities, and residential income. Counties whose populations reside almost entirely within incorporated areas, for example, will have fewer citizens to support than more rural counties. At the same time, counties with high seasonal residential rates may bear service costs that are not recognized by the state whose formula takes account of resident population only. Similarly, viewed from an expenditures perspective, wealthy counties may receive a disproportionate amount of assistance because their costs for welfare services and crime protection are often substantially less than poorer counties. Significantly, the LAO report found the present system “exceedingly complex and difficult for residents and policy-makers to understand” and concluded that “because the revenue variations shown...cannot be explained by differences in current local preferences, program needs, or the rate of local taxation, ...the legislature *should* be concerned by these differences in resources.” (California. Legislature. Joint Legislative Budget Committee. Legislative Analyst, 1998, p. 20). This is worth underscoring: because county tax formulas are linked to voter preferences at the time Proposition 13 was passed, they reflect neither current demographic patterns nor changes in voter preferences since 1978.

While these problems can be linked directly to Proposition 13, they did not become manifest until the 1990s. In the years immediately following the tax initiative, California was able to offset the loss in county revenues through a special bailout. This stopgap measure sufficed as long as the economy remained strong and state tax receipts held up. By 1987, however, strains were already beginning to show. In August, Orange County officials testified before a joint hearing of the Senate and Assembly local government committees that they would be forced to consider as many as 140 staff reductions to meet the budget shortfall that year (California. Leg-

islature. Assembly. Committee on Local Government, 1987). Unable to accommodate the county's request with additional financial support, the Legislature adjusted the county's responsibilities for mandated services.

These traditional tools were not the only managerial devices employed by the state. Legislators supplemented the county bailout and occasional redistribution of responsibilities with a relaxation in regulatory restrictions on county finance. Baldassare identified nine pieces of legislation passed between 1978 and 1994 that liberalized county investment policies (1998, p. 72) and suggested that as many as nineteen bills had been enacted overall that could affect the safety of local government investments. The most important of these for Orange County were AB 346 in 1979, which authorized the use of reverse repurchase agreements, and AB 3576 in 1992 that enabled treasurers to invest as much as twenty percent of their portfolios in a variety of collateralized mortgage instruments. Other legislation either expanded the range of investments counties could hold in their portfolios to include the guaranteed portion of Small Business Administration loans, certain mortgage securities, and medium-term corporate notes or increased the percentage of county funds that could be invested in commercial paper, banker's acceptances, and medium-term corporate notes. As Baldassare observes, these changes occurred gradually over fourteen years and while some of the motivation was clearly in response to Proposition 13 and the Legislature's desire to encourage greater fiscal autonomy, other factors may have had more to do with the growing national interest in deregulation and the availability of new financial instruments.

That the Legislature accompanied this move toward greater autonomy with a relaxation of reporting requirements is more difficult to fathom. However, in 1983 SB 389 was passed. This bill eased the quarterly reporting requirements of local treasurers in place since 1933. Specifically, it allowed the treasurer to prepare reports only when requested by a local agency that was willing to absorb the costs of preparing the report. While this legislation was superceded the following year when San Jose's investment policies brought it close to bankruptcy, this impulse toward more responsible oversight was short-lived. In January 1991, the stricter reporting re-

quirements were allowed to expire and the more relaxed provisions of the 1983 legislation reinstated. In 1993, the Legislature made even the requested treasurer's reports voluntary. By this time, however, the state was in a serious recession, and this appeared simply as one among many efforts to reduce the cost of government.

### The Convergence

In 1990 the state of California faced the first of several multi-billion dollar budget shortfalls. The national economy had been slowing since 1989, but the end of the Cold War, with its concomitant reductions in defense expenditures, hit Californians particularly hard. Between 1990 and 1993 California lost 400,000 jobs and its unemployment rate jumped from 5.8 to 9.4 percent (Baldassare, 1998, p. 77). This not only meant that the state could no longer afford to subsidize counties for their loss of property tax revenues, but that it would be forced to take extraordinary measures to address its own fiscal crisis. Accordingly, the state transferred many service responsibilities to counties. The shift in county revenue sources since Proposition 13 had already been dramatic; property taxes, once accounting for over 30 percent of all revenues, fell to just over 15 percent in sixteen years. In the meantime, "other revenue" sources that had accounted for less than one percent of county revenues rose to a level of almost three percent.

Table 3:1  
California County Revenue Changes 1978-1994<sup>18</sup>  
(in millions)

Revenue Sources	1977/78	% of Total	1990/91	% of Total	1993/94	% of Total	Orange Cnty % Tot. '94
Property taxes	\$2,763	31.9	\$5,313	20.9	\$394	15.4	13.3
Sales & Other taxes	270	3.1	596	2.3	67	2.6	1.1
Other Gen. Purp. Revenue	307	3.5	1,227	4.8	691	2.7	3.9
Service Charges	1,049	12.1	5,157	20.3	312	12.2	15.3
State Aid	1,987	22.9	7,946	31.3	10,774	42.1	39
Federal Aid	2,208	25.5	4,311	17	568	22.2	15.4
Other Revenue	80	0.9	852	3.4	717	2.8	12
Total Revenue	8,664		25,406		25,592		

While the shift from property taxes to state support is clear from these numbers, the change for Orange County was more dramatic. In fiscal 1994, Orange County could count on substantially less support from property taxes and both federal and state support than other

<sup>18</sup> These data are taken from two sources: (Sokolow, 1993) and (Baldassare, 1998); both derived their numbers from annual reports of the State Controller.

California counties. To compensate, it relied heavily on “other revenues,” including interest and other cash management income, to the tune of *twelve percent* of all county sources—almost as much as it received from property taxes (Baldassare, 1998, p. 69). Yet within this group of revenues there were problems. The Federal Reserve discount rate, which influenced bond yields, had reached the lofty heights of 14 percent in 1981 but by 1993-94 hovered around a paltry three percent. Even though inflation was low, averaging 2.6 percent for the year, little room was left for profit. Robert Citron responded to these myriad pressures by diversifying his portfolio, so that it now included a greater variety of federal agency bonds, and then leveraging his assets through the purchase of reverse repurchase agreements.

In April 1994 the Orange County Investment Pool consisted of the following:

Table 3:2  
OCIP Portfolio Statement for April 30, 1994<sup>19</sup>

Asset	Face Value (\$ millions)	% of Total
Treasury Notes	582	3.00
Agency fixed-rate notes	8,480	42.70
Agency floating-rate notes	5,693	28.60
Corporate notes	1,912	9.60
Mortgage-backed securities	127	.64
Certificates of Deposit	1,609	8.10
Mutual Funds	421	2.10
Discount notes	686	3.45
Commercial paper	350	1.76
<b>Total Securities</b>	<b>19,860</b>	
Reverse Repurchase Agreements	-12,529	
Net	<b>7,331</b>	
Leverage	2.71%	

<sup>19</sup> This table appeared in (Jorion, 1995, p. 92).

We have already seen that the California State Auditor recommended the legalization of repurchase agreements in 1975 and that the Legislature authorized them in 1979. It is time, now, to re-examine their use in the Orange County Investment Pool. First, it should be recalled that repurchase agreements involve the “selling” of existing assets or securities with the expressed provision of repurchasing the securities at a specified time in the future. Because of this repurchase provision, these financial instruments more closely resemble collateralized loans, like home equity loans, than they do traditional securities. Repurchase agreements (repos) and reverse repurchase agreements (reverse repos) refer to the same instrument; the difference is one of perspective. Repurchase agreements (financial contracts) are “sold” by securities dealers who give the holders of securities money in exchange for the security and agree to resell that security to the original owner; reverse repos are “bought” by the original holder of securities who agrees to repurchase the security. If the original holder does not have adequate funds to repurchase the security at the time specified in the future, the dealer assumes its ownership.

Jorion (1995, pp. 32-35) explains the process as it applied to Orange County succinctly and the following description relies heavily on his insight. Among the fixed-rate agency notes listed above, OCIP held \$100 million from the Federal National Mortgage Association. The note paid a fixed rate of 5.38% (its coupon) and was worth more than its face value on the market as the discount rate was then at 3 percent. In fact, it sold for \$100.4375 for every \$100 in face value. When Orange County entered into a reverse repurchase agreement with Crédit Suisse First Boston, it did not receive the market value, however, because the difference or margin provided a cushion for the dealer in the event of default. It did receive the face value of \$100 million and continued to collect coupons at the rate of 5.38 percent. At the time of repurchase, though, it would have to pay the dealer interest on the “loan.” Assuming that the agreement stipulated repurchase in thirty days, the net profit for Orange County would be:

$$\text{\$100 million} \times (5.38\% - 3.00\%) \times 30/360 = \text{\$198,333}^{20}$$

If this process were repeated by using the \$100 million “loan” to purchase more FNMA securities at 5.38 percent and then reselling them to Crédit Suisse First Boston, the monthly profit would double. And, if the second \$100 million were again used to purchase FNMA securities, the monthly profit would triple. This is how Citron leveraged OCIP’s assets by 2.71 percent—and one of the principal ways in which he achieved the high rate of return on his investments. It should be noted, however, that the entire calculation makes a basic assumption: that the difference between the coupon (yield on the government bond) and the interest rate will remain positive. If interest rates rise, however, the difference or spread between the two figures will quickly diminish. As important, the market value of the original securities will also decline.

Here, it is important to recall that government bonds (or bills and notes) consist of two elements: the principal, or the amount to be repaid when the bond matures, and the return or yield. A five-year \$100,000 note paying 5% interest would pay \$25,000 over the course of five years. Ignoring inflation, one could then say that the note was worth \$125,000. However, if the owner were to sell (or lend in a repurchase agreement) the note two years after the purchase, the note would not trade for the full amount. First, some of the interest would already have been paid to the original buyer so the note’s value over time, or duration, would need to be recalculated. Also, if interest rates had risen to 6%, the note would be less attractive to potential buyers who could then earn more from other investments and the value of the note would decline accordingly. Fixed income securities provide predictable returns as long as they are not sold. Their value on the market, however, can vary greatly over time depending on changes in interest rates and inflation. Their repayment may be assured by the issuing government authority, making them a good *credit* risk; but highly fluctuating market conditions, on the other hand, can simultaneously make them a poor *market* risk.

In the latter part of 1994, when it was clear the Orange County Investment Pool was in trouble, Citron repeatedly referred to “paper losses” in the pool—losses that he apparently be-

<sup>20</sup> (Jorion, 1995, p. 33)

lieved would not be realized. The reason for his optimism was that he believed in holding securities to maturity. Ostensibly, bonds held to maturity are not susceptible to fluctuations in market conditions. By leveraging his assets, however, through reverse repurchase agreements, Citron exposed the bonds to market fluctuations. This market exposure could have been mitigated with sufficient cash on hand to repurchase the bonds. Indeed, Citron had started the year with over \$1 billion in cash, so he had ample reason to believe that the losses would have remained only on the books. Unfortunately, other forces conspired against him.

In February 1994 the Federal Reserve raised the discount rate from 3 to 3.25 percent. While the economy in California remained stagnant, business activity in other parts of the country was expanding and the Fed grew increasingly concerned that inflation would undermine the solid gains that had been achieved through its conservative monetary policy. By the end of the year, the Federal Reserve had raised the discount rate six times—a highly unusual but not unprecedented action. That said, more wealth (at least in terms of book value) was lost that year than at any time since the Great Depression (Jorion, 1995, p. 20). Robert Citron was not the only one to lose money in 1994.

Still, reverse repurchase agreements were not the only way Citron had exposed the Orange County Investment Pool to interest rate fluctuations. Almost thirty percent of the pool was invested in agency floating-rate notes. These financial instruments are issued by federal agencies and government corporations, rather than directly by the U.S. Treasury. As such, they provide higher yields and carry more risk than Treasury bonds. However, floating-rate notes differ from other agency notes with fixed-rate yields; as such they are called structured notes and greatly resemble derivatives, both in their management of uncertainty and their difficulty to price. Structured notes, like other government securities, have two components: principal and interest; however, their yields vary considerably, often resembling derivatives.

The simplest structured note is one in which the yield varies with interest. In other words, if yields are distributed semi-annually, the discount rate (or whatever measure of interest has been agreed upon) will be calculated before coupons are distributed. These notes have great appeal because they adapt to market conditions, allowing the value of the principal to remain unaffected by the market. A more complicated note is the inverse floater. This structured note provides yields that are *inversely related* to interest rates, usually calculated using the London Interbank Offer Rate or LIBOR. For example, if the six-month yield on a \$100 million note were set at nine percent minus LIBOR and LIBOR were at eight percent the yield would be:

$$\$100 \text{ million} \times (9\% - 8\%) \times 180/360 = \$500,000$$

Inverse floaters often carry caps or floors within their formulas to prevent negative yields if interest rates move too high (i.e. if LIBOR rose to 10 percent in the above example) or fall too low. While the yields on inverse floaters may be attractive, Jorion explains that the notes themselves are almost impossible to price. How much would the above structured note be worth? How would one go about making an estimate? Structured notes produce a yield that is derived from something other than interest in order to protect the issuing agency from economic downturns. They are therefore like derivatives and are exceedingly difficult to price even though they are not formally options or futures contracts. Citicorp purchased a Cray supercomputer in the early 1990s solely for the sole purpose of making such pricing calculations of complex financial instruments. (Jorion, 1995, p. 55).

Where this apparent digression becomes relevant to Orange County is that some of the institutions selling these structured notes are federal agencies like the Federal National Mortgage Association (FNMA or “Fannie Mae”), the Federal Home Loan Bank (FHLB), the Federal Home Loan Mortgage Corporation (“Freddie Mac”), and the Student Loan Marketing Association (Sal-lie Mae). The FHLB ventured into this area in 1986, in the aftermath of the Savings and Loan debacle, to protect federally subsidized mortgages against inflation. In 1994, Orange County held \$100 million of these FHLB structured notes. Jorion explains (p. 51) that the yield was calculated to pay 15.5% minus two times LIBOR. The formula if coupons were paid every six months would be:

$$\$100 \text{ million} \times (15.5\% - (2 \times \text{LIBOR}) \times 180/360)$$

But Jorion traces the rise in LIBOR and explains:

<u>Date</u>	<u>LIBOR</u>	<u>Coupon payment</u>
January 1992	3.625%	8.25%
November 1994	6.50%	2.50%

Because the note is indexed to twice the LIBOR rate, the note is equivalent to 3 conventional fixed-rate notes (FRNs) minus 2 FRNs plus some options. Its exposure is about *three* times that of a conventional fixed-rate note with the same maturity (Jorion, 1995, p. 51).

As with Citron's repurchase agreements, the pool's holdings of inverse floaters provided handsome yields as long as interest rates remained low, but they made it vulnerable to substantial losses when rates rose. Whether he understood the nature of this risk is open to question. However, neither the financial instruments involved nor their distribution in the pool was illegal by California standards.

By October 1994 the pool's cash reserves had declined from over \$1 billion to less than \$450 million. Matthew Raabe, Citron's assistant, alerted the county's chief administrative officer, Ernie Schneider, to the problem. Schneider employed the services of Capital Market Risk Advisers (CMRA) to assess the pool's financial standing. CMRA found that the pool had already lost \$1.5 billion and that there was not sufficient cash on hand to meet the interest payments coming due later in the year. The crisis was precipitated when Cr dit Suisse First Boston (CSFB), holding a \$110 million Federal National Mortgage Association note with the county's promise to repurchase, announced its intent to sell the note on the market if Orange County did not come up with the cash. The county had only \$100 million. Moreover, CSFB announced its intent to call in additional loans of \$1.2 billion. County administrators had explored other options to liquidate their portfolio but sunshine laws governing their meetings and time pressures

forced them into bankruptcy in order to prevent a run on their remaining assets. They filed for Chapter 9 protection from bankruptcy on December 6, 1994.

### The Voters

Virtually absent from the discussion thus far have been the citizens of Orange County. Their re-election of Robert Citron in June 1994 suggests that they supported the results of his investment strategy even if they lacked an appreciation for the fine points that made such a strategy successful. Yet this impression is contradicted by their resounding defeat of a half-cent increase in the sales tax six months after the bankruptcy and just one year after Citron's re-election.

Chapter 9 prevented participants in the investment pool from withdrawing their assets and protected the county from creditors' claims until it was able to stabilize its financial position, but it had no effect on the bonds the county had issued, which were scheduled to come due in the coming months. In order to honor the county's commitment to bond holders and to begin repaying other obligations, the newly appointed county administrator, William Popejoy, recommended a sales tax increase of one-half cent that was limited to ten years' duration. This would have taken the county sales tax from 7.75 to 8.25 percent.<sup>21</sup> Consistent with Proposition 13, the increase required the 2/3 vote of all registered voters in the county. A special election was scheduled for June 27, 1995.

Baldassare (1998, pp. 147-153) points out that as early as April 6, only a third of those polled supported the proposed tax increase, known as Measure R. Despite tax proponents significantly outspending opponents (*ibid.*, p. 157), Measure R was decisively defeated. Admittedly, proponents had little time to change voters' attitudes. Nevertheless, only 39 percent of those voting endorsed the proposition, while 61 percent opposed it. Curiously, this was the converse of what voter support had been in Citron's re-election where he received 61 percent of

<sup>21</sup> Counties in California share sales tax revenues with the state, so Orange County would have received the entire half-cent increase in sales tax revenues had Measure R passed, but it would have returned 6.0416 percent to the state.

the popular vote. As importantly, public support for Measure R was little affected by party affiliation—only 45 percent of Democrats, 41 percent of Independents, and 38 percent of Republicans endorsed the measure. In post-election polls, 70 percent of those who rejected the measure said they did so either because they opposed new taxes under any circumstances or they did not believe they should pay for someone else’s mistakes. To Wall Street and others in the financial community, such action by the voters was tantamount to abrogation of contract. Indeed, the voters’ refusal to secure adequate funding to honor their debt was almost as shocking as the bankruptcy itself, as it undermined the very principle of creditworthiness that had so long been associated with public debt and that continues, at least in theory, to justify lower yields in the public sector. Undergirding this aphorism is the expectation that governments will, if necessary, raise taxes to meet their obligations to bond holders.

Almost as surprising as the vote was the rate of participation in the election. Despite the widespread attention accorded the bankruptcy throughout the nation, most Orange County residents were only moderately concerned with the bankruptcy and did not believe that it affected them. On the day of the election, only 381,000 of 1.1 million registered voters bothered to cast ballots—a mere 34.5 percent of the electorate. The turnout was virtually identical in Citron’s election where 34 percent of the voters had expressed their views (Baldassare, 1998, p. 107). A frequent refrain among citizens was that both the bankruptcy and repaying bondholders was “government’s problem,” not theirs.

During the recovery effort, county and state officials considered ways in which similar circumstances might be avoided in the future. One proposal, which they submitted to voters in March 1996, would have converted the treasurer’s position from an elected office with direct responsibility to the voters to an appointed one. The rationale was that an appointed position might attract better qualified candidates and ensure greater accountability through administrative channels. Orange County voters, however, rejected the proposal—giving the appearance at least that they wanted to retain authority over the treasurer’s dealings. In the same election, they also

turned down a proposal to shift from a general law county to a charter form of government, which would have given citizens more direct control over county government and greater independence from the state. Their rejection of both proposals suggests that voters either did not want that much responsibility for county government or they did not trust local officials to carry out their wishes. Baldassare attributes it to the latter, suggesting that county officials' relations were strained not only with citizens, but also with other local government officials. Cities and towns, with which voters had closer ties, retained their position with the electorate but contributed to political fragmentation.

### The Investigations' Findings

There have been myriad investigations into the causes and consequences of the bankruptcy—both official and unofficial. Among the official findings are the reports of the California Senate Special Committee (California. Legislature. Senate. Special Committee on Local Government Investments, 1995), the State Auditor (California. Bureau of State Audits., 1995), the Securities and Exchange Commission, and the findings of U.S. bankruptcy court, the U.S. District Court, and the State Superior Court. Among the unofficial findings are several scholarly investigations by Mark Baldassare (1998), Phillippe Jorion (1995) and Will, Pontell, and Cheung (1998)—in addition to the responses of the financial community that have, necessarily, been more indirect. Here I will summarize some of the more noteworthy findings.

State courts, of course, investigated the bankruptcy and found both Robert Citron and his assistant, Matthew Raabe, guilty of misappropriating public funds and securities fraud. With Citron, it was not only that he had lied to investors about the safety of the investment pool, but that he had illegally transferred funds across accounts in an attempt to camouflage problems before bankruptcy was declared. In the end, Citron served no time in jail but was fined \$100,000 and allowed to perform community service at the county jail for ten months. He could have received fines as high as \$10 million and a sentence up to fourteen years.<sup>22</sup> In granting Citron this

<sup>22</sup> *The Los Angeles Times*, May 17, 1997, downloaded in machine-readable form the Dow Jones News Service.

modified punishment, the court recognized the treasurer's extensive cooperation with the investigation. Matthew Raabe, the Assistant Treasurer who had initially reported the problem to the Board of Supervisors and served very briefly as county treasurer, was not as fortunate. Raabe had had little role in devising the investment strategy but had full responsibility for explaining it to investors—largely because of Citron's inability to articulate complex financial transactions. Raabe was also found to have been involved in the illegal transfer of interest from the investment pool to county coffers when the county's financial strategy started to unravel. In May 1997 he was convicted on five counts of misappropriating public funds and securities fraud, later sentenced to three years in prison, and ordered to pay a \$10,000 fine. Throughout most of the proceedings, Raabe insisted he was innocent of any wrongdoing. The essence of his defense was that he had been a "loyal subordinate" merely following the orders of his immediate supervisor.<sup>23</sup> Toward the end of his appeal, however, he finally admitted wrongdoing. Raabe's three year sentence was upheld.

State Superior Court proceedings were initiated against several others, but no one was convicted or judged negligent. Noncriminal charges of willful misconduct were dropped against two members of the Board of Supervisors. The budget director, Ronald Rubino, was implicated in the misappropriation charges, but a jury failed to agree on a verdict. Later, Rubino pleaded no contest to one misdemeanor and received one hundred hours of community service. The county brought charges against Merrill Lynch in both federal criminal and civil court. After two and a half years of proceedings and five thousand pages of testimony, Judge Capizzi allowed Merrill Lynch to settle the criminal suit for \$30 million--\$3 million of which went directly to the Orange County District Attorney's Office to cover court costs.<sup>24</sup> The civil suit for \$2 billion was settled out of court in June 1998 with Merrill Lynch agreeing to pay \$417 million in exchange for the county dropping all of its charges. It also returned \$20 million in county funds it had been holding in reserve since the bankruptcy. Other investment firms also settled with county offi-

<sup>23</sup> *Orange County Register*, March 6, 1997, downloaded in machine-readable form the Dow Jones News Service.

<sup>24</sup> *Ibid.*, October 5, 1997.

cials. KPMG Peat Marwick L.L.P. settled for \$75 million in 1998. LeBoeuf, Lamb, Greene & MacRae agreed to restore \$12 million to the county's Community College District, making it the first depositor to have been refunded in full.<sup>25</sup> Finally, CSFB settled with Orange County for \$55 million in May, 1998 after it had been sued by the SEC the previous November for fraud and deceptive securities practices hastening the bankruptcy.

The State Auditor, Kurt R. Sjoberg, focused his attention on Robert Citron and the county's investment strategy (California. Bureau of State Audits., 1995). Sjoberg found that Citron had exposed the county to excessive risk by failing to observe the basic public investment priorities of safety, liquidity and yield. This was due, as we have seen, to the leveraging arrangement accomplished through reverse repurchase agreements and the purchase of interest rate sensitive, structured notes at a time when interest rates were rising. In addition, the Auditor noted that Orange County had managed several pools: a commingled investment pool, a commingled bond investment pool, and several separate investment accounts. As the county identified shortfalls in its principal investment pool, the treasurer's office inappropriately transferred monies from the separate accounts to make up the shortfall. It also transferred funds inappropriately to the county general fund and failed to use competitive bidding prior to its employment of brokerage firms and debt underwriters.

In response to these practices, the State Auditor submitted recommendations to both the county board and the state legislature. Among the recommendations to the California Legislature were the limit of reverse repurchase agreements to 20 percent of a unit's portfolio, prohibiting the use of debt for speculative purposes, requiring the submission of regular financial reports, and establishing a "prudent person" rule for all local investment officers.

Unlike the courts and the State Auditor, however, the California Senate's Special Committee on Local Government Investments, as noted earlier, cast the blame more broadly. Generally speaking, committee members attributed the bankruptcy to a "lethal mixture of corporate

<sup>25</sup> *The Los Angeles Times* June 3, 1998, Orange County edition, downloaded in machine readable form.

and political culture, where the public trust has taken a back seat to corporate profit and political expediency” (California. Legislature. Senate. Special Committee on Local Government Investments, 1995, p. 29). More specifically, they recognized that Citron had sacrificed the conventional standards of safety, liquidity, and yield for higher profits and had done so by imprudently leveraging the pool’s assets while borrowing short and investing long. At the same time, they acknowledged that 35% of the county’s “own source” revenues had derived from interest income and that there had been tremendous pressure on the Treasurer to offset the shortfall in county revenues resulting from the combined forces of Proposition 13 and a slowdown in the California economy. As a result, they charged the Board of Supervisors with inadequately supervising the Treasurer’s activities, allowing investment transactions to be reported on a consent calendar rather than calling for wider discussion, and generally promoting inadequate public disclosure of county investments.

Also included in the list of those warranting opprobrium were Citron’s assistant, Matthew Raabe; the elected County Auditor and Controller, Steven Lewis; the County Administrative Officer, Ernie Schneider; and the County Attorney, Terry Andrus. Raabe, it should be recalled, had first reported the fund’s difficulties and, for a while, was widely praised for his attempt to correct a failed investment strategy. Once charged with felonious activities, however, he assumed the role of innocent assistant merely following the orders of his superior. He was the only person invited by the Special Committee who refused to testify and the Committee itself noted only this refusal. The County Auditor had raised questions in writing about the pool’s investment strategy, which the Special Committee acknowledged, but it criticized Lewis for failing to follow up on these concerns or bring them to the Board of Supervisors’ attention. Similarly, County Administrator Ernie Schneider was acknowledged to have raised concerns about the use of bond revenues, but again he did little to pursue those concerns. Finally, counsel to Orange County, Terry Andrus, was commended for his role after the bankruptcy but his failure to raise sufficient questions prior to December 6, or to alert the Board of Supervisors to suspicious activity, were duly noted by the Committee.

Still, the Special Committee did not limit its criticism to public sector employees. It castigated bond rating agencies for failing to identify any risk in the county's portfolio and charged them with actively contributing to the bankruptcy. The Special Committee also drew attention to both Moody's and Standard and Poor's responses to John Moorlach's 1994 challenge when both agencies accused Moorlach of engaging in political rhetoric. This intrusion into the political debate was at the very least unprofessional. The committee also criticized securities agencies and brokerages for failing to recognize the portfolio's risk. While the advisory group did not go so far as to include financial advisers among those responsible for the bankruptcy, it did blame securities firms for narrowly interpreting issues of authority and legal responsibility and charged them with "insufficient regard for the special nature of public funds" ((California. Legislature. Senate. Special Committee on Local Government Investments, 1995)p. 37).

Finally, the Special Committee on Local Government Investments drew attention to the victims of the bankruptcy—the 186 cities, schools and special districts that had invested in the pool and whose savings were now in jeopardy. The advisory committee did not spare them but, rather, charged them with abrogating their own fiduciary responsibility to their respective publics by failing to raise more questions about the pool and the treasurer's investment strategy. In effect, the Special Committee found fault with everyone who had direct contact with Citron and his investment strategy, suggesting that public officials reaped the benefits of the strategy while being unwilling to delve into its details for fear of what they might discover.

The Securities and Exchange Commission conducted several investigations in the aftermath of the bankruptcy. Among the more salient were investigations into the securities activities of county officials, the influence of brokerage firms in crafting state investment legislation, and the potential conflict of interest of firms such as Merrill Lynch in advising public officials. It censured Citron, Raabe, CAO Steiner, and four members of the Board of Supervisors for misleading and defrauding pool participants, although no formal admission of guilt was required or

fine extracted. The parties did agree not to violate securities law in the future.<sup>26</sup> While the SEC found no direct evidence of misconduct on the part of brokerage firms in the passage of state legislation, it did issue subsequent rulings prohibiting campaign contributions to officials with securities responsibility within two years of any formal transactions. It also worked with investment banks issuing derivatives to develop self-regulating procedures in which the firms will disclose to the SEC information on their trades, risks and customers.<sup>27</sup> Finally, the SEC developed educational packages on derivatives and strategies of risk management for state and local officials and promulgated new rules making brokerage firms legally responsible for taking their public clients' financial goals into consideration when recommending investments. Apprising the U.S. House Commerce Committee of its intent, SEC Chairman Arthur Levitt said "The notion of 'caveat emptor' is unacceptable, and the notion that institutions are 'babes in the woods' also is unacceptable."<sup>28</sup>

It is important to note that none of the people or groups assessing the bankruptcy acknowledged their own complicity. For example, both Matthew Raabe and Merrill Lynch, who were closest to Citron and the investment strategy, maintained their innocence throughout the years of investigation. But there are less obvious parties as well. The Special Advisory Committee, for example, cast its net widely—and had critical words for all who were caught, but failed to mention the legislature's own role in relaxing reporting requirements and encouraging localities to pursue higher yielding investments. Similarly, the State Auditor made no mention of his office's role in authorizing reverse repurchase agreements, although it might have done more to monitor their use or issue protective guidelines. Only Citron admitted openly and freely to any wrongdoing, although he had very little choice.

<sup>26</sup> *The San Diego Union-Tribune* January 26, 1996, machine readable download.

<sup>27</sup> *The Los Angeles Times* March 10, 1995, machine readable download.

<sup>28</sup> *The Los Angeles Times* August 23, 1996, machine readable download.

## Other Responses

The financial community responded to the bankruptcy in less official, but nonetheless important ways. Most significant for public administrators was the increased reliance on bond insurance for managing municipal debt. When county residents rejected William Popejoy's proposed half-cent sales tax increase on June 27, 1995, they forced officials to devise a backup plan. After considerable discussion with the legislature and business community, officials bought time by persuading bondholders to postpone repayment of the bonds for one year and accept additional interest payments in the interim. But this solution was not a precedent that anyone wanted to set.

Prior to the bankruptcy, only municipalities with low bond ratings had been required to take out insurance; afterwards, bond insurance became almost commonplace. It was the financial community's way of protecting investors against citizen abrogation of their debt and it increased the cost of borrowing in two ways. First, it added to the costs of the borrowing community by including insurance as well as interest payments to lenders. Second, it distributed those costs among all purchasers of bond insurance—in other words, other municipalities. While the rates of those who default will be greater than those who honor their debt, all pay to some extent when shirking occurs. It represents a classic collective action problem.

Among the academic investigations into the bankruptcy, I have relied heavily upon the works of Baldassare and Jorion. In his chapter on findings, Baldassare attributed the bankruptcy to three factors, in addition to Citron: political fragmentation, voter distrust, and fiscal austerity. Within political fragmentation, he included not only the geographic loyalty of supervisors within the county and the complicated division of labor between the state and county governments, but fragmentation within county lines as well. This duplication and fragmentation of effort within the county, among city, town and county officials complicated relationships and contributed to voter distrust. Fiscal austerity served to exacerbate already tense relationships. Jorion, on the other hand, concentrated on the role played by complex financial instruments. He concluded that greater political oversight was necessary, but that this oversight would be inadequate without

sufficiently sophisticated financial analyses. I have tried to weave the political and financial accounts together—not with the intention of critiquing either analysis. Rather, I believe that additional insights can be gleaned by integrating political and economic perspectives.

### Concluding Observations

There can be little doubt that Robert Citron was pivotal in the Orange County bankruptcy. He negotiated with representatives of private investment firms and adopted the investment strategies that eventually led the county into bankruptcy. At the same time, Citron had been widely recognized for his investment bravado—from the voters who re-elected him in spite of serious warnings about the portfolio's safety to financial observers who rated the county's bonds or praised Citron directly in print. Moreover, his public approbation was not accompanied by personal financial remuneration—he received no bonuses or financial incentives for his efforts. Although years later Citron admitted to the psychological disorder “cognitive deficit,” which caused memory loss and faulty interpretation of information, it is possible to discern other factors influencing his actions. First, Citron was being entrepreneurial at a time when public officials were widely criticized for their bureaucratic rigidity and antipathy toward private sector initiatives. Orange County citizens were particularly sympathetic with this move toward innovation, especially when it lowered their own taxes.

It was also well known that Robert Citron was a Democrat—indeed, the only Democrat holding elected public office in Orange County at the time. His actions also suggest a strong commitment to the traditional Democratic principle of government as social safety net or counterforce to the economy. This vision of government has been prevalent since at least the Great Depression, with the economic rationale being provided by John Maynard Keynes. Undergirding this arrangement, however, was a view of government as economic stabilizer. The Bretton Woods Agreement, negotiated among the Western allies after WW II, provided the monetary stability that made many of these social programs possible. Viewed in this way, Citron appears to

have adapted his investment policies to entrepreneurial forces, while simultaneously upholding the public sector's traditional commitment to maintain social services and support the poor. In other words, he was able to please libertarian and liberal constituencies simultaneously and insulate the Board of Supervisors from having to consider either raising taxes or reducing services. He was a hero who, overnight, became the goat. In psychological terms, he played the role of "rescuer."

Robert Citron used his investment strategy to offset county revenue losses, attributed first to the passage of Proposition 13 and later to California's recession. With the Board of Supervisors' unwillingness to challenge voters' preferences and entertain either a tax increase or a curtailment of county services, Citron embarked on a strategy that favored high yields. Yet the financial instruments he purchased were not only legal, they had been considered safe at the time they were introduced. As we have seen, reverse repurchase agreements had been proposed by the Auditor General in 1975 to take advantage of the state's financial assets during a period of high inflation when the value of assets, left untouched, could easily erode. Similarly, mortgage securities issued by an agency of the federal government were widely considered at the time to be the next safest instrument to U.S. Treasury securities. Safety, in the case of Treasury bonds, means that Congress promises to use its taxing authority to ensure that the Treasury's debts will be repaid. U.S. government agency bonds carry similar assurances, although the commitment is more implicit, and they normally provide a slightly higher yield to offset this difference.

Yet we have also seen that economic circumstances, such as inflation, can erode the value of principal without the investor taking any action. Safety, then, insofar as it refers to the *value of principal over time*, must be considered a relative concept that depends on other economic factors. With the rise of the global economy, these economic factors have, themselves, become more dependent on international forces. It is not only that local economies are more affected by economic conditions in other parts of the world, but that the financial community has responded to these conditions by designing new financial instruments. Derivatives enable companies to cope with uncertainty. Options and futures make it possible for companies to hedge against changes

in currency exchange rates and other circumstances that might prove unfavorable in the future. Since options do not have to be exercised, they operate like insurance. Structured notes, such as those issued by the FHLB, contain inverse floaters that operate as a hedge against possible inflation. Yet as we have seen, hedges are double sided—they affect the holder differently depending both upon the economy and the holder’s position relative to the hedge.

Corporations have learned to manage domestic political uncertainty through lobbying and generous campaign contributions to both major political parties. The substantial growth in contributions over the past twenty years is, at least in part, testimony to the general acceptance of hedging as a means of managing uncertainty. However, this strategy becomes more problematic when the number of countries is multiplied. Domestic labor conditions, inflation, currency rates, political unrest, etc. are all factors that must be considered by any business seeking to operate internationally. Derivatives help them narrow the range of uncertainty and hedge against certain events.

The U.S. federal government has both responded to changes in the global economy and contributed to them. Deregulation loosened federal oversight of many business activities, allowing American firms to be more competitive in a global market. Financial institutions were especially affected as restrictions on the range of services banks, brokerage houses and financial advisors could offer were lifted. Competition among financial institutions involved not only the services offered but also the geographic areas where the services were provided. Yet increased competition for customers has been accompanied by a more subtle increase in opportunities for conflict of interest. Brokerage houses may, for example, design derivatives in one division and market them to customers in another. Federal regulations require these brokerage businesses to protect themselves against financial losses, but these same regulations have been almost silent when it comes to the matter of conflict of interest. That appears to fall increasingly under the market’s admonition “*caveat emptor.*”

The gold standard had provided an economic anchor, set by the United States and maintained by the Western alliance. When that anchor was dislodged and allowed to drift in the global economy's turbulent waters, national currencies became tradable commodities and the nation-state subordinated to the discipline of the market. Voter preferences can still be debated and seriously considered, but *meanings have changed*. *What was basically stable is now fluid*. *As important for Public Administration, the relationship of the administrator to citizens is now implicated*.

## Chapter 4: Risk Management

The Orange County bankruptcy presents at least three reasons for pursuing the question of risk. First, and most important, an official investigation into the causes of the bankruptcy (California. Bureau of State Audits., 1995) found that Robert Citron's investment strategy was excessively risky. Yet, as we have seen, the county's bonds were given the second highest rating only a few months earlier, suggesting at the very least that risk is easier to detect after the fact than at the time in which it is engaged. This leads to the question: how can risk be identified? What, in other words, constitutes risk? Can it be measured scientifically or does its meaning derive from other sources? Second, the financial instruments responsible for at least a portion of the county's difficulties were structured notes—similar to derivatives—that were issued by an agency of the federal government. These instruments were designed to manage risk, yet they clearly exposed Orange County to greater risk rather than serve as a buffer against it. This suggests another question: How do these financial instruments contribute to the management of risk? At their base, are they merely a sophisticated form of cost, or risk, transfer? Finally, in the aftermath of the bankruptcy, Orange County citizens repudiated the debt the county had incurred at their behest, forcing the county to negotiate a one-year delay in repayment of its bonds. While this substitute commitment was honored, the bond market responded by requiring greater municipal dependence on bond insurance. This prompts two questions: First, what role, if any, did the Citron's re-election play in distributing accountability for the failed strategy, given that the portfolio's relative risk was the central issue in the campaign? And, second, how does bond insurance mitigate risk and what are the implications of increased reliance on it for public administration?

To address these questions, I would like to place the present analysis in the context of a more general discussion of risk—at least its political dimensions. As will become apparent, much of this work is concerned with risk's obverse—that is, how government can more effectively en-

sure public safety in modern, post-industrialized societies. This will be followed by a more focused discussion of risk as it pertains to finance. Here, the historical origins of the concept and its relationship to probability theory will be reviewed. Embedded in this history are fundamental debates about the applicability of statistics to the social world and the position of the individual vis à vis uncertainty. These debates pave the way for considering more recent attempts to understand the multiperspectival dimensions of risk—specifically the application of anthropological tools to the *perception* of risk through culture theory. Here, the work of Mary Douglas proves particularly useful. I will conclude the chapter by returning to the aforementioned questions. While I do not expect to provide definitive answers to these questions, I do hope to present a different perspective than those already available in the Public Administration literature. At the same time, I hope to suggest some tentative next steps that hold promise for moving us along toward better public administrative practice.

### The Public Administration Context

While it is generally held that public sector employees are risk-averse, questions surrounding risk have received increasing attention in the public administration literature over the past twenty-five years. Some of these efforts have been conducted by the National Research Council (NRC), which is the author of at least five reports on risk management and the public sector. In an early effort, (1983) the NRC sought to establish formal links between the scientific research being conducted in specific areas of risk, such as toxic chemicals, and policy making efforts to cope with risk situations. Here, the team emphasized professional spheres of influence and specialized roles, both for the scientists whose work needed to be insulated from politics and for policy makers whose responsibility it was to mediate between scientific findings and the public. Distinguishing between scientific knowledge (risk assessment) and public perceptions and acceptance (risk management) constituted an important advance at the time. A few years later, the NRC embellished upon these ideas in a report that focused on the communication of risk situations between policymakers and the (1989). Improved communication between scientists and the public continues to be the goal of two additional NRC reports conducted in (National Research Council, Board on Environmental Studies and Toxicology,, 1994a, 1994b).

Both reports focus on public participation in the risk assessment phase, especially when information is incomplete, and the development of guidelines—however tentative—for evaluating risks to human health. This focus on public perceptions in the face of inadequate information led the National Research Council to reformulate its original approach in 1996, and consider “risk characterization” as the central process that both builds on scientific analysis and encourages public contribution to that analysis (Stern & Fineberg, 1996). The committee conducting the study understood risk characterization essentially as a decision-driven activity, that is, a process whose goal is to inform policy choices and solve problems. That said, the authors argue that problems should be understood in their broadest sense—including possible social and ethical dimensions—as well as the purely technical aspects. Moreover, the committee thought that risk characterization should be the product of an “analytic-deliberative process” where public participation and scientific assessment are complementary, each phase informing the other in a mutual and recursive fashion, not in a linear sequence. It is this shift from a linear to a recursive, dialogical process that fundamentally altered NRC thinking. The authors stress that risk characterization requires not only “getting the science right,” but “getting the right science” (ibid., 1996, p. 16). In other words, they argue that it serves no purpose for risk assessment to address the concerns of experts if, in the process, it fails to meet the needs of citizens who consume that research or who, in the final analysis, must live with the day-to-day consequences of risks identified by scientists.

When considering the nature of risk, most of the NRC studies emphasize environmental factors and threats to human health and safety. The 1996 report even concentrates on those areas of safety where public distrust is highest, such as radioactive waste, toxic chemicals, and hazardous facilities. They specifically exclude airline and automotive safety, and earthquake engineering, where expert opinion and risk management efforts seem to benefit from widespread public trust. This attention to environmental hazards and workplace safety is typical of much of the literature on risk. Douglas and Wildavsky (1982), for example, identify four kinds of danger (or risk) that are of general concern to policymakers:

- foreign affairs: the risk of foreign attack or encroachment; war; loss of influence, prestige and power;
- crime: internal collapse; failure of law and order; violence versus white collar crime;
- pollution: abuse of technology; fears for the environment; and
- economic failure: loss of prosperity (ibid., 1982, p. 4).

Nevertheless, they choose to emphasize the third category in an important study on risk perception and social policy.

In *Risk and Culture* (ibid., 1982), Mary Douglas and Aaron Wildavsky argue that there is little agreement within society on which of these four kinds of risk is most important. Moreover, they suggest that there is little agreement on the nature or severity of these risks—even among people who might share a rank ordering. In brief, they contend that how people perceive risk varies considerably. At the same time, they suggest that patterns among these perceptions can be discerned. For example, those who see danger from abroad are less likely to be sensitive to environmental dangers. Similarly, those who are concerned about crime are far less likely to care about income inequality. Moreover, experts regard risks differently than laypersons—even when the two groups are concerned about the same area—and experts even disagree among themselves about the nature and severity of given risks.

Still, Douglas and Wildavsky devote most of their analysis to tracing the historical origins of American interest in risk—and the myriad approaches to its prevention—which grew substantially after the mid-1960s. They attribute this change to several factors, including: a decline in trust in American institutions; greater educational opportunities, and hence social awareness of risk; technological advances that generate unintended risks; and a greater propensity for citizens to mobilize political capital in the service of particular causes. This last trend, fueled by successes in the Civil Rights movement, produced interest groups in areas ranging from consumer and environmental protection to workplace safety and hazardous materials. Beneath this diversity of interests, however, they found a common distrust of authority—be it public or private—and a commitment to employ whatever resources could be mustered to assert the rights of

individuals (often victims) against aggressive actions of the powerful. In the language of cultural theory, Douglas and Wildavsky attribute this growing interest in public safety in the face of increased societal risk to what they label “sectarian” movements against both the political bureaucracy and the market. Their use of “sectarian” will be examined later, but they were referring to environmental and other socially active, left-wing groups.

Theodore Lowi (1990) examines the role that individual rights have played in the approach taken by United States courts to myriad social movements. Like Douglas and Wildavsky, Lowi traces the shift in Americans’ interest in risk to the mid-sixties, although he credits the federal courts with incorporating the concept of individual rights into what had previously been a fairly straightforward legal calculation. Throughout the 19<sup>th</sup> century, he explains, the advantages of risk taking were widely recognized, but the pursuit of risk was not unencumbered. Rather, responsibility for balancing the interests of risk takers with those of society was assumed by the states. Lowi identifies seven areas where government intervention was critical for the expansion of capitalism. These include deliberate provisions for a) law and order; b) ownership of private property; c) the fulfillment of private contracts; d) enforcement of industry or production standards; e) licensing of various “privileges,” including professions; f) provision of public goods such as communications, transportation, and defense; and g) provision of social services such as public education and welfare. While some of these roles are now performed by the federal government, most have remained the responsibility of the states. This gave the appearance of a *laissez-faire* environment, but lack of visibility, Lowi contends, should not be confused with absence of authoritative structuring. Moreover, such diverse provisions of social stability reduced the environmental or social risks required of private enterprises and made it easier for them to operate in the market and incur economic risks.

What has changed over time, then, in Lowi’s view, is not so much the legal environment for risk taking as the *allocation of responsibility for risks after failures occur*. Prior to the 1840s, he explains, responsibility for entrepreneurial initiatives lay essentially with the organization or

employer, whose role was one of *in loco parentis* or guardian of its employees. This approach took a dramatic turn in the 1840s when courts began to allocate responsibility *in proportion* to the degree to which each party contributed to an accident. Accountability, in other words, was joined to responsibility and apportioned among the participants. Liability for accidents required the determination of fault before it could be assessed proportionately. This enabled entrepreneurs and other risk takers to share the blame with, and on occasion even transfer blame completely to, the victims of their risk taking. At the same time, the courts served as mediators and balancers of this blame.

This system of apportioning blame proved enduring, for it was not until the late 1960s that things again changed. Two divergent trends emerged. First, Lowi suggests, was a shift within the social sciences to treat individuals less as products of their own making and more as interdependent beings, both responsive to social forces and contributors to them. Since the courts had assumed a greater role in the balancing of negligence, this philosophical shift toward interdependence meant that the cause of accidents and blame became more difficult to identify and clearly apportion. At the same time, the victims of risk taking remained unmistakable. Courts responded by compensating the victims with money. Lowi attributes this propensity to compensate victims financially to the expansion of the welfare state, where society at large took on the responsibility of insurer. Whether insurance was public or private, however, the goals are the same—namely, to identify as many contributors to insurance as possible so that the per unit costs will be minimized.

This trend toward socializing individual culpability and compensating victims was coupled with a growing propensity within Congress to enact goal-oriented legislation, rather than laws that specified inappropriate conduct in particular situations. With environmental legislation, for example, Congress set the goal of improved air quality standards but left the details to the Administration. This legislative move toward abstraction meant that executive agencies were required to take on the task of translating program goals, such as clean air or safe work places, into specific actions. Doing so required public agencies not only to conduct more research, but to

issue more, and increasingly complex, regulations. This approach not only fueled the explosion of agency rulemaking in the 1970s, it reinforced the view that citizens were *entitled* to the outcomes stipulated in legislation *as a matter of individual right*. This combination—the socialization of costs and the expansion of individual rights—altered our understanding of risk and paved the way for a backlash against public agencies. The outcome, according to Lowi, has been a culture that values *both* greater safety at the social level *and* expanded risk taking by individuals.

A third perspective is provided by the German sociologist, Ulrich Beck, whose base of reference is clearly Europe but whose interest lies in modern, industrialized societies and the growing importance of risk in all of them. Beck has coined the term “risk society” to describe both the sociological conditions in which modern states and people find themselves as well as the epistemological orientation required to understand these changes. His thesis (1992, 1998; Franklin, 1998) is that we have reached a new stage of industrialization where advances in science and technology, intended initially to reduce risks and hazards, have themselves begun to create new forms of risk. Beck calls this paradoxical turning of science and technology onto itself “reflexive modernization” and contends that it has altered both the nature of risk and the role of the individual in managing it. In terms of the nature of risk, Beck argues that we previously understood hazard to be function of nature; that is, risks included natural phenomena like storms and earthquakes, which humans attempted to control through probability and forecasting, or at least manage their catastrophic results with insurance. In this second phase of industrialization, however, we face hazards such as BSE, commonly known as mad cow disease, AIDS, and global warming. Each is “beyond nature” in that it is to some extent an outgrowth of scientific progress. At the same time, these hazards are “beyond tradition” in that they present us with a form of risk that cannot be managed by simple probability calculations. In the past, humans have attributed most risk to fate. Today, we know enough about them to implicate ourselves in these risks, but not enough to fully control them. Exposure is both uncertain and indeterminate. Indeed, it is as if we are all participants in a grand experimental laboratory but no one is in charge.

Beck compares the earlier industrial era with today's version by describing the former as concerned with social classes and the distribution of goods. Today, by contrast, our concern is with "individualization," and we are engaged in the distribution of "bads." By individualization, Beck means that each of us is no longer safeguarded by institutions;<sup>29</sup> we no longer trust them to give us accurate information, and we are forced to take action in the face of institutional uncertainty and misinformation. When Beck uses the word "bads," he is referring to pollution and other unwanted side effects of scientific and technological progress, whether from medical procedures or power plants. It is not only that we must now make decisions about who will live near these hazardous facilities or scientific waste, but that today's decisions may also affect future generations or people in remote locations who may be exposed to these hazards. In the second industrial era, then, many of the risks we face are bound by neither space nor time.

Beck is careful throughout his writing to avoid association with either the term postmodernism or the postmodern philosophical tradition. It is the principal reason he avoids the term "post-industrial" and refers to a second phase of industrialization, or reflexive modernization. Importantly, Beck understands postmodernism as essentially negative and anti-political, even though he sees contingency, irony, uncertainty, and lack of trust as basic features of our present condition. Still, he remains decidedly optimistic about the future. The reason is linked to his sense of possibility for human beings to respond to these conditions in a new and hopeful way. Specifically, he links this to his understanding of individualization.

The principal source of human disassociation from institutions is the bad faith that exists between individuals and them. This pertains whether the institution is public or private. Private institutions, according to Beck, have the greatest autonomy in today's environment, and initiate most activities. But they are also the creators of much of the risk with which we are faced. Public institutions, by contrast, attempt to respond to situations involving risk, but can no longer

<sup>29</sup> Ulrich Beck uses the term "institution" in a generic sense to describe both public and private organizations. There is no indication in the works cited that Beck distinguishes among organizations by size or that he gives much consideration to non-profit organizations as distinguished from public or private.

perform the welfare function or provide the safety net against the old forms of hazard. Instead, he sees public institutions vacillating between scare-mongering and cover-ups, neither of which is effective at reducing risk or citizens' propensity to cast blame. Indeed, such vacillation serves mainly to decrease trust. One example of the quandary we are facing is the worsening of our physical environment at the same time that we promulgate more environmental regulations than at any time in our history.

In the face of new and more problematic risks, with institutions that either generate many of these risks as part of their standard operating procedures or operate with less capacity than previously to manage these risks, the individual is forced to come to terms with the problem of providing for his or her own safety and protection. It is in these complex circumstances that Beck takes hope in the possibility for new forms of relationship. Knowledge, he says, can no longer provide the essential glue that holds societies together; rather, it is human relationship in the face of uncertainty and risk that must provide the connection. A contributor to one of the books in which Beck expresses these views, Anna Coote (1998), argues that we have modeled the relationship between government and citizens on the nuclear family, with government serving the role of parent and citizens that of children. Reflexive modernization can no longer support this type of relationship, she contends. Rather, it requires that both citizens and state, collective actor and its members deal with each other as adults—honestly sharing uncertainties and fears.

Ulrich Beck is one of the few social commentators writing about risk who includes financial considerations in his discussion. Importantly, he includes global capital markets among the new sources of risk in the second phase of modernization. Yet to public administrators, risk has been anathema to the fiduciary role required of the public agent. Conventional wisdom, after all, holds that financial return should follow safety and liquidity in public investments. Implicit in this aphorism is the notion that the higher the yield, the riskier the investment, for paying higher returns is the way the market compensates innovation. Of course, there is always the possibility that the investment will fail, so it might also be argued that the higher the return, the greater the

likelihood of failure. This suggests that any time there is a return on investment, there is the possibility of failure. If this is indeed the case, when does this probability become excessive? Yet have we not also seen that failure to invest, especially when inflation is high, can reduce the value of principal and therefore jeopardize the safety of public funds? In other words, in some situations is it not also risky to do nothing with one's assets? These questions lead us to ask what the words "safety" and "risk" mean, especially in the context of public finance. To address them, I shall review the evolution of the concept of risk and our attitudes toward it.

### Historical Origins

The distinction between risk and uncertainty is a relatively recent contribution to Western thought. In his engaging history of risk, *Against the Gods: The Remarkable Story of Risk* (Bernstein, 1996), Peter Bernstein explains that the concepts of probability and uncertainty were closely intertwined in Greek thought, and neither concept involved measurement. The Greek word εἰκος (eikos) meant probability in the sense that something was "to be expected with some degree of certainty" (ibid., p. 16), but it was not entirely certain because it could not be proven through logic and axioms. As Socrates is reputed to have said, that which is *probable* is mere "likeness to truth" and should not be taken for truth. Preventing the Greeks from developing a more modern understanding of probability was not, in Bernstein's view, a lack of mathematical sophistication. Rather, it was the combination of an inhospitable Roman numbering system, lacking a zero among other things, and a personal orientation to the future that relied upon Oracles and external forces rather than individual talents or knowledge.

With the advent of Christianity, emphasis shifted from external gods interacting with people in the present to a single deity whose judgment would influence life in the hereafter. This change was accompanied by an allocation of responsibility for one's salvation to the individual, with the Church serving as intermediary, interpreter, and guide. The Crusades brought Europeans into contact with two critical innovations: the Arabic-Hindu numbering system and dice. The numbering system not only contained the zero, but its representation in columns also facilitated

the development of new methods of calculation and accounting devices that eventually transformed commerce. Dice, in the meantime, proved more amenable to quantification than other games of chance then more familiar to Europeans. (Evidence of this influence is suggested by the etymology of the word “hazard,” which is derived from the Arabic word for dice, *al zahr*. Bernstein argues that neither innovation would have its full impact upon Western thought, however, until the printing press expanded communication and the Reformation further altered people’s relationship with the divine.

With the Protestant Reformation, the Church hierarchy was challenged, and individual believers were accorded greater responsibility for their destiny. Faith and good works remained essential for salvation, but many believers assumed a more active role in determining what faith and good works meant. Together with the Enlightenment’s shift in focus from otherworldly affairs to this world, the ground was laid for change. Bernstein observes “Who determines our future: the fates, the gods, or ourselves? The idea of risk management emerges only when people believe that they are to some degree free agents” (ibid., 1996, p. 35).

Advances in mathematics were also under way. As early as 1545, Girolamo Cardano (1500-1571) began to associate dice and probability. At that time, the term probability did not have a quantitative connotation. Rather, its meaning was reminiscent of the Greek in that it carried the connotation “worthy of approbation” (ibid., 1996, p. 48) where approval was linked epistemologically to proof. Thus, something was said to be *improbable* when the logic of its presentation did not meet with general approval. It was Cardano who linked the idea of probability specifically to chance. A gambling aficionado, he had encountered a problem posed by Paccioli years earlier. The puzzle involved two players of *balla* who had agreed that the first to win six games would win the match. The problem posed by Paccioli was how to divide the stakes if one player decided to stop early, when player A had won five games and player B only three. Cardano failed to solve the puzzle, but he did make important progress towards its solution. Using algebra to calculate the possible combinations of numbers on a pair of dice, he not

only calculated the number of possible combinations ( $6^2$  or 36) but he correctly expressed the problem in fractions. If there was a one-in-six chance of rolling the correct number on the first throw, there would be a one-in-thirty-six chance of rolling it two times in succession ( $1/6 \times 1/6$ ). Calculating odds in this fashion represented a major breakthrough in managing risk.

Pascal encountered the same problem in the 1650s and discovered that factors of two arranged themselves in a triangular pattern, thus facilitating the calculation of combinations in games of chance.<sup>30</sup> Moreover, this symmetry suggested to him that beneath the apparent chaos of uncertainty lay divine order. As important, perhaps, was Pascal's integration of mathematics into Christian morality. He contended, for example, that the player leaving the game early would have the right to the gains anticipated *in proportion to* the probability that she had of winning the unfinished games. Proportionality was thus equated with morality. (It should be no surprise, then, that the American legal system embraced a similar notion of proportionality in the 19<sup>th</sup> century, as Theodore Lowi has pointed out.) Later, Pascal extended his understanding of probability to the very existence of God. He reasoned that God's existence was uncertain, but given the enormity of the stakes involved, it was worth the wager that God did exist. In doing so, Pascal introduced the notion of *consequences* into the calculation of risk.

This idea of consequence was later formalized by Daniel Bernoulli, who explained its importance in terms of the following paradox: He asked how much should someone pay to get into a game where the amount paid to the winner doubled after each throw. As overall earnings increased, he reasoned, the *value* of each additional win would decline because each increment rep-

<sup>30</sup> Pascal's triangle appears in most basic algebra texts and provides an elegant key to functions for the number two. For example, two teams playing six games in a competition will have  $2^6$  or 64 possible ways of winning. Pascal's triangle shows this progression:

$$\begin{array}{c} 1 \\ 1 \ 1 \\ 1 \ 2 \ 1 \\ 1 \ 3 \ 3 \ 1 \\ 1 \ 4 \ 6 \ 4 \ 1 \end{array}$$

The internal numbers (between the border one's) represent the sum of the two numbers above. Moreover, each line, after the first, gives the answer to the next power of two. For example,  $2^1$  (second line) is 2;  $2^2$  (third line) is four;  $2^3$  (fourth line) is eight;  $2^4$  (fifth line) is sixteen, etc.

resented a smaller portion of one's total wealth. In other words, the *consequences* or *utility* of continuing in the game would decline over time as one's winnings increased. In fact, Bernoulli theorized, the utility resulting from a small but constant increase in wealth was *inversely proportional* to the wealth already owned—the greater the wealth, the less valuable a specified increment. At the same time, he reasoned that a loss would result in *disutility*—but losses worked differently. According to Bernstein, Bernoulli believed people disliked losses more than they liked gains, so there was an asymmetry between the two outcomes. In a fair game of chance, then, the *disutility* resulting from loss would always exceed the utility realized from winning and it is for this reason that, all things being equal, people are *risk-averse*. While these concepts are commonplace today, Bernoulli's contribution was significant for he not only developed this dual aspect of utility, he was the first to quantify the more subjective components (i.e., consequences) of risk.

At the same time that advances were being made in combinatorics, the nation-state was taking advantage of advances being made in statistics. Statistical sampling had been used as early as 1279 by Edward I of England to test the reliability of gold and silver coins, but it was demographic sampling in the 17<sup>th</sup> and 18<sup>th</sup> centuries that proved most beneficial to emerging nation-states. Both Graunt in England and Halley in Germany examined birth and death records in order to estimate population size and density as well as to calculate their respective rates of change. These data proved invaluable, not only for public health and taxation purposes, but also for the expansion of trade. The British government, for example, relied upon these data when issuing annuities used to finance wars and trading expeditions. At the same time, an embryonic insurance industry tapped these data in order to underwrite the operations of merchant ships. Hacking (1990, p. 19) points out that demographic data were sufficiently valuable by 1700 that proposals to centralize data collection in government statistics offices were being actively considered in both England and Prussia. The Prussian proposal was authored by Leibniz, whose population estimates later proved instrumental in negotiations to unify Brandenburg and Prussia. With population counts came categorization. Leibniz, for example, had proposed collecting demo-

graphic data in 57 separate categories. Hacking suggests that this process had the eventual effect of altering even the way people saw themselves. This transformation took time, however, for initially the only data publicly available were those collected by private individuals while state-sponsored statistics were collected for the exclusive use of the monarch.

### Applying Lessons to the Social Domain

Only gradually were theoretical advances in probability applied to real life. Peter Bernstein credits Jacob Bernoulli (1654-1705), Daniel's uncle, with extending the lessons of probability in games of chance to real world events and, in the process, of taking the conceptual leap from calculating odds in a game of dice to conjecture about the future (1996, pp. 120-4). Hacking (1990) credits Poisson (1781-1840) with this achievement. In either event, both mathematicians relied on large number counts to make the connection.

Bernoulli knew that the probability of a six being rolled with a die is one-in-six or 16.6%. He discovered that actual experience would more closely approximate this mathematical calculation as the number of actual rolls of the die increased. According to *the law of large numbers*, the divergence between the ratio experienced and the one predicted mathematically will decline as the number of rolls increases. In ten or twenty rolls, for example, the six may appear more than half of the time or it may not appear at all. The *variance* with only a few rolls is considerable. However, as the number of rolls increases, the ratio of sixes to other numbers on the die will more closely approximate the calculated ratio (1:6). To express this in mathematical terms, the variance or error between *a posteriori* experience and *a priori* calculation will decline as the number of throws increases. This is not to suggest that a six is more likely to be rolled if it has not been thrown for a while; each time the die is rolled, there is still only a one-in-six chance of it appearing—as long as the die is fair. This law was formally proven by Poisson in 1837 (Hacking, 1990, p. 95), although Bernoulli clearly experimented with the idea earlier.

To make this leap from theory to practice, however, it was important that the real world resemble the game of chance as much as possible. Bernoulli suggested this could be accomplished *if and only if*:

- one assumed *full information* about the events in question (they had to resemble the throw of a die where all of the sides were known),
- one ensured the *independence* of each trial (rolling heads one time does not influence the next roll), and
- quantitative valuation was *relevant* to the problem at hand (the calculation of odds had to make sense logically in a given context).<sup>31</sup>

Bernstein speculates that Bernoulli, having gotten this far in the application of probability to experience, despaired of ever achieving the conditions he intuitively understood were required for the statistics to pertain.

Hacking recognizes Bernoulli's contribution, but accords greater weight to Poisson, not only because the latter formally articulated the law of large numbers, but because he appreciated the dual sense in which probability was beginning to be used. The context in which Poisson developed his law of large numbers was a treatise on juries and the number of jurors required to convict someone accused of a crime. He asked whether it was fair for only a portion of the jurors to render a judgment of conviction or whether unanimity was required.<sup>32</sup> Poisson's treatise thus presented a moral argument and in this respect he was using the term *probability* in its earlier sense of approbation. At the same time, Poisson drew on the achievements of Bernoulli and others, and also used probability in its more recent guise—as a calculation or attribute of chance. Importantly, Poisson cautioned against using a given ratio of jurors to prove someone's innocence. Anticipating Popper by one hundred years, Poisson argued that the decision for jurors was not guilt or innocence but rather guilty or not guilty.

<sup>31</sup> Bernstein, op. cit., p. 121.

<sup>32</sup> Hacking (Hacking, 1990, p. 95) cites Gleaned and Solomon who returned to Poisson's argument after the U.S. Supreme Court declared it constitutional for juries to decide cases by majority in 1967.

Additional advances in statistics came relatively quickly. A third Bernoulli, Nicholas, examined the rolls of a die from a different perspective. He began by assuming a specific number of observations and then calculated the probability that a given throw would fall within a set range. This inverted the description of evidence from probable error to a positive range of probability, and paved the way for asking questions such as what chances a given individual had of living to age 50. A few years later, de Moivre, experimenting with draws of black and white pebbles from a jar, calculated the average number of black pebbles obtained repeatedly after a set number of draws. Assuming a jar with black and white pebbles in a 3:2 ratio, he calculated how close to this ratio each draw would produce, thus estimating the dispersion around the mean—or standard deviation. Importantly, de Moivre continued to attribute these patterns in nature to God and regarded mathematics as merely a tool to help humans gain insight into the workings of the divine. Hacking (1990, p. 13) notes that this interpretation is consistent not only with Hume but with Newton's claim that the effects of gravity may be observed but that gravity itself was unknowable. In other words, 19<sup>th</sup> century mathematicians were content to gain insight into nature, but believed that human understanding of God's creation would always be limited. Throughout this period of scientific advance the idea of *pure* chance was still widely regarded as irrational; some even considered it atheistic. Uncertainty was attributed to inadequate human understanding, rather than as characteristic of the natural or empirical world (ibid., 1990, p. 103).

By 1810 Gauss was making estimates of the earth's curvature, and calculating the average of several averages. In the process, he discovered that dispersion around the mean could be reduced; this was the basic insight behind the central limit theorem, formally articulated by Laplace the previous year. Experience in the field was reinforcing theoretical insights, paving the way for new or improved applications. For example, life insurance premiums, merchant ship underwriting, and government annuities could all be calculated with greater precision, and with less risk to insurers who based their premiums on distribution curves calculated with the revised formulae.

## From Probability to Correlation

As more applications were identified, scientists delved into the area of correlation. Francis Galton's (1822-1911) fascination with measurement was typical of many in the 19<sup>th</sup> century, although his selection of objects for measurement was broader than most. Galton examined not only social phenomena such as morbidity and mortality, but characteristics of human physiognomy as well; height, weight, length of arms and legs—even size of brains—were all part of his repertoire. While he is credited with originating the idea of the “average man,” his more important contribution for purposes of understanding risk lay in his study of eugenics. Galton's interest in human physiognomy was part of a deeper concern with talent and why qualities held in high regard were not more often passed on by heredity. Studying cross-generational patterns of personal attributes, Galton concluded that moderating influences tended to temper more eminent qualities in genetic transfer. In other words, he reasoned that regression to the mean was a natural phenomenon and extraordinary talent would always be diluted by mediocrity.

Yet, as the variance between testing and the calculated mean was reduced, and as more physical phenomena and more social factors were counted, the importance of the mean shifted. In some contexts, it was associated with normality, with deviations from the mean taking on the negative connotation of *deviancy*. This was particularly true in the area of medicine. Broussais (Hacking, 1990, pp. 81-5) was one of the more ardent spokespersons for the physiological theory of disease that linked illness with a particular organ. Treatment, then, consisted of various operations on the tissue of the diseased organ, with bloodletting being among the preferred. To test the various treatments, however, Broussais applied statistics to the remedies. In studying diseased organs, he also distinguished between pathological organs and other organs; these “other” organs he called “normal” (ibid., 1990, p. 164). Normal, in this sense, then, referred to the norm—what was typical or usual.

## Backlash

Despite the appearance of straightforward progress, statistical advances were not uniformly well received, especially as they related to social questions. One concern involved the implications for free will, if social laws in fact governed human behavior. For example, if it could be demonstrated that there would be “x” number of divorces, thefts, or suicides in a given year, what responsibility did the individual have for his or her actions? If deeper, social forces were operating upon us, weren’t people merely instruments of these forces? The most straightforward response was that provided by Quetelet, who essentially distinguished between macro forces and micro causality. He argued that individuals still acted freely, with their decisions being motivated by specific, discrete causes. These causes, however, cancelled each other out, enabling the larger regularities to be observed (Hacking, 1990, p. 123).

Others were not as sanguine. Hacking explains that the answer to this question of individual will—indeed, the very posing of the question itself—revealed significant differences in culture across Europe (1990, pp. 35-40). In England and France, where individualistic values tended to be given priority, laws found in nature were accorded the status of facts, and distinguished most decidedly from values. By extension, social laws were seen as “distillations of individual behavior” (ibid., 1990, p. 37), rather than as group abstractions. Quetelet and Farr are perhaps the best representatives of this perspective. In Germany and countries to the east, on the other hand, the collective tended to be accorded priority. As a result, laws in these countries were understood as social products, for they described the culture at large. Social laws were likened to customs—they changed over time and, as such, could not be represented statistically.

Where individualistic values were dominant, people were more willing to interpret statistical laws as fact because this was consistent with their belief that the group is constituted by individuals. Statistics, then, provided a rational way of aggregating individuals. Where the collective was favored, statistical laws made little sense—for they did not represent a social product. Statistical patterns might be described as regularities, but they could not be raised to the status of laws—or even rules—since laws required specific causal forces and these were not germane to

culture. The question of free will was therefore of far greater concern in liberal cultures than in more collectivist ones.

These differing attitudes toward individual responsibility also influenced their countries' respective social policies. Hacking suggests that in the West, use of statistics supported philanthropic and utilitarian priorities (*ibid.*, 1990, p. 118). For example, statistics on health, crime and other social conditions were collected in part so that changes might be made in the conditions associated with these social maladies. Implicit in this approach was a belief in the ability of social groups to change their environment as well as in the ability of those affected to change their behavior; in other words, implicit in the utilitarian approach was a belief in the perfectibility of humankind. By contrast, social reform in collectivist cultures entailed creating institutions of self-help, such as savings banks, mortgage insurance, workmen's compensation, and old-age pensions. Ernst Engel, who headed the Prussian statistics bureau from 1860 to 1882 and invented both the savings bank and mortgage insurance, is often associated with this approach (*ibid.*, 1990, pp. 128-9). Engel's response to the question of free will was direct: Statistical regularities were distinct from laws in that they revealed patterns of social behavior, not causal forces. The question of individual free will was not at issue because statistical laws had not been demonstrated. Engel's promotion of social welfare was consistent with the collectivist idea that the group constitutes individuals, not the other way around. Industrialization had produced considerable squalor, and he believed it was incumbent upon the nation-state to establish institutions to help resolve the resultant tensions between capital and labor. According to this logic, the state, existing prior to the individual, had an interest in promoting such institutions.

Anti-statistical sentiment was not restricted to the East. Hacking identifies five distinct forms of reaction emerging after 1848: political, philosophical, medical, literary, and nihilistic (1990, pp. 142-9). With the expansion of state data collection efforts, statistics assumed an increasingly important role in political debate. At one point, Disraeli is alleged to have denounced statistics as one of three types of lies, and this sentiment is suggestive of the first form of back-

lash. Philosophical opposition was expressed by Auguste Comte. Hacking describes this as ironic, for it was Comte who coined the terms “positivism” and “sociology,” which have come to be associated by many with the statistics movement. Yet Comte, he explains, opposed the social uses to which statistics was being put. While Comte was responsible for transferring the ideas of “normal” and “pathological” from physiology to individual health, he did not intend either word to connote statistical deviancy; rather, they were intended as mere descriptors, representing norms, on the one hand, and disease, on the other. The physiologists Claude Bernard and Pierre LePlay were also opposed to the extension of statistics to the social realm. Their goal was to use statistics to identify causes of disease; extending the use of statistics to the social world impeded the tool’s development for more profitable applications such as medicine or public health. When studying human beings, they recommended the use of *representative* individuals or families who could be studied in their context and not as numerical abstractions.

The fourth reaction Hacking identifies was that of Dostoyevsky. Hacking likens the Russian author’s distaste for statistics to that of Dickens. Both, he suggests, regarded utilitarians as so concerned with humanity that they neglected actual individuals. Dostoyevsky, however, was the more radical, for he went so far as to advocate caprice as a form of resistance against numerical controls. Nietzsche, the fifth and final example, provides the most extreme expression of this sentiment—often associated with Romanticism. Interest in the miraculous, destiny, and creation itself gave rise to an alternate perspective of the world that accepted chance as a basic condition of life. Whereas previously scholars had associated the divine with order and predictability, Nietzsche found evidence of divine intervention in the improbable.

Hacking includes Charles Peirce among those who believed chance was ubiquitous. A straightforward example of this pervasiveness was life itself: the statistical odds that any individual would come into being were so miniscule that *necessity* or destiny must be at play in any individual’s life. This necessity, then, suggested there might be a purpose to one’s existence, and this purpose could be discerned by exploring the apparent (but only apparent) order in the world and how one fit into it. Necessity and chance were thus two sides of the same coin. At issue

was not only one's view of the external world, and whether or not it was ordered, but also one's view of the self acting in the world. Hacking suggests that statisticians even acknowledged the pervasiveness of chance—albeit inadvertently—with their insistence upon random drawings in experiments intended to simulate real life.

While this backlash did little to arrest the development of statistics, it suggests that what was initially a mathematical puzzle evolved, over time, into a cultural phenomenon—linked geographically to nation-states—and mutated as ideas crossed territorial boundaries. Whether resistance spurred advocates of statistics to examine causality more carefully is difficult to say. It was only a matter of time, however, before statistical innovations found their way into finance.

### Probability and the Market

Application of statistics to economics in general and the stock market in particular did not occur until the latter part of the 19<sup>th</sup> century. A critical link between human behavior and the market had first been provided by Pascal's subjective concept of consequence or utility, as we have seen. Incorporating this idea into economics was facilitated by Jeremy Bentham (1748-1832), who understood pleasure and pain to be the dominant forces motivating human action. He described utility as:

that property in any object, whereby it tends to produce benefit, advantage, pleasure, good or happiness...when the tendency it has to augment the happiness of a community is greater than any it has to diminish it (in Bernstein, 1996, p. 189)

Utility, then, became the connection between human desire for pleasure (or avoidance of pain) and the objects people sought to satisfy that pleasure (or reduce pain). Bentham's insight was adopted by economists to explain supply and demand. They reasoned that demand for an object, like additional gains from a game of dice, would decline as overall supply (or individual wealth) increased. William Stanley Jevons even developed formal measures of utility, relying upon probability theory and the inverse relation of value to the amount already owned.

Other applications soon followed. When evaluating stocks, regression to the mean can encourage risk taking; indeed, this is the principle underlying the maxim “buy low; sell high.” If the price of a given stock will, over time, regress to the mean, then careful examination of the stock’s price should reveal a pattern, making it possible to sell the stock when it is below this average (preferably toward the nadir) and sell it when above (preferably toward the zenith). Analysts who identify stocks as being undervalued are making essentially this calculation. Of course, stock prices are not identical to phenomena in nature—they are the direct outcome of decisions by human beings. In fact, people respond to market data as they do to statistical norms—information will both *describe and influence* human behavior, and it is this dynamic that prevents probability theory from being more useful in human affairs. In addition, average stock prices will vary over time—the mean is not constant. Moreover, average prices may be affected in the short term by shocks and other unanticipated events. Finally, the mean can only be known for certain after the fact. In other words, it can be calculated over a period of time, but because it is always in flux, the mean is never completely certain. Stock market performance since 1994 provides ample evidence of this as the Dow Jones industrial average has continued to rise. But it took some time before this general dynamic was fully appreciated. Advances in probability theory and statistics undoubtedly contributed to this appreciation.

For many years, there was so much faith in probability theory and efforts to quantify social and economic phenomena that uncertainty, both as an intellectual concept and everyday possibility, was widely held to be a function of limited human knowledge, rather than discontinuous events in the real world. Nature, after all, observed patterns, and observable events were deemed to have identifiable causes. If the patterns were not apparent, it was generally understood that humans lacked the knowledge necessary to recognize them. This optimism did not begin to erode until events in WWI dampened the human spirit.

Frank Knight is generally credited with taking the next significant step in the evolution of thought about risk and, in the process, with altering the direction of economics. Writing his dis-

sertation in 1921, Knight took issue with the laws of probability and economists' then prevailing views toward uncertainty. He argued that past experience was an inadequate basis for predicting the future because it failed to "reflect the tentative, creative nature of the human mind in the face of the unknown" (Bernstein, 1996, p. 220) and because even with the best human planning available, there were still *unintended consequences* of our actions. Embedded in the future, in other words, was an element of radical indeterminacy. The difference between the real world of economics and the experimental one of dice rolling was that events in the latter were homogeneous. For the laws of probability to operate effectively in the real world, Knight argued, it was necessary not only to assume full information and independence of events, but to ensure *identical* events as well. This, however, was rarely possible. The implications for risk management were substantial: Knight distinguished risk from uncertainty on the basis of measurability. Those events that could be measured were subject to the probability calculus and defined as risk; those that were not measurable became uncertainty.

Other economists also questioned excessive faith in probability theory. Among them was John Maynard Keynes, who regarded uncertainty in a positive light because it afforded human beings an opportunity to take action and influence the future—independently of any deterministic laws of probability. It appears that the philosophical debate about individual will and uncertainty at the turn of the 20<sup>th</sup> century was being repeated by economists fifty years later. As importantly, Keynes believed the nation-state could reduce economic uncertainty, either through programs of social support or through the enforcement of contracts. The latter were, after all, merely commitments to action in the future. (Unlike Lowi who, as we have seen, regarded government's responsibility to enforce contracts positively but not its provision of welfare support, Keynes regarded both programs as mitigating the negative effects of a market.) Finally, Keynes viewed financial investments differently than many of his colleagues since, to him, they represented a commitment of resources. In an uncertain world, liquidity provided flexibility. If resources were tied up in investments, one's flexibility was reduced. The inclusion of liquidity as

one of the three basic tenants of fiduciary responsibility in public finance must surely be attributed at least in part to Keynes' insight.

Bernstein includes a third, more contemporary economist who also thought differently about probability: Kenneth Arrow. He quotes Arrow as offering the sober assessment that: "Vast ills have followed a belief in certainty, whether historical inevitability, grand diplomatic designs, or extreme views on economic policy" (1996, p. 203). While Arrow embraces the Schumpeterian assumption that risk taking is necessary for economic growth, and applauds insurance mechanisms that encourage such behavior, he is careful to distinguish among types of insurance.

Reduced to its most basic, insurance is a gamble: on one side are the insured, who take a small, guaranteed loss (the premium) in exchange for a bet against the odds that they will face catastrophe and, as a consequence, collect a substantial gain. The insurer, on the other hand, takes the opposite position. Since the laws of probability pertain only when the numbers are large, the insurer attempts to attract as many *independent* insurees as possible in order to keep costs (mostly catastrophic payments) within projected limits. "Independent," in this context, suggests that the actions of one insuree are unrelated to, or affected by, the actions of another. Arrow differs from Keynes, however, in his view of government. Whereas Keynes saw a legitimate role for government in providing a social safety net against the vagaries of the market, Arrow cautions against bank deposit insurance, for example, on the grounds that it creates a moral hazard, here meaning an unwarranted protection that induces carelessness. The difference is reminiscent of Hacking's comparison of statistics in Western and Eastern Europe—where individualistic responses to social circumstances, on the one hand, and collectivist ones, on the other, were tried.

Bank deposit insurance protects depositors; it is a form of collective security. The insurer is the federal government and the bank is the insuree. The bank pays the insurance (although the costs are invariably transferred to depositors) even though the insurance protects depositors against losses from the bank's own actions. In this instance, insurance enables the bank

to take greater risks than it might otherwise do. In the case of automobile insurance, by contrast, the insurer charges premiums to its insurees in accordance with their driving record, age and other demographic characteristics that have been related probabilistically to driving performance and accident costs. There is a direct link, in other words, between the premium paid and the anticipated costs to the insurer. With deposit insurance, on the other hand, banks are required by law to insure their depositors. Doing so neither enhances their market position nor discourages risk taking; indeed, many contend that mandatory insurance only makes it easier for banks to take unnecessary risks with their depositors' funds because the deposits will be covered no matter what they do. Corroboration for this perspective is found in the savings and loan crisis of the 1980s where citizens at large picked up the tab through their taxes. Of course, deposit insurance was inadequate to cover those losses and politicians—Democrat and Republican alike—agreed to bail the banks out because the problem was so widespread and threatened the general economy. The banking industry as a whole also contributed to the cleanup. Nevertheless, the different perspectives provided by Keynes and Arrow mirror Hacking's observations regarding social policy in individualistic and collective cultures.

Arrow's concern with moral hazard is grounded in the utility calculus. Other contributors to this line of thinking include John Von Neumann and Oskar Morgenstern, who introduced game theory to economics in their seminal work *The Theory of Games and Economic Behavior*, in 1944. Von Neumann was a physicist who proved in 1936 that the laws undergirding quantum physics were not deterministic—even nature was not completely controlled by scientific laws. One implication of this for economics, and the social sciences in general, was to settle the question of individual responsibility: if nature was not controlled by causal laws, neither were human beings. Von Neumann and Morgenstern focused on decision making. Like Knight, they understood that market actors took predictions into account when making decisions; this was not only an important source of uncertainty, it also a critical factor in undermining the accuracy of predictions about the stock market. However, they argued that the secret to maximizing one's utility was not second-guessing other people and then altering forecasts but, rather, in disguising one's

own motives and carefully evaluating trade-offs within the rules of the game. Trade-offs, however, were not limited to binary options; they frequently involved three or more possibilities. Moreover, Von Neumann and Morgenstern demonstrated not only how ranked preferences might yield different utilities, they quantified the different rankings based on the probability of each preference's occurring. By incorporating probability theory into the utility calculus, they captured "the essence of risk aversion—that is, how far we are willing to go in making decisions that may provoke others to make decisions that will have adverse consequences for us" (Bernstein, 1996, p. 239).

Markowitz agreed that people were the principal source of uncertainty but suggested an approach to the market that resembled insurance. He reasoned that just as large numbers of independent policyholders help distribute the costs of catastrophic events, so too can stockholders distribute their exposure to risk by diversifying their portfolios. Here, the logic entails limiting one's exposure to the inevitable variances in the price of a given stock. Since market conditions influence stock prices, stocks within a given product group will be similarly affected. A portfolio that contains a mix of stocks from different market segments will tend to reduce a person's exposure to that variance. Markowitz understood from probability theory that co-variance altered normal predictions; stocks are not always independent of one another. As important, he understood that volatility could also be Janus-faced; the perspective depended upon one's position. Volatility is risky when the stockholder fears a loss. However, it can also provide an opportunity if others are dissuaded from purchasing the stock, causing its price to decline. In that instance, volatility may provide an opportunity to "buy low." The crucial lesson here is that *risk is relative to one's position*—it is grounded in context and not a purely objective phenomenon—even if the risk can be calculated.

One of Markowitz's students, William Sharpe, studied the effect of changes in wealth on risk-aversion and found that increases in wealth enabled people to absorb more loss, allowing them to take greater risks. By the same token, decreases in wealth tended to make them more risk averse. This might appear, on the surface, to contradict Bernoulli's axiom, which undergirds

utility theory, that incremental gains will have less value as wealth increases. The difference lies in the amount of the increment. Utility theory assumes a situation where gains remain constant, so that each gain represents a smaller percentage of the total. Sharpe's insight involves risk, where reward is theoretically proportional to the degree of risk involved. As wealth increases, then, investors tend to take greater risks because they are able to absorb larger losses but also because the rewards are proportionately greater. The theories may thus be seen as compatible. Sharpe cautions that this predisposition toward ever greater risk helps to explain the market's tendency to vacillate between extremes (*ibid.*, 1996, p. 264).

Human motivation and the failure of human rationality to live up to the expectations of economic logic continued to occupy the interest of economists throughout the 1970s. Examples include Kahneman and Tversky's work in prospect theory and Shefrin and Statman's psychological split hypothesis. Kahneman and Tversky found that people tend to regard costs and uncompensated losses differently—even when the amounts are identical. Moreover, people weigh losses differently than gains, tending to be more risk seeking when losses are involved and risk-averse when gains are. Although counter-intuitive on the surface, the context in which the questions were posed, and the values at issue in the choices presented, suggested to Kahneman and Tversky that people take many subjective factors into consideration other than what would be predicted by a narrow understanding of rationality.

Shefrin and Statman hypothesized that investors are psychologically split between the short and long term when acting in the market. In their long-term planning, investors tend to act rationally. When it comes to short-term gratification, however, they are only quasi-rational in that they give too much weight to new information, especially crises, and too little weight to overall market conditions. While these contributions have proven important, none has altered the basic individualistic orientation of game theory and its calculation of a complex, probabilistic utility. Attention has been directed toward the tails of the bell curve plotting human behavior in

the market; theoretical advances are thus made at the margins. As Bernstein presciently observes, however, it is here at the margins where disorder lurks—where the wildness is.

Bernstein suggests that psychological factors were particularly important to economists in the 1970s when political-economic conditions were in flux. As we have been reminded, the United States had allowed its currency to float, inflation had reached double digits, oil and political crises had combined to influence the market in numerous, unanticipated ways. Yet human ingenuity and technology combined to create a novel response to this uncertainty: derivatives. Derivatives, it should be recalled, are financial instruments, akin to bonds or stock, whose value is *derived* from an underlying stock, commodity or other asset. Often the return is calculated by a formula, such as the difference between short and long-term interest rates or the exchange rate between two currencies. But their function, in this history of risk, is more important than their formal definition since their purpose is to manage uncertainty. In fact, Bernstein describes them as instruments for trading in uncertainty (1996, pp. 304-5). The reason they can be traded is that people (or organizations) experience uncertainty differently: as Markowitz anticipated, risk is relative to one's position. Forestalling the use of derivatives in the market, however, was less the prevalence of uncertainty than an inability to price them.

There are essentially two types of derivatives: forward type transactions and options. Forward type transactions include forwards, futures, and swaps. Both forwards and futures are contracts to buy or sell a specified amount of an asset (be it a commodity, a security, a financial instrument, or currency) at a specified time in the future and for a specified price. The difference between them is that forwards are private contracts; they not traded on exchanges and no deposit is required. Futures, by contrast, are forward agreements that are traded on an exchange. As such, deposits are required to secure the agreement and the exchange assumes the risk of any default. The purpose of a forward or future contract is to secure an exchange down the road. Often this involves currency rates where a company needs yen, for example, in six months to purchase Japanese goods and it wants to protect itself against a rise in the value of yen. If it purchases a

forward or future, it can secure a particular exchange rate and protect itself against a rise in the value of yen. Simply put, forwards and futures provide a hedge against uncertainty.

Swaps are similar to forwards and futures although multiple payments are required. The most common type of swap is an interest-rate swap, where someone with a poor credit rating and high interest loan trades his payment stream with someone who has a strong credit rating and low interest loan. They do not trade the debt, only the interest payments. Swaps like this usually occur when the party assuming the higher payments can also benefit from a tax write-off that she otherwise would not have and thereby not only offset the additional cost of the interest payments but, on balance, realize a net gain. Swaps, then, enable participants to take advantage of their different relative positions in the market.

Options are generally regarded as more risky and complex than forward type transactions. These agreements give the holder of the option the right, but not the obligation, to either buy or sell a specified amount of an asset (commodity, security, financial instrument, currency) within a specified period of time and for a specified price. An option to buy is a call; an option to sell, a put. Normally, a premium is paid to secure the option. If the option is not exercised within the specified time, it lapses and the premium is forfeited. In this respect, options resemble insurance policies where the premium is forfeited in exchange for the possibility of a large gain in the event of catastrophe. Call options allow the purchaser to hedge against a rise in prices; put options allow the purchaser to protect against a decline. The purchaser of the option risks only the loss of the premium; the seller bears the full market risk. Banker's Trust took the early lead in this market and its former clients included companies like Proctor & Gamble and Gibson Greetings, both of which later sued Banker's Trust for losses incurred from trades in these exotic financial instruments. Generally, options make it possible to protect oneself against disadvantageous events in the future. Like forwards and futures, they help participants cope with uncertainty.

Although derivatives have existed in their present form only since the 1970s, variations on the present instruments have existed for thousands of years. Options were allegedly mentioned by Aristotle, and futures existed in European agriculture as early as the 12<sup>th</sup> century. And, despite their reputation for being exotic, they are widely held by homeowners who have a provision in their mortgage agreement allowing them to payoff their debt ahead of schedule. Still, several factors prevented the widespread use of derivatives before the mid-eighties. First, they were difficult to price. What, for example, should be the fair market value of a currency exchange option? Scholes, Merton and Black, building on work by Bachelier in 1900 and Samuelson in the 1950s, identified four factors to consider when setting the price of derivatives: time, prices, interest rates, and volatility. Their innovation involved *disregarding the direction of the volatility*. Previously, it had been assumed that increases in price were good and decreases bad, but Markowitz demonstrated that stock declines could also present opportunities. Second, high-speed computers made it technically possible to perform the sophisticated calculations necessary to set premiums. Yet as important as these technical innovations was the demand factor itself—there had to be a *need* for derivative instruments. Almost one hundred years after Peirce concluded that uncertainty was ubiquitous, the financial community came to a similar conclusion. Using over-the-counter trade in derivatives as an indicator, the Bank for International Settlements estimates growth in this market from approximately \$1 trillion in 1986 to over \$81 trillion in 1999.<sup>33</sup>

### Risk and Culture

The pervasiveness of uncertainty does not imply that the empirical world is completely random. Clearly patterns exist, but they are approximate, imperfect, and dynamic. However, with greater consensus between the philosophical and financial communities on the prevalence of uncertainty, the important question then becomes “how do people respond to it?” Response to uncertainty, in turn, raises the question of perception—how do people regard uncertainty? What

<sup>33</sup> These figures were cited in McCarthy, (McCarthy, 1999).

does it mean to us? Bernstein concludes his historical excursion by summarizing the contributions of the many luminaries he investigated as follows:

...all of them have transformed the *perception of risk* (emphasis added) from chance of loss into opportunity for gain, from FATE and ORIGINAL DESIGN to sophisticated, probability-based forecasts of the future, and from helplessness to choice (Bernstein, 1996, p. 337).

To Bernstein, then, advances in probability theory have empowered human actors and made it possible for them both to manage risk with greater precision and to cope with uncertainty.

This question of risk *perception* is not so easily captured, however. Indeed, it has been the principal concern of cultural anthropologist, Mary Douglas, for over thirty years.<sup>34</sup> Surprisingly, her conclusions are closely akin to the findings of Ian Hacking, a philosopher of science. Culture, they both contend, plays a significant role in shaping our perceptions of risk and, concomitantly, our response to excessive or failed risk, especially as it involves blame. Douglas's findings are important for Public Administration, not only because they corroborate Hacking's work, but also because they provide a valuable perspective for assessing the complex situation in which public administrators find themselves.

Mary Douglas is a cultural anthropologist who applies the cultural archetypes of primitive cultures to modern societies. Yet she understands culture not as a collection of individuals or social groupings, but as a mental or philosophical predisposition:

In the theory a typology of cultures is derived from cultural biases...a cultural bias is a point of view, with its own framing assumptions and readily available solutions for standardised problems. Scattered persons not in any group at all may share a similar cultural bias....A common culture is a source for salient reference points and heuristics..." (Douglas, 1999).

<sup>34</sup> Mary Douglas wrote *Purity and Danger: An Analysis of Conceptions of Pollution and Taboo* in 1966. It was published by Routledge & Kegan Paul.

Douglas identifies two dimensions by which these points of view are organized: “groups” and “grids.” Group identification may be low or high, depending upon the kinds of distinctions members make between insiders and outsiders, and the importance they place on membership. “Grids” represent rules of behavior and are, again, divided into low and high categories. Low grids involve loosely established or enforced sets of rules, while high grids represent strictly enforced, clearly articulated rules. These patterns are depicted in the following matrix:

Table 4:1  
Cultural Archetypes  
**Group**

		<b>Low</b>	<b>High</b>
<b>Grid</b>	<b>High</b>	Isolates	Hierarchists
	<b>Low</b>	Individu- alists	Sectarians or Enclaves

Douglas argues that most modern societies support a combination of cultures, with the major power axis extending from the upper right (high group, high grid) to the lower left (low group, low grid) quadrants. Those with a hierarchical mind set are located in the upper right quadrant. This is, perhaps, the most familiar quadrant as it appears in many areas—from government bureaucracies to religious organizations and corporate establishments. Hierarchical cultures value clear delineations across groups; not only are the boundaries between inside and out well demarcated, but the distinctions within the hierarchy are clearly established. Roles are highly differentiated, and there is a clear ordering among them. Professions, for example, play an important role in ordering society. As important, responsibilities and obligations are straightforward and unambiguous. The justification for the hierarchical order is provided through the culture’s history.

Hierarchists also liken order to nature—it is the way things have evolved, and there is an inevitability about this. Accordingly, they value history for it is the way in which the culture

documents its progress. In terms of time, hierarchists emphasize the long term—whether one is considering future planning or historical patterns. Education is also important, not only for its explanatory power in terms of the existing order, but as a screening device for the placement of people within the hierarchy. Conflict is resolved internally, with punishment often carrying both punitive and exemplary dimensions. Disloyalty to the group is the greatest offense to hierarchists and expulsion or exile to low status is the consequence. Inequality is generally tolerated because it is seen as part of the natural order of things; indeed, inequality pervades nature.

Located at the other end of the power axis are individualists. This is a low grid, low group culture, meaning that rules are minimal and group boundaries are permeable. The emphasis in this quadrant is on the individual, rather than the collective, and individuals often re-write the rules. Power resides in persuasion; individual expression is valued and competition for time and attention is ubiquitous. With competition, however, also comes change. Change, too, is ubiquitous and uncertainty is accepted as part of everyday life. In terms of time, then, individualists focus on the immediate or short-term, and accord history or tradition little weight. Roles are not well defined. Responsibility and accountability remain implicit in the individualistic culture. Because group boundaries are low, obligations are understood as being to other individuals, but are not clearly spelled out. Education is important, but more for individual advancement and self-expression than for purposes of group justification. Of course, individualistic values are transmitted through education, as it provides an important means for the belief system to sustain itself—as it does in other cultures. Equality is valued primarily in terms of opportunity, although equality before the law is important. Individual talent and effort are rewarded through recognition and material benefit, so material or economic equality is not expected. Individualists believe in meritocracy, where merit is rewarded and punishment is delivered to the deserving. Because this reward system is assumed, the way in which material goods are allocated is deemed to be fair; rewards, in other words, become proof of one's performance. The poor, disabled and diseased are virtually invisible.

In the upper left and lower right hand quadrants are located the minorities. In the high group-low grid (lower right) quadrant are the “sectarians” or “enclaves.” The example most often provided by Douglas and her associates for people who fall into this category are environmentalists and social reformers. People with this affinity find group membership important and exert strong pressures to maintain it. They also share the requirement of loyalty and the valuing of education with those in the hierarchical culture, but they distinguish themselves with their emphasis on equality and their suspicion of authority. In this latter sense, they are closer to individualists, with whom they share low grid characteristics. This makes leadership, and thus group cohesion, problematic. One approach to this dilemma is the Christian model, mentioned by Hargreaves-Heap and Ross (1992), where Christ is presented as the leader but his leadership is qualified by axioms such as “the first shall go last.” This humbling of leadership helps to maintain equality while holding the group together. Douglas notes that people with this predisposition often serve as the conscience of society; they include environmental activists and social reformers who challenge both bureaucratic authority and market imperatives.

Another familiar example of this ideal type is the voluntary association. Douglas (1992a) associates this category with Alexis de Tocqueville, but reverses his argument. Tocqueville saw the voluntary association as an organizational response to the condition of equality in which Americans found themselves after the founding. He understood equality to be an unstable condition, so the voluntary association provided a means of stabilizing society. Inverting Tocqueville’s logic, Douglas believes that Americans experienced a power vacuum after the founding and responded by valuing equality. Drawing on Mancur Olson (1982), she suggests that voluntary associations do have difficulty remaining cohesive and, absent measures to institute hierarchy, are obliged first to establish clear boundaries for the group and, second, to ensure that all members feel an equal responsibility to contribute to the common effort. Equality in this view becomes a means of ensuring loyalty to the group and discouraging free-riding. In early 19<sup>th</sup> century America, where institutional structures were minimal and everyone’s efforts

were required to set the new nation on a firm course, equality served the group's needs. In other words, it was a response to the situation, not a precondition—as Tocqueville suggested. While this example adds a footnote to the civil society discussion, it illustrates Douglas's way of thinking and the nature of her contribution to scholarship.

The fourth category is often omitted from taxonomies of culture, especially when applied to political or economic contexts.<sup>35</sup> This is the low-group, high-grid quadrant occupied by isolates. Here, group cohesion is accorded little status, as with individualists, but the rules of behavior are highly structured. While there may be many who fall into this category, the size of each group will be small—largely because of the rigid behavioral requirements and the individualistic predisposition of members. Moreover, because of their suspicion of authority, they are marginalized from most social orders. Anarchists and various militia groups are often found in this quadrant.

According to Douglas, the pattern of thought with which each of us identifies also makes us sensitive to certain risks, aware of their indicators, and guides us in our response to these warning signs (1992b). While most of us tend to disregard low probability events, even when the outcome could be disastrous, we are especially attentive to risks that reinforce the predispositions already in place. Individualists, for example, will be particularly attentive to actions of large organizations—especially government, while hierarchists will be attentive to threats to the system or established groups. Douglas argues that it is not only our attentiveness to risk that is molded by our culture or thought processes, but also our responses, especially as they involve the assignment of blame. People with different predispositions view responsibility differently and, accordingly, discharge punishments in various ways. Blame, in other words, is a means of keeping people mutually accountable to the common belief system. *Risk perception, then, is functional because it helps to maintain the set of beliefs that undergirds the community.*

<sup>35</sup> Mary Douglas and Aaron Wildavsky, for example, used this taxonomy in their 1982 collaborative venture, *Risk and Culture* (Douglas & Wildavsky, 1982), but omitted this fourth category.

At the same time, risk perception can be influenced by physical context. People who work in the nuclear power industry, for example, have a different perspective on the risks involved than many in the general public. Those trained in scientific disciplines often view risks differently than those in the arts. Similarly, some people may have a more sophisticated sense of risk when they are regularly engaged in activities that bring them close to risk. Fishermen, for example, have a keener sense of danger from changes in weather than do day sailors who practice their sport intermittently. Douglas suggests that this variation in perception is one instance of the divergence that has taken place over time between experts and lay people (1992b, p. 11). She also traces this divergence to the attempt of myriad experts to remain “scientific” and “objective” in their treatment of risk, ignoring politics (or subjective considerations) as if they would contaminate inquiry. This bias against the political, coupled with a methodology that emphasizes the individual, distorts risk analysis in Douglas’s view:

The gap between lay and expert opinion has given rise to a whole new sub-branch of the psychology of risk, a whole new specialized branch of adult education, and a whole new sub-discipline for communicating about and labeling risks, and a whole new industry for cataloguing them. But the baffling behaviour of the public...continues as before.

The single cause of why the subject is swathed in bafflement is the practitioners’ commitment to methodological individualism. This follows from the way they see their need for objectivity....Absence of motivation on the part of the subjects matches the purity of the researcher’s motives....Anger, hope, and fear are part of most risky situations....Placing all the focus on individual cognition excludes the problem. The risk perception analysts say practically nothing about intersubjectivity, consensus making, or social influences on decisions. (Douglas, 1992b, pp. 11-12)

Writing before the National Research Council (Stern & Fineberg, 1996) developed its recursive methodology to mediate the gap between scientists and the lay public, Douglas attributes the chasm to research methodology and cultural mindset.

Indeed, risk has an entirely different meaning to the lay person than to the expert. Rather than representing something that can be measured and expressed probabilistically, risk often carries the connotation of danger. Douglas (1992b) compares modern society's use of risk to the use of sin and taboo in primitive cultures in that both carry negative connotations and are regarded by society as things to be avoided. Yet the role played by sin and taboo in traditional cultures differs in at least two respects from that played by risk and blame today. Both sets of terms clearly involve sanctions. It appears, however, that today people tend to anticipate risk and view it as something to be avoided in the future, whereas sin and taboo were explained after the fact in primitive cultures. Actions were often interpreted as sins well after the act to explain why punishment or ill fate followed. With risk, on the other hand, there is premeditation. Moreover, Douglas explains (1992c, pp. 27-9) that the forensic or explanatory uses of these sanctions are quite different. In primitive cultures, groups identified certain acts as sins or taboos to *protect the community's values* and ensure its survival. In other words, sins were committed by individuals against the group. Risk, on the other hand, has been reconstructed as a danger that threatens individuals and is normally perpetrated by groups—be they corporations, government agencies, or other collectives—against individuals and their welfare. Hazardous waste, environmental pollution, and economic disaster are all collective actions that threaten individuals.

The new emphasis on risk has come about, Douglas contends, for two basic reasons. First, its threat to individual quality of life is consistent with an individualistic orientation that now pervades much of the developed world. (Here, Douglas is not necessarily repudiating her earlier work with Wildavsky, where they attributed an increased interest in risk to growing sectarian concerns, because both sectarian and individualistic cultures share “low grid” attributes.) Secondly, recent emphasis on risk fills a need presented by the global economy. In focusing on the global economy, Douglas is more concerned with the heightened sense of contingency and insecurity experienced by people in their day-to-day lives than with the myriad financial instruments that have emerged to help businesses cope with global interdependence.

In her essay “The depoliticisation of risk,” Douglas describes culture as a “dialogue that allocates praise and blame” (1999, p. 226). Yet the co-existence of several cultures in society means that this allocation will be contentious or agonistic. Members of hierarchical cultures, for example, will tend to apportion responsibility for risk management by specialization and encourage the professional development of risk measurements. At the same time, with its focus on the long term, hierarchical dialogue may underplay intermediate hazards. The individualistic or market culture, by contrast, emphasizes the short term and accepts risk as a necessary part of reality. Nevertheless, it, too, relies upon professional assessments of risk and encourages the development of technical definitions, if not standards. While probabilities may be assigned to given risks, individuals are accorded responsibility for assuming them and are held personally accountable when they fail. Douglas says little about the isolates and their propensity to take risks or attribute blame, but she credits the sectarians with providing the moral conscience of society (1999, p. 227) insofar as risks are concerned. They assume responsibility for exposing risk whenever possible, blaming both the authority structure of hierarchy and the material power of the market for both groups’ lack of concern with the consequences of risk. It might even be suggested that sectarians sustain their group boundaries by exposing social hazards.

### Revisiting Risk and the Orange County Bankruptcy

It is now possible to return to the bankruptcy and ask: What is risk and how do we<sup>36</sup> know it? There are several levels at which risk can be appreciated. First, we have learned from Frank Knight that risk differs from uncertainty in that risk can be measured. Yet both risk and uncertainty existed in the events leading up to the bankruptcy. The portfolio was sensitive to interest rate increases, which could be measured, but the extent to which the Federal Reserve would raise interest rates was uncertain. Moreover, it was not only that the pool was sensitive to interest rate increases, but also that too much of it was vulnerable. We have learned from Markowitz that statistical co-variance influences probability calculations and the best way to protect against overexposure to any given market segment is through diversification of

<sup>36</sup> In this context, “we” refers to the readers of this dissertation.

investments. Limiting exposure to any given segment protects the bulk of the pool while enabling it to benefit occasionally from high yields. This was essentially the recommendation of the State Bureau of Audits (California. Bureau of State Audits., 1995), which investigated the bankruptcy and recommended restricting the percentage that any public investment pool in California could invest in derivatives to ten percent.

At a second level, we know that risk is at least in part a function of one's position in a given situation. Californians, for example, were more vulnerable to interest rate increases than many others in the early 1990s because they were in the midst of a recession while the economy was booming elsewhere in the country. Preventing the economy from overheating was, in fact, the Federal Reserve's motivation in raising interest rates. At the same time, participants in the County's pool were sensitive to risk to varying degrees. School districts, for example, were very dependent upon the pool's revenues and were required by law to invest there while transportation authorities had much greater flexibility in both respects. We also know that risk is perceived differently—both by laypersons and experts, and by people with different philosophical predispositions. According to Douglas, our perception of risk is functional in that it enables us to preserve our values and ways of understanding the world. Often we do not even register low probability events, even when their consequences are high. Citron's failure to recognize risk in the investment pool may be attributed at least in part to the role his investment strategy played in holding things together in the county: It kept voters from paying more taxes, allowed the Board to fund visible projects, and made it possible for the Democratic Citron to retain his position in a Republican administration. The possibility that this investment strategy carried within it the seeds of its own destruction was most likely inconceivable.

Voters, for their part, are likely to have understood financial risk quite differently from others more familiar with the investment pool. If risk, to citizens, was less a probability calculation than a form of danger, then it is easier to understand why they blamed government for the bankruptcy and defeated Measure R, which would have raised taxes one half cent over ten

years, even if this action meant repudiating their obligations to bond holders. Douglas has made us aware that risks are viewed as dangerous actions, taken on the part of organizations, that threaten the safety of individuals. At the same time, the safety of the Orange County Investment Pool was the principal issue raised during Citron's re-election campaign. Yet Knight, and later Von Neumann and Morgenstern, have pointed out that investor confidence can be a critical factor in market performance. These scholars have demonstrated that investors take predictions into consideration when acting in the market. In this case, the confidence at issue was that of the pool participants and influential actors such as Marian Bergeson, former chair of the Senate Local Government Committee who represented Orange County. Bergeson's vote became a political issue during the campaign. While she personally favored Moorlach, Citron's opponent, and expressed an inclination to vote for him, she was persuaded that a vote of no confidence in the incumbent treasurer and his investment strategy could itself cause the withdrawal of funds from the pool and lead to bankruptcy.<sup>37</sup> Perceptions of risk, then, and its potential impact, played a complex and often subtle role in the bankruptcy and the events leading up to it. This is an important factor in any public discussion of risk and will be mentioned again in the conclusion.

What role did derivatives play in the bankruptcy? Orange County had purchased Federal Home Loan Bank bonds that contained inverse floaters in the calculation of dividends. The formula made it possible for the Board to raise funds for mortgages during periods of relatively low interest rates and, at the same time, prevent the Board from depleting its financial resources when interest rates rose, as had occurred during the Savings and Loan crisis. Derivatives, in this instance, served to stabilize the mortgage industry and keep affordable housing available to the average American. At the same time, it transferred risk from the mortgage sector to bond holders. This use of derivatives provides a clear example of what is meant by positioning oneself for risk in a global economy. Risk, in the housing context, is greatly influenced by interest rates. Mortgage brokers need to offer sufficient incentives to attract depositors and at the same time guarantee repayment, with interest, of the bonds they issue. The Savings and Loan crisis was due partly to the fact that S&Ls had offered loans at relatively low rates but found themselves

<sup>37</sup> This dilemma was reported in (Fulton, 1996).

obliged to pay higher interest rates than they were receiving on their loans to attract new investments. By purchasing FHLB bonds, Citron was adding to the liquidity of the mortgage industry, and he received high returns when interest rates were low. What he apparently failed to understand was his vulnerability to any change in rates. Ignoring his position vis à vis the financial market in general or interest rates in particular made his investment strategy risky, not necessarily derivatives per se.

In the aftermath of the bankruptcy, and the Orange County citizens' repudiation of their debt to bond holders, the market responded by encouraging greater use of bond insurance. The reasons were severalfold. First, bond-rating agencies had clearly been caught off guard by the bankruptcy; their traditional tools for rating municipalities had failed to detect the financial problem lurking beneath the surface in Orange County. If bankruptcy could be filed by as wealthy a county as Orange, it could happen anywhere. Secondly, the voters' response to the bankruptcy, especially their refusal to increase taxes even on a temporary basis, violated one of the basic tenets of public finance: government bonds offer lower yields than corporate issues because they are securely backed by the electorate. The concept of creditworthiness, as opposed to market safety, was clearly shaken.

The market responded with a familiar tool: insurance. As Arrow observed, insurance of any kind is a gamble. It represents the wager of a guaranteed small loss (the premium) against the possibility of a large gain in the event of a crisis. Insurance spreads the risk among many parties, and the greater the number of policyholders, the smaller the guaranteed loss. Bond rating agencies responded to the bankruptcy by rewarding municipalities that held insurance with higher bond ratings, and hence lower interest rates. Municipalities with poorer bond ratings would not even have a choice: bond insurance was now required by the financial community. Yet bond insurance is not without cost, for it raises the transaction costs for all municipalities that seek to finance operations through debt. In this respect, the Orange County voters created a new collective action problem for all municipalities. The spread of bond insurance, however, might even create

its own moral hazard, especially if other voters were to follow Orange County and repudiate their debts.

It is now clear that risk is not merely a financial calculus; it is a complex phenomenon with multiple dimensions and factors to consider. As importantly, we have seen that measurement alone is not sufficient to manage risk; in other words, risk cannot merely be delegated to experts. Yet we have also seen that risk, and its unmeasurable counterpart uncertainty, are increasingly part of the everyday fabric of our lives. They are ubiquitous. What steps public administrators can take in the future to mediate this condition is the subject of the next and final chapter.

## Chapter 5: Conclusion

The Orange County Board of Supervisors filed for Chapter 9 protection from bankruptcy on December 6, 1994. In the ensuing investigations, there was never a doubt that the investment strategy adopted by Robert Citron was at fault. Yet several examiners cast their net more broadly. The Senate Special Committee, for example, concluded that numerous actors had contributed to the disaster, including the Board of Supervisors, pool participants, investment advisors, and bond rating agencies. Why do the findings vary? Mary Douglas's insights into risk perception and blame suggest an answer. An individualistic predisposition would tend to focus on a single actor. This is especially the case when government is involved. A hierarchist's predisposition, by contrast, would tend to focus on groups and their inter-relationships. The Senate Advisory Committee, itself only one link in an investigatory chain, conformed to the latter pattern and thus spread the blame more widely—including even pool participants among those generally culpable for the failure, even though others considered them victims.

Curiously, however, none of the official investigations identified their own contributions to the bankruptcy. The state auditor's office, for example, failed to mention its role in introducing reverse repurchase agreements to public agencies. Similarly, the Senate Advisory Committee made no mention of the state legislature's role, first in expanding the range and volume of investments available to local governments and then in relaxing their reporting requirements. Later, John Moorlach even accused the SEC of being partially complicit for its failure to investigate the County earlier. In this respect, the investigators were much like Orange County voters—they had no difficulty finding others responsible but had less success in appreciating their own entanglement.

Douglas's insights into cultural archetypes help us to understand even the actions of voters in the bankruptcy. At a time when risk is being ever more precisely calculated by experts, lay people—citizens—are increasingly treating risk as a danger to which they are exposed, rather

than as something over which they might exert some control. Indeed, the citizens of Orange County treated the financial crisis no differently than they would a natural disaster—although they might have received more public notice of the latter. Yet this perception of risk as danger raises serious questions about the possible involvement of citizens in matters of public finance. If citizens can repudiate the actions of government, which they themselves have encouraged or endorsed, can public officials be simultaneously responsive to public wishes and financially accountable? This question has particular significance for Orange County as voters were asked in the aftermath of the bankruptcy whether they wanted the treasurer's position to be appointed rather than elected. Proposal initiators made a strong case for administrative accountability, including the probability that this would attract stronger candidates, but voters rejected the ballot measure. Such division of accountability among public offices, which Baldassare calls fragmentation and identifies as one of the principal factors in the bankruptcy (1998, pp. 46-50, 218-226), has been raised repeatedly by government reformers in California. In Douglas's typology, such a proposal is consistent with the views of hierarchists; it is also consistent with the United States' tradition of checks and balances.

In his conclusion, Baldassare charges Citron with "woodenheadedness," a term he borrows from Barbara Tuchman and that is described as "assessing a situation in terms of preconceived fixed notions while ignoring or rejecting any contrary signs" (1998, p. 236). This characterization greatly resembles the predisposition Douglas takes for granted in *all* cultural archetypes, specifically, that human patterns of thought have tended to reinforce themselves across time and cultures. Yet Tuchman associates this tendency exclusively with government officials. Baldassare, however, is more generous, including actors in the Barings collapse as well. Yet another scholar who has studied single-focused strategies that failed in the private sector, was more charitable in his assessment of their performance, labeling executive misdeeds the "Icarus paradox" (Miller, 1990). Among those with wax wings who flew too close to the sun was Harold Geneen, whose misguided strategy in the early 1980s bankrupted ITT. Organizational theorists often repeat the mantra that "all institutions are public" and advocates of entrepreneurial government have certainly sought to remake public organizations in business's image, but ethicists

understand that the *people* within public and private organizations are often held to different standards. I submit that this variance can be largely attributed to differences in our perceptions of risk and blame across sectors.

Mental predispositions become complex in the area of public finance because the streams of thought influencing them are drawn from both individualistic and hierarchical waters. The result is a brackish mix. We have seen evidence of this with investor doubts about the creditworthiness of municipal bonds after Orange County voters defeated Measure R. If the electorate cannot be trusted to stand behind its debt obligations, then alternate means of protecting investors must be identified. The financial community turned to bond insurance while occasionally raising rates—reflecting the increased risk to creditors but, at the same time, increasing costs to local governments and reducing the financial differences between sectors—an undesirable outcome for any public agency. Yet that was not the only complication raised by the crisis. At the outset of the bankruptcy, Matthew Raabe alerted the county administrator to problems in the investment pool, but the Board of Supervisors could not meet to discuss them because sunshine laws required any gathering of more than three officials to be made public, that is, open to the press. As a result, in the days immediately preceding the bankruptcy, board consideration of any alternatives had to be *seriatim*—involving only two or three members at a time. Again, public interests came in conflict with financial considerations and complicated any resolution.

Finally, we have seen that prominent voters had difficulty being candid in public about their preferences during Citron's re-election campaign because any lack of confidence in the incumbent and his investment strategy might easily have produced a run on the pool—creating the circumstances they were trying to avoid. At the very least, these public finance constraints suggest that the timing of financial discussions should be well in advance of any action, so that strategies and options can be weighed without fear of immediate repercussions.

Yet this observation begs the subtler and more important issue of voter ownership of public finance decisions. Interest in civil society has been motivated primarily by concerns about widespread citizen disaffection from government. As we have seen, advocates have espoused many different views. Some have been drawn to the voluntary sector because it provides a non-coercive means of achieving social goals. Others have looked to the non-profit sector as a source of norms or values that might provide a common bond for an increasingly fragmented society. Here, fragmentation refers to Americans' alleged division into ever-smaller groups with fewer ties linking them to each other or providing common ground. The appeal to abstract principles, such as freedom or equality, is unlikely to provide the commonality intended because proponents misunderstand the problem. Use of the terms "civil society" and "risk" are themselves illustrative: they mean different things to different groups; in other words, meaning is not shared. This presents an awkward situation for value proponents because the very tools they propose to reduce fragmentation are likely, in the end, to increase it. This is not to suggest that civil associations will not inculcate values among their members. It is rather that the values will become a source of inspiration for some but an authoritarian imposition for others; they will connect some and alienate others—still, fragmentation will remain. An approach that is more likely to succeed is that proposed by White, where meanings are not assumed but are, instead, created through group deliberation of common, concrete concerns. Moreover, we should not expect meanings to be settled; indeed, it is better to assume that they will perpetually change, with changes among the participants, changes in the problems, and changes in people's perceptions. In this view, the public administrator assumes the position of drawing people out, enabling citizens and groups to be part of the process; she certainly does not impose solutions or insulate citizens or other leaders from problems.

Such an approach is important in the area of public finance for several reasons. While it is highly improbable that another locality will invest in structured notes or leverage a portfolio in the way Robert Citron did, we have seen that the emergence of a global economy has brought uncertainty and contingency into our everyday lives. At the same time, it has increased the cost of certain government actions or brought certain programs under greater scrutiny. At the level of the

nation-state, national currencies are traded on the market for speculative purposes, with the result that countries whose domestic policies are out of synch with their currency value are likely to experience global dumping and devaluation of the currency. The threat alone can force government officials to consider significant policy changes. Because of the size and overall strength of its economy, the United States is less vulnerable to these threats than others, although as international trade increases so will local vulnerability. Nevertheless, Americans experience market discipline through actions of the Federal Reserve and other economic players. At the local levels of government, the effect can be experienced less directly. Economic development policies, sources of revenue, unemployment, and vulnerability to trade or weather fluctuations all have a bearing on the flexibility and direction of local government.

Two areas that are particularly sensitive for Californians include the state formula for re-allocating property tax revenues and the heavy dependence of most localities on the sales tax. As noted above, the Legislative Analyst's Office has recommended that the Legislature revise the formula for local property taxes so that voters can more easily understand how their taxes are being used (California. Legislature. Joint Legislative Budget Committee. Legislative Analyst, 1998). In the absence of any reform, local officials merely play out the "heroic" role Citron adopted when he insulated citizens and supervisors alike from the unpleasant discussion of taxes. As local officials identify more, and more complex, ways of financing public operations, they place themselves in a position toward the electorate much like Robert Citron's. Even if an official wanted to discuss local finance with citizen groups, the effort would be trying because state formulas control so much. The trend, in fact, has been in the other direction with financing arrangements, especially for more populous localities, becoming increasingly exotic.

At the same time, heavy reliance on the sales tax places local governments in a position as vulnerable to changes in the economy as Citron was to interest rates. Discretionary consumption is one of the first items sacrificed when there is an economic downturn, and while recessions are

increasingly concentrated in market segments so that widespread depression is less likely, the impact on a given community can be severe.

The global economy has created an interesting paradox: On the one hand, it has brought us closer to the ideal of a global market where each country benefits from others' strengths. The result has been a concentration of specializations—each country or firm produces that which it does best and relies on trade for everything else. As each producer or service provider concentrates on its strengths, firms merge and become more efficient, controlling even more of that market segment. Those operations that are most efficient set the standard for the industry, causing others to go out of business if they cannot compete. To the extent that governments follow private sector trends, they must also specialize—and select fewer things to do well. Privatization and deregulation have strengthened and accelerated this trend, whether intended or not.

For consumers, however, the situation is reversed. As the internet and other technologies have made global communication faster and easier, the consumer has been presented with more choices—she may have more options, but she also has more decisions to face. Individuals increasingly bypass professional service providers, obtaining everything from books to stocks on the Internet. People have more choices, but are also expected to assume more responsibility. Individuals require more, and more sophisticated, skills to function every day. The only exception occurs when we have sufficient resources to purchase our own prepared goods and services—in which case we take on many of the attributes of an employer. The difficulty for both people and government is determining how best to function in this new environment.

Greater transparency in organizational operations has replaced regulation so that increasingly government agencies like the SEC work to ensure that rules are clear and that public and private institutions alike disclose their operations. Greater government support for education—at all levels of government—has been another approach, providing opportunity but leaving outcomes to the individual. The Keynesian view of government as a counterforce to the economy has all but disappeared; government is less an opponent of business, or even safety net,

than a private sector partner, making it easier for business to succeed. This does not mean that government must withdraw from the lives of people entirely and embrace *caveat emptor*. Government can create and help to maintain institutions of self-help, such as those Hacking described in 19<sup>th</sup> century Germany. The new federal welfare system might be characterized as self-help: Job training and placement services, personal counseling, as well as transportation and child care services are now routinely part of most state welfare operations. However, it does mean that public administrators cannot afford Citron's heroic posture, insulating citizens and officials alike from the unpleasantness of tax increases or reduced services. Partnership with citizens, not patronage, is the stance better suited for the 21<sup>st</sup> century.

This may seem like a bitter pill for those already overburdened with daily commitments. If government is to act more like a business, should it not carve out its professional niche and become expert in one or two areas, relying on others to fulfill their responsibilities? Partnerships with both for-profit and non-profit agencies are, as we have seen in the discussion of civil society, also part of the equation. Yet, again, the emphasis should be on concrete actions and straightforward talk, recognizing that institutions will differ and have their own set of aspirations. Fragmentation appears to be increasing, suggesting that partnerships should also be developed across sectors.

The political, economic and social changes that have occurred during the past thirty years are breathtaking. The financial community has been quick to recognize these changes and to take the lead in responding. Significantly, its responses have recognized both the ubiquity of uncertainty and fast pace of change. It has also developed sophisticated tools to cope with this uncertainty, but few would describe these tools as instruments of control. They may be used to manage uncertainty, but their appropriate use is highly contextual—it depends both on one's position and on circumstances. Since these change with little advance warning, taking more than small steps can prove counterproductive.

Economic actors may hedge bets, calculate odds, or even take Von Neumann and Morgenstern's advice and disguise their motives while carefully evaluating trade-offs within the rules of the game, but government officials cannot. This has been one of the more valuable lessons of the bankruptcy—for public and private sectors alike. The SEC may now hold brokerage firms liable for their financial advice to public agencies, but the principal benefit lies in drawing attention to the different standards of care required in the two sectors—distinctions often ignored by advocates of entrepreneurial government. The private financial groups involved in the bankruptcy compensated the County financially, and were hurt by their involvement—both in their pocket books and in public esteem. In psychological terms, if Citron was the “rescuer” in the bankruptcy and the pool participants (including citizens) were the “victims,” then the brokerages and bond assessors were the “persecutors”—and they paid dearly for that role. The pathological triangle identified by White at the end of Chapter 2 now becomes clear.

In these unsettled circumstances, diversity of perspectives may appear at first only to add to the confusion. However, straight talk, myriad perspectives, and small steps are more likely than elaborate theories or grand designs to prove workable in the 21<sup>st</sup> century. The field of public administration, with its emphasis on implementation and concrete, day to day practice, should be better suited to this approach than many theoretically sophisticated disciplines.

These myriad and complex changes at the turn of a new century invite comparisons with 1900 and this is especially true in the field of public administration, which gained its status as a profession with the rise of the Progressive era. Three similarities stand out. Both centuries witnessed the emergence of a new economic base that created unforeseen levels of wealth and new modes of employment for decades to come. In 1900, it was industrialization; today it is information technology. In both centuries the United States witnessed a change in demographics, adding to concerns that the social fabric was coming unraveled. In 1900, it was a rise in immigration from previously underrepresented areas of Europe; today, it is a combination of immigration from the Far East and repeated waves of civil rights movements—by African Americans, women, other ethnic minorities, and gays and lesbians. Increased interest in civil society has, in part, been

fueled by the fear that the United States has gone too far in recognizing the rights of individuals within previously unrecognized groups.

Finally, both centuries witnessed widespread disillusion with government. In 1900, disillusion centered upon the excesses of the Jacksonian spoils system. The Progressives responded with a three-pronged approach: separating the partisan “politics” of government from its “administration”; applying scientific principles to public administration; and embracing the goals of efficiency, economy and effectiveness in administrative operations. Today, the response is again to curb the “excesses” of government—this time of the welfare state. It has again entailed a three-pronged approach: deregulation; downsizing the federal bureaucracy through privatization and devolution; and stimulation of a third social sector—the institutions of civil society. In both centuries, business has been held up as the model for government to emulate.

The turn of the last century also witnessed the emergence of pragmatism as an alternate response to new conditions. Some of the tenets on which the movement was based, however, were disparaged. These included the pervasiveness of uncertainty and the notion of contingency. Today, as we have seen, these conditions have become part of the United States’ economic or material base. Perhaps the insights of pragmatists like Peirce, James and Whitehead will find more fertile soil in the 21<sup>st</sup> century than they did in the last.

## BIBLIOGRAPHY

- Baldassare, Mark. (1998). *When Government Fails: The Orange County Bankruptcy*. Berkeley, CA: University of California Press.
- Baltodano, Andre Perez. (1997). The Study of Public Administration in Times of Global Penetration: A Historical Rational for a Theoretical Model. *Public Administration Research and Theory*, 7 (4)(October), 615-638.
- Barber, Benjamin. (1984). *Strong Democracy*. Berkeley, CA: University of California Press.
- Barber, Benjamin. (1995). Searching for Civil Society. *National Civic Review*(Spring), 114-118.
- Beck, Ulrich. (1992). *Risk Society: Towards a New Modernity*. London: Sage.
- Beck, Ulrich. (1998). Politics of Risk Society. In J. Franklin (Ed.), *The Politics of Risk Society* (pp. 9-22). Malden, MA: Blackwell Publishers Inc.
- Beem, Christopher. (1996a). Civil Is Not Good Enough. *The Responsive Community: Rights and Responsibilities*, 6 (3)(Summer), 47-57.
- Beem, Christopher. (1996b). *Civil Society in America: A Public Debate about Political Theory*. NY: Institute for American Values.
- Bellah, Robert N., Madsen, Richard, Sullivan, William M., Swidler, Ann, & Tipton, Steven M. (1985). *Habits of the Heart: Individualism and Commitment in American Life*. New York: Perennial Library (Reprint. Originally published: Berkeley: University of California Press).
- Bellone, Carl J., & Goerl, George Frederick. (1992). Reconciling Public Entrepreneurship and Democracy. *Public Administration Review*, 52 (2)(March-April), 130-134.
- Bendix, Rienhard. (1956, 1974). *Work and Authority in Industry: Ideologies of Management in the Course of Industrialization*. Berkeley, CA: University of California Press.
- Bennett, W. Lance. (1998). The Uncivic Culture: Communication, Identity, and the Rise of Lifestyle Politics. *PS: Political Science & Politics*, 31 (1)(December).
- Berger, Peter, & Neuhaus, Richard John. (1996). *To Empower People: From State to Civil Society* ( 2nd ed.): AEI Press.
- Berman, Sheri. (1997). Civil Society and Political Institutionalization. *American Behavioral Scientist*, 40 (5)(March/April), 562-574.
- Bernstein, Peter L. (1996). *Against the Gods: The Remarkable Story of Risk*. New York: John Wiley & Sons, Inc.
- Box, Richard C. (1998). *Citizen Governance: Leading American Communities into the 21st Century*. Thousand Oaks, CA: Sage.
- Bradley, Bill. (1995). America's Challenge: Revitalizing our National Community. *National Civic Review*, 84(2)(Spring), 94-.
- CACI Marketing Systems. (1992). *The Sourcebook of County Demographics: 1990 Census Edition* ( Vol. Two). Arlington, VA: CACI.

- California. Bureau of State Audits. (1995). *Orange County: Treasurer's Investment Strategy was Excessively Risky and Violated the Public Trust*. Sacramento, CA: California Bureau of State Audit.
- California. Legislature. Assembly. Committee on Local Government. (1987). *County Fiscal Problems: A Staff Summary Report for the Joint Hearing by the Assembly Local Government Committee*. Sacramento, CA: Joint Publications.
- California. Legislature. Assembly. Committee on Local Government. (1990). *Summary of proceedings, alternatives for reforming local government finance: summary report of the interim hearing of the Assembly Local Government Committee*. Sacramento, CA: Joint Publications Office.
- California. Legislature. Joint Legislative Budget Committee. Legislative Analyst. (1998). *Why County Revenues Vary: State Laws and Local Conditions Affecting County Finance: an LAO report*. Sacramento, CA.: Legislative Analyst's Office.
- California. Legislature. Senate. Special Committee on Local Government Investments. (1995). *The Orange County Bankruptcy: Broad Repercussions, New Public Policy: Report of the Senate Special Committee on Local Government Investments*. Sacramento, CA: Senate Publications.
- California. Office of the Auditor General. (1975). *Evaluation of General Proposals to Allow State and Local Investment Authorities in California to Increase Interest Income by Temporarily Lending Investment Securities Through "Security Loans" and "Reverse Repurchase Agreements."*. Sacramento, CA: California. Office of the Auditor General.
- California. Legislature. Assembly. Local Government Committee. (1994). *Summary of Proceedings: Interim Hearing on Allocation of Sales Tax and Other Local Government Revenues: Developing Workable Incentives for Balanced Development*. Sacramento, CA.: The Assembly.
- Callender, Guy. (1998). *Twenty-five Years After Bretton Woods: Private Good or Public Good?* Paper presented at the Eleventh National Conference of the Public Administration Theory Network., Colorado Springs, Colorado.
- Cohen, Jean L. (1998). American Civil Society Talk. *Philosophy & Public Affairs*, 18 (3)(Special Issue), 14-19.
- Cohen, Joshua, & Rogers, Joel. (1992). Secondary Associations and Democratic Governance. *Politics & Society*, 20 (4)(December), 393-472.
- Coleman, James S. (1988). Social Capital in the Creation of Human Capital. *American Journal of Sociology*(94), 95-120.
- Connolly, William E. (1991). *Identity\Difference: Democratic Negotiations of Political Paradox*. Ithaca, NY: Cornell University Press.
- Coote, Anna. (1998). Risk and Public Policy: Towards a High-Trust Democracy. In J. Franklin (Ed.), *The Politics of Risk Society* (pp. 124-132). Malden, MA: Blackwell Publishers Inc.
- Council on Civil Society, & Elshstain, Jean Bethke. (1998). *A Call to Civil Society: Why Democracy Needs Moral Truths (A Report to the Nation from the Council on Civil Society)*.: Institute for American Values

University of Chicago Divinity School.

Crane, Edward. (1997). Civil Society vs. Political Society. *Vital Speeches*, 63 (20)(August 1), 615-618.

DiIulio, John J., Jr. (1997). In America's Cities: The Church and the Civil Society Sector. *The Brookings Review*, 15 (4)(Fall), 27-35.

Dionne, Jr., E. J. (1996). Why the Right is Wrong. *The Utne Reader*(May-June), 27-?

Dionne, Jr., E. J. (1997). Why Civil Society? Why Now? *The Brookings Review*, 15 (4)(Fall), 4-7.

Douglas, Mary. (1992a). An Institutional Ecology of Values. In S. Hargreaves-Heap & A. Ross (Eds.), *Understanding the Enterprise Culture: Themes in the Work of Mary Douglas* (pp. 32-40). Edinburgh: Edinburgh University Press.

Douglas, Mary. (1992b). Risk and Blame. In M. Douglas (Ed.), *Risk and Blame: Essays in Cultural Theory* (pp. 3-21). London and New York: Routledge.

Douglas, Mary. (1992c). Risk and Justice. In M. Douglas (Ed.), *Risk and Blame: Essays in Cultural Theory* (pp. 22-37). London and New York: Routledge.

Douglas, Mary. (1999). The Depoliticisation of Risk. In M. Douglas (Ed.), *Implicit Meanings: selected essays in anthropology* (2nd ed., pp. 218-230). London and New York: Routledge.

Douglas, Mary, & Wildavsky, Aaron. (1982). *Risk and Culture: An Essay on the Selection of Technical and Environmental Dangers*. Berkeley: University of California Press.

Drydyk, Jay. (1991). Capitalism, Socialism, and Civil Society. *Monist*, 74 (3)(July), 457-477.

Dryzek, John S. (1996a). *Democracy in Capitalist Times: Ideals, Limits, Struggles*. New York and Oxford: Oxford University Press.

Dryzek, John S. (1996b). Political Inclusion and the Dynamics of Democratization. *American Political Science Review*, 90 (3)(September), 475-487.

Edwards, Bob, & Foley, Michael W. (1998). Civil Society and Social Capital Beyond Putnam. *American Behavioral Scientist*, 42(1 (September)), 124-139.

Eisenberg, Pablo. (1997). A Crisis in the Nonprofit Sector. *National Civic Review*, 86 (4)(Winter), 331-241.

Elshtain, Jean Bethke. (1994). Democracy and the Politics of Difference. *The Responsible Community*, 4(2), 9-21.

Elshtain, Jean Bethke. (1995). *Democracy on Trial* ( paperback ed.). New York: BasicBooks.

Farazmand, Ali. (1999). Globalization and Public Administration. *Public Administration Review*, 59 (6)(November/December), 509-522.

Foley, Michael W., & Edwards, Bob. (1996). The Paradox of Civil Society. *Journal of Democracy*, 7(3), 38-52.

Foley, Michael W., & Edwards, Bob. (1997). Editors' Introduction: Escape From Politics? Social Theory and the Social Capital Debate. *American Behavioral Scientist*, 40(5 (March/April)), 550-561.

Franklin, Jane (Ed.). (1998). *The Politics of Risk Society*. Malden, MA: Blackwell Publishers Inc.

Fulton, William. (1996). Marian Bergeson: Working at Home. *Governing*, 60.

- Galston, William A. (1995). Liberal Virtues and the Formation of Civic Character. In M. A. Glendon & D. Blankenhorn (Eds.), *Seedbeds of Virtue: Sources of Competence, Character, and Citizenship in American Society* (pp. 35-60). Lanham, MD: Madison Books.
- Galston, William A., & Levine, Peter. (1997). America's Civic Condition. *The Brookings Review*, 15 (4)(Fall), 23-26.
- Garrett, Geoffrey, & Lange, Peter. (1996). Internationalization, Institutions and Political Change. In R. O. Keohane & H. V. Milner (Eds.), *Internationalization and Domestic Politics* (pp. 48-75). Cambridge, UK: Cambridge University Press.
- Gellner, Ernest. (1994). *Conditions of Liberty: Civil Society and its Rivals*. London: Penguin Books.
- Glendon, Mary Ann. (1997). *The Current State of the 'Civil Society' Debate*. New York City: Institute for American Values.
- Glendon, Mary Ann, & Blankenhorn, David (Eds.). (1995). *Seedbeds of Virtue: Sources of Competence, Character, and Citizenship in American Society*. Lanham, MD: Madison Books.
- Greeley, Andrew. (1997). Coleman Revisited. *American Behavioral Scientist*, 40(5 (March/April)), 587-594.
- Habermas, Jurgen. (1987). *The Theory of Communicative Action* (T. McCarthy, Trans.). Boston: Beacon Press.
- Habermas, Jurgen. (1996). *Between Facts and Norms: Contributions to a Discourse Theory of Law and Democracy* (1998 (paper) ed.). Cambridge, MA: MIT Press.
- Hacking, Ian. (1990). *The Taming of Chance*. Cambridge: Cambridge University Press.
- Hargreaves-Heap, Shaun, & Ross, Angus (Eds.). (1992). *Understanding the Enterprise Culture: Themes in the Work of Mary Douglas*. Edinburgh: Edinburgh University Press.
- Hart, David K., & Wright, N. Dale. (1998). "The Civic Good": "The Public Interest" of Civic Humanism. *Administrative Theory & Praxis*, 20 (4)(Winter), 406-421.
- Havel, Vaclav. (1985). The Power of the Powerless. In J. Keane (Ed.), *The Power of the Powerless: Citizens against the state in central-eastern Europe* (pp. 23-96). Armonk, NY: M. E. Sharpe, Inc.
- Heying, Charles H. (1997). Civic Elites and Corporate Delocalization: An Alternative Explanation for Declining Civic Engagement. *American Behavioral Scientist*, 40 (5)(March/April), 657-668.
- Hirschman, Albert O. (1986). *Rival Views of Market Society and Other Recent Essays*. New York: Viking.
- Ingraham, Patricia W., Romzek, Barbara S. , & Associates, and (Eds.). (1994). *New Paradigms for Government: Issues for the Changing Public Service*. San Francisco: Jossey-Bass.
- Jorion, Philippe. (1995). *Big Bets Gone Bad: Derivatives and Bankruptcy in Orange County*. San Diego, CA: Academic Press.
- Keohane, Robert O. (1984). *After Hegemony: Cooperation and Discord in the World Political Economy*. Princeton, NJ: Princeton University Press.
- Keohane, Robert O. , & Milner, Helen V. (Eds.). (1996). *Internationalization and Domestic Politics*. Cambridge, UK: Cambridge University Press.

- King, Cheryl Simrell, & Stivers, Camilla. (1998). *Government Is Us: Public Administration in an Anti-Government Era*. Thousand Oaks, CA.: Sage.
- Krasner, Stephen D. (Ed.). (1983). *International Regimes*. Ithaca, NY: Cornell University Press.
- Lemann, Nicholas. (1996). Kicking in Groups. *The Atlantic Monthly*, 227 (4)(April), 22-26.
- Lowi, Theodore J. (1990). Risks and Rights in the History of American Governments. *Daedalus*, 119(4)(Fall), 17-40.
- Markovits, Andrei, & Silverstein, Mark. (1988). *The Politics of Scandal: Power and Process in Liberal Democracies*. New York: Holmes & Meier Publishers, Inc. p. vii.
- McCarthy, Ed. (1999). Derivatives Revisited. *Journal of Accountancy*, 189 (5), 35-43.
- Melchior, Alan C. (1998). Public Entrepreneurism: A New Paradigm for Public Administration? In T. D. Lynch & T. J. Dicker (Eds.), *Handbook of Organization Theory and Management: The Philosophical Approach* (pp. 441-463). New York: Marcel Dekker, Inc.
- Miller, Danny. (1990). *The Icarus Paradox: how exceptional companies bring about their own downfall: new lessons in the dynamics of corporate success, decline, and renewal*. New York?: HarperBusiness.
- Minkoff, Debra C. (1997). Producing Social Capital: National Social Movements and Civil Society. *American Behavioral Scientist*, 40(5 (March/April)), 606-619.
- Morgan, Gareth. (1997). *Images of Organization*. Thousand Oaks, CA: Sage Publications.
- National Commission on Civic Renewal, Bennett, William, & Nunn, Sam. (1998). *A Nation of Spectators: How Civic Disengagement Weakens America and What We Can Do About It, Final Report of the National Commission on Civic Renewal*. College Park, MD: National Commission on Civic Renewal.
- National Research Council. (1983). *Risk Assessment in the Federal Government: Managing the Process*. Washington, D.C.: National Academy Press.
- National Research Council, Committee on Risk Assessment of Hazardous Air Pollutants, Board on Environmental Studies and Toxicology,. (1994a). *Building Consensus Through Risk Assessment and Management of the Department of Energy's Environmental Remediation Program*. Washington, D.C.: National Academy Press.
- National Research Council, Committee on Risk Assessment of Hazardous Air Pollutants, Board on Environmental Studies and Toxicology,. (1994b). *Science and Judgment in Risk Assessment*. Washington, D.C.: National Academy Press.
- National Research Council, Committee on Risk Perception and Communication. (1989). *Improving Risk Communication*. Washington, D.C.: National Academy Press.
- Newton, Kenneth. (1997). Social Capital and Democracy. *American Behavioral Scientist*, 40(5 (March/April)), 575-586.
- O'Connell, Brian. (1995). Impact of Nonprofits on Civil Society. *National Civic Review*(Spring), 126-129.
- O'Connell, Brian. (1996). A Major Transfer of Government Responsibility to Voluntary Organizations? Proceed with Caution. *Public Administration Review*, 56 (3)(May/June), 222-225.
- Olson, Mancur. (1982). *The Rise and Decline of Nations*. New Haven: Yale University Press.
- Partnoy, Frank. (1997). *F.I.A.S.CO.: Blood in the Water on Wall Street*. New York, N.Y.: W. W. Norton & Company.

- Powers, Mark J., & Castelino, Mark G. (1991). *Inside the Financial Futures Market* ( Third ed.). New York, N.Y.: John Wiley & Sons, Inc.
- Putnam, Robert D. (1993). *Making Democracy Work: Civic Traditions in Modern Italy*. Princeton, NJ: Princeton University Press.
- Putnam, Robert D. (1995a). Bowling Alone: America's Declining Social Capital. *Journal of Democracy*(January), 3-9.
- Putnam, Robert D. (1995b). Bowling Alone Revisited. *Responsive Community*, 5(2).
- Putnam, Robert D. (1996). The Strange Disappearance of Civic America. *The American Prospect*, 24(Winter), 34-48.
- Putnam, Robert D. (2000). *Bowling Alone: The Collapse and Revival of American Community*. New York: Simon & Schuster.
- Riessman, Frank, & Banks, Erik. (1996). The Mismeasure of Civil Society. *Social Policy*, 26 (3)(Spring), 2-5.
- Salamon, Lester M., & Anheier, Helmut K. (1997). The Civil Society Sector. *Society*(January/February), 60-65.
- Sandel, Michael J. (1996a). America's Search for a New Public Philosophy. *The Atlantic Monthly*(March), 57-71.
- Sandel, Michael J. (1996b). *Democracy's Discontent: America in Search of a Public Philosophy*. Cambridge, MA: Belknap Press of Harvard University Press.
- Sandel, Michael J. (1996c). The Politics of Community: Robert F. Kennedy versus Ronald Reagan. *The Responsive Community*, 6 (2)(Spring), 14-27.
- Scott, W. Richard. (1995). *Institutions and Organizations*. Thousand Oaks, CA: Sage.
- Seligman, Adam. (1992). *The Idea of Civil Society*. Princeton, NJ: Princeton University Press.
- Skocpol, Theda. (1996). Unraveling From Above. *The American Prospect*(March-April).
- Skocpol, Theda. (1997a). Building Community: Top-Down or Bottom-Up? *The Brookings Review*, 15 (4)(Fall), 16-22.
- Skocpol, Theda. (1997b). The Tocqueville Problem. *Social Science History*, 21 (4)(Winter), 455-479.
- Sokolow, Alvin D. (1993). State Rules and the County-City Arena: Competition for Land and Taxes in California's Central Valley. *Publius: The Journal of Federalism*, 23(Winter), 53-69.
- Stern, Paul C., & Fineberg, Harvey V. (1996). *Understanding Risk: Informing Decisions in a Democratic Society*. Washington, D.C.: National Academy Press.
- Stivers, Camilla. (1990). Active Citizenship and Public Administration. In G. e. a. Wamsley (Ed.), *Refounding Public Administration* (pp. 246-273). Newbury Park, CA: Sage.
- Stivers, Camilla. (1994). The Listening Bureaucrat: Responsiveness in public administration. *Public Administration Review*, 54(4 (July-August)), 364-369.
- Stolle, Dietlind, & Roche, Thomas R. (1998). Are All Associations Alike? Member Diversity, Associational Type, and the Creation of Social Capital. *American Behavioral Scientist*, 42 (1)(September), 47-65.

- Taylor, Charles. (1989). *Sources of the Self: The Making of Modern Identity*. Cambridge, MA: Harvard University Press.
- Taylor, Charles. (1990). Modes of Civil Society. *Public Culture: Bulletin of the Project for Transnational Cultural Studies*, 3(1 (Fall 1990)), 95-118.
- Tocqueville, Alexis de. (1990). *Democracy in America* (H. R. a. r. b. F. Bowen, Trans. Vintage Books Edition ed.). New York: Vintage Books.
- Volcker, Paul A., & Gyohten, Toyoo. (1992). *Changing Fortunes: The World's Money and the Threat to American Leadership*. New York, NY: Times Books.
- Walzer, Michael. (1991). The Idea of Civil Society. *Dissent*(Spring), 293-304.
- Walzer, Michael. (1992). The Civil Society Argument. In C. Mouffe (Ed.), *Dimensions of Radical Democracy: Pluralism, Citizenship, Community* (pp. 89-107). London: Verso.
- Walzer, Michael. (1994). Multiculturalism and Individualism. *Dissent*(Spring), 185-191.
- Walzer, Michael. (1999). Rescuing Civil Society. *Dissent*(Winter), 62-67.
- Wamsley, Gary L., Bacher, Robert N., Goodsell, Charles T., Kronenberg, Philip S., Rohr, John A., Stivers, Camilla M., White, Orion F., & Wolf, James F. (Eds.). (1990). *Refounding Public Administration*. Newbury Park, CA: Sage Publications.
- Wamsley, Gary L., & Wolf, James F. (Eds.). (1996). *Refounding Democratic Public Administration: Modern Paradoxes, Postmodern Challenges*. Thousand Oaks, CA: Sage Publications.
- White, Orion F. (1998). Seminar: Understanding Civil Society. Unpublished Seminar Notes.
- Whittington, Keith E. (1998). Revisiting Tocqueville's America: Society, Politics, and Association in the Nineteenth Century. *American Behavioral Scientist*, 42(1 (September)), 21-32.
- Will, Susan, Pontell, Henry N., & Cheung, Richard. (1998). Risky business revisited: white-collar crime and the Orange County (California) bankruptcy. *Crime and Delinquency*, 44(3)(July), 367-388.
- Wilson, James Q. (1995). Liberalism, Modernism, and the Good Life. In M. A. Glendon & D. Blankenhorn (Eds.), *Seedbeds of Virtue: Sources of Competence, Character and Citizenship in American Society* (pp. 17-34). Lanham, MD: Madison Books.
- Wolfe, Alan. (1989). *Whose Keeper? Social Science and Moral Obligation*. Berkeley, CA: University of California Press.
- Wolfe, Alan. (1997). Is Civil Society Obsolete? Revisiting Predictions of the Decline of Civil Society in *Whose Keeper? The Brookings Review*, 15 (4)(Fall), 9-12.

Susan Hardie MacDonald

Home

1021 Tornell Avenue  
Turlock, CA 95382  
tel: (209) 669-1517  
e-mail: smacdonall@mac.com

Office:

Dept. of Politics & Public Administration  
California State University—Stanislaus  
801 W. Monte Vista Avenue  
Turlock, CA 95382  
e-mail: SMacDONALD@stan.csustan.edu  
tel: (209) 667-3291 (direct)  
(209) 667-3388 (office)  
fax: (209) 667-3724

**Education**

Ph.D. Public Administration and Public Affairs  
August 2000 Virginia Polytechnic Institute & State University (Virginia Tech)  
Blacksburg, Virginia  
Dissertation: Alternative Responses to the Orange County Bankruptcy: An Inquiry into the Images Underlying Theory

M.A. Liberal Studies  
1989 Duke University, Durham, North Carolina  
Thesis: Dilemmas of Developing Country Debt

M.L.S. Library Science  
1972 University of Denver, Denver, Colorado  
Thesis: Qualitative Content Analysis of Catalog Use Studies

B.A. History  
1970 University of Wisconsin, Madison, Wisconsin

**Career History**

August 1999 – Assistant Professor, Department of Politics and Public Administration,  
Present California State University—Stanislaus.  
Responsible for teaching budgeting and other courses in the MPA program as well as undergraduate courses in Political Science.

August 1997 – Graduate Teaching Assistant, Center for Public Administration & Policy.  
May 1999 Responsible for assisting the director in the organization of center activities, including creating databases to automate the center's student directory and course offerings across four campuses, and organizing center projects under the director.

### **Career History (continued)**

August 1996 – Instructor, Department of Political Science, Virginia Tech.

May 1998     Responsible for the smaller sections of Introduction to American Government (average class size was 45 students).

July 1994 -     Graduate Assistant, Center for Public Administration & Policy.

May 1996     Responsible for coordinating the visits of Dutch officials and students as part of an exchange agreement with the Netherlands School of Government.

Sept. 1990 -   Research Associate, Office of the Provost, Virginia Tech.

June 1994     Responsible for coordinating searches for nine deans and vice presidents reporting to the Provost, and for other miscellaneous duties including, but not restricted to, staffing the five year review of deans and revision of the *Faculty Handbook*.

1987 -         Assistant Provost, Duke University.

Aug. 1990     Responsibilities included the design and oversight of a faculty database with information on faculty appointment terms, salaries, leaves and other employment data; staffing the Academic Priorities Committee and Trustee Committee on Academic Affairs; representation of Duke University at the AAU Data Exchange and Higher Education Data Sharing Consortium (HEDS); oversight of miscellaneous institutional research projects, including faculty teaching effort reports, annual salary comparisons, and race/gender analyses; as well as maintenance of the *Faculty Handbook*.

1979 - 1987   Executive Assistant to the Provost; Duke University.

Responsibilities included editing the *Faculty Newsletter* and *Faculty Handbook*; supervision of the University Bulletins Office; and staffing the Provost's Long Range Planning Committee, Academic Affairs Committee of the Board of Trustees, Deans' Council, and Provost Staff Committee.

1976 - 1979   Head, Public Documents and Maps Department

Perkins Library, Duke University.

Responsibilities included administration of public and technical services in the Public Documents and Maps Department at Perkins Library with one professional and three clerical staff in addition to numerous student assistants; service on the Library's Long Range Planning Committee and chair of the Public Services Task Force of that committee; and Chair, Joint Faculty-Staff Screening Committee for a new Collection Development Officer.

### **Career History (continued)**

1973 – 1976 Head, Public Documents Department

Miami University Libraries, Oxford, Ohio.

Responsibilities included administration of public and technical services in the Public Documents Department whose collections included federal, state and local documents as well as a federal and state law collection.

1972 – 1973 Assistant Documents Librarian, Public Documents Department

Miami University Libraries, Oxford, Ohio.

### **Publications**

MacDonald, Susan H. and Janet Prolman (1978) *Centralized Access to Municipal Information in the City of Durham*, National League of Cities, Lexington, Ky.

MacDonald, Susan H. and Charles Sieger (1978) "GPO Micropublishing-an Historical Review and Critical Analysis" in *Library Acquisitions: Practice and Theory* v.2 pp. 33-44.

MacDonald, Susan H. (1976) "Municipal and Local Publications" in *Draft Syllabus of Resources for Teaching Government Publications* Education Task Force, Government Documents Roundtable, American Library Association, Chicago, Ill.

MacDonald, Susan H., Joanne Tortoriello and Jeanne Sears (1975) *Ohio Documents Classification Scheme 1803-1974*. State Library of Ohio, Columbus, Ohio. (260 p.)

### **Honors**

Duke University Award for Merit for Exemplary Service to the University: July 1, 1976-August 31, 1990

Administrative Tenure, Duke University Library, 1979

Administrative Tenure, Miami University Library, 1976

Beta Phi Mu Library Honorary Society, 1972

### **Professional Affiliations**

Member, American Society for Public Administration, 1994-

Member, Public Administration Theory Network, 1996-

### **Other Professional Activities**

Invited lecture, Center for Public Administration and Policy's Ph.D. Forum: "John Dryzek's *Democracy in Capitalist Times* and Its Implications for Public Administration," March, 1998.

Presented the Honorific Student Toast at CPAP's Annual High Table Celebration of the Life of the Mind: Spring, 1997.

Guest Lecturer, Public Budgeting and Finance course by Professor Gary Wamsley; spoke on cash management and the Orange County bankruptcy: Spring 1996, 1997, and 1998.

Guest Lecturer, Public Administration Theory course by Professor Gary Wamsley: Fall 1998.

**Other Professional Activities (continued)**

Member of the Higher Education Data Sharing Consortium (HEDS) Board of Advisors (1988-90)

Coordinated preparation of 1987 Academic Plan for Duke University

Coordinator of the 1984 Third World Conference sponsored by the Provost Office, Duke University

Member 1972-79 American Library Association with active involvement in Godort (Government Documents Roundtable)

Spring, 1978 Lecturer in Government Documents, North Carolina Central University

Fall, 1977 Consultant to the City of Durham, North Carolina regarding the creation of a municipal documents collection

Spring, 1976 Guest lecturer on Government Documents, Ohio Library Association

Spring, 1974 Consultant, City of Middletown, Ohio regarding their government documents collection

**Research Interests**

Tension between private and public sector values

Public Budgeting and Finance, especially Cash Management

Internationalization, the global economy, and local government

Citizen participation and democratic theory

Process theory and pragmatism

Organization and Public Administration Theory

Critical theory and discourse theory

**Other Skills**

Competent in French; reading ability of Spanish; exposure to German and Greek (Attic dialect)

Familiarity with Pascal programming language

Ability to work with both IBM compatible and Macintosh computers, including database applications.

Familiarity with software applications such as powerpoint and experience with their use in the classroom.

Familiarity with web page construction and the internet