

STRUCTURE OF ORGANIZATIONS FOR PRODUCTION OF PUBLIC AND PRIVATE GOODS

Shyam Sunder
Graduate School of Industrial Administration
Carnegie Mellon University
Schenley Park
Pittsburgh PA 15213
(412) 268 2103
(412) 268 6837 Fax
sunder@cmu.edu

Abstract

Business organizations produce and sell private goods for a price. Since their customers, if not satisfied by the product, can withhold revenue, it is possible for the shareholders to control the performance of hired managers through residual net income-based contracts. Public good organizations, on the other hand, have beneficiaries, who have no simple and direct way of imposing a comparable discipline on the managers. This weakness, even absence, of the product market discipline greatly complicates the task of establishing effective management control in public good organizations. Weber's model of bureaucracy is close to the best one can do to accomplish the more arduous task of efficiently producing public goods. It is hardly surprising that a quarter century of efforts, since the New York City bankruptcy, toward harmonizing the organizational designs for public and private good producing organizations have borne little fruit. Barnard and Simon's view of organizations as a set of contracts among various participants provides a useful platform for building a unified theory to compare and contrast the design of public and private good organizations.