

## **Allocation, redistribution, and public choice**

Some men look at constitutions with sanctimonious reverence, and deem them like the ark of the covenant, too sacred to be touched. They ascribe to the men of the preceding age a wisdom more than human, and suppose what they did to be beyond amendment. I knew that age well; I belonged to it; and labored with it. It deserved well of its country. It was very like the present, but without the experience of the present; and forty years of experience in government is worth a century of book-reading; and this they would say themselves, were they to rise from the dead. I am certainly not an advocate for frequent and untried changes in laws and constitutions. I think moderate imperfections had better be borne with; because, when once known, we accommodate ourselves to them, and find practical means of correcting their ill effects. But I know also, that laws and institutions must go hand in hand with the progress of the human mind. As that becomes more developed, more enlightened, as new discoveries are made, new truths disclosed, and manners and opinions change with the change of circumstances, institutions must advance also, and keep pace with the times. We might as well require a man to wear still the coat which fitted him when a boy, as civilized society to remain ever under the regimen of their barbarous ancestors.

Thomas Jefferson

Rules for collective decision are needed, quite simply, because people live together. Their mere grouping into circumscribed geographic areas creates the potential and necessity for collective action. Some collective decisions can benefit all individuals involved; other decisions benefit only some. Even when everyone benefits, some do so more than others, raising an issue of how the “gains from trade” are shared. Thus, collective choices can be grouped into two categories: those benefiting all members of the community and those benefiting some and hurting others. These two categories correspond to the familiar distinction between moves from off the Pareto frontier to points on it and moves along the frontier – that is, to allocation and redistribution.

The potential to make collective decisions benefiting all members of a community has undoubtedly existed for as long as it has been legitimate to call a group of humans living in proximity to one another a community. So, too, has the potential for redistribution. Did the state come into existence to enable its members to better achieve the allocative efficiency gains that social organization and technology made possible? Did the state come into existence so that some members of the community could exploit their neighbors? Does the modern state grow by providing an

ever-increasing amount of collective benefits to the community, or does its growth reflect an escalating series of programs for transferring wealth from one segment of the community to another? Do the rent-seeking and wealth-transferring efforts of different groups in society stifle the potential for making moves that benefit all society? These questions have puzzled anthropologists, economists, and political scientists. They lie at the heart of the public choice literature.

It was one of Wicksell's (1896) great insights to recognize the importance of the distinction between allocation and redistribution decisions, *and* to recognize the need to make these decisions by separate voting procedures. More fundamentally, his contribution to the literature can be seen as the recognition that the characteristics of the outcomes of government action, the allocation or redistribution decisions, cannot be discussed without taking into account the inputs from the citizens via the voting process bringing these outcomes about. This latter contribution was virtually ignored by the profession for half a century until the public choice literature began to appear. It may be regarded as one of the cornerstone postulates of this literature.

Although Wicksell made use of the distinction between allocation and redistribution decisions, his analysis focused on the former. The redistribution decisions were assumed to have been justly decided at some prior point in time. This left only the allocative efficiency improvements to resolve, decisions of potential benefit to all. Here Wicksell's work takes on a distinctly contractarian and individualistic tone. Each citizen takes part in the collective decision process to advance his own ends, and via the quid pro quo of collective decision-making outcomes are reached to the mutual benefit of all. Voting achieves in the market for public goods the same outcome as exchange achieves in markets for private goods. This contractarian, quid pro quo approach to government has underlain much of public choice and the public expenditure theory of public finance, most visibly in the work of Buchanan and Musgrave.

Often this literature takes on a very optimistic tone concerning the potential of collective decision making. In *The Calculus of Consent* Buchanan and Tullock describe government institutions that bear more than a passing resemblance to those of the United States and that seem capable of satisfying a society's collective wants. Redistribution decisions are separated from allocative efficiency decisions, however, and unanimously resolved at the constitutional stage. Thus, the day-to-day work of parliament is limited to deciding those issues in which unanimity is potentially possible. In the past 30 years several new and "superior" voting procedures have been put forward. All have attractive properties that seem to circumvent most if not all of the paradoxes of collective choice. All are capable of achieving this magic only when limited to deciding allocative efficiency improvements.

The literature that focuses upon redistribution, or ignores the distinction between redistribution and allocation, thereby implicitly combining the two, has a discernibly more pessimistic tone. Equilibria do not exist. Their absence enables agenda setters to dictate outcomes. Outcomes of all voting procedures can be manipulated by strategic misrepresentation of preferences unless someone is allowed to be dictator. Outcomes may be Pareto inefficient. The mood of this new "dismal" science is accurately captured by Riker (1982b). It is interesting to note that while Green and

Shapiro (1994) cite Arrow's work in their attack on the rational choice approach to politics, Riker, one of this approach's strongest proponents, makes heavy reference to the Arrow impossibility theorem and subsequent developments in the social choice literature to question, if not attack, "populist democracy." Majoritarian democracy cannot produce outcomes that maximize any sort of SWF that satisfy "the will of the people"; the most that society can hope for is to develop and maintain political institutions capable of deposing bad leadership – some of the time.

It is difficult to reject Riker's pessimistic interpretation of the implications of the social-public choice literature. Moreover, his examples and countless others that one could present illustrate too vividly that the instabilities, inefficiencies, manipulated agendas, and other diseases of democratic decision making, which public choice predicts, do sometimes occur. But I am reluctant to write off the achievements of the first 50 years of public choice as a catalogue of the deficiencies of democratic decision making. There are strands in this literature that suggest a more optimistic picture, a picture perhaps more of what might be than of what is. We close by sketching this picture.

To begin with, one must distinguish between decisions to improve allocative efficiency and to redistribute income and wealth. Certainly one of the major achievements of the public choice literature has been to underline the importance of this distinction first recognized by Wicksell. Not to make use of it when designing political institutions is to handicap the exercise from the start. Second, one must distinguish clearly between designing institutions for direct democracy and designing institutions for electoral politics.

Nowhere is the importance of the distinction between allocative efficiency and redistribution made more vivid than in the literature on clubs and voting-with-the-feet. Allocative efficiency can be improved when individuals with homogeneous tastes for bundles of public goods form clubs and local polities. When local polities attempt to provide redistribution programs and other programs unwanted by some taxpayers, individuals vote with their feet and move to communities where such programs do not exist. In a mobile society significant amounts of redistribution at the local level cannot occur if those who must pay for the redistribution are unwilling to do so. Just as redistribution proposals would be screened out under a unanimity rule leaving only proposals to improve allocative efficiency, the unanimity achieved silently through voting-with-the-feet eliminates redistribution programs from local budgets. If significant redistribution is to occur, it must take place at higher levels of government.

Much of the pessimism regarding the potential of democratic institutions stems from Arrow's theorem and the flood of theorems in its aftermath. The objective of Arrow's search was to find an SWF that based its rankings of alternatives on the aggregation of individual ordinal rankings. That none was found indicates that interpersonal utility comparisons must be made either directly via the decision rule, or indirectly through restrictions placed on the preference domain or the types of issues that can be decided.

The same conclusion emerges from the literature on real-valued welfare functions. Ordinal utility functions plus the Pareto postulate do not allow one to choose

from among the set of points along the Pareto frontier. To make such a choice, additional postulates must be introduced incorporating stronger value judgments than contained in the Pareto postulate. Most writers have shied away from making these additional value judgments and have stopped short of defining an SWF that will select from among the Pareto-preferred set. Those who have introduced additional value postulates, for example, Harsanyi (1955) and Ng (1975), have invariably come up with additive SWFs whose arguments are the cardinal, interpersonally comparable utilities of the citizens.

Several of the new voting procedures aggregate cardinal utility information supplied by the voters (the demand revelation process, Smith's auction process, Hylland and Zeckhauser's point voting). If their use is restricted to decisions that could improve allocative efficiency, then they contain the potential for achieving Pareto-optimal allocations of resources. Experimental work and some limited applications indicate that they can work as theory predicts. Although each is potentially vulnerable to strategic and coalitional manipulation, such strategic behavior is both complicated and risky. The extent to which these procedures would be manipulated needs to be demonstrated experimentally rather than assumed on the basis of hypothetical examples and impossibility proofs. Voting by veto is strategy-proof and relies only on ordinal utility information. It thus provides another option for achieving a Pareto-optimal allocation of resources in deciding public good-externality issues, an option that would allow one to avoid the implicit weighting of cardinal utilities in proportion to initial incomes inherent in the demand revelation and auction procedures. Even a two-thirds (64 percent) majority rule can avoid cycles and achieve Pareto-optimal allocations *if* its use is restricted to certain classes of allocative efficiency issues like choosing public goods quantities when tax rates are fixed.

These voting procedures all assume that voting is by those whose welfare is affected by the outcomes of the voting process, as in a direct democracy. Were these procedures to be employed by a committee of representatives, then these representatives should be chosen in such a way that each group of citizens is represented in proportion to their number in the polity. A form of proportional representation is required. To ensure that the representatives do vote in accordance with the preferences of those they represent, their (re)election should depend on their record of voting on the public good-externality issues to be decided. The function of choosing a government (executive) should be separated from that of deciding allocative efficiency issues. Under such a reform the ideal proportional representation system would differ from those now extant. So be it. The proportional representation systems functioning today reflect the best ideas of political theorists of a century and a half ago. We know more today than we did then. We know that deciding levels of national defense, police protection, and other public goods are positive-sum games in which all can possibly gain. Forming a cabinet by majority rule is a zero-sum game in which nearly half of the parties represented must lose. The same institution and voting rule are not optimal for both tasks.<sup>1</sup>

<sup>1</sup> For further discussion see Mueller (1996a, chs. 8–10).

If one assumes that political institutions can be designed to reveal preferences on allocative efficiency changes adequately, the question remains how to resolve redistributive questions. In answering this question it is again critical to recognize that the procedures required are different from those employed for allocative efficiency gains. Beyond this important insight, the public choice literature points in two distinct directions. First, the uncertainty inherent in the long-run nature of constitutional decisions can induce individuals, out of self-interest, to incorporate certain redistributive measures and the protection of civil liberties into the constitution. The potential for this kind of redistribution could be enhanced by organizing a constitutional convention in such a way as to maximize uncertainty over future positions or impartiality (e.g., have the constitution not go into effect until several years after ratification). Parliaments could be freed to concentrate on allocative efficiency improvements by confining redistributive measures to constitutional guarantees.

The literature on majority rule suggests a second way of handling redistributive property rights issues. When these issues are of a binary nature and equal intensities can be assumed by individuals on both sides, then majority rule can be an attractive rule for settling distributive questions. The requirement that issues be binary immediately suggests a court of law, and the Supreme Court in the United States has used majority rule to resolve distributive questions (e.g., abortion and desegregation of schools). Other institutional arrangements can be envisaged once one recognizes the need to resolve redistributive questions using a procedure different from that used for allocative efficiency improvements.

An alternative to institutionally separating allocative efficiency and redistribution issues and allowing the citizens to decide them directly is to limit the citizen's role to that of selecting an agent or set of agents, and to have the agent(s) decide the issues. The models of Chapters 11 and 12 are relevant here, and this literature contains a more optimistic view of the results of voting than does the literature on committee voting in the Arrow tradition. When voting is limited to a pair of candidates or parties that compete for the privilege of running (forming) the government, an equilibrium pair of platforms exists (Chapter 12). The properties of this equilibrium (Pareto optimality, the maximization of a particular SWF) are not obviously inferior to those achieved by (claimed for) the market, or to those one might reasonably demand of a collective choice process. These results place the outcomes from collective decision procedures in a radically different light.

There is much evidence consistent with this model of electoral competition. Although the cycling literature implies that a candidate forced to run on her record is always doomed to defeat, incumbents generally face much better odds. The evidence reviewed in Chapters 12, 15, 19, and 20 indicates that intense efforts are made by candidates to win votes, and by interest groups to influence candidates. Political competition is real and results in predictable and stable outcomes with reasonable normative properties. Wittman (1995) goes so far as to argue that political competition produces the same sorts of efficient outcomes as market competition does. Breton (1996) makes similar claims placing heavy emphasis upon the competition among governments that exists in federalist systems.

Competition between candidates increasingly takes the form of spending money to “buy” votes. This money comes from interest groups that seek to “buy” legislation. The weights given to individual utilities in the SWF that political competition maximizes depend on the resources and organizational skills of the interest groups to which individuals belong. Although the process of competition for votes may achieve a welfare maximum of sorts, it is not necessarily one in which all will be happy with the weights their interests receive in the resulting equilibrium.

Moreover, the money candidates spend does not really buy votes. It buys television commercials, posters, placards and buttons, pollsters, canvassers, and consultants. It buys all of the instruments that modern marketing can devise to influence how an individual votes on election day. But in the end it is the decision the voter makes that determines the outcome of the election. The quality of these outcomes rests on the quality of this choice.

An important implication of the rational choice approach to politics is that it is irrational for an individual to vote if the act of voting is predicated on the assumption that the individual’s vote will affect the outcome of the election. Given this observation, voting must be explained as satisfying some motivation of individuals other than one directly tied to the outcomes of the election. Several hypotheses have been put forward that do not rely on the assumption that the voter believes that her vote will “make a difference.” None of these hypotheses guarantees, however, that voters gather sufficient information to make a discriminating choice. Nor is the “information” supplied to them by the candidates likely to aid in this task. Candidate competition may lead to an equilibrium set of platforms defined over an “issue” space, but the nature of the issues over which this competition takes place is undefined; thus, also, is the significance of the welfare maximum achieved through this competition.

The candidate competition models help to dispel concern over the existence of an equilibrium in policy space. They raise questions, however, about the nature of the policy space over which competition takes place, and about the weights given to individual preferences in the welfare function that this competition implicitly maximizes. More generally, they suggest that the emphasis in public choice research needs to shift from the outputs of the political process to its inputs, to shift from an emphasis upon the quality of the aggregation process to what it is that is being aggregated.<sup>2</sup> Much of the public choice literature has analyzed outcomes of procedures in which each individual’s vote(s) receives equal weight and all voters are well informed about the issues. But in representative democracies, rules of representation and the nature of competition give radically different weights to voter interests, and these are often poorly defined and expressed.

Thus, a number of important issues in public choice require further research. In its first 50 years, a rich harvest of results has been brought forth. Most do seem to be rather disheartening descriptions of how political institutions function and malfunction. But I have tried to suggest that there is also a brighter side to the public choice literature. Some parts offer insights into when and why political institutions work well.

<sup>2</sup> See Sen (1995) and Schofield (1996b).

Other parts make proposals to improve the performance of political institutions. To some, this latter literature will appear utopian. And so it is. But the constitutional governments of Switzerland and the United States today would have seemed utopian to a vassal living in Europe during the Middle Ages, and even today must seem utopian to some citizens living under autocracy and other nondemocratic forms of government.

Indeed, what is most utopian of all is the idea that knowledge is cumulative, and that from a knowledge of past mistakes we can design institutions that will avoid similar mistakes in the future. Public choice does provide us with this knowledge. Because of this, I remain optimistic not only about the ability of the field to continue to attract fine scholars, and about the ability of these scholars using the methodology of public choice to make contributions of high quality to the scientific study of politics, but I even am optimistic that this research may someday help to improve the democratic institutions by which we govern ourselves.