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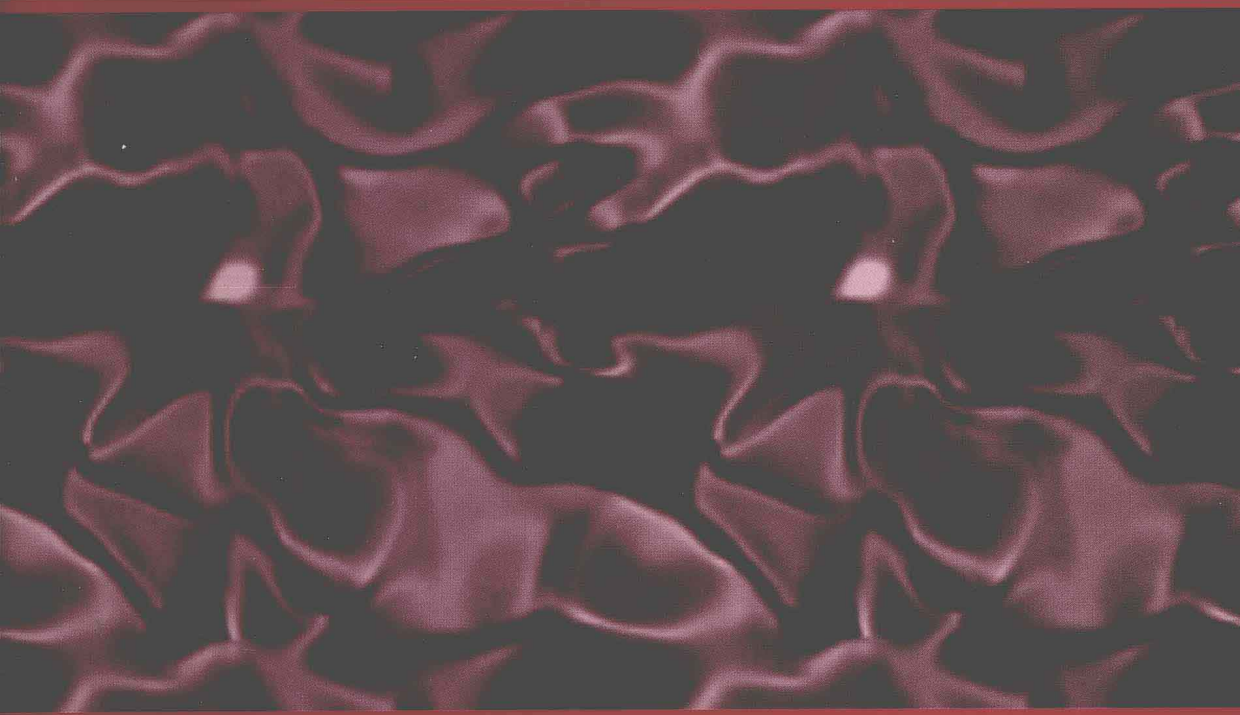
Public Choice and Public Law

Edited by **Daniel A. Farber**



ECONOMIC APPROACHES TO LAW 6

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Edited by

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Introduction

Daniel A. Farber

Public choice theory is, essentially, the application of economic reasoning to political institutions. It has become an increasingly significant aspect of public law scholarship in the United States.[1] Public law concerns the governance of public institutions and their activities. Thus, a deeper understanding of those institutions can illuminate our understanding of how legal rules shape the behavior of those institutions. This volume collects key papers in the evolution of this subject, with the aim of giving the reader a firm grasp of the fundamental issues in the field.

The articles reprinted in this book introduce readers to the main themes of public choice scholarship as applied to law. To include all of the best-known articles would take two or three volumes this size, especially given the propensity of American law professors to publish monograph-length works in article form. In addition to work by legal academics, the literature also includes contributions from competing schools of economists and political scientists, who share a basic conception of rational political choice but use the concept as the basis for very different models. Including representatives of every school of thought would be desirable but difficult. Apart from methodological differences, there are also sharp disagreements about the overall role of government in society, which are then reflected in approaches to modeling, empirical work, and normative conclusions. In short, in a relatively short time, the field has developed a very broad and diverse body of scholarship.

Since full coverage is impossible, the selections are designed to introduce readers to the most relevant issues. They are also chosen to represent diverse perspectives within public choice theory. I have also tried to include a mix of classic articles and more recent contributions. Most of the articles are seminal works in the field; the exceptions were chosen because they synthesize a leading author's previous work or contain particularly useful surveys of relevant literature. Of course, as with any selection of this kind, the results partly reflect a particular viewpoint about which issues are the most important and which bodies of inquiry the most fruitful.

For the benefit of readers who are unfamiliar with public choice, this introduction will begin with a brief survey of some key concepts, then turn to a discussion of what kinds of legal problems are most likely to be illuminated by public choice theory. I will then briefly survey the papers in this book and then close with a few comments on the normative implications of public choice.

I. Foundations of Public Choice Theory

The key assumption underlying the field is economic rationality. In other words, political actors are presumed to behave rationally in the sense of maximizing the value to them of

political outcomes (whether in terms of public or personal interests), taking into account both the costs and benefits of political activities. There are, clearly, possible alternatives to this view: political actors may attempt to optimize outcomes but suffer from systematic cognitive defects; their goals may be too conflicting, incoherent, or unstable for optimizing to be possible; they may be driven by such strong cultural or emotional currents that they are incapable of thinking rationally about consequences; or they may be rational but in some noninstrumentalist sense, perhaps following religious or ethical edicts such as Kant's. Notwithstanding these potential alternatives, public choice theory rests on the premise that instrumental rationality is, if not an entirely realistic psychological model, at least an effective basis for predicting political behavior.[2]

Like public choice, microeconomics also takes economic rationality as a starting point. But there is an important difference in how public choice and microeconomics develop this assumption. Microeconomics centers on a vision of institutional success – the ability of markets to efficiently allocate production and consumption. Of course, market failures are an important topic, but they are conceptualized as exceptional rather than pervasive. In contrast, public choice theory centers on the defects of governmental institutions; the central stories involve institutional failure rather than success. This is in part a reflection of the history of the field, but it also reflects the inherently greater difficulty of the task faced by government, which is to deal with the collective action problems posed by public goods.

Public choice theorists have focused on two distinct difficulties in collection action. The first relates to the incentive for free-riding, which impedes efforts to organize political groups. Interest group theories of government focus on this issue. The second difficulty faced by governmental institutions relates to the inherent, mathematically inescapable limits of mechanisms for making group decisions. This difficulty is the subject of social choice theory, beginning with Arrow's Theorem and its implication.

The free-rider problem is easy to explain. A rational person would prefer to avoid investing in the production of a benefit if virtually the same benefit can be enjoyed without making the investment. This simple point has manifold implications in economics, ranging from the instability of cartels (because individual members of the cartel have an incentive to cheat) to the inadequate market supply for public goods such as clean air (because individuals prefer to enjoy the clean air without having to pay for the pollution control equipment). Legislative enactments may benefit everyone in a group, perhaps everyone in society, but the statute's benefits can be enjoyed by everyone once the statute is passed even without having contributed to the lobbying effort. Hence, there is an incentive to free-ride by letting other people pay the price of obtaining the new legislation.

As it turns out, the free-rider problem is often inversely related to the size of the group. For instance, when the issue is air pollution, it is much easier to mobilize a handful of car companies than the millions of individuals who are affected by automobile pollution. The result is a skew in politics, giving relatively greater influence to 'special interests' (relatively concentrated groups with high individual stakes) than to the diffuse interests of taxpayers, consumers, and citizens generally. Earlier, more optimistic, views of the political process posited that all groups would be represented in proportion to the strength of their interests, making politics an accurate gauge of social welfare. But interest group theory suggests that some groups have inherent political advantages and will exploit those advantages contrary to general interests of society.

The other root of public choice theory requires more explanation because it rests on some subtle mathematical reasoning. Arrow's Theorem provides the fundamental insight into the inherent limitations of group decisionmaking mechanisms such as voting. In a sense, this is a more fundamental problem than interest group influence, since the point of Arrow's Theorem is that such flaws are a mathematical inevitability.

Professor Arrow approached the question of group decisionmaking at a very general level. The question Arrow raised was whether, given only individual rankings of outcomes, it is possible to derive a coherent ranking of those outcomes for society as a whole, using any mechanism whatsoever. Arrow placed only modest restrictions on the decisionmaking method. The assumptions include two key requirements about outcomes, both of which seem to obviously hold for voting procedures. First, the mechanism had to be nondictatorial. It would obviously be easy to construct a societal ranking by simply picking one individual as dictator and adopting that person's ranking, but this 'solves' the problem of collective decisionmaking only by retreating to an individual-level decision. Hence, Arrow required that no one person's preferences be decisive. This is a very minimal form of democracy. Arrow also required that the voting technique satisfy the Pareto standard. That is, if at least one person in society favors an outcome and no one else is opposed, the outcome gets group approval. Again, this is a very weak requirement. It speaks only to situations in which there is no conflict among members of the group.

Arrow proved that, combined with the technical restrictions needed to define a ranking technique, these simple requirements were impossible to meet. More precisely, Arrow proved that no voting method can satisfy the following five basic requirements:

1. If *A* beats *B*, and *B* beats *C*, then *A* beats *C* in a direct vote between the two.
2. If one person votes for *A* over *B* and no one else cares, then *A* beats *B*.
3. More than one person's vote counts.
4. If *C* is not on the agenda, whether *A* beats *B* does not depend on how either one would fare in a vote against *C*.
5. The voting method produces some winner given any possible combination of voter preferences; there are no deadlocks.[3]

These requirements do not amount to much – for example, all but the first one are satisfied by majority voting (assuming an odd number of voters so there are no ties). Yet it is impossible to come up with any decisionmaking procedure that satisfies all five requirements.

Majority voting is crucial in democratic institutions, but it stumbles badly over the first requirement. As Condorcet discovered over two centuries ago, it is possible for the electorate to choose *A* over *B* in a majority vote, and *B* over *C* but for *C* to beat *A*. This cycling of outcomes raises some obvious normative questions about democratic institutions. We may wonder whether majority rule is too capricious to deserve the central role it has sometimes played in political theory.

The potential for cycles is pervasive in legislatures that are faced with multi-dimensional issues – for example, producing a budget covering diverse activities. Yet cycles are rarely observed. This poses a major puzzle: how are real world legislatures able to produce stable outcomes? Efforts to solve the puzzle tend to involve sophisticated use of game theory, with careful attention to the effects of institutional procedures on outcomes. Much of the focus has

been on the operation of institutional structures such as committees, voting rules, agenda restrictions, and inter-institutional conflicts.

For political scientists, Arrow's Theorem is only the starting point in attempting to model legislatures. Much of the later research in public choice theory has been devoted to two issues: just how much influence do interest groups have, and how do legislatures produce coherent, stable outcomes despite Arrow's Theorem? It is primarily these questions, rather than Arrow's Theorem itself, that feature in the papers in this volume.

The larger issue for public choice theorists is how rational actors advance their interest through the political process. To the extent that public choice theory can illuminate the functioning of the political process, it can help us understand how legal rules are produced by legislatures, courts, and administrators. In turn, this understanding may illuminate questions about what restrictions should govern the actions of these government officials and about how the legal rules that they issue should be interpreted and applied. But the key assumption is instrumental rationality, and its validity (or at least predictive power) determines the scope of the theory.

II. Uses and Limits of Public Choice as a Descriptive Enterprise

As we have seen, the project of public choice theory is to test how much political behavior can be explained as the product of rational choice. The usefulness of the theory depends on the extent to which this assumption has traction in explaining particular political behaviors and institutions. In short, the limitations of instrumental rationality as a predictor of behavior are also the limits of public choice as a useful model.

In this setting, 'rationality' means that individuals each choose the means that best advance their goals. As an explanation for politics, there are some obvious other possibilities, some of which can be accommodated more easily than others in terms of an economic analysis. For instance, perhaps individuals do not act rationally because of cognitive limitations. This would lead to something like behavioral economic analysis in the political sphere. Such an approach would be likely to modify the conclusions of public choice theory, but could probably be accommodated within the general economic approach to political science.

Another possibility is that individuals have strong preferences about means as well as ends. These preferences could arise from cultural or religious factors, or from philosophical commitments. For instance, some individuals might favor majority voting because of a belief in democracy rather than an expectation that this decisionmaking process will advance their interests compared to alternatives. We have good reason to think that such meta-preferences play some role in political life. Most notably, it is difficult to account for voting in popular elections simply on the basis of a desire to influence the outcome, since the chances of doing so in a large political entity are infinitesimal. Taking these non outcome-based preferences into account is a challenge to public choice theory.

Thus, the rationality premise of public choice is clearly too simple. It will probably be modified in future efforts to model politics, but it may be 'good enough' to provide some real insights into political life. The result will be an improved understanding of political processes and structures. This improved understanding cannot help but illuminate issues in public law.

Yet we cannot expect that all of political life can be explained by assuming fixed preferences and approximately instrumental rationality. It is not likely that any model of this sort will be able to explain fully such major historical events as the fall of the Soviet Union, without taking into account other factors such as large-scale changes in preferences. Also, essentially unpredictable individual factors may have major consequences – history might have been different if Gorbachev had not been who he was.

The same is true in more mundane contexts. If Humphrey in 1968 or Carter in 1980 had received a few more votes, history would have been different. The legal system would also have developed differently if people in the 1960s and 1970s had not developed new beliefs about gender equality and environmental preservation. Public choice theory can reasonably expect to tell us a lot about the formation and influence of political structures and processes – but history may be driven by other forces as well.

In short, public choice is essentially a theory of the political process, but process does not explain everything about outcomes. Consequently, the utility of the theory depends on the extent to which a legal problem can be tied to process concerns. Given its inherent limits as an explanatory theory, public choice is likely to be most illuminating when legal problems directly relate to governmental structure and process or to problems of interest group influence. These topics are close to the core of public choice theory, so legal applications are not difficult to find.

In contrast, public choice has faced greater difficulty in illuminating issues such as individual rights, where process concerns are not necessarily dominant. Some theories about individual rights do focus on flaws in the political process that make individuals vulnerable, which provides an opening for public choice theory. Nevertheless, the implications of public choice for individual rights have remained controversial. It is not necessarily easy to identify systematic process failures that make particular individual interests peculiarly vulnerable to abuse. The complexity of the political process can make it difficult to establish firm conclusions about the scope of constitutional protection for specific rights, and process theories are far from being the only approach to rights issues.[4] Some public choice theorists have argued that the inherent flaws in government require a very libertarian constitutional structure, but most versions of public choice theory do not support such sweeping conclusions.

Thus, at present public choice seems to have been more successful in its application to administrative law, statutory interpretation, federalism, and similar areas, rather than to defining individual or minority rights. Issues of structure and process lie close to the surface in the former areas. Consequently, this book focuses on such process-oriented areas of public law.

III. An Overview of the Volume

The book begins with the subject of interest group theory. The classical account of the theory is found in the contribution by the late George Stigler.[5] Soon thereafter, Posner and others began to explore the implications of the theory for law; a leading work in this mode follows Stigler.[6] In contrast, Einer Elhauge and others have argued that interest group theory had limited application to law, and in particular, that the theory does not justify more stringent judicial enforcement of limits on legislative activity (in part because the judicial process has

similar flaws). Elhauge's argument should be considered in tandem with Posner and Stigler's versions of interest group theory.[7]

Other theories of political behavior are discussed next. Thomas Ginsburg argues for a milder form of interest group theory together with attention to other influences on political outcomes.[8] Keith Krehbiel explores alternative theories of how legislatures are organized internally and their implications for legislative outcomes.[9] Finally, Daryl Levinson surveys and critiques 'agency' theories, under which political institutions work to expand their own power and resources rather than responding to outside constituencies and their needs.[10]

The preceding articles focus primarily on legislative behavior. The next group of articles turns to the executive branch. Jerry Mashaw makes the case for assigning broad power to administrators,[11] while the trio of scholars known as McNollgast explores the ways in which legislators put strings on their delegations to agencies.[12] Terry Moe and William Howell then discuss the power of the chief executive to seize the initiative through unilateral action and thereby control the legislative agenda.[13] The potential importance of this power is illustrated by the anti-terror efforts of the Bush administration, which have often proceeded in the absence of explicit legislative authorization. This is an even more important power in constitutional systems that explicitly provide chief executives with independent lawmaking authority.

The final topic to be discussed is statutory interpretation. Frank Easterbrook made an important argument in favor of formalism based on public choice theory in a 1983 article.[14] Kenneth Shepsle argues on similar grounds against reliance on 'legislative intent' in statutory interpretation.[15] In response to such arguments, William Eskridge and 'McNollgast' argue for more restrained application of public choice theory, though they agree that it contains important insights for lawyers and judges.[16]

At least two additional areas would have been worth more extensive discussion in this volume but for space limitations. The first is federalism, which has been the subject of an extensive, economically oriented body of scholarship.[17] Much current research is dedicated to exploring the institutional supports for federalism, including the structure of American political parties, competition between states to offer the optimal packages of regulations, taxes, and services, the influence of state governments as federal lobbyists, and the role of the judiciary as enforcers of the federalist bargain. This is a very fruitful subject for public choice analysis. However, the topic is not included in this volume because it will be covered in another planned volume in this series.[18]

Another topic that has resulted in an extensive literature, but which will only be covered in this volume in passing, is that of constitutional limitations on economic regulation, such as requirements of compensation for regulatory 'expropriations'.[19] While this topic has been the subject of extensive scholarly discussion, much of the work has been tied to the specifics of American constitutional law doctrines. Given space limitations, inclusion of this topic had a lower priority because of its lesser interest to an international audience.

IV. The Normative Implications of Public Choice

For many legal scholars, the most pressing issue about public choice has less to do with applications to specific legal problems and more to do with its general normative implications about the legal system. Especially in its earliest and starkest forms, public choice seemed to

have dark implications for those who care about democracy. On the one side was the interest group theory that law is driven by concentrated special interest groups, who grow fat at the expense of the populace. On the other side was the social choice view that legislative outcomes are chaotic or at best unrelated to any coherent conception of the public interest.

These cruder forms of public choice lent themselves to the view that government was inherently bad – corrupt or at least arbitrary – and therefore that government should be limited as much as possible. Perhaps not coincidentally, public choice theory began to receive recognition during the Reagan years, often at the hands of advocates of those who favored the least possible government. This ideological association continues to be attached to the field in the minds of some outsiders, though the political views of those who work in the public choice tradition today are much more diverse.

As public choice theory has developed, its normative implications have become more nuanced. It is clear that pre-public choice versions of pluralism, which assumed equal representation for all interests in the political process, were too simplistic. But we know that politics is more than rent-seeking by concentrated interests. Not only does that cynical view leave much of political behavior unexplained – in particular, public participation through voting and as well as legislators who seem to have motivations beyond courting interest groups. The reductionist version of interest group theory also makes it hard to account for large bodies of law, such as environmental regulation or civil rights protections, which seem to rest on public values rather than the interests of concentrated interest groups. Still, interest group theory cannot be lightly dismissed. What we are left with is the keen awareness that rent-seeking interest groups may have undue influence, and that institutional design needs to keep that risk firmly in mind.

If anything, the initial implications of Arrow's Theorem for democracy seemed even worse than those of interest group theory. Majority rule was revealed as being often indeterminate or simply the product of arbitrary agendas. Yet, legislatures often seemed functional and predictable rather than incoherent or unresponsive. Here, the problem was the focus on majority voting as the essence of democracy. What we have come to understand is that democracy, to be functional, must be far richer institutionally than a simple mechanism to count votes. More sophisticated analyses have revealed the importance of intermediate institutions that provide coherence to outcomes, such as legislative committees, political parties, and executive agencies.

None of these devices are perfect, so that it would be a mistake to view democracy as even potentially a perfect system of government. But then, there are no perfect systems for governing societies – as Churchill famously said, democracy is the worst system of government except for all the others. Even Churchill's formulation may be too narrow. Thinking only in terms of the flaws of 'government' institutions may be misleading – there are no perfect *non*government institutions either, including unregulated markets. For markets, too, are subject to Arrow's Theorem, and they too cannot always overcome collective action problems.

Besides giving us an appreciation for the institutional complexity of democracy, public choice theory promises to show how political structures and processes shape outcomes for better or for worse. It can thereby help us understand how to improve institutional design. Much of that institutional design is expressed in the form of law, so there is much to learn here for legal scholars. The articles reprinted here should give the interested reader a firm foundation for understanding this important area of scholarship.

Notes

1. For overviews of public choice, see ROBERT COOTER, THE STRATEGIC CONSTITUTION (2002)/ JERRY MASHAW, GREED, CHAOS, AND GOVERNANCE: USING PUBLIC CHOICE TO IMPROVE PUBLIC LAW (1997); DANIEL A. FARBER AND PHILIP P. FRICKEY, LAW AND PUBLIC CHOICE: A CRITICAL INTRODUCTION (1991). It is important to note a terminological issue. Some social scientists would reserve the term 'public choice' only for a libertarian strand of work by followers of Buchanan and Tullock, referring to other portions of the field as 'social choice theory' or 'rational choice theory' or 'positive political theory'. Legal academics generally use the term 'public choice' more broadly, to cover all of these bodies of work.
2. It should be noted that this is not an uncontroversial assumption among political scientists. See JEFFREY FRIEDMAN (ed.), THE RATIONAL CHOICE CONTROVERSY: ECONOMIC MODELS OF POLITICS RECONSIDERED (1996); DONALD P. GREEN AND IAN SHAPIRO, PATHOLOGIES OF RATIONAL CHOICE THEORY: A CRITIQUE OF APPLICATIONS IN POLITICAL SCIENCE (1994). 'Rational choice' is a somewhat more comprehensive term that includes what legal scholars call 'public choice' as well as the use of game theory.
3. For fuller discussions of Arrow's theorem and allied work, see DENNIS MUELLER, PUBLIC CHOICE II 384–99 (1989); Amartya Sen, *The Possibility of Social Choice*, 89 AMER. ECON. REV. 449 (1999).
4. The classic defense of process theory in constitutional law is JOHN HART ELY, DEMOCRACY AND DISTRUST (1980). For a critique, see Laurence H. Tribe, *The Puzzling Persistence of Process-Based Constitutional Theories*, 59 YALE L.J. 1063 (1980). For a response to the criticisms, see Michael Klarman, *The Puzzling Resistance to Political Process Theory*, 77 VA. L. REV. 747 (1991).
5. Stigler, George, *The Theory of Economic Regulation*, 2 BELL J. ECON. & MGMT. SCI. 119 (1971).
6. Richard Posner and William Landes, *The Independent Judiciary in an Interest-Group Perspective*, 18 J. L. & ECON. 975 (1975). For other perspectives on judicial independence, see Matthew C. Stephenson, *'When the Devil Turns . . .': The Political Foundations of Independent Judicial Review*, 32 J. OF LEG. STUD. 59 (2003); Daniel Farber, *Rights as Signals*, 31 J. OF LEG. STUD. 83 (2002).
7. Einer R. Elhauge, *Does Interest Group Theory Justify More Intrusive Judicial Review?*, 101 YALE L.J. 31 (1991).
8. Tom Ginsburg, *Ways of Criticizing Public Choice: The Uses of Empiricism and Theory in Legal Scholarship*, 2002 U. ILL. L. REV. 1139 (2002). For some other perspectives on interest group theory, see Keith Poole and R. Steven Daniels, *Ideology, Party, and Voting in the U.S. Congress, 1959–1980*, 79 AMER. POL. SCI. REV. 373–99 (1985); Joseph Kalt and Mark Zupan, *Capture and Ideology in the Economic Theory of Politics*, AMER. ECON. REVIEW. 279 (1984).
9. Keith Krehbiel, *Legislative Organization*, 18 J. ECONOMIC PERSP. 113 (Winter 2004). Other useful work on legislative organization includes Barry Weingast and James Marshall, *The Institutional Organization of Congress*, J. POL. EC. 132 (1988); Kenneth A. Shepsle, *Studying Institutions: Some Lessons from the Rational Choice Approach*, 1 J. THEORETICAL POL. 131–47 (1989).
10. Daryl J. Levinson, *Empire-Building Government in Constitutional Law*, 118 HARV. L. REV. 915 (2005).
11. Jerry Mashaw, *Prodelegation: Why Administrators Should Make Political Decisions*, 1 J. OF LAW, ECON. & ORG. 81 (1985).
12. Mathew D. McCubbins, Roger Noll, and Barry R. Weingast, *Political Origins of the APA*, 15 J. LAW, ECON. & ORG. 180 (1999).
13. Terry M. Moe and William G. Howell, *The Presidential Power of Unilateral Action*, 15 J. LAW, ECON. & ORG. 132 (1999).
14. Frank H. Easterbrook, *Statutes' Domains*, 50 U. CHI. L. REV. 533–52 (1983).
15. Kenneth A. Shepsle, *Congress Is a 'They,' Not an 'It': Legislative Intent as Oxymoron*, 12 INT. REV. OF L. & ECON. 239 (1992). For a response to this line of argument, see Arthur Lupia and Mathew D. McCubbins, *Lost in Translation: Social Choice Theory is Misapplied Against Legislative Intent*, 14 J. CONTEMP. LEG. ISSUES 585 (2005).

16. William Eskridge, *Politics without Romance: Implications of Public Choice Theory for Statutory Interpretation*, 74 VA. L. REV. 275 (1988); Mathew D. McCubbins, Roger Noll, and Barry R. Weingast, *Legislative Intent: The Use of Positive Political Theory in Statutory Interpretation*, 57 LAW AND CONTEMPORARY PROBLEMS 1 (Winter 1994).
17. See, e.g., Rui J.P. de Figueiredo, Jr. and Barry Weingast, *Self-Enforcing Federalism*, 21 J. LAW, ECON. & ORG. 103 (2005); Richard Revesz, *Federalism and Environmental Regulation: A Public Choice Analysis*, 115 HARV. L. REV. 553–640 (2001); *Symposium: The Law and Economics of Federalism*, 82 MINN. L. REV. 249–564 (1997); William Eskridge and John Ferejohn, *The Elastic Commerce Clause: A Political Theory of American Federalism*, 47 VAND. L. REV. 1355–1400 (1994).
18. LARRY RIBSTEIN AND BRUCE KOBAYASHI, ECONOMICS OF FEDERALISM (forthcoming).
19. Efforts to apply public choice theory to 'takings' questions have led to a fertile scholarly discussion. The case for expansive judicial review to prevent rent-seeking economic legislation is made in Richard Epstein, Private Property and the Power of Eminent Domain (1985). Some counter-arguments can be found in Farber and Frickey, supra note 1, at 63–73, and in Elhauge, supra note 7. Although Epstein's work represents one end of the spectrum, there have also been very interesting applications of public choice to takings law by scholars who lack his libertarian agenda, but space precludes any discussion of their efforts in this volume.

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Interest Group Theories