

# Reflections on the Political Economy of Government\*

## The Persistent Growth of Government

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### I. The Issue

A central theme of our time concerns the role and interpretation of "government". Two contrasting views influence intellectual attitudes and affect the social evaluation of political institutions. One view emphasizes the importance of a "limited government" with severe constitutional constraints on the admissible range of political action. Political institutions offer a stable and predictable general framework guiding the detailed voluntary interaction among the members of society. A constitutional consensus establishes and legitimizes the existence and limited scope of "government". It is moreover expected under this view that the consensus can be effectively established and even usefully monitored with the aid of suitable social designs.

An alternative view essentially rejects the idea of a limited and controlled government. It denies that human affairs are in general better served under a strictly limited government. The position denies in particular that limited government assures a better chance for evolving human welfare. Political institutions appear in this view as the essential instrument of "human progress". "Government" is the "objective representation of the principles of justice, equity and human values". An increasing "government" and a widening reach of political institutions are presented as necessary conditions of human achievements. Responsible political action thus requires deliberate removal of constitutional limitations. It also requires a conscious effort to expand the range of political action in man's social affairs. Political institutions need be more, according to this view, than a *general* framework for social interaction. They should properly attend to specific and detailed intervention in social transactions over an open-ended range with little inhibition by general and stable rules<sup>1</sup>.

The case for "limited government" seems a lost historical cause at this stage. We hardly need comment on the state of affairs in the Second and the Third Worlds.

\* Many discussions with *William Meckling* and *Allan H. Meltzer* over the past years have shaped my thinking on the issues examined in the paper. The contribution made by these discussions is gratefully acknowledged. The paper forms part of a project bearing on socio-political aspects of inflation supported by a grant from the National Science Foundation. The first draft of the paper was prepared as a visitor at the Hoover Institution (Stanford University) during the winter 1977/78.

<sup>1</sup> These two positions can be explained in terms of two alternative perceptions (or theories) about man. The connection between the view of man and the interpretation of government was explored in the paper "The Perception of Man and the Conception of Government", jointly authored by *Karl Brunner* and *William Meckling*, *Journal of Money, Credit and Banking*, February 1977.

The dominant role of political institutions among the mass of member countries in the United Nations is well documented. More important for our immediate purpose is the longer-run evolution in Western democracies. The broad facts summarized in the second section of the paper reveal that any constitutional consensus about limited government ever existing in the past substantially vanished over time. But the historical erosion of the thesis advising severe limitations on government does not establish the validity of the second position linking human achievement with "unlimited government". The historical evidence effectively dismisses any such claims. More significant in the present context is the simple fact that the second view offers no explanation of the relevant observations. It advances an interpretation of government as the salvation of mankind and justifies an appropriate political activism. But such normative constructions are logically incapable to provide useful accounts of our reality. We also note that the historical evolution, described in the following section, emerged in all Western societies irrespective of extent and political organization of the "ideological commitment" expressed by the second position.

The political events in numerous countries actually revealed in recent years a rising concern about the growing burden imposed by government. President Carter mobilized during his campaign for the Presidency the voters' frustrations fostered by an increasing exposure to an expanding government. Local "rebellions" of tax payers emerged in the USA with rising frequency and their recent "rebellion" in California has projected a wide shadow. But the meaning of these political events remains unclear until we possess a coherent explanation of the observed trend. They may be disturbances at the surface without import for the basic thrust of the social process producing an ever-expanding government sector in Western democracies. Similarly, promises and attempts to raise efficiency and performance levels of government bureaus may just form an exercise in useless frustrations. The relevance (or irrelevance) of such attempts depends on the nature of the underlying social process. The evaluation of recent events depends thus on our systematic interpretation of the social forces shaping the growth of the government sector. This general and persistent growth attracted increasing attention in the social sciences. A growing number of economists applied over the past fifteen or twenty years their analytic tools to explorations of this problem. My paper draws on these contributions and offers a programmatic analysis of the crucial interaction between voters, legislators, bureaus and the judiciary which produces the unrelenting growth of government irrespective of the specific intentions pursued by participants in the process. Some major implications of the analysis bearing on current trends and the future are explored at the end.

## II. The Facts

The growth of government has not been invented by the "New Politics" of the 1960's. It also emerged before the latter-day saviours of mankind relying on political institutions and political processes. Neither was the growth of government produced by the "Keynesian Revolution". Admittedly, any measures used to trace our phenomenon contain a variety of more or less serious errors. Measurement procedures are usually faulty and the data obtained rarely correspond adequately to the analytic concept most appropriately used for the specific purpose on hand. Still, the potential errors do not obscure the broad and dominant pattern revealed by diverse measures obtained by a number of authors.

Two distinct measures were presented by Allan H. Meltzer. He examined the relative magnitude of tax collection and the relative absorption of labor by the government sector. The real value of taxes collected by the Federal Government in the United States rose since 1792 at a rate of 5.5% p. a. This growth rate exceeds the rate of growth of private sector output over the same period. The growth rate was however not uniform. It moved along to 4.75% from 1792 to 1902 and rose to about 7% in the 20th Century. Both figures exceed the growth rate of real gross national product. Total real taxes (accruing to all levels of government) grew over the 20th century at a rate of 5.4 p. a., whereas real gross national product increased at a lower rate of 3.2%. A similar pattern prevails for government employment. According to this measure, the government of the United States expanded over this century at more than twice the rate of the private sector<sup>2</sup>.

Tables I and II present additional information for this century about the United States from another source<sup>3</sup>. The share of public employment (table I) increased from 1900 to 1970 by a factor of more than 3. Even if the defense establishment is disregarded, the growth in the share over the seventy years is only slightly less than 200%. The expansion in the proportion of national income absorbed by the government sector, exhibited in table II, confirms the general pattern. This proportion measured 6.8% in 1902. This share rose by 1970 to 34.1%. The relative absorption of national income by the government sector thus expanded over 70 years by approximately 400%.

We should look beyond the United States however. Warren Nutter published recently an informative summary of the trends prevailing over the postwar period in OECD countries<sup>4</sup>. The patterns exhibited by government expenditures are summarized by tables III and IV. The sample median (for the fixed sample) of the share

<sup>2</sup> A more detailed discussion can be found in the paper "Why Government Grows (and Grows) in a Democracy", by Allan H. Meltzer and Scott Richard, *The Public Interest*, 1978.

<sup>3</sup> "Budgets and Bureaucrats, The Sources of Government Growth", edited by Thomas E. Borcherding, Durham, 1977. Tables III and IV are drawn from this book.

<sup>4</sup> Warren Nutter, "Growth of Government in the West", American Enterprise Institute for Public Policy Research, Washington, D.C., 1978.

of government expenditures in national income rose from 34% in 1953 to 49% in 1973. It rose from 31% in 1950 to 52% in 1974 for the variable sample. The fixed sample median increased between 1953 and 1973 by somewhat more than 40%, whereas the variable sample median increased from 1950 to 1974 by slightly less than 70%. The boundaries of both sample ranges rose concurrently with the median. Supplementary information is contained in table IV. It presents the average annual growth rate (over indicated periods) for the share of government expenditures in national income. The data cover 16 countries. The largest growth rate of the *share* of government expenditures (for the period 1960–1974) is observed at 1.84% p.a. for Sweden. The smallest growth rate is shown at .44% for France (covering 1950–1974). Apart from Sweden, a growth rate of at least 1% p.a. can also be noted for Denmark, Norway, Netherlands and Belgium. The median growth rate of the sample is .69% p.a.

Table I  
Public Employment as a Percentage of the Labor Force in the United States

1900 .....	6.0
1910 .....	6.4
1920 .....	8.2
1930 .....	9.8
1940 .....	12.2
1950 .....	15.2
1960 .....	17.9
1970 .....	20.1

*Source:* "One Hundred Years of Public Spending: 1870–1970", in: "Budgets and Bureaucrats; The Sources of Government Growth", edited by Thomas E. Borcharding, Durham, 1977, p. 26.

Table II  
Total Government Expenditures in Constant (1929) Dollars as a Percentage of  
Gross National Product in the United States

1902 .....	6.8
1913 .....	8.0
1922 .....	12.6
1932 .....	21.3
1940 .....	20.3
1950 .....	42.7
1960 .....	30.1
1970 .....	34.1

*Source:* "One Hundred Years of Public Spending: 1870–1970", in: "Budgets and Bureaucrats; The Sources of Government Growth", edited by Thomas E. Borcharding, Durham, 1977, p. 26.

**Table III**  
**Government Expenditures as a Percentage of National Income: Median and Range for Samples of OECD Countries, Selected Years, 1950–1974**

Year	Fixed Sample <sup>1</sup>		Variable Sample <sup>2</sup>	
	Median <sup>3</sup>	Range <sup>4</sup>	Median <sup>3</sup>	Range <sup>4</sup>
1950			31	22–39
1953	34	19–44	34	19–44
1955	35	19–42	35	19–42
1960	39	22–43	38	22–43
1965	41	25–49	42	25–48
1970	48	24–57	48	24–57
1973	49	27–62	49	27–62
1974			52	29–64

<sup>1</sup> Covers the same thirteen countries in all years, excluding Australia, Luxembourg, and Sweden.

<sup>2</sup> Covers varying countries: nine in 1950; fourteen in 1953 and 1955; sixteen in 1960, 1965, and 1970; fifteen in 1973; and thirteen in 1974. For lack of data, the following countries are excluded in the designated years: Australia, Belgium, Italy, Japan, Luxembourg, Norway, and Sweden in 1950; Australia and Sweden in 1953 and 1955; Luxembourg in 1973; and Austria, Italy, Luxembourg, and the United States in 1974.

<sup>3</sup> The middle percentage in the sequence of percentages arranged in ascending order for the countries covered.

<sup>4</sup> The lowest and highest percentages recorded for the countries covered.

Several aspects of the broad facts should be noted at this stage. The information provided by data from the United States reveals that the growth of government is neither a postwar nor a post Keynesian experience. It developed over many decades and stretches over the history of the United States. I conjecture that this pattern extends beyond the United States. This seems certainly worth exploring in further research covering a variety of European nations. The postwar data indicate more-over the broad perspective required in approaching the problem. All Western democracies are apparently exposed to the same social process with some obvious variation in detail. We also note that a persistent operation of the postwar trends would raise the (variable) sample median of table III by the year 2000 to about 68%. The upper boundary of the range would reach 80%. One naturally wonders whether such developments are feasible or probable. Will government continue to grow until government expenditures coincide with national income? Or should we expect that the share approaches an equilibrium level definitely below 100%? What are in this case the characteristics of the social process which determine such an equilibrium, and what is the nature of this equilibrium? Is it a viable state or an essentially unstable position defining a transition to a non-democratic political arrangement? Moreover, what is the connection between the expansion of the government sector and the mode of financing government expenditures? And lastly,

**Table IV**  
**Estimated Average Annual Increase in Government Expenditures as a Percentage**  
**of National Income: Sixteen OECD Countries, Varying Periods, 1950–1974**

	Average Annual Increase (Percentage Points)	Period
Sweden	1.84	1960–1974
Denmark	1.42	1950–1974
Norway	1.38	1951–1974
Netherlands	1.13	1950–1974
Belgium	1.00	1953–1974
Luxembourg	.92	1952–1972
Canada	.82	1950–1974
Italy	.72	1951–1973
Austria	.66	1950–1973
Switzerland	.62 <sup>1</sup>	1950–1969
United Kingdom	.55	1950–1974
Federal Republic of Germany	.54	1950–1974
United States	.51	1950–1973
Japan	.49	1952–1974
Australia	.46	1960–1974
France	.44	1950–1974

<sup>1</sup> Taken for the series based on former SNA (see Appendix A) because the composite series is significantly biased. See section 1 of Appendix C.

*Note:* The estimated average annual increase is derived for each country from a linear regression of government expenditures as a percentage of national income on a time trend. In the case of countries with more than one OECD series, the regression coefficient is taken from the composite series

*Source:* Tables III and IV are copied from *Warren Nutter's* book.

what is the relation between inflation and this mode of financing? These are the major questions guiding an examination of the political economy of government. We should not expect to obtain definite or reliable answers at this time. Serious work beyond the exercises of normative judgments or religious commitments is comparatively young. We possess at this stage an assembly of promising fragments and also, in my judgment, an array of blind alleys. I propose to explore blind alleys and the fragments with potential promise for useful explanation.

### III. A Survey of Approaches

A. C. Pigou was probably the first to apply an efficiency criterion in order to establish a norm for the relative size of government. The size and composition of the budget maximizes social welfare provided the marginal satisfaction of every dollar spent “inside” or “outside” the government coincides for any taxpayer. Govern-

ment is too small, whenever the marginal satisfaction of a dollar spent via government exceeds for any taxpayer the marginal satisfaction of "privately spent dollars". An expansion of the government budget raises social welfare under the circumstances. "Government" is too large on the other hand whenever the marginal utility of "publicly spent money" drops below the marginal utility of "privately spent money" for any taxpayer.

This general norm yields however little information about the division between private and public activities. The efficiency criterion requires supplementary characteristics in order to achieve more content or useful guide-lines. The basic idea governing a rational division of labor suggests that the government should provide a range of services and goods with a comparative advantage derived from its monopoly of coercive power. This argument opened two distinct but related avenues. Both avenues circumscribe the range of appropriate governmental activities with the aid of general characteristics or properties attached to goods or activities. One line explored the implication of externalities resulting from private transactions. The occurrence of externalities lowers the welfare of members in the social group. Activities with negative externalities are too large from a social perspective, even if they maximize individual transactors' welfare. Activities producing positive externalities on the other hand are too small in a social context. Such imbalances reveal opportunities to raise the level of general welfare. But this improvement cannot be expected to emerge from the voluntary interaction of private interests. The government possesses the required coercive power to intervene and suitably regulate with various devices the relative magnitude of externality producing activities. The government functions in this manner as an "internalizer" of privately produced externalities. This argument justifies apparently the operation of government and defines an admissible range for its activities.

The other line of investigation addresses the properties of various goods and services. Samuelson introduced the notion of a "public good" in contrast to the "private goods" usually considered in standard price theory. The goods acquired in ordinary transaction are controlled by the purchaser. Others have no access to the use of such goods without the consent of the owner. Such exclusion and separability seems not to extend however to all goods. A public good can be used or consumed by some group without impairing its use by other groups. Any person paying a full price for the public good will realize under the circumstances that others may have access to the good without paying or at a lower cost. The buyer has no exclusionary rights. It follows apparently that the private production of "public goods" remains too small from a social perspective. The conclusion seemed unavoidable that "public goods" should be produced by government.

A closer inspection of these arguments reveals that we obtain no useful explanation of our phenomenon. They exhibit essentially a normative character in the tradition of welfare analysis. It is logically impossible under the circumstances to pro-

vide an explanation of our observations. Normative statements can be transformed into positive statements bearing on descriptive material with the aid of suitably selected supplementary hypotheses. The “goodwill theory” or “public interest theory” of government provides the necessary addition in this case. The normative ideas bearing on socially optimal size and composition of government are transformed into descriptive statements about the world, whenever we assume that “government” essentially pursues the public interest and attends to the general welfare of all citizens. But this translation still provides no relevant explanation. The “goodwill theory” of government hardly offers a serious proposition about the reality of observable governments<sup>5</sup>. Moreover, the pattern of activities covered by the government sector is difficult to reconcile with the story emerging from the translation of normative prescriptions. Lastly, it cannot explain the observed growth in the *relative* size of government without speculative and dubious artifices. One would need to argue that economic growth accelerates privately produced externalities or increases the public’s demand for public goods at a faster rate. There is however little evidence, if any, in support of these special assumptions. They would appear with an essentially ad hoc character not founded in substantial studies.

Some additional considerations cast further doubt on the special assumption. The rejection of the “goodwill theory” of government frees our view for the actual behavior of government, its bureaucratic apparatus and its interaction with the legislature. There is little reason to expect that “government” itself does not produce substantial externalities lowering the welfare of the citizens. A realistic theory of government behavior offers no systematic expectation that interventions designed to correct privately produced externalities do not create more serious distortions of another kind. Moreover, an examination of externalities suggests that they involve either a specification problem of property rights or are essentially reducible to a distributional problem. Neither aspect requires, per se, a large government or a government continuously expanding in relative size<sup>6</sup>.

Similar problems attach to the argument based on “public goods”. It was demonstrated in recent literature that the exclusion argument actually poses a problem of property rights. It follows that these aspects do not justify government actions beyond the traditional function of enforcing private agreements. “Publicness” of goods does not obstruct moreover an efficient private production, or private group arrangement to finance the supply of public goods. The leap from “publicness of goods” to the necessity of government production is generally fallacious and unwarranted<sup>7</sup>.

<sup>5</sup> The reader is referred once more to the argument presented in the paper listed under footnote 1.

<sup>6</sup> The reader may consult in this context *Cotton M. Lindsay* and *Dan Norman*, “Reopening the Question of Government Spending”, in *Budgets and Bureaucrats*, edited by Thomas E. Borcharding, Durham, 1977.

<sup>7</sup> A summary of the issues and of the relevant literature is presented in the paper by *Cotton M. Lindsay* and *Dan Norman* listed in the previous footnote.

A second level of work contributed a variety of propositions bearing on the size of government. Barro explored an interesting model on “the control of politicians”. Citizens can use their income to acquire private goods or obtain via tax payments “public goods”. Politicians derive some reward or income beyond their salary as legislatures from the provision of public goods. A budget constraint links the citizens’ tax payments with the total cost of producing public goods. The analysis implies that the size of the government sector, expressed by the amount of public goods supplied to citizens, exceeds the optimal amount desired by the voters. The excess depends on the reelection probabilities faced by politicians. The excess is larger with legislatures not confronted with any reelection problems. The analysis thus establishes the nature of the control over the budget exercised by politicians relative to the optimum determined by voter preferences<sup>8</sup>.

Barro’s examination addresses the role of politicians in producing, at any moment in time, an “excessive” government sector. The model offers, as it stands, no information about the relative *growth* of the government sector. Baumol attempted to cope with our phenomenon in the context of a standard two-sector model. The private sector exhibits a systematic growth of factor productivity, whereas the government sector settles on a stagnant productivity level. The remuneration of factors in both sectors is determined however by the marginal product of the private sector. Economic growth raises consequently the real cost of government per unit of public good. With appropriate assumptions about price and income elasticities of the demand for public goods one derives a persistent increase in the cost of government relative to national income.

A more sophisticated analysis of the growth context was developed by Mackay<sup>9</sup>. The citizens behave according to a utility function containing a private good, a public good, and a future private good representing current savings. Accumulation of capital is accompanied by a constant growth rate of the population. The supply of the private and the public good is governed by production functions characterizing the two sectors. This analysis implies that the actual output of the public good expands along the steady state path at the rate of population growth. Moreover, the division of employment between the two sectors is constant along the steady state path. Similarly, the value shares of the two sectors remain constant on this path, whereas the output of the public good declines relative to the output of the private sector.

The Baumol and Mackay model do not seem to cope adequately with our phenomenon. The Baumol model requires very special ad hoc constraints on price and income elasticities in order to yield a relative growth of the government sector. Mackay’s model on the other hand cannot be reconciled with the long-run trend of

<sup>8</sup> Robert J. Barro, “The Control of Politicians: An Economic Model”, *Public Choice*, Spring 1973.

<sup>9</sup> Robert J. Mackay: “Private Versus Public Sector Growth: A Collective Choice Approach”, in *Budgets and Bureaucrats*, edited by Thomas E. Borcharding, Durham, 1977.

relative growth exhibited by the government sector expressed in terms of employment or in terms of value shares. Relative growth of government has been observed for almost 200 years in the United States. The OECD data seem also difficult to reconcile with the steady state patterns of the model. Mackay's analysis hardly offers a relevant explanation of the observations summarized in section II.

Another group of contributions emphasizes a variety of "biases" built into social conditions and political institutions which affect the relative size of government. Downs' pioneering approach to the political economy of government centers on the role of parties in the political process. Parties compete in a democratic context for power with tax and expenditure programs. Information about the costs and benefits of programs are not easily or uniformly accessible to voters. They approach their political options with incomplete information. Downs argues in particular that information (or awareness) is asymmetrical. Voters are, in his judgment, more aware of the costs than of the benefits of government programs. The value of the benefits appear thus at a discount relative to the cost. The "government" is therefore smaller than its optimal size determined by fully informed voters<sup>10</sup>.

Buchanan-Wagner offer an opposite asymmetry under the label of "fiscal illusion". They argue that for a variety of reasons voters underestimate the tax price of government services. "Fiscal illusion" emerges as a result of the institutional arrangements shaping legislative processes and most particularly the procedures involved in budgetary policies. The information bias is reinforced by deficit policies and encourages an excessive size of the government<sup>11</sup>.

The arguments based on asymmetric fiscal awareness remain somewhat inconclusive. Some evidence appears to support the contention that a lower "tax price" of government services raises the demand for such services. But there is little systematic association between deficits and government debt and the size of the government<sup>12</sup>. Most importantly however, these arguments offer no explanation of the *relative growth* of the government sector. They are preoccupied with a static efficiency problem, the size of the government relative to an optimum defined in terms of voter preferences and full information.

The short survey encounters many interesting ideas and potentially useful fragments. But the candidates for an explanation of our phenomena, reviewed in previous paragraphs, suffer from a pervasive and common flaw beyond the specific re-

<sup>10</sup> Anthony Downs, "An Economic Theory of Democracy", New York, 1957.

<sup>11</sup> James Buchanan and Richard Wagner, "Democracy in Deficit". We should note that James Buchanan and Gordon Tullock offered a different explanation for the emergence of an excessively large government (relative to an optimum determined by voter preferences) in their "The Calculus of Consent", Ann Arbor, 1962. Buchanan/Tullock argued that benefits of government programs are mostly addressed to specific coalitions, whereas costs of programs are borne by the general taxpayer. Coalitions are induced to push for a program size at which their marginal cost (equal to the general taxpayers' marginal cost) coincides with their marginal benefit.

<sup>12</sup> The reader may find an interesting discussion of these issues in the Symposium on "Democracy in Deficit", Journal of Monetary Economics, July 1978.

servations noted above. They describe government more or less implicitly as a producer of public goods uniformly available to all voters. The production is financed by general contributions made by voters in the form of tax payments. These aspects of the approaches surveyed cannot be reconciled with the reality of government. The provision of "public goods" forms a small and declining portion of total government activities. The dominant portion of governmental operations involves the supply of *private* goods, services and benefits to specific groups of voters<sup>13</sup>. The argument also misses the redistributive thrust implicit in every provision of private or public goods. It omits any reference to the redistributive incentives unavoidably built into every government program. The analysis thus overlooks the crucial consequences of any constituted government. These flaws of the public goods approach expressed by a factual error and a serious omission account for the failure to provide a coherent story about the social process producing the relative growth of government.

#### IV. The Growth of Government

##### 1. *The Nature of Politics*

This section presents a general outline for an explanation which essentially defines a program of future research. The elements and strands of ideas used for our purposes are not new. They were drawn in various combinations from existing contributions and most particularly, of course, from economic analysis.

The starting point is the fundamental ambivalence of government. This ambivalence is expressed by the mixture of benefits and risks associated with a political structure. Hobbes and others have eloquently described the state of anarchy. We also note that anarchy or unstructured social processes appear at most as transition phases. Nozick and Buchanan offer a lucid and detailed analysis of the transition from anarchy to elementary forms of political structure<sup>14</sup>. Both authors demonstrate that anarchy is not a viable state and spontaneously evolves forms of political structure. This spontaneous evolution requires no mysterious "social" forces beyond man's interests and resourceful endeavors. The social interaction between self-interested men produces the transition into patterns of political structure.

The benefits to individual members of these associations are very substantial indeed. Their security is enhanced and the political structure encourages an economic

<sup>13</sup> Peter A. Aranson and Peter C. Ordeshook present an excellent argument on this score: "Incrementalism, Fiscal Illusion and the Growth of Government in Representative Democracies". The paper was presented at the Fourth Interlaken Seminar on Analysis and Ideology, June 1977.

<sup>14</sup> James Buchanan: "The Limits of Liberty. Between Anarchy and Leviathan", Chicago, 1975. Robert Nozick: "Anarchy, State and Utopia", New York, 1974.

organization raising the productivity of labor and thus improving the standards of living. This story is clear enough. But the emergence of political structure shifts opportunities and incentives in a peculiar way. Nozick addresses this aspect when he notes that already the constitution of a "minimal state" unavoidably involves some measure of coercive redistribution of wealth.

In a state of anarchy each individual has essentially three options: to engage in productive activity or voluntary exchange, to allocate efforts to protect his product and possessions, or to engage in piracy and acquire wealth through violent extraction from others. It should be obvious that only the first option increases social wealth. The occurrence of the other two options determines the brutal uncertainty of anarchy and the vanishing incentive to invest any resources or efforts for returns beyond the immediate horizon. The appearance of political structure replaces this vast uncertainty confronting the individual with some "rules of the social game" represented by specific political institutions. The crucial fact requiring some emphasis in this context bears on the range of options available to individual members of the political association. These options include of course the application of resources controlled by individuals to produce wealth. The evolution of political structure enhances and safeguards this option. But the very nature of political institutions cannot prevent alternative options. Their existence offers opportunities to invest resources in political activity, guided by implicit (or explicit) rules of the institutions, in order to extract wealth from other members of the political association. The occurrence of this option implies the existence of a last option, i. e. investment in political activities designed to fend off extraction of wealth threatened by the political activities of other groups. Under both anarchy and a state of political structure individual agents can thus acquire wealth by productive effort and voluntary exchange or via extractions from others. The ambivalence of political structure is defined by the persistence of socially non-productive private wealth extraction. This kind of wealth acquisition does not distinguish anarchy from systems exhibiting political structure. The crucial difference appears in the range of uncertainty and the existence of rules confining the processes of wealth extraction in the context of political structure. Such rules lower the uncertainty confronting individual agents. This difference implies that opportunities for socially productive wealth acquisition via productive efforts and voluntary exchange are enhanced. Such enhancement assures the viability of the political structure. Viability is endangered whenever political institutions develop complex and pervasive incentives for potential wealth extraction. There emerge under the circumstances ever widening organizational efforts to exploit the political process for persistent acquisition of wealth at the expense of others. The change from anarchy to political structure may also be formulated as a shifting mixture of a positive-sum game (productive effort) and a negative-sum game (piracy). The negative sum game looms so large under anarchy that most political structures offer a better mixture of positive and negative sum

games. But the crucial fact is that every political structure necessarily contains characteristic incentives yielding its own peculiar range of negative sum games<sup>15</sup>.

Every political institution thus projects opportunities for redistribution. This follows from a permanent and historically invariant pattern of human behavior. Many aspects concerning human preference systems are culturally conditioned or historically influenced. Human preferences (and beliefs) are quite similar in this respect to the inheritance of capital accumulation. But the most basic and pervasive patterns are independent of institutional setting and historical circumstances. They are revealed by the fact that man forever searches and resourcefully gropes to improve his position. This searching and groping is guided by evaluations of current and prospective states according to individual agents' vision of the world. This basic pattern or drive built into man's life implies that all circumstances, including political institutions, are resourcefully assessed and used to improve his position. The resulting probing eventually disseminates information bearing on the use of political institutions for purposes of wealth acquisition<sup>16</sup>.

The redistributive character of political institutions and political actions can hardly be missed upon closer examination. A few examples should usefully illustrate my point. Economists may be impressed by the rhetoric of stabilization policies. But the political reality of these programs is at best randomly related to the issues of macro-stabilization. Interested groups may use the general state of the economy as a cover in order to minimize objections or summon support from the intellectuals. But changes in expenditure and tax programs unavoidably involve specific items affecting distinct groups very differently. The pattern of relative changes on the expenditure and tax side of the budget implicitly redistributes wealth between the members of society. This implicit redistribution proceeding under cover of a stabilization policy attracts the central attention of the political process. The impact of these redistributions on the position of individual agents or groups usually exceeds in their evaluation the results associated with the ensuing general macro-policy. This differential effect is probably reinforced by the fact that information about the distributional consequences is more direct than information about the consequences of the macro-policies as such. It follows that "stabilization policies" are in general quite tenuously related to the requirement of economic stabilization. The political reality converts "stabilization policies" into conflicts about

<sup>15</sup> Non-productive wealth extraction is usually labelled as a zero-sum game. But this is false. First, occurrence of such extractions includes defensive political investments. Secondly, and probably more important, it lowers expected returns from productive application of resources. The level of productive application will be lowered.

<sup>16</sup> The basic thesis has been elaborated by *William Meckling*, Values and the choice of the model of the individual in the social sciences, *Schweizerische Zeitschrift für Volkswirtschaft und Statistik*, 1976. The REMM (resourceful evaluating, maximizing man) model has been developed in the context of economic analysis and contrasts with the VARM (vacuous, aimless, reactive man) model widely appearing in the sociological literature. The REMM model is advanced here as a basic framework of analysis applicable to any human pattern.

redistribution of wealth. The emerging policies hardly qualify very effectively as “stabilization policies”.

The implicit wealth redistribution associated with any program for economic stabilization also explains the adamant refusal of Congress in the United States to cede authority on short-run tax and expenditure adjustments for stabilization purposes to the President. This concession would lower the influence of Congress relative to the Presidency. The position of a legislator depends at least partly on his opportunities to affect redistributions in one way or another. He should not be expected to impair voluntarily his opportunities.

President Carter’s proposed “energy policy” offers another instructive illustration. Similar to programs of economic stabilization the package proposed under the label of “energy policy” is poorly designed with respect to the essential purpose. This purpose may be described as a rational development and use of energy resources in the United States. It is hardly a secret among professional economists that the legislative proposals will obstruct the development of energy resources and lower the productivity of our labor. The rhetoric of an “energy policy” is deliberately used to extend the range of political institutions which engineer a massive redistribution of wealth. This redistribution mobilizes the political forces behind the President’s energy bill. Moreover, the President’s difficulties with Congress in these matters reflect a conflict about the nature of the wealth redistribution. Substantive concern for the future course of our economy associated with a rational exploitation of our energy resources has been submerged by the distributional conflict implicit in the legislative proposal.

A similar fate befell the proposal to restructure the financial system of the United States. There is hardly a competent economist which would not agree on a broad range of measures well designed to improve the efficiency of our financial system. The substantive case is quite clear and well documented. But the general improvement of our welfare possesses no relevant political constituency. The distributional impact on various groups of financial institutions (or borrowers) of changing arrangements overshadows the rise in general welfare. The appropriate proposals, worthy as they are, become unavoidably lost in a morass of distributional conflicts. The same fate affects also any price-wage body instituted by the government to control or curb inflation. It will be converted into a device to extract wealth via publicly sanctioned *relative* price concessions. Its relation to inflation remains restricted to its name.

We need not extend our examples in further detail. It is sufficient to repeat that the distributional conflicts permeate all public institutions, be it state owned or state controlled railroads, banks, airlines, or be it tariffs, export subsidies or more traditional aspects of government activities. *The essence of politics is redistribution and political conflicts center on matters of distribution.* This central aspect of political processes, the very motor force of politics, has been discarded by the public

goods approach to “collective choice” and government, and similar approaches fail to comprehend therefore, in my judgment, the crucial mechanism producing the relative growth of government. The basic flaw of this literature is revealed by the following quotation: “... there remains the question of government involvement in wealth redistribution. There have been efforts to identify appropriate levels of this activity... While each of these considerations remains a plausible point of view, neither captures what appears to us to be the essence of the appeal for, nor the defense against, wealth transfer in society. The overriding issues here are ethical...” And so we read that “the redistributive aspects ... will be ignored”<sup>17</sup>. One may indulge in the intellectual challenge of ethical studies pertaining to the distribution of wealth. But these studies offer little understanding or explanation of observed political processes or of the relative growth of government. The recent contributions made by Rawls and Nozick are certainly remarkable and worth pondering. Attempts to explain political conflicts in terms of ethical positions are bound to fail however. We need not invoke any ethical systems or moral considerations to explain the incentives of political institutions and observe the responses of men to these opportunities. The function of the scientist concentrates on the development of valid explanation and a proper understanding. It should be recognized that an adequate execution of this function also involves an ethical commitment or moral obligation. The scientist would therefore argue that moral judgment and ethical valuations of social aspects are useless and basically immoral when pronounced independently and in the absence of validated positive explanations. All this does not mean that ethical valuations and moral judgments are per se irrelevant. They occur as pervasive social phenomenon and their role in the social process deserves some attention. As such, both ethical valuations and moral judgments are frequently used as intellectual weapons of the political conflict. Such occurrences are *part* of the phenomena to be *explained* and cannot reasonably explain the nature of political conflict. Serious studies, exemplified by Rawls and Nozick, may ultimately affect our evaluation of alternative social arrangements and political institutions. But they cannot explain the central contours of political conflict and its relation to the relative growth of government. The quotation thus misconstrues the nature of the problem and proceeds to discard the central mechanism of a potentially useful explanation<sup>18</sup>.

<sup>17</sup> Cotton M. Lindsay and Don Norman, “Reopening the Question of Public Spending”, *Budgets and Bureaucrats*, edited by Thomas E. Borchert, Durham, 1977.

<sup>18</sup> Some comments on a frequently encountered description of “politics” and “economics” may be appropriate here. One reads on occasion that “politics is concerned with equity, whereas economics is concerned with efficiency”. This is a remarkable obfuscation of the problem posed by the shifting mixtures of the positive sum and the negative sum social games. It is well designed to distract attention from the crucial properties of political institution and the essential characteristic of political conflict.

## 2. The Pure Wealth Transfer Model

The basic nature of political structure suggests that the fact of wealth-redistribution be placed into a central position of the analysis of government, at least for the context of modern democracies. Allan H. Meltzer and Scott F. Richard recently offered an important contribution systematically linking wealth-transfers induced by rational behavior on the part of voters with the persistent growth of government<sup>19</sup>. The authors base their analysis on three postulates consistent with elementary economic analysis. The postulates are stated as follows:

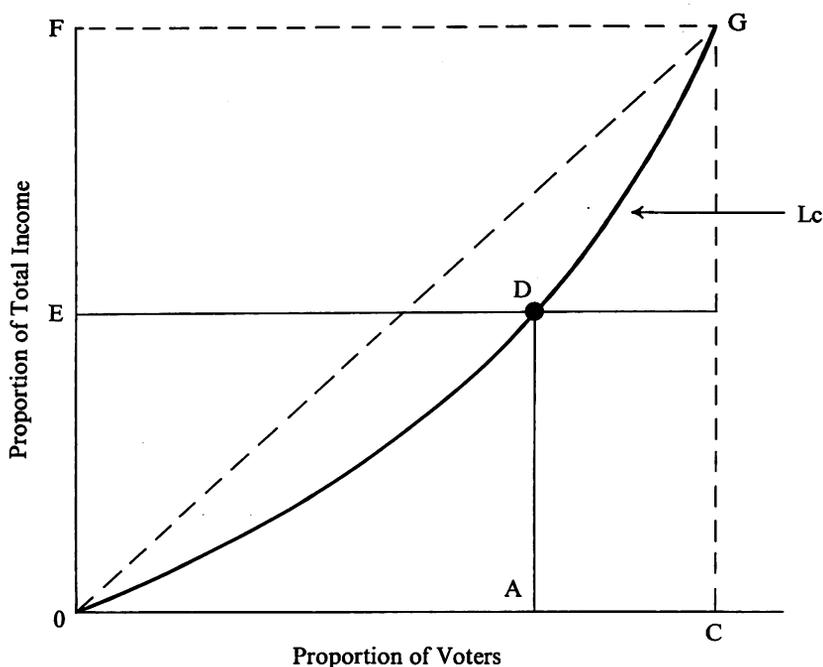
- “1. Candidates and officials propose many more programs than they enact. Their purpose is to find issues which attract attention and votes.
2. A voter chooses a candidate who promises to act in his interest and votes to reelect a candidate who does so.
3. Voters compare the benefits they expect to receive to the costs they expect to pay.”

The three postulates yield the major conclusions derived by the pure wealth-transfer hypothesis of political processes. Incumbent and aspiring politicians sample the political market with a variety of proposals and programs in order to discover a package enhancing their longer-run position. Postulates two and three imply that this competition eventually yields a tax-structure which redistributes income from the upper parts to the lower parts of the distribution. Wealth is redistributed in this manner from a minority to a majority.

Voters can be grouped according to income classes. The description offered by the Lorenz curve in figure I can be usefully exploited for our purposes. The vertical axis measures along OF proportions of national income. The segment OF is necessarily one. The horizontal axis measures on the other hand proportions of voters. The segment OC is again unity. The solid line Lc describes an association between proportions of total income and proportions of voters. In particular, a proportion OA of all voters receives just half of total income expressed by OE along the vertical. This means of course that the other half of total income is absorbed by the proportion AC of voters. It is clear upon inspection that the magnitude of the curvature exhibited by the curve Lc indexes the degree of inequality of the income distribution. This curvature also implies that the *median* voters' income level is below the *average* level of income. But this means of course that *more than half the potential voters* experience an income below the *average* level. Voters in the upper tail beyond the median voters' income could possibly form a coalition with the median voter group in order to shift tax burdens to the lower end. Assuming however that differences in coalition costs are small, the interests of the median group are better served by join-

<sup>19</sup> The reader is referred to the paper listed in footnote 2. The authors also prepared their argument in a rigorous analytic form presented originally at the Fourth Interlaken Seminar on Analysis and Ideology, June 1977.

Figure I



ing and mobilizing the lower portions of the distribution for its purposes. The net gain in wealth to be expected via the political process will be larger. The process can be understood as a continuous sampling of politicians. Competition among politicians implies that the tax schedules preferred by the median group eventually dominates.

The analysis need not assume that all potential voters actually vote or clearly perceive the issues. It is sufficient that a portion of voters recognizes the relative benefits of different tax schedules and vote accordingly. The government's budget thus expands under the persistent incentive for redistribution unleashed by the fundamental properties of an income distribution characterized above.

The story requires at this stage some extension. One needs to explain why the voters under the higher branch of the Lorenz curve, i. e. the voters to the right of the median on the horizontal axis, are not immediately "taxed down" to an average income. Some additional strands enter the story and these strands account for the gradual and persistent operation of the redistributive process and the essentially incremental growth process of government.

Among the additional strands should be noted that redistribution lowers the incentives for the voters with higher income. Rising taxes lower the relative price of leisure and also the relative price of current consumption. Moreover, redistribu-

tional achievements require investment of resources into the political process which are withdrawn from the positive sum game of productive activities. The redistribution achieved offers income options for voters under the lower branch of the Lorenz curve independent of productive application of their resources. Some substitution from productive application towards leisure should thus be expected also for this group. These social costs of redistribution are eventually revealed by comparatively lower real income or lower growth of real income. An accelerated or cumulative redistribution thus endangers eventually the prospects of the median voter groups. They will suffer increasing uncertainty and hesitate or revise their tax policy conceptions. This hesitation and revision operates in the nature of a brake on the redistributive process. Some forms of democratic processes incorporating strong elements of federalism operate probably also to retard the process.

Another important aspect is the prevailing uncertainty pertaining to the median voter group. Neither politicians nor members of the group are certain about the range of this group. This uncertainty induces a cautious sampling and extensive probing. At any given stage substantial time will be required for the political process to produce further adjustments in tax schedules. The movement may occasionally be interrupted with revisions lowering the progressivity of the tax schedule or lowering the whole schedule, whenever evolving experience reveals that the politicians' sampling misjudged the position of the median voter group.

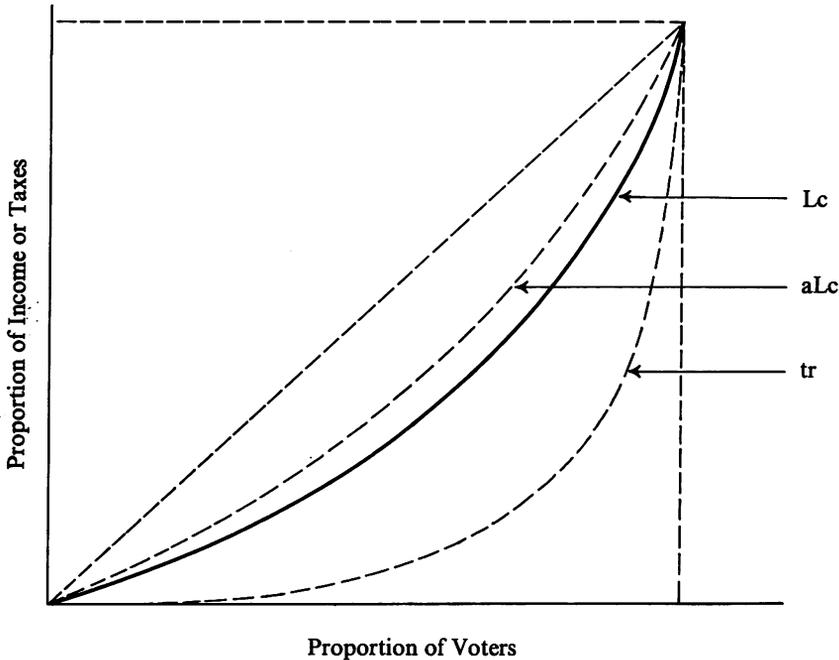
The gradual extension of the franchise since 1800 contributed in the United States significantly to the process summarized above. The last extensions actually occurred in the postwar period over the 1950's and 1960's with the mobilization of Negro voters. Any broadening of the franchise usually extends the group of potential voters to the left of the established median voters in the Lorenz diagram. The horizontal segment covering the voters and anchored on the right at point C moves on the left closer to 0 with every extension of the franchise. An extension of the franchise thus pushes the median voter group to the left in the diagram and opens new opportunities for redistributive tax policies. It should be noted moreover that the lower income groups among voters in a system of limited franchise have an interest to extend the franchise. Such extensions raise the likelihood of additional redistributions benefiting these voter groups. The redistributive adjustments of tax schedules converge eventually over time to an equilibrium state. This equilibrium is however not invariant. It depends on a number of factors including the demographic profile, the preference structure of the voters and the nature of the franchise.

Some aspects of the pure wealth transfer hypothesis of political processes are interestingly supported by observations. Table V offers remarkable information about the distribution of tax payments among income classes in the United States<sup>20</sup>. We note first that the lower half of the income distribution pays almost no

<sup>20</sup> The table was published originally by *Paul Craig Roberts* in an article "Disguising the Tax Burden", in *Harper's*, March, 1978.

taxes in this country. The upper 50% of income recipients pays 93% of total tax revenues, whereas the lower 50% pays only 7%. The lowest 25% pays less than one-half of one percent of total taxes, whereas the highest 5% of income recipients pays 37% of all the taxes. These facts can be represented with the aid of a diagram. Figure II describes again a Lorenz curve  $L_c$  of gross income:

Figure II



The curve  $tr$  describes the distribution of tax payments with an outline reflecting the broad properties exhibited by the table. The third line,  $aL_c$ , introduces an adjusted Lorenz curve based on income net of tax payments. The adjusted Lorenz curve is moved substantially closer to the diagonal line. Another interesting item in table V is the change in the tax distribution between 1970 and 1975. The tax proportion of the upper 50% of income recipients rose by 3.2 percentage points from 89.7% to 92.9%. The tax proportion of the lower 50% of income recipients fell correspondingly from 10.3% to 7.1%. This tax proportion of the lower branch of income distribution thus fell over five years by about 30%.

Table V  
Percent of Total Taxes Paid By High- and Low-Income Taxpayers, 1970 and 1975

Adjusted Gross Income Class	Income Level		Percent of Tax Paid	
	1970	1975	1970	1975
	\$	\$		
Highest 1%	<sup>1</sup> 43,249	<sup>1</sup> 59,338	17.6	18.7
Highest 5%	<sup>1</sup> 20,867	<sup>1</sup> 29,272	34.1	36.6
Highest 10%	<sup>1</sup> 16,965	<sup>1</sup> 23,420	45.0	48.7
Highest 25%	<sup>1</sup> 11,467	<sup>1</sup> 15,898	68.3	72.0
Highest 50%	<sup>1</sup> 6,919	<sup>1</sup> 8,931	89.7	92.9
Lowest 50%	<sup>2</sup> 6,918	<sup>2</sup> 8,930	10.3	7.1
Lowest 25%	<sup>2</sup> 3,157	<sup>2</sup> 4,044	.9	.4
Lowest 10%	<sup>2</sup> 1,259	<sup>2</sup> 1,527	.1	.1

<sup>1</sup> Or more.

<sup>2</sup> Or less.

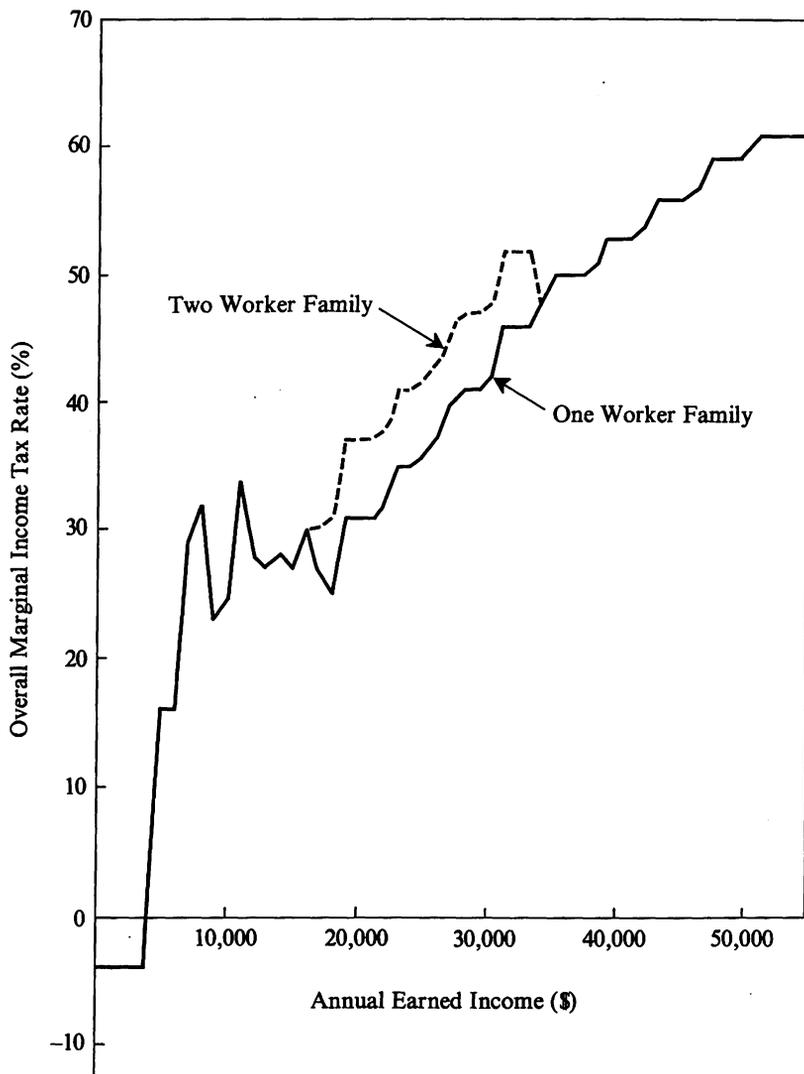
*Source:* Congressional Record, Proceedings and Debates of the 95th Congress, Second Session, Washington, March 9, 1978, No. 33.

A previous paragraph emphasized the uncertainty pertaining to the location of the median voter group. It should be emphasized that this problem is reenforced by shifting and uncertain voter participation. The tax schedules governing the redistribution of income which emerge from the political process reflect this information pattern. It implies in particular that the tax schedules exhibit a middle range holding the marginal effective tax rate along an approximately constant level. Figure III summarizes the pattern for the year 1976 in the United States. An inspection of the diagram reveals immediately that the marginal effective tax rate for typical families of four moves around a horizontal trend for annual incomes between \$ 8,000 and \$ 22,000. The marginal effective tax rate rises rapidly at incomes below \$ 8,000 and continues to increase steadily for incomes beyond \$ 22,000.

### *3. An Extension Beyond the Pure Wealth Transfer Model: The Entrepreneurial Behavior of Politicians and Bureaus*

The pure wealth redistribution hypothesis deserves our close attention. It addresses the crucial aspect of political conflict and political processes. It recognizes and fully reflects that politics is essentially concerned with the negative sum game of human endeavors, proceeding however in a somewhat regulated manner according to an implicitly accepted set of rules. We seem to be offered a useful hypothesis with

Figure III  
 Marginal Income-Tax Rates for a Typical Family of Four in the United States  
 (1976)



Source: "The roller-coaster income tax" by *Martin Anderson*, in: *The Public Interest*, No. 50, Winter 1978.

substantial content. Some reflection indicates however that the pure wealth redistribution hypothesis is incomplete and only describes one strand of the full story. This can be recognized by the circumstance that the pure wealth transfer model explains the growth of government by equating the size of government with the magnitude of the budget. But the two phenomena, the budget and the government apparatus, raise separate issues. The pure wealth transfer model is consistent with a minimal apparatus which essentially operates a fund transfer business. In other words, the pure wealth transfer hypothesis explains only one facet of the observed trend. It explains the relative growth of the budget, whether measured in expenditures or tax revenues. But the pure transfer model cannot explain, by itself alone, the relative growth of employment in the public sector or the increasing ramifications of the governmental apparatus. Neither can it explain the observable fact that wealth transfers do not occur in form of a single, uniform and huge system shifting money from the richer to the poorer. Few programs actually affect the lower income groups across the whole range of income classes. The mass of programs are directed towards *specific* and *limited* groups. The programs are moreover usually organized and implemented in more complicated forms than the basic wealth transfer, per se, would require. All these aspects may not be germane for a useful proximate explanation of the relative growth of the *budget*. They are however relevant, in my judgment, for attempts to explain the relative growth of "government"<sup>21</sup>.

The problem may be approached from a different side. The Lorenz curve Lc in figure II was modified by the tax schedule into the adjusted net income curve aLc. This cannot be the final story however. We need to incorporate the effect of government expenditures on the final distribution of real income. The pure transfer model may assume that tax revenues are redistributed in inverse proportion to the size of income. But the nature of the expenditure programs, noted above, crucially affects the growth of "government" in contrast to the growth of the budget. Many of these programs involve provisions of (private) services and goods to specific income classes or particular social groups of society. The resulting distribution of net income including the full array of real services and goods obtained via governmental operations requires thus an independent and separate examination. Important recent work established for the United States that the relevant distribution of net real income is actually substantially closer to the diagonal line in the Lorenz diagram than the original distribution of gross income<sup>22</sup>. It also seems that this net real income distribution moved closer to the diagonal over the past decades. These observations confirm the basic theme introduced in the early paragraphs of this sec-

<sup>21</sup> The nature of the issue should be clearly recognized. It does not concern our ability to predict specific programs. It concerns the *general* fact, that they exhibit pervasive properties of the kind described in the text.

<sup>22</sup> *Morton Paglin*, "Transfer in Kind, Their Impact on Poverty, 1959-1975", Hoover Institution Conference on Income Redistribution, October 1977.

tion, a theme interpreting political processes in modern democracies in terms of the negative sum game of wealth redistribution. But the “other side of the budget” covering the expenditure pattern forms a crucial link in the social mechanism generating the observed growth in the governmental apparatus. A second strand must be added to the analysis. This second strand involves the entrepreneurial behavior of bureaus and politicians. Meltzer-Richard properly criticize an approach concentrating on the monopoly power of bureaus or politicians, a monopoly power essentially disregarding voter preferences. Such disregard implies that citizens appear forever doomed to ignorance about the state of affairs. But the recognition of the role of bureaus and politicians is not confined to this objectionable interpretation. A parallel with standard price-theory may clarify the issue. Market phenomena emerge from the interaction between demanders’ preferences (subject to constraints) and suppliers optimizing adjustments to these preferences. These preferences are not revealed by a supernatural information channel. They are sampled and explored by the searching behavior of entrepreneurial suppliers. This entrepreneurial behavior proceeds with imaginative exploration of potential preferences and the development of production programs expected to be validated by actual preferences. Entrepreneurial actions are thus a crucial link in the adjustment of services and goods produced in accordance with evolving consumer preferences.

A similar process prevails on the political scene. Bureaus (more appropriately bureaucrats) and politicians (incumbent and aspiring legislators, persons holding or seeking appointments, functionaries of political organizations) correspond to producers on the market place sampling the consumer preferences and adjusting competitively their supplies. Both politicians and bureaus thus respond to the preferences of the citizen. But this response proceeds in the context of information patterns and organizational arrangements which open opportunities for the self-interested behavior of politicians and bureaus. They operate under the circumstances not just as mere vehicles executing the median voter groups’ preferred transfer of funds. Their operation implies that a portion of the total funds collected are absorbed by the “governmental apparatus”. This absorption corresponds to the normal profit in the competitive market place. The voter benefitting from redistribution cedes this portion of the tax revenues to the political and administrative entrepreneurs organizing the benefits. The nature of the political institutions determines extent and form of the competition between politicians and bureaus, or seen from the “other side”, the extent and form of monopoly achievable by politicians and bureaus and their potential of collusive behavior. It seems useful for our purposes in order to focus attention on the major strands of the argument to introduce seven “postulates”:

1. Politicians are entrepreneurs competing in a market for votes and influence. They compete with proposals, programs and the systematic exploitation of non-cognitive aspects of language. The politicians prefer more votes and influence to less votes and influence. They also share with other men a preference for higher permanent real income.

2. "Bureaus" sample the political market with proposals, reinterpretations of their mandate, and the detailed manner of administering the tasks developed. This entrepreneurial behavior is designed to maintain or increase the budget.
3. Costs and benefits associated with *general* programs are more evenly distributed than the costs and benefits of *specific* programs.
4. Information costs about costs and benefits of *general* programs are *large* relative to benefits.
5. Information costs about costs and benefits of *specific* programs are relatively *small* to "positively affected group" and comparatively *large* to "negatively affected group".
6. The marginal cost of political operation (for example, lobbying in various forms) is much smaller for *established* than for *potential* organizations.
7. Potential voters weigh expected costs and benefits associated with the bureaus potential offers and with the alternative packages represented by different politicians.

The crucial information patterns are formulated under assumptions 3 to 5. These assumptions differ substantially from the information assumption made by Buchanan or Downs. The latter postulate an "awareness discrepancy" operating uniformly across all voters and expenditure and tax programs. The distribution of information costs, recognized here, emphasizes on the other hand a highly uneven incidence depending on the relation between voter groups and types of programs. This distribution of information costs reflects important aspects of our reality. Rational adjustment by voters to such costs should not be interpreted to express some "flaws in awareness" or "ineradicable illusions". There is no illusion in staying less than fully informed. It is an illusion on the other hand to expect voters to invest in information at a cost substantially beyond the expected return from such investments.

The major consequences of the patterns summarized by the "postulates" can be summarized according to a previous description<sup>23</sup>:

"...entrepreneurial competition thrives on a continued search for *new* proposals, *new* programs, *new* twists, modifications, or *extensions* of existing programs. It encourages a continuous search for suitable means to focus public attention. This is a necessary strategy for politicians to establish themselves in the competitive political market. Continuous market research and sampling of the public market with the aid of an expanding staff is therefore a competitive necessity for the politician.

There are no rewards in attempts to abolish existing laws or programs. This strategy has no competitive market value. According to proposition 5 above, the beneficiaries of a program know the significance with respect to their wealth or political power of a curtailed program. 'Outside groups' will barely appreciate their own welfare gain resulting from the cut in a program. 'Insiders' opposition to a proposed reduction tends to override consequently the feeble support of 'outsiders' for the change. The basic postulates also imply that 'outside groups' can reasonably expect larger returns for any given costs by investing efforts in lobbying for *new specific* programs adjusted to their special benefits. The returns from political investment in organizing opposition to the other groups specific programs are comparatively small relative to the cost of investment. It follows that proposals to cut programs are neither frequently offered by politicians (with a few exceptions immediately ridiculed by the

<sup>23</sup> Karl Brunner, Comments, The Journal of Law and Economics, December 1975.

media) nor frequently advanced by 'investors in the political marketplace'. A political entrepreneur finds thus in general that offering 'new programs' or 'variations on existing themes' assures a higher survival value in the political market. A recent article in *The Banker* noted with interest that in the budget debates proceeding in the British Parliament over ten years not a single MP ever proposed a single time to cut expenditures.

The politicians' appraisal is reinforced by the media. An examination of commentators in the press and on television demonstrates a preference for 'fresh ideas', a *new* rhetoric or a *new* fad. The media rhetoric prefers a *new* word to almost any thoughtful proposal to abolish or reduce an obsolete or dangerous program. The media themselves find a higher market value with new words in the mass college education market. Attention to old programs, inherited legislation or institutions may infrequently have some market value. But such occurrences form usually the initial preparations for 'more, better, new and larger programs'. Political entrepreneurs find it more advantageous to propose new legislation favoring this or that other group as a way of 'offsetting' the negative effect of previous legislation. But the global welfare effects are not offset. Total welfare is further reduced, government programs increase, the budget balloons and the range of influence open to a bureaucracy expands.

The asymmetry in the distribution of costs and benefits and also the asymmetry in the distribution of information costs summarized above establishes that the emergence of new programs dominates the removal of old programs. They also determine that *specific* programs dominate *general* programs. The capital value expected by organizers proposing *general* and *undifferentiated* tax reductions or expenditure increases is quite small compared to the returns achievable for the same efforts invested to effect *specific* and *highly differentiated* programs. Complex and differentiated programs concentrate benefits on a smaller (interested) group with comparatively low information costs and impose diffuse costs on the 'outsiders' who suffer high costs of information and organization. It will in general not be worth much effort for members of an outside group to organize opposition to a specific and specialized program before or after its imposition. The capital value of investing political activity in specific new programs, differentiated for specific purposes with suitable complexity, tends to be much higher. This pattern of asymmetry in the distribution of costs and benefits explains the entrepreneurial choices of the prevalent types of programs and proposals offered by politicians. This analysis also reveals the unavoidable emergence and increasing range of complexity in tax law or regulatory arrangements. 'Tax loopholes' should be understood as a necessary result of the process. The indignant rhetoric attacking and condemning 'loopholes' reflects on the other hand the entrepreneurial opportunities politicians acquire from their own previous endeavors. This analysis suggests furthermore the fundamental irrelevance of most chapters in the theory of economic macro-policy and implies that systematic and deliberate macro-policies are somewhat improbable."

The bias for new programs and extensions of existing programs inherent in the political process and the associated redistributive mechanism contributes a major strand to the incremental growth of government. We also note that the concentration on specific and relatively complex programs emerges directly from the entrepreneurial behavior of bureaus. A particular bureau explores the political market with programs addressed to well defined groups in order to exploit the information pattern summarized previously. The relative success of the bureaus sampling determines simultaneously magnitude of budget and government, and also the allocation of the apparatus.

Some attention should be directed at this stage to postulate six in this context. The cumulative effect of the incremental growth of the government apparatus gradually raises the expected returns from potential organization by various voter groups. The significant aspect in this context is not the prevailing relative growth of government, but its cumulative effect over time. This rise in expected returns fosters the emergence of new organizations. The resulting wider array of organizations extends the range of political conflict. It extends in particular the range of relative price or income changes, or the range of "desirable objectives" which induce political activities geared to specific redistributions.

It is important in this context that the organizational evolutions and the redistributive process not be arbitrarily narrowed to pecuniary consideration. Voter groups may organize in order to extract directly services and goods from the political process highly valued according to their preferences. The environmentalist movement offers an excellent illustration in this respect. The spread of "single cause movements" in the United States should also be noted in this context. In all these cases substantial organizational efforts are invested in order to achieve via the political process a guaranteed supply of valued services. A redistribution producing direct utilities for the interested voter group offers an incidental advantage over monetary redistribution; it is not subject to taxation. This aspect may not be quite irrelevant in a phase of increasing marginal effective tax rates due to permanent inflation.

The entrepreneurial role of bureaus and politicians may be exemplified with a few selected illustrations. The Department of Health, Education and Welfare of the US Government sampled "client groups" all over the nation and mailed 100,000 letters in order to survey attitudes pertaining to the program for a national health insurance. This exercise is a fine example of suggestive exploration or entrepreneurial sampling. It also reveals the interaction between voter groups, organizations and bureaus. It reveals in particular the entrepreneurial probing of voter's preferences by bureaus and the responses of political organizations<sup>24</sup>. A similar case emerged in the Department of Housing and Urban Development. The Federal National Mortgage Association (the "Fannie Mae") developed over the postwar periods an important position in the national mortgage market. It essentially contributed to the efficient functioning of this market. It acquired in this context over the years large resources invested according to expected returns and risks. But the Secretary of the Department of Housing and Urban Development recognizes here a potential opportunity and proposed that a substantial share of the available resources be offered at advantageous conditions to selected groups. An existing institution should thus be converted into a vehicle of redistribution benefitting a clientele to be mobilized for the benefit of the bureaus or their chief officers<sup>25</sup>. We may also mention in this context political proposals in Massachusetts addressing insur-

<sup>24</sup> Wall Street Journal, April 17, 1978, page 16, "Outreach".

<sup>25</sup> Wall Street Journal, April 24, 1978, page 18, "The Fannie Mae Raid".

ance companies located in the state to invest a good part of their resources in politically designated "assets". Behind the usual rhetoric justifying the proposal threatens a redistribution of wealth from owners, policyholders and employees to particular voter groups. It is also noteworthy that the agencies responsible for the administration of anti-trust-legislation gradually reinterpret apparently their mandate and provide it with a redistributive thrust<sup>26</sup>. We note moreover in passing the battle about "red-lining". Financial institutions supplying mortgage funds in major cities are increasingly accused to discriminate systematically against loan applications made from the "inner city" or more generally from "disadvantaged areas". The political rhetoric evolved with little concern or interest about the nature and the validity of the issue<sup>27</sup>. But cognitive truth is hardly the motive force of politicians and bureaus. The motor force behind the rhetoric are systematic attempts to exploit the political process for redistribution at a new front. Politicians and bureaus recognize opportunities to control assets of financial institutions for, as yet, unattended wealth redistribution.

The Equal Employment Opportunity Commission of the Department of Labor changed its procedures recently. The new procedures open avenues of substantially more aggressive behavior for the bureaus. "The Equal Employment Opportunity Commission outlined plans to sue companies that it says discriminate" against whole classes of employees. "Formerly, the government had just tried to make sure that companies had set affirmative action goals for the future and had'n't discriminated against specific individuals." The new approach of the Commission created a major uncertainty among the business firms affected. Representatives of business objected that the Commission violated established and well understood rules of procedures. A representative of the Labor Department found this objection "ludicrous". We learn in particular "that these rules merely set minimum standards of procedure and specify that the Federal Contract Compliance Director can modify them and request any additional data reasonable for conducting a review". This response of a "bureau" to objections reveals with remarkable clarity the bureaus basic interest to erode constraints and to probe freely for new opportunities of implicit transfers<sup>28</sup>.

The educational bureaucracy and the judiciary also offer useful illustration for the central thesis advanced in this paper. The educational bureaucracy initiated over the postwar decade large changes in the political arrangements bearing on the school system. The number of school districts was radically lowered in the United States. This consolidation was accompanied by a substantial expansion of the bu-

<sup>26</sup> Wall Street Journal, April 14, 1978, page 14, "Anti-Trust: The Coming Battlefield", by *Fred Weston*.

<sup>27</sup> *George Benston* (University of Rochester) found in his preliminary results of a systematic examination no support for the political claims.

<sup>28</sup> Wall Street Journal, February 17, 1978, page 1, "Battle over Bias", by *Liz Roman Gallese*.

reaucratic apparatus and large increases of the budgets. These changes were probably made feasible by an implicit wealth transfer between former districts consolidated into a larger unit. A similar pattern of entrepreneurial legislatures and bureaus modified in New Jersey the rights of local school boards. The legislature granted the State Education Commission authority to overrule budget decision of local communities. A commission instituted by the state legislature proposes now (spring 1977) that local voters be disfranchised in matters concerning their local school system. Less affluent communities can reasonably expect to benefit from this proposal, and more affluent communities lose the right to determine the quality of their own schools. The initiative of legislature and bureau does not proceed in a vacuum of voter preferences as an expression of "political monopolies". They reflect an assessment of politically dominant voter preferences exploitable however in a context of relative monopoly powers determined by the nature of the inherited political structure.

The judiciary also developed in the United States a role which can hardly be overlooked. Litigation increasingly evolved into a major avenue of wealth-acquisition. The expansion of the legal profession and the entrepreneurial behavior of lawyers widened over the decades the range of potentially profitable litigation. But these probing ventures at reinterpretations of existing legislation and the modification of prevailing juridical practices initiated by lawyers are essentially conditioned by expectations of appropriate behavior on the part of the courts and judges. The courts engage in corresponding entrepreneurial behavior of their own and open new avenues for legal action involving implicit wealth transfers. They innovate reinterpretations, evidential procedures and standards of punishment, offering new opportunities for private investments in the "negative sum game" of wealth acquisition. The sums awarded by courts for torts, damages and liabilities exceed in the United States at this stage any reasonable assessment of the values involved by a multiple. This excess is a measure of the implicit wealth transfer operated via the judiciary and the legal system<sup>29</sup>.

<sup>29</sup> The nature of the institutional incentives responsible for this development in the United States in contrast to other countries deserves some careful research. The reader is also referred to two illuminating articles in the Wall Street Journal bearing on the entrepreneurial behavior of the judiciary. On March 31, 1978 (page 16, "Coming Attractions, 1984") an editorial addressed a decision made by a National Labor Relations administrative law judge. The issue involved the right to union representation at a specific plant. A secret ballot arranged according to existing regulations revealed that a large majority of workers expressed opposition to unionization. The judge dismissed this result and imposed unionization on the workers involved according to an arbitrarily selected criterion. The history of the Seabrook Nuclear Power Station (Wall Street Journal, February 24, 1978, page 16, "Berserk Proceduralism") offers some further illustration. It is almost a classic example of the adjustments made by bureaus to limited ranges of organized voter preferences and arbitrary juridical decisions and procedures. The example reveals with particular force the reason for the *negative* sum game built into this specific redistributitional process.

These illustrations are not offered as substantial evidence bearing on a completed and developed piece of analysis. They are designed to elaborate in a suggestive vein the important role of bureaus and politicians in the political process to be determined eventually in the context of a coherent and completed analysis. It is not claimed that bureaus and politicians impose their proposals and procedures on the citizen. They contribute to the incremental expansion of government by probing and searching for ranges of voter preferences to be satisfied. Successful sampling of selected and limited ranges of voter preferences producing appropriate wealth or utility-transfers also benefits the bureaus and legislators involved. Successful probing of voter preferences determines the longer-run return to be expected by these political entities.

### V. Concluding Remarks

The central theme of the paper addresses the fundamental ambivalence of political structure. Such structures raise the expected returns from productive effort and voluntary exchange. But they do not remove all aspects of negative sum games. Man's resourceful coping with his natural and social environment unavoidably induces the systematic exploitation of any political institutions for purposes of wealth-acquisition via investments in the political process. Political institutions offer opportunities to acquire control over resources via privately productive and socially non-productive methods. The crucial difference between anarchy and political structure is not the occurrence or non-occurrence of negative sum games, but their relative magnitude and the absence or prevalence of more or less explicit rules of this game. This fundamental property of political structure explains, in my judgment, the persistent relative growth of government and the erosion of both concept and practice of limited constitutional government. The interaction between voters, bureaus and legislatures produces a persistent process of wealth (or utility) transfers accompanied by an incremental growth of the government apparatus.

Advocates of a contractarian approach to an examination of "government" and political structure argue the need or necessity for a "new constitution" in order to prevent the final emergence of Leviathan. The analysis outlined in section III reveals however a basic flaw in the contractarian view. The contractarian thesis suggests that an established constitution representing the voluntary transaction of individual agents will in general be maintained in the absence of groups insisting on *total* renegotiation. The contractarian position thus misses the crucial consequence of any political structure and the essence of politics. Every constitutional design defines incentives and offers opportunities to exploit the political structure for socially non-productive wealth-acquisition by specific groups or individual agents. No "re-constructing" can avoid this consequence. This does not mean that different political

structures, even within the broad range of democratic arrangements, do not yield substantially different incentives and opportunities with corresponding differences in the growth of both budget and government<sup>30</sup>. But the crucial fact following from the analysis sketched in section III should be fully appreciated: The opportunities created by any constitutional design originally contracted by the social partners produce responses by participants in the social game which gradually modify meaning, operation and range of political institutions. No political structure can ever be fixed by a constitutional contract<sup>31</sup>.

But where does the process evolving in democratic nations eventually lead? I venture some tentative and somewhat speculative thoughts in concluding the paper. The speculative element reflects the unfinished and incomplete state of analysis. It also defines lines of future research bearing on various aspects of the "political economy of government".

The pure wealth-transfer model explains the relative growth of the budget and its eventual convergence to an equilibrium. This equilibrium is determined by the condition that the median voter group discerns no advantage derivable from additional changes in tax schedules producing a larger wealth transfer. But the extension of the analysis incorporating the role of politicians, bureaus and organizations of voter groups introduced additional considerations. The cumulative effect of persistent relative growth of government encourages the formation of political organizations. The larger and wider ranging the government apparatus, the larger is the expected private productivity of political organization. The relative growth of government is thus accompanied by a growth in number and importance of political organizations. Investments in these organizations occur whenever the accumulated stock of political institutions reveals opportunities for wealth or utility transfers. At this stage we observe that changes in relative prices or relative incomes affecting particular social groups yield incentives for new political formations. These formations raise the cost to politicians and bureaus for disregarding or neglecting these social groups. The longer-run effects of relative growth of government are thus re-

<sup>30</sup> A comparison of Sweden with the United States, and Switzerland with the United States, may offer some useful insights in this respect.

<sup>31</sup> The general interpretation of political structure offered in this paper can be usefully extended to non-democratic regimes. The viability of an oligarchy or dictatorial group depends on suitable redistributive arrangements via the operation of political institutions. Inadequate attention or misjudgment of the appropriate redistribution endangers the viability of the ruling group. A variety of events in Eastern European Countries, in Russia or African and/or Latin-American dictatorships offer observations deserving detailed examination from the vantage point elaborated. These investigations would show, according to my conjecture, that even a totalitarian regime *cannot* disregard *completely* the preferences of disenfranchised citizens. Some concessions to these preferences seem a necessary condition for the viability of the regime. A totalitarian regime with all its heavy ideological apparatus cannot escape *some* subtle and indirect influence exerted by the preferences of the citizens. An authoritarian regime with little ideological commitment and a smaller range of political institutionalization suffers even greater exposure to citizen preferences.

flected by an increasing range of political conflict. The frontiers of political conflict cover a widening space of issues. This implies furthermore that the range of negative sum games in society expands relative to the range of positive sum games. The cumulative long-run consequences of relative growth in government are thus gradually made visible by a declining rate of real growth and eventual stagnation. The social structure will be molded more and more in rigid political organizations involved in permanent political conflicts. These conflicts become under the circumstances increasingly irresolvable. The laments deploring the “ungovernability” of the political structure mount in frequency and intensity<sup>32</sup>. Whatever “political capital” elected executives or appointed officials may have originally acquired rapidly decays when confronted in all directions with rigid lines of political conflict. This weakens the central administration and exposes the government to aggressions of the larger or weightier political organizations. There emerges thus a danger of increasing instability of the political process. The political evolution leads under the circumstances with rising probability to various forms of non-democratic societies. This process may evolve gradually over many years. It will also be interrupted by intermittent countermovements. And most particularly, it need not and quite likely will not involve dramatic (or romantic) events of any “deep significance”<sup>33</sup>.

I have drawn admittedly a somber scenario. Fortunately, it may be wrong. There is no guarantee that my analysis is correct. Moreover, even accepting the general analysis laid out in section III, the concluding scenario represents only my *most probable* assessment. Political processes and history are beyond any deterministic schemata, at least in the context of serious cognitive endeavors. Systematic knowledge about political processes and the political economy of government is still in its infancy. We still grope for major answers in a world of pervasive uncertainties. The outline offered and the scenario presented are submitted as an intellectual challenge to cope with this uncertainty<sup>34</sup>.

<sup>32</sup> The general model corresponds to the patterns observed in Italy and New York City.

<sup>33</sup> The importance of May 1968 in France pales somewhat from a ten year perspective. It formed a residual disturbance in the longer-run process.

<sup>34</sup> The analytic program outlined in the paper need also examine the role of socio-political beliefs in the political process. Their pervasive occurrence is hardly disputable and deserves systematic integration into the analysis.

## Zusammenfassung

### *Betrachtungen zur politischen Ökonomie des Staates Das stetige Wachstum des staatlichen Sektors*

Der Aufsatz hebt die grundlegende Ambivalenz aller politischen Strukturen hervor. Diese Ambivalenz drückt sich aus in einer Mischung von gesellschaftlichen Positivsummen-Spielen und Negativsummen-Spielen, die durch die Natur der politischen Struktur geformt werden. Die Negativsummen-Spiele stehen im Zusammenhang mit den Anreizen zur Redistribution, die von jeder politischen Institution ausgehen. Die Vermögensumverteilung stellt somit die treibende Kraft für das politische Geschehen dar. Das reine Vermögens-Transfer-Modell zur Erklärung des Budgetwachstums wird kurz dargestellt. Es zeigt sich zudem, dass der reine Vermögens-Transfer-Mechanismus ergänzt werden muss durch eine Theorie des unternehmerischen Verhaltens der Politiker und der staatlichen Büros.

## Résumé

### *Considérations sur l'économie politique du gouvernement L'expansion continue du gouvernement*

L'exposé met en relief l'ambivalence fondamentale qui caractérise toutes les structures politiques. Ce double aspect contraire s'exprime sous forme d'un amalgame de jeux sociaux à somme positive et négative, combinaison qui est conditionnée par la nature même des structures politiques. Les jeux sociaux à somme négative s'associent aux stimuli de redistribution présentés par chaque institution politique. La redistribution des richesses constitue donc la force d'impulsion propre au processus politique. Un pur modèle de transfert des richesses décrivant la croissance budgétaire y est sommairement résumé. L'argumentation montre par ailleurs qu'un transfert pur et simple des richesses doit être parachevé grâce à l'esprit d'entreprise des hommes politiques et des bureaux chargés de l'exécution.

## Summary

### *Reflections on the Political Economy of Government The Persistent Growth of Government*

The paper emphasizes the fundamental ambivalence of all political structures. This ambivalence is expressed by a mixture of positive and negative sum social games conditioned by the nature of the political structure. The negative sum games are associated with the redistributive incentives offered by every political institution. Redistribution of wealth is thus the motive force of the political process. A pure wealth transfer model explaining the growth of the budget is summarized. The discussion shows moreover that the pure wealth transfer must be supplemented with the entrepreneurial behavior of politicians and bureaus.