Committee 3
Values and the Social Order:
Order by Rules and Rules by Order

DRAFT--7/21/95
For Conference Distribution Only

FEDERALISM AS COLLECTIVE ACTION

by

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The Twentieth International Conference on the Unity of the Sciences
Seoul, Korea August 21-26, 1995

These relationships arise because the states share a collective action problem (Olson 1971) with respect to the national government, a problem that increases with their number. This problem appears in somewhat different forms if politics involves allocative margins (based on welfare criteria) or distributional ones (based on rent-seeking). this problem also affects the political and economic character of the states and may vary depending upon why the number of states increases: because of initial or subsequent choices of internal divisions or because of territorial expansion. But the states' collective action problem pervades all of these possibilities.

Section Two develops the theory and discusses its variants as a function of the nature of politics (welfare-regarding or rent-providing), the political and economic character of the states and the national government, and the cause of the increase in the number of states. Section Three provides some very preliminary evidence concerning whether the predicted relationships hold true. Section Four concludes with some implications of the theory for the prescriptions of Madison's Federalist #10, the notion that the political process, and not judicial intervention, can best protect state sovereignty, the Tiebout model, and the construction of modern federal states.

II. The Theory: Federalism and Collective Action

The theory of federalism as collective action initially requires a notion of political environments at state and federal levels. The two principal views within liberal theories of the public sector are politicians as welfare maximizers and politicians as rent-providers. I explore the implications of each of these views in turn.[3]

A. Federalism in a Welfare-Regarding Nation

Politicians who seek to maximize citizens' welfare try to find ways to create additional surplus. They do so by enacting and administering programs that address well defined problems in the economic theory of welfare. These include the optimal supply of public goods, the optimal encouragement of the supply or abatement of external economies and diseconomies, respectively, the development of policies to address market power, and the coordination of otherwise consensual redistributions.

The partition of jurisdictions in such a federalism ordinarily would follow the calculation of efficient scale. The production of those public goods that are national in scope, such as military defense and foreign relations, fall to the central government. Those that are more nearly local or regional, such as city and county road construction, public health, and public peace, fall to the states. In addition, where preference-revelation problems may arise or inter-polity competition is

3. This paper does not seek to decide, finally, which view is correct. My earlier writings lean toward finding rent-seeking (more generally, the public supply of private goods) as the principal animus of politics. See Aranson and Ordeshook, 1981; 1985. More recently, other possibilities, including elements of public-goods supply, seem relevant. See Aranson, 1990b.

desired, there should be as many state or local governments as is consistent with minimum efficient scale.[4]

How the political process in a federalism converts citizens' preferences into a *national* public choice is important for understanding the theory. Assume that tax shares are set exogenously and that citizens have well formed preferences over levels of a public good that the national government might produce; they elect representatives from their states, who pledge to try to enact the positions of their respective median voters. Each representative then goes to the national legislature, to form a smaller electorate that votes for a public policy at its own median voter's (representative's) position. That policy, within reasonable measurement error, represents the position of the median voter taken nationally. If we satisfy some further heroic assumptions, such as that preferences in both states and in the representative assembly are symmetrically distributed about the respective median voters' positions, then the policy ultimately adopted is also efficient.[5]

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4. Tiebout, 1956. I do not explore the considerable literature and debates over the "Tiebout Hypothesis." See generally the review in Mueller, 1989, pp. 149-176 and references cited therein. Nor do I take completely seriously the application of the Tiebout model to modern state jurisdictions, with respect to states as large as those found in the United States.

5. I assume that these levels are voted on one at a time in both state and legislative ballots, and that no logrolling coalitions form. Hence, there exists a parliamentary stable point, even if the simultaneous aggregation of preferences over all issues would produce no Condorcet winner. See generally Shepsle and Weingast, 1984, and McKelvey and Ordeshook, 1984. I also assume that there are no problems of aggregation on account of the sampling problem itself.

Two problems arise in this casting of national collective choice. First, precisely because the government *is* national, it is a monopoly producer of such public goods. If we invoke the standard monopoly model, output will be too low and price will be too high. If we invoke models of budget-maximizing bureaucrats (Niskanen 1971; Orzechowski 1977), both output and cost will be too large (but price to users may be too low; see Lindsay 1976).[6] In either case national government expenditures as a percentage of properly measured GDP will be greater than would prevail if the national government acted as if it were a producer in a perfectly competitive market. And, surplus will be less.

Second, administrative and executive branch officials may shirk in a variety of ways. Their ability to do so arises from the same principal-agent problem found in firms where a separation of ownership and (some measure of) control prevails. Here, we analogize citizens to shareholders, elected representatives to the members of corporate boards of directors, and executive branch officials and other administrative bureaucrats to agent-managers.

But the principal-agent problem is deeper in the political context. First, ordinarily there are more citizens than there are shareholders in individual private-sector firms. Second, the

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6. Rubinfeld, 1987, reports price elasticities of demand for public services in the range -0.2 to -0.4. Private sector firms with market power ordinarily will operate on the elastic portion of their demand schedules. That the demand for public services appears to be inelastic suggests that Niskanen's model makes a correct prediction of "overproduction." Of course, the same elasticities may be observed to occur in competitive markets.

interests of citizen-"shareholders" and the activities of bureaucratic "agents" cover far more dimensions of evaluation than do the interests and activities of their private-sector counterparts. Third, the public sector has but a muted version of the market for corporate control that works to discipline managers in publicly traded private-sector firms.[7]

In the extreme case of a unitary state, each citizen stands as but one of millions. It is in no individual citizen's interest to monitor, sanction, and reward the bureaucracy for its performance. Nor do the usual institutional arrangements prevail to reduce agency costs to optimal levels. If there are but two or three states, however, each with its own representative, then such activities become reasonable. But as the number of states grows larger, the free-rider problem emerges.[8] Indeed, we may

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7. While I identify shirking principally with the bureaucracy, the same phenomenon doubtless afflicts elected representatives. The reason that the public sector's version of the market for corporate control -- interparty competition -- is muted compared to that of the private sector, is precisely because of this shirking and the "cartel of incumbents" that has enacted legislation to protect itself from competition. See generally Anderson, Shugart, and Tollison, 1989; Aranson, 1992; Aranson and Hinich, 1979; Aranson and Shepsle, 1984; Lott, 1986; 1987; and 1989. Tullock, 1965, first identifies the problem of entry barriers in politics. Holcombe, 1991, links residency requirements to run for office as a means for protecting incumbents in a federalism against each other's "predatory" actions.

8. Olson, 1971. Large institutional investors, such as pension and mutual funds and well capitalized commercial bankers, monitor and sanction managers' actions concerning large, publicly traded corporations. Their actions gain force through the threat of a corporate takeover. Olson identifies a similar mechanism with respect to political collective action problems, where small groups free-ride on the actions of larger ones, which he calls the exploitation of the great by the small. A similar effect may occur in a federalism, where a few large states monitor the

interpret Fiorina's (1989) analysis of Congress to say that elected representatives hold a plurality-producing stake in bureaucratic shirking, because it allows them to act as ombudsmen by intervening with the bureaucracy on behalf of aggrieved constituents.

The same structure of free-riders emerges with respect to the problem of market power. The representatives of a few states might act successfully, for example, to regulate the national government's market power in the production of public goods. But where the number of states is large, they probably could not accomplish the same end. In sum, as the number of states grows larger, we expect the national government's size, share of GDP, and jurisdictional authority to increase absolutely and in proportion to that of the states.

B. Federalism in a Redistributive Order

The preceding discussion takes politics to be welfare-regarding. The national government grows larger as the number of states enlarges because of increasingly imperfect monitoring and sanctioning of national agents' activities. That is, public policy decisions are well motivated and representative of the

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national bureaucracy to the same effect. Hence, the theory that this essay elaborates may have a subsidiary hypothesis concerning the relationship between the size distribution of states and the relative and absolute size and jurisdictional authority of the national government.

median voter's preference on each dimension, but they are not well executed.[9]

Now suppose that politics reflects not public interest criteria but the demand and supply of private, divisible benefits at collective cost, an activity commonly (but perhaps over broadly) known as rent-seeking. How will an increase in the number of states affect this activity? To answer this question we must explore the nature of legislative rent-provision.

Stigler (1971) and those who follow in the tradition of the classical model (see, e.g., Peltzman 1976; Buchanan, Tollison, and Tullock 1980), regard the potential presence of rents as automatically creating a demand for and supply of them. But this process is not automatic, because rent-provision, *ex ante*, is welfare-degrading. In the absence of transactions costs and free-rider problems, rent-provision might not occur.[10]

Rent-provision occurs for two reasons. First, it is in legislators' interest to create a market in rents. This

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9. While our predictions rest on a "pure" public-interest model, one could argue that in acting as Niskanen-monopolists or by shirking, bureaucrats and elected representatives engage in their own form of rent-seeking activities. "Faction, Sir, is the vehicle of all transactions in publick bodies," William Symmes said to the Massachusetts convention that ratified the Constitution of 1789, and "The prevalent faction *is the body* . . . [W]e know that all governments have degenerated, and consequently have abused the powers reposed in them, and why we should imagine better of the proposed Congress than of myriads of publick bodies who have gone before them, I cannot at present conceive." Storing, 1981, vol. 4, Essays 5, entry 12.

10. The same is not true if rents already have been demanded and supplied, and if rents have been capitalized into asset prices. See Tullock, 1975. In that case it would cost more to buy a rent-receiver out of his position than one could gain in added surplus.

inversion of welfare theory's prescriptions happens because it is difficult to make a political market in public goods.[11] The supply of such goods benefits all voters, even if they have opposed the election of the incumbent legislator. But one can make a political market in the public supply of private benefits, because legislators can design programs that exclude nonsupporters as beneficiaries (Aranson and Ordeshook 1985).

Second, in the ordinary rent-seeking configuration of benefits and costs, benefits are large and concentrated in identifiable groups or constituencies, while costs are small per person and diffused across the population. Hence, rational ignorance retards detection, except by those who benefit from the rents (Downs 1957; Aranson 1989/90). So, legislators face incentives to organize themselves to supply private benefits at collective cost (Gamm and Shepsle, 19??). And voters and legislators who would oppose this process would themselves be in the position of supplying the public good of economic efficiency. Given territorially based representation, as the number of states grows larger, free-rider and transaction-cost problems emerge and intensify, making such opposition increasingly unlikely.[12]

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11. An exception occurs if voters' demands for public goods are not homogeneous, and if "high demanders" are present. This configuration of preferences ordinarily leads to the oversupply of the public good, in a manner that resembles rent-provision. See Niskanen, 1975, an article that briefly anticipates but does not explicate the theory described here. The most poignant of high demanders, of course, are those suffering from rare, incurable illnesses, who seek greater government subsidies for research. See Aranson, 1989/90.

12. It remains unclear what effects will prevail if representation in a federalism is not territorially based. Many

Rent-provision at the national level, in a national with more rather than fewer states, will expand the national government's jurisdiction (with respect to regulation) and spending (absolutely, as a percentage of GDP, and in comparison with the states) in two ways. First, rent-provision will reduce the denominator of GDP. Second, spending at the national level will increase, both absolutely and relative to spending by the states.

C. Federalism and the States

To this point we explore the effect of the number of states on the jurisdictional authority and size of the national government. But the number of states also will affect their own jurisdictional authority and size. The argument is not that small states, *ceteris paribus*, individually spend less than do larger ones. That claim doubtless holds true for states with both efficient and inefficient regimes. Instead, the argument is that (a larger number of) smaller states collectively will spend less and individually will have contracted regulatory jurisdictions, compared with (a smaller number of) larger states covering the same territory.

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federalisms use single-member district systems, but some use proportional representation. Many of those, however, elect from regional or state lists (Lander in Germany and Austria). National government budgets as a percentage of GDP are significantly larger in unitary nations and in those that use national lists for proportional-representation elections.

Three patterns may occur. First, heterogeneity among states, especially with respect to the distribution of firms and industries, may lead individual state governments to try to cartelize their respective constituents' markets. If all steel producers are domiciled in Pennsylvania, for example, then its government may try to treat them as a monopoly and add subsidies as well, thereby expanding the state's jurisdiction and increasing its spending.

But this kind of rent-provision grows more difficult as the number of states grows larger within a constant geographical area (Aranson 1990a). As states grow larger in area and population, rent-provision by state governments becomes more likely. As they grow smaller and more numerous, rent-provision becomes less likely.[13] Even if state politics reflect allocative, public-goods margins, as states shrink in size they are likely to demand more national-level coordination to resolve spillover problems.[14] This tendency will shift spending and jurisdictional authority from the states to the national government.

Second, regions containing more than one state may be economically homogeneous, while different regions are

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13. Agricultural cartelization in the United States shows the appropriate pattern. The California raisin market succeeded only as a consequence of national legislation. The same holds true of the Florida orange juice market. Montana's huge severance tax applied to coal survived a Supreme Court challenge and probably succeeded as an economic strategy because Montana enjoys forty percent of known soft-coal reserves, giving it some market power.

14. I am grateful to John Lott, Jr., for discussions on this point.

heterogeneous in comparison with one another. The American South, for example, is more agricultural than is the Northeast, which in turn is more industrial than is the South. Cartelization along regional lines, or, more generally, policies that favor one region at the expense of another, may occur if the number of regions is sufficiently large. More likely than not, however, major regions will not be able to cartelize their producers' markets if the national economy is open to foreign trade. Success at cartelization will require a national policy, which will face opposition if the number of regions remains small. If cartelization in favor of a particular region succeeds at the national level, then secession may become a predictable consequence, as occurred in the United States in 1861.

Third, apart from the homogeneity or heterogeneity of product and factor markets, factor owners may organize to extract subsidies and rents through cartelization. Here the states sometimes can have only a very small role, which diminishes as their numbers increase and their individual sizes grow smaller. Local cartelization may succeed for location-specific goods and services, such as those supplied by members of the learned professions. California, for example, can license hypertricologists and astrologers and can require warning labels on packages holding arguably carcinogenic contents. But if California became ten separate states, such a policy probably would work less well. Successful pursuit of subsidies and rents for mobile factors, goods, and services must take place at the national level, as occurred in the United States concerning organized labor with the passage of the Clayton Act (1911), the Norris LaGuardia Act (1927), and the Wagner (National Labor Relations) Act (1935).

D. Federalism and the National Government

The preceding discussion anticipates that national politics and public policy might differ in federalisms with small and large numbers of states, extending to unitary states themselves. Where the number of states is small, we expect state governments to sponsor more local cartelization, but the national representatives of such states will oppose (geographically derived) cartelization at the national level. Reduced inter-polity competition will undergird the first result, while lower transaction costs (for coalitions opposing national cartelization) will support the second.

Where the number of states is large, *ceteris paribus*, we can expect state governments to sponsorship relatively less state-specific cartelization, but the national representatives of such states will support (geographically derived) cartelization at the national level. Increased inter-polity competition will provoke the first result, while higher transaction costs (for opposing coalitions) will support the second.

The presence of these conflicting forces leads us to hypothesize that as the number of states grows larger, the character of public policy at the state and national levels will change in predictable ways: state politics will produce more efficient public policies, with less successful rent-seeking; national politics will produce less efficient public policies, with more successful rent-seeking. Stated differently, those who find cartelization and related private-interest policies blocked by inter-polity competition at the state level will allocate their political resources to gain these policies at the level of national politics, where the high transaction costs and free-rider problems associated with forming pro-efficiency and welfare-improving coalitions make opposition to rent-seeking more difficult.

This hypothesis suggests an institutionally based explanation for the highly redistributive character of politics in unitary states such as Great Britain, France, Italy, and Israel, and the relatively diminished force of redistributive *national* politics in federalisms such as Switzerland, Canada, and Australia.

D. The Growth of a Federalism

Two related matters reflect likely strategies for expanding a federalism or for changing its composition. First, the number of states may grow larger from external additions or from further internal divisions. Either strategy will increase the jurisdictional authority and budgetary size of the national government, both absolutely and as compared with those of the states. But external expansion seems less likely to reduce the jurisdictional authority and budgetary size of the states, while internal division seems more likely to do so. External additions will keep most local monopolies and taxing ability in place, but further internal divisions will make these more difficult to maintain. This result follows directly from (the spirit of) the Tiebout hypothesis and its implications for inter-polity competition.

Second, the theory carries some strategic political implications. If territorial size is fixed, but at the beginning of the national government the number of states remains variable, then "centralizers" should prefer to divide the nation into more states than will "decentralizers."[15] If the number of states remains fixed but territorial expansion occurs, centralizers should support that expansion, while decentralizers should oppose it.[16]

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15. Venezuela apparently has twenty states when the centralizing party is in power and ten when the decentralizing party is in power. Under the terms of the treaty of Guadeloupe-Hidalgo, by which the Republic of Texas joined the United States, Texas remains entitled to become five separate states. Texas has never exercised this option, perhaps because it prefers to maintain some local monopolies or regulation-related market power (e.g., in petroleum), or perhaps because Texas officeholders understand that an eight percent increase in the number of states would bring about some unwanted policy consequences at the national level and a concomitant reduction in state spending and jurisdictional authority.

16. Not surprisingly, the "Eurocrats" in Brussels prefer to expand the European Union into Central and Eastern Europe, while the "Brugge Group," consisting largely of unreconstructed British Tories, prefers to keep the Union small. Expansion, of course, would reduce the benefits of the trading union, which probably makes the Eurocrats' preferences inexplicable in terms other than a desire for further centralization.

III. Evidence (Very Preliminary)

We now offer five hypotheses, only some of which I have begun to test:

H1: As the number of states in a federalism increases, national government expenditures as a share of GDP will increase;

H2: As the number of states in a federalism increases, the ratio of total state government expenditures to national government expenditures will decline.

H3: As the number of states in a federalism increases, national government expenditures for redistribution as a proportion of total national government expenditures will increase.

H4: As the number of states in a federalism increases, total state spending for redistribution as a proportion of total state spending will decline.

H5: As the variance (or Herfindahl Index, or GINI Coefficient) of state populations (or number of seats in the legislature) in a federalism increases, national government expenditures as a percentage of GDP will decline.

I am presently compiling some data series to test these hypotheses. I can now report only some very preliminary and tentative results concerning H1-2. Cross-sectional tests rely on various OECD publications reported in Lane, McKay, and Newton (1991). A single longitudinal test relies on U.S. series of federal spending and GDP.

Table 1 reports cross-sectional regressions for 22 OECD countries, six of which are federalisms.[17] Variable definitions are as follows:

NSPEND: National government spending as a percentage of GDP;

SSPEND: Total state government spending as a percentage of GDP;

STATES: Number of jurisdictions (states) at first level below national level;

F: = 1 if the nation is a federalism, = 0 otherwise.

The results reported in Table 1 jointly test H1 and the hypothesis that a federal system matters. The independent variable in Regression I (STATES) simply counts the number of units immediately below the national government. None of the pertinent measures are statistically significant. Regression II tests for the same proposition but with a different functional

17. These include Austria, the Federal Republic of Germany, Switzerland, the United States, Australia, and Canada.

Table 1
Dependent Variable: NSPEND
22 OECD Nations

	Equation I	Equation II	Equation III
Constant	27.758 (10.254*)	24.415 (6.622*)	29.080 (13.614*)
STATES	-0.019 (-0.218)	---	---
1/STATES	---	37.068 (0.945)	---
F/STATES	---	---	-83.018 (-1.694+)
Adj. R2	-0.048	-0.005	0.087
F	0,048	0.893	2.869
Prob>F	0.830	0.356	0.106

*significant at better than .05-level
+nearly significant at the .10-level

form; the results are similar to those found with Regression I. Regression III, by contrast, counts as "0" the independent variable for unitary states and develops a rational-number measure for federalisms. These become more like unitary states (the independent variable approaches zero) as the number of states grows larger. While the results are not terribly impressive, the t-statistic on the independent variable is nearly significant at the 0.10-level, as is the F-statistic. The sign, of course, is in the right direction.

Table 2 is based on longitudinal data for national government spending in the U.S. as a percentage of GDP. Variables are as follows:

RATIO:	National government spending as a percentage of GDP;
RATIO(-1):	RATIO lagged on year;
STATES:	Number of states during year;
WAR	= 1 if U.S. was at war; = 0 otherwise;
MA:	Moving average of error terms to control for serial correlation.

Table 2
Dependent Variable: RATIO
1792-1970

Variable	Coefficient	Std. Error	T-Statistic	Prob.
Constant	-0.0101	0.0090	-1.1176	0.2653
RATIO(-1)	0.7953	0.0417	18.8588	0.0000
STATE	0.0005	0.0003	1.7735	0.0779
WAR	0.0350	0.0067	5.2761	0.0000
MA	0.3605	0.0763	4.7231	0.0000

R2 = 0.893; DW = 2.012; F = 364.882; Prob>F = 0.0000

The regression shows a small but statistically significant positive effect of the number of states on national government spending as a percentage of GDP.[18] While comparisons are not particularly apt, the results in Table 2 are somewhat better than those in Table 1, because the longitudinal analysis based on a single national experience removes inevitable country-by-country variations in omitted political and economic variables, The analysis requires further refinement, and I am presently developing a data set for state spending, to test H2.

Table 3
Dependent Variable: SSPEND/NSPEND
22 OECD Nations

	Equation I	Equation II	Equation III
Constant	0.358 (6.475*)	0.360 (4.652*)	0.287 (7.039*)
STATES	-0.001 (-0.582)	---	---
1/STATES	---	-0.295 (-0.358)	---
F/STATES	---	---	2.423 (2.594*)
Adj. R2	-0.033	-0.043	0.214
F	0.339	0.128	6.727
Prob>F	0.567	0.724	0.017

*significant at better than .05 level

18. Lagging the number of states does not affect the estimated parameters reported in Table 2. Differencing the number of states does not produce statistically significant results on the differenced variable.

Table 3 reports results of initial tests of H2, for the effects of changing the number of states on the ratio of total state spending to total national government spending. Here again, Equations I and II show little effect of the number of states on the dependent variable, but Equation III does so. These results are more important than those reported in Table 1 because they predict ratios of relative spending, thus netting out some of the effects of omitted economic and political variables. Equation III, of course, as in Table 1, provides the best fit. This result gives us some confidence not merely that the number of states matters, but also that the federal structure itself makes a difference. The sign is as predicted, and the coefficient on F/STATES is statistically significant.

IV. Implications

Our theory, if not disconfirmed, contributes to an understanding of how and why a federal arrangement matters for politics and public policy. But it also carries important implications for related areas in political and economic theories of government. Here, I briefly review four of these implications: the presence of a crucial omission in Madison's argument for an "extended republic" in Federalist # 10; the Supreme Court's increasingly mistaken reliance on the protections of political process for preserving the federal arrangement; the misplaced reliance of the Tiebout hypothesis on competition among competing jurisdictions to make an efficient market in public goods; and the problem of constructing an enduring federal arrangement in light of the predictions of our theory.

A. The Extended Republic[19]

Madison's Federalist Paper #10, written to urge New Yorkers to adopt the Federal Constitution of 1789, is probably the greatest single document in American political philosophy. Madison fully recognized the problem of "factions," which was his word for modern rent-seeking groups and coalitions. Madison proposes the "extended republic" as a constitutional design to "break and control the violence of faction." Where a faction is a minority, "relief is supplied by the republican principle, which enables the majority to defeat its sinister views by regular vote." But the matter is different "when a majority is included in a faction . . . ." Here, the solution is to make "the majority, having such coexistent passion or interest . . . rendered, by their number and local situation, unable to concert and carry into effect schemes of oppression." That is, "the impulse and the opportunity" must not be "suffered to coincide."

Republics, as compared to democracies, can separate impulse and opportunity by a careful choice of elected representatives. But republics also can descend into kleptocracy. "Men of factious tempers, of local prejudices, or of sinister designs,

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19. This section relies heavily on Aranson, forthcoming publication.

may by intrigue, by corruption, or by other means, first obtain the suffrages, and then betray the interests of the people."

Republics, Madison argues, unlike democracies, can separate impulse from opportunity, because through the delegation of lawmaking authority, they can grow much larger than democracies. An important result follows:

> Extend the sphere and you take in a greater variety of parties and interests; you make it less probable that a majority of the whole will have a common motive to invade the rights of other citizens; or if such a common motive exists, it will be more difficult for all who feel it to discover their own strength and to act in unison with each other.

This is essentially a transaction cost explanation for the difficulty of majority coalitions to form in extended (large) republics; its prediction resembles that of Stigler's (1964) theory of oligopoly. But if our theory about the effects of increases in the number of states hold true, then Madison has made a crucial mistake: the majority will find it most difficult to form a coalition against a rent-seeking minority.[20] This much we gather from our earlier observations about the effects of variations in the number of states on the character of national politics and public policy.

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20. The identification of this mistake is anticipated (though not so clearly identified) in Aranson and Ordeshook, 1977.

Madison's extended republic, of course, covered thirteen states, aggregated into clear sectional interests. While sectional interests remain today, there are now fifty states, with a larger number of regional groupings. We can be more nearly certain, therefore, that Madison's extended republic makes it more difficult to curb the expansion of the national government's spending and jurisdiction, both absolutely and as compared with those of the individual states.

B. Political Protection of State Sovereignty

A related theme often emerges in constitutional argument. In several cases over the years, the Supreme Court has been asked to rule if Congress has exceeded its enumerated powers (U.S. Constitution, Article I, Section 8) and taken away incidents of state power. The Court often replies that the best protection for the states is the political process, through their representation in the Senate, House of Representatives, and even in the electoral college.[21] The Court notes (in some detail) that, "the principal means chosen by the Framers to ensure the

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21. See, e.g., Garcia v. San Antonio Metropolitan Transit Authority, 105 S. Ct. 1005 (1985), overturning National League of Cities v. Usery, 426 U.S. 833 (1976). At issue in *Garcia* was the application of federal wage and hours regulations to municipalities, which the Court ordinarily takes to be agencies of state government. *National League of Cities* had held that setting wages and hours was an essential feature of state sovereignty. The Court changed its mind in *Garcia*.

role of the States in the federal system lies in the structure of the Federal Government itself."[22]

If the theory described here is correct, then the Supreme Court's reliance on protections of political procedure cannot hold true. State and national politics in a nation of thirteen states differ materially from politics in one of fifty states. A nation where state legislatures elected the members of the national Senate (as the original Constitution provides), furthermore, differs systematically from one where the electorate in each state chooses its senators (as the seventeenth amendment provides). The expansion in the number of states and in the voting population doubtless has made protections of political process a frail reed on which to build guarantees of state sovereignty.[23]

Following *Garcia*, Congress did partially roll back the application of the relevant laws that the Supreme Court had upheld.

22. 105 S. Ct. at 1018. For the seminal discussion of "process protections" for the states, see Wechsler, 1961. A critical analysis is found in Rapaczynski, 1986.

23. Justice Blackmun's opinion in *Garcia* offers as evidence of states' political influence in the national government the substantial number of programs that subsidize the states themselves. These are predictable examples of the third pattern of enactments that we review in Section II, where the states themselves seek federal spending for pork-barrel purposes and federal regulations to cartelize various markets.

I ignore here the important influence of expansions in the number of House and Senate seats. These increased with population until Congress decided in 1929 to cap the size of the House of Representatives at 435. The size of the Senate continued to increase with the addition of each new state. While some preliminary analysis based on the OECD sample of 22 nations gives mixed results, a more nearly complete accounting for the relationships discussed here must incorporate the effects of cross-national variations in the sizes of legislatures.

C. The Tiebout Model

At the time of their modern political formation, Great Britain and France shared elements of a federal structure. These structures soon perished, however, because, consistent with our theory, there were so many political subdivisions in each nation. That proliferation of subdivisions probably came close to satisfying Tiebout's assumptions concerning the nature and variety of smaller divisions, and thereby made it likely that his assumption of zero mobility costs could be satisfied as well. But in satisfying these assumptions of the Tiebout model, the forces of collective (non)action were in place ultimately to destroy the very conditions that Tiebout describes.

Stated differently, the economist's studied reliance on small states to make an efficient market in public goods, without more, remains seriously misplaced. It ignores the larger political forces that operate at the national level to eviscerate any efficiency gains from the otherwise beneficial competition that accompanies markets with large numbers of buyers and sellers.

Those who prefer a federal political system, for reasons of economic efficiency, (European) liberalism, or communitarianism, must then confront an essential tradeoff: The smaller and more numerous are the states, the larger and more pervasive will be the central government. Make the states larger, and they lose their characteristics of efficiency, as well as their liberal or communitarian nature.[24]

D. Constructing the Modern Federalism

What, then, is to be done? How do we avoid simultaneously the "rock" of state-level inefficiencies, to achieve a desirable national efficiency, and the "hard place" of national inefficiency, to achieve a desirable state-level efficiency? There are two possibilities for useful constitutional construction, neither of which seems likely to gain acceptance among the national cartel of officeholders, bureaucrats, and interest groups.

The first possibility is to make large nations smaller. At little or no loss in scale economies, the United States could be decentralized into six separate national governments, united in a military confederation and common market. These would include, respectively, the Northeast, the South, the Midwest, the Southwest, and the Northwest. California could be a separate nation. Or, Southern California could go with the Southwest, while Northern California went with the Northwest. (It is not clear where we should place Alaska and Hawaii.) Each nation, on average, would contain nine or ten states.

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24. The Swiss appear to have recognized the second part of this conundrum, as is evidenced by frequent proposals to break up the largest canton, Zurich, whose population in 1980 was 1,122,839. The argument advanced for this proposal is that a community that large cannot enjoy a vital political or social life. See, e.g., Frenkel, 19xx.

The second possibility addresses the problem of making the states too large to achieve efficiency (which probably already holds true). The regions just mentioned could become the states, leaving the preexisting states within them, while trying to strengthen county governments within these states. This solution rests on the notion of "nested institutions."[25] The problem of discerning appropriate jurisdictional authority will remain with this proposal, but it is not likely to be as severe as the present shift of spending and jurisdictional authority from the states to the national government.

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25. I am indebted to Elinor and Vincent Ostrom for discussions about this possibility.

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Committee 3
ICUS-95

31 pp.

Preliminary Draft, 3/5/95
Not for quotation without
permission of the author

Federalism as Collective Action[1]

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I. Introduction

Here I report on some theoretical relationships between the number of states (or provinces, Lander, or cantons) in a federalism and the tendency to centralize (or decentralize) spending and subject-matter jurisdictions in the national government (or state governments). The theory predicts that for a territory under a single national government, an increase in the number of states will result in an increase in the national government's spending and subject-matter jurisdictions relative to those of the states.[2] It also predicts that an increase in the number of states will produce national governments with greater spending levels as a percentage of gross domestic product and more expansive subject-matter jurisdictions.

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1. Earlier versions of this paper were presented at the Workshop in Political Theory and Policy Analysis, Indiana University, and at the Dissertation Workshop, Emory University Department of Economics. I thank the participants for their helpful comments. I have also benefited from discussions with George Benston, John Lott, Jr., and Elinor and Vincent Ostrom. The usual *caveat* applies.

2. To avoid confusion, I refer to political subdivisions below the national government as "states," unless the meaning of an alternative term is clear from the context.