

Published in *Encyclopedia of Public Choice*, edited by C.K. Rowley and F. Schneider, Kluwer Academic Publishers, 2004.

## Direct Democracy

*John G. Matsusaka*

*University of Southern California*

“Direct Democracy” is an umbrella term for a variety of decision processes by which ordinary citizens pass laws directly, without using representatives. The most prominent of these processes is the *initiative*, which allows citizens to place proposals on the ballot that become law if a majority of the electorate votes in favor. California’s tax-cutting Proposition 13 is the best-known example. The *referendum* is a relative of the initiative that permits voters to reject proposals/laws made by their representatives but does not permit citizens to make their own proposals. European governments use referendums for issues concerning European integration, Swiss cantons and municipalities use them to approve new spending programs, American school districts require them to approve annual budgets, and many governments rely on them to amend their charters/constitutions. The *town meeting* is another form of direct democracy, albeit a dwindling one, even in its former bastions of Switzerland and New England. Although most common in the public sector, direct democracy is not a stranger to the private sector. Shareholders in many corporations vote on proposals made by management, and in some are allowed to initiate their own proposals. Referendums and town meeting type government are often employed in condominium and homeowner associations.

The choice between direct and representative democracy has interested thinkers for centuries. Madison’s Federalist No. 10 contains one of the best known arguments against direct democracy, that it will lead to tyranny of the majority: “A common passion or interest will, in almost every case, be felt by a majority of the whole; a communication and concert results from the form of Government itself; and there is nothing to check the inducements to sacrifice the weaker party, or an obnoxious individual.” This view was

incorporated in the U.S. Constitution, and continues to feature prominently in legal scholarship.

Public choice scholarship, on the other hand, has gone down a rather different path. The study of direct and representative government from a public choice perspective began with Buchanan and Tullock (1962). As they framed the problem, the optimal form of government involves a tradeoff between “external” and “internal” costs. External costs arise when a group makes a decision unfavorable to an individual (such as when a smoker becomes subject to a cigarette tax). Internal or “decisionmaking” costs include the time and effort required to participate in a decision (for example, costs of collecting information and time spent voting). In the *Calculus of Consent*, direct democracy was for the most part dismissed as a practical option because of the great internal costs involved in having every citizen participate (page 213): “Direct democracy, under almost any decision-making rule, becomes too costly in other than very small political units when more than a few isolated issues must be considered. The costs of decision-making become too large relative to the possible reductions in expected external costs that collective action might produce.” This argument, in some respects, is the economics principle that labor specialization is efficient, applied to political markets.

While the framework developed in the *Calculus of Consent* has stood up well over time, its conclusion about the relative costs of direct and representative democracy is less secure. For one thing, direct democracy is popular, widely used, and growing in importance across the world. For example, the best available evidence indicates that over 70 percent of American citizens currently have the initiative available to them at either the state or local level (Matsusaka, 2002). If referendums, town meetings, and county initiatives were included, the fraction of people with some access to direct democracy would be even higher. Outside the United States, Switzerland, Italy, and Australia have made use of direct democracy for decades, and virtually all countries have held national referendums at one point or another to decide important issues. The institutions of direct democracy have even spread to former Soviet Union: at least 6 of its 15 successor states have incorporated the initiative in their new constitutions. Either people are willing (and increasingly so) to live with inefficient decisionmaking procedures, or the basic theory is not capturing the benefit-cost tradeoff that is important in practice.

Much of the recent literature can be seen as fleshing out the somewhat skeletal structure of *The Calculus of Consent* to show that the calculus is not quite as unfavorable to direct democracy as it might first appear. The external costs of representative government have received the most attention, particularly the growing appreciation of agency problems. It is now well understood that elected officials sometimes fail to pursue the interests of their constituents, either because they are disproportionately influenced by “special interest” groups, corrupt, or simply ignorant (classic work includes Stigler (1971), Peltzman (1976), Niskanen (1971), Kau and Rubin (1979), and Kalt and Zupan (1984).) When representatives “misbehave” (often defined as failing to implement the median voter policy), theory suggests that voters may be better off if they retain the right to nullify the government’s laws or to propose and pass laws directly. The argument is fairly straightforward: since the median voter would never approve a policy that makes himself worse off, having the right to reject new proposals cannot hurt and possibly can help. The situation becomes somewhat more complicated when agents are asymmetrically informed, and under some conditions the initiative and referendum can make voters worse off. See Gerber (1996) for a clear development of the perfect information model, and Matsusaka and McCarty (2001) and Marino and Matsusaka (2001) for asymmetric information models of the initiative and referendum. All of these models walk in the footsteps of Romer and Rosenthal (1979). See also the “Initiative and Referendum” entry.

The fact that elected officials have limited information gives rise to another external cost of representative government. In the original formulation of Buchanan and Tullock, external costs arise primarily from the risk that a person’s wealth might be deliberately expropriated via the collective choice process. It is also possible for wealth to be expropriated inadvertently, when representatives make a bad decision based on faulty or incomplete information. In situations where the information necessary to make the “right” decision is widely dispersed in the population, centralized decisionmaking by a select group of representatives can be inefficient compared to (decentralized) direct decisionmaking by the populace as a whole. For example, representative decisionmaking is likely to be efficient for narrow technical problems, such as acceptable safety standards on a proposed dam. The necessary information can be collected from a small set of

experts. However, experts cannot provide the relevant information to decide whether the power generated from the dam is worth the environmental damage from flooding upriver. This problem requires information on the preferences of the population regarding the tradeoff between power costs and environmental amenities. That information resides in each person's head and the most efficient way of tapping it may be to hold a referendum on the question. The argument, in short, is that direct democracy can be the optimal form of government for decisions in which the relevant information is widely dispersed among the population. See Matsusaka (1992) and Matsusaka and McCarty (2001) for an intuitive and formal development of these ideas, and supporting evidence.

Another line of research has begun to re-examine the assumption that the internal or decisionmaking costs of direct democracy are prohibitive. To be sure, the cost of becoming fully informed on public policy issues is substantial, and most people have better things to do with their time. Indeed, survey data confirm that voters are ignorant of even the most basic political facts. An obvious concern with direct democracy, then, is that it places decisionmaking power in the hands of the uninformed. However, a promising new line of research suggests that people may not need to be informed to vote their interests. The idea, roughly speaking, is that voters can rely on information cues (endorsements) from like-minded individuals or groups to identify if a ballot proposition is in their interest. If enough cues are available, the electorate can vote as if it is fully informed without having to pay the costs of actually acquiring the information. The early evidence from laboratory experiments and actual election returns indicates that voters are quite skilled at using cues. To the extent cues are available and used, the internal costs of direct democracy may be far lower than originally suspected. The work of Arthur Lupia is central here, for example Lupia (1994) and Lupia and McCubbins (1998). Bowler and Donovan (1998) and Kahn and Matsusaka (1997) provide additional evidence that citizens manage to vote their interests.

The building blocks for the theories just discussed enjoy empirical support—legislatures do fail to follow constituent wishes at times, agenda control does affect the nature of proposals and policy, asymmetric information is correlated with outcomes, and voters do use information cues. However, only a few attempts have been made to see if these pieces add up to a theory of institutional choice. Sass (1991) and Fahy (1998) study

the choice between town meeting and representative government in samples of Connecticut and Massachusetts towns, respectively. The strongest result is that town meetings are more likely to be used in small communities, which they attribute to high decisionmaking costs from direct democracy in populous towns. But this interpretation is undercut by the fact that the initiative is much more common in large cities than small cities (Matsusaka, forthcoming.) Sass and Fahy also find a correlation between direct democracy and population homogeneity, although the relation is weaker. One interpretation is that external (deadweight) costs of rent-seeking are larger when the population is unequal, but it is not clear that this cuts disproportionately against direct democracy. The maintained assumption in these studies is that institutions adapt in the direction of efficiency. This seems like a natural starting point for inquiry, but further research is needed to assess its plausibility. Hersch and McDougall (1997) study the votes of Kansas legislators on a proposal to add the initiative to the state's constitution. They also explore the role of population heterogeneity, but are unable to find a strong relation.

A related question is what determines how often direct democracy is used, given that it is available. Banducci (1998) and Matsusaka and McCarty (2001) provide some evidence on initiative use in American states. Banducci reports that political factors are important, for example, initiatives are more likely to appear on the ballot in states with divided government (the legislature and governor's office are not controlled by a single party.) Matsusaka and McCarty (2001) find that initiatives are used more often in heterogeneous states, possibly a proxy for the difficulty of determining the (median) voter's preferences. Evidence on what issues are addressed by initiatives as opposed to legislatures appears in Matsusaka (1992). The main finding is that "divisive" issues—primarily taxes and social issues—are resolved by initiatives while more narrow issues (for example, pertaining to the administration of government or regulation) tend to be resolved by legislatures. This would be consistent with efficient decisionmaking if the so-called divisive issues are those in which information is widely dispersed.

While the empirical evidence on institutional *choice* is ambiguous, the evidence on institutional *effects* is relatively clear. One result that has emerged from study after study is that institutions matter: the process used to make decisions influences the outcomes. We are still trying to understand how and why they matter by fitting together

the many empirical findings. Evidence from the United States shows that the initiative significantly changes fiscal policy of state and local governments, including the amount of spending, amount of revenue raised, centralization of spending, method of financing, and amount of borrowing (Matsusaka, 1995, 2000, 2002; Kiewiet and Szakaly, 1996). The initiative also brings about changes in social policies, the death penalty and parental abortion notification laws (Gerber, 1996, 1999). Research on Switzerland finds similar fiscal effects of the initiative and referendum at the cantonal and local level (Pommerehne, 1978; Feld and Kirchgassner, 1999; Feld and Matsusaka, 2001; Schaltegger and Feld, 2001). This is a very selective sample of recent work; see the “Initiative and Referendum” entry for more. A number of studies have also shown that cities governed by town meetings spend different amounts and on different things than cities governed entirely by representatives. See, for example, Chicoine, Walzer, and Deller (1989), Santerre (1989), and Sass (1991).

One challenge to research on direct democracy is that its forms vary in practice. We expect town meetings to have different consequences than voter initiatives. Recent research has approached this problem by moving away from indexes of direct democracy that arbitrarily aggregate these processes. Instead, researchers are now focusing on specific procedures. This has heightened sensitivity to the role played by the mechanics of procedures, most notably the importance of agenda control (beginning with Romer and Rosenthal (1979)).

Direct democracy has received far less research attention than representative democracy, and the questions we have far exceed the answers. Yet theory suggests that the demand for direct democracy will continue to grow. The average citizen is now as educated as his representatives and with the dramatic fall in communication costs, can easily be as informed. This should push down the internal costs of direct decisionmaking, and make voters less willing to endure the agency costs of representative government. As *The Economist* (Dec. 26, 1996) recently argued, “what worked reasonably well in the 19th century will not work in the 21st century. Our children may find direct democracy more efficient, as well as more democratic, than the representative sort.”

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