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**Working Paper**

## Democracy, Citizen Sovereignty and Constitutional Economics

Freiburger Diskussionspapiere zur Ordnungsökonomik, No. 06/2

**Provided in Cooperation with:**

Institute for Economic Research, University of Freiburg

*Suggested Citation:* Vanberg, Viktor J. (2006) : Democracy, Citizen Sovereignty and Constitutional Economics, Freiburger Diskussionspapiere zur Ordnungsökonomik, No. 06/2, Albert-Ludwigs-Universität Freiburg, Institut für Allgemeine Wirtschaftsforschung, Abteilung für Wirtschaftspolitik, Freiburg i. Br.

This Version is available at:

<https://hdl.handle.net/10419/4362>

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ISSN 1437-1510

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# Democracy, Citizen Sovereignty and Constitutional Economics\*

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This paper is an exercise in conceptual clarification. Its purpose is to explore the contribution that constitutional economics can make to the theory of democracy. Constitutional economics as the *economics of rules* is concerned with the study of how the choice of rules in the social, economic and political realm affects the nature of the processes of human interaction that evolve within these rules. The theory of democracy is concerned with institutional-organizational problems of self-governing polities. The purpose of the paper is to examine some of the fundamental issues that are brought into focus by applying the perspective of constitutional economics to the rules and institutions of a democratic polity. Sections 1 and 2 discuss general characteristics of the constitutional economics paradigm that are of particular significance to the study of democratic institutions. Sections 3 and 4 explore the contribution that a constitutional economics perspective can make in diagnosing organizational problems of democratic polities.

## 1. Constitutional Economics as Applied Science

Constitutional economics in the Buchanan-tradition is based on a methodological as well as a normative individualism. It starts from the presumptions that, firstly, social aggregate phenomena should be explained in terms of the behavior of individual human beings plus the combined effects of their interaction, and that, secondly, the values of the individuals involved should be regarded as the normative measuring rod against which the legitimacy of social institutions and collective arrangements is to be judged. Because of its normative individualism constitutional economics is often considered a “normative” branch of economics. If this is meant to imply that, by contrast to “positive” economics, constitutional economics issues *value judgments* rather than refutable statements about matters of fact, it is a misleading description. It is misleading because it tends to blur the important distinction between what one might call “*genuine*” value judgments and the kind of “*conditional*” normative statements that *applied* sciences typically make. Or, in technical philosophical terms, it tends to blur the distinction between *categorical* and *hypothetical* imperatives.

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\* Prepared for conference on “The Problems Democracy Faces,” Madrid, December 1 to 3, 2005.

Theoretical sciences provide insights into how the world works, and applied sciences make use of such theoretical insights in order to propose potential solutions to practical problems. As a *theoretical* science constitutional economics seeks to provide insights into how the framework of rules and institutions conditions the ways in which individuals interact with one another, and the social outcomes that result from their interaction. As an *applied* science constitutional economics seeks to provide knowledge for how the choice of suitable rules – or, respectively, suitable changes in the existing institutional framework – can help to solve problems in human interaction. All applied sciences, including applied constitutional economics, make statements about what one “should” do or “ought” to do, if one wants to solve certain problems. By contrast to “genuine” value judgments or *categorical* imperatives, such “should” or “ought” statements are *hypothetical* imperatives that can be rationally discussed on empirical and theoretical grounds. They are false if the remedy that they suggest is in fact not a suitable means for solving the problem envisaged. They are in need of further refinement if alternative and potentially preferable problem solutions can be shown to exist. And they provide irrelevant advice if the addressee at whom they are directed is not interested in solving the problem in question.

Its normative individualism does not turn constitutional economics into a normative economics any more than its interest in solving human problems turns an engineering science into a normative physics. What its normative individualism does is to provide a selective focus to the kinds of questions that constitutional economics seeks to answer.<sup>1</sup> It chooses to concentrate its analytical attention on exploring the *theoretical issue* of how alternative institutional arrangements affect the wellbeing of the individuals living under those arrangements, and the *practical issue* of how institutions may be designed so as to further the common interest of the individuals involved. The arguments constitutional economics advances in answering these questions are, however, refutable statements about matters of fact, not value judgments. To be sure, such statements are of interest – and in this sense “of value” – only to someone who is interested in the questions that they are supposed to answer. But, again, the fact that their “value” depends on the interests of the addressee does not make them value judgments as long as they answer the noted questions purely in terms of refutable conjectures about matters of fact.

Another way of describing the analytical focus of *constitutional* economics – as compared to *standard* economics – is to say that its principal concern is with the issue of how

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<sup>1</sup> As J.M. Buchanan (1999a: 41f.) states his view of the constitutional economics research program: “I am simply proposing, in various ways, that economists concentrate attention on the institutions, the relationships, among individuals as they participate in voluntary organized activity, in trade or exchange, broadly considered.”

individuals can realize mutual gains *by jointly committing to suitable rules*, rules that guide their interaction into socially more productive paths than would otherwise be the case. If, as James Buchanan suggests, the “gains from trade” paradigm is indeed at the very essence of economics in general,<sup>2</sup> constitutional economics can be said to systematically extend the “gains from trade” perspective from the study of voluntary exchange in markets to the “voluntary exchanges of commitments” that individuals may engage in at the *constitutional level* by jointly submitting to mutually beneficial rules. While the economics of markets is about how mutual gains can be realized through voluntary exchange of ordinary goods and services, constitutional economics explores the mutual gains that can be had from adopting better rules of the game, in all arenas – economic, social and political – in which individuals interact with each other.

It is instructive to contrast the perspective of constitutional economics with that of traditional welfare economics. Like constitutional economics welfare economics can be said to belong to the *applied* branch of economics in the sense that it uses theoretical economic insights in order to propose solutions to practical problems, specifically the problem of how a polity can improve its “welfare.” In other words, both approaches advance conjectural advice about what kinds of policy measures promise to advance the “welfare” of the polity concerned. And, because welfare economics defines welfare in terms of individual utilities, i.e. the wellbeing of the individuals involved, it may appear to share the same normative individualism on which constitutional economics is based. Yet there is, as Buchanan has repeatedly stressed, a paradigmatic difference between the two approaches, a difference that he describes as the contrast between the constitutional economist’s “gains from trade perspective” and the welfare economist’s “allocational or maximizing perspective” (Buchanan 2001: 137).<sup>3</sup>

What is different about the two perspectives becomes apparent as soon as one takes a closer look at the way in which they model the individual and at the nature of the advice that they provide, specifically in regard to the question of who is, explicitly or implicitly, the addressee at whom the advice is directed. Arguing from a gains-from-trade perspective the

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<sup>2</sup> Buchanan (1999a: 36): “(T)hat mutual gains can be secured through cooperative endeavor, that is, through exchange or trade ... is the one important truth of our discipline.”

<sup>3</sup> Buchanan describes the difference between the two perspectives in terms of their respective definitions of “market failure.” From the gains-from-trade perspective market failure “means that there exist unexploited gains-from-trade, and the economist diagnoses such failure by identifying that prevent the potential gains from being exploited” (Buchanan 2001: 137). By contrast, from the maximizing perspective market failure “implies inefficiency in resource usage, and the economist performs his diagnostic task when he identifies departures from those conditions that must be satisfied to insure optimality” (ibid.). Accordingly, the allocationist economist “calls explicitly for a shift in allocation, independent of direct reference to the institutional setting” (ibid.), the gains-from-trade economist “calls, quite simply, for a removal of the barrier” (ibid.).

constitutional economist looks at individuals as sovereign choosing agents who, by their actual choices, express what they judge to be in their interest and who, by their voluntary agreement, express what in social matters they consider to be in their *mutual* interest or, in this sense, to be “welfare enhancing.” Accordingly, as advisor in matters of “social welfare” the constitutional economist’s analytical focus is on advancing conjectures about how, as politically organized groups, individuals may be able to realize mutual gains, in terms of their own judgment, and, in particular, conjectures about what kinds of collective choice procedures may better enable them to advance their common interests. The addressees of such advice are the individuals themselves, and the test of the adequacy and relevance of the advice is in whether the individuals addressed consider the constitutional economist’s suggestions to serve, indeed, their interests, and in whether the factual assumptions implied in the respective conjectures are correct.

By contrast, arguing from an allocational, maximizing perspective the welfare economist looks at individuals as preference or utility functions from which he “reads” the utility values that serve as entries in the social welfare function upon which he, in turn, bases his judgment on what policy measures can be said to enhance the welfare of the respective polity. In this construction the individual disappears as a sovereign choosing agent<sup>4</sup> and is reduced to the role of providing the utility-measurements that the welfare economist uses as informational input into his welfare calculations.<sup>5</sup> The analytical problems welfare economists encounter in deriving their social welfare functions (measuring utility, interpersonal comparison of utility) are well known and need not be recounted here. Even if we assume that all these problems could be satisfactorily solved, the issue that is of principal interest in the present context would still remain, namely, who is supposed to be the addressee of the welfare economist’s advice or, in other terms, who – apart from those interested in the theoretical exercise as such – might be interested in being advised about how the welfare economist’s aggregate function of “social welfare” may be maximized. Put in still another way, since, as

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<sup>4</sup> As Buchanan (1999a: 34) notes: “If the utility function of the choosing agent is fully defined in advance, choice becomes purely mechanical. ... (A) computer can make all of my choices for me.” – This is, in fact, what Walras and his followers intended to achieve in representing the individual as a utility function. As Walras (1954: 256) noted: “In our theory each trader may be assumed to determine his own utility or want curves as he pleases. Once these curves have been determined, we show how prices result from them under a hypothetical régime of absolutely free competition.” And, as Georgescu-Roegen (1971: 343) reports, Walras’ successor on the Lausanne chair, Vilfredo Pareto, stated, in quite similar terms, that once we have obtained “a photograph of his tastes ... the individual may disappear.” As a comment on this quotation (as reference for which he cites V. Pareto, „Mathematical Economics“, *International Economic Papers*, Nr. 5, 1955, p. 61) Georgescu-Roegen (ibid.: 343) remarks: „The individual is thus reduced to a mere subscript of the ophelimity function  $\Phi_i(x)$ .”

<sup>5</sup> Buchanan (2001: 138): “The allocational economist defines an individual strictly in terms of a preference or utility function. ... In this analytical construction, efficiency or optimality in resource use is defined in terms of individual values, but these values are ‘disembodied’.” – For a critique of the implicit collectivism of the ‘social welfare function’ approach see Vanberg 2005: 10ff..

noted before, applied sciences advise addressees about how they can better solve problems they face, the question that the welfare economist needs to answer is, who they suppose might care about solving the problem for which they propose solutions. As far as individual citizens as principals are concerned, we can safely assume that they will be interested in proposals for how their own welfare, jointly with that of their fellow citizens, might be improved. They will, however, hardly care for advice on how aggregate social welfare may be enhanced as such, irrespective of whether this increases or decreases their own welfare. As far as politicians, who act as citizens' agents, are concerned it does not seem to be very plausible either to assume that they have a personal interest in heeding the welfare economist's advice, at least not any more than they expect that by maximizing "social welfare" they can successfully solve problems they personally care about, such as the problem of advancing their political career. If, however, neither citizens nor politicians can be reasonably assumed to be interested in solving the problem of maximizing "social welfare," it is difficult to see, to whom welfare economists think they are talking – other than to themselves.<sup>6</sup>

## 2. Constitutional Economics and Contractarianism

With its gains-from-trade perspective constitutional economics adopts a *procedural* normative standard for judging social matters. By contrast to approaches that, like welfare economics, seek to evaluate social outcomes in terms of attributes of the outcomes *per se*, constitutional economics bases its normative judgment on attributes of the process from which outcomes result.<sup>7</sup> The measuring rod for what can count as "socially preferable" or "welfare enhancing" is located in the subjective preferences or interests of the individuals who are involved in the transaction or social arrangement, preferences or interests that they express with their own *voluntary choices*. It is not because of attributes that he could read from outcomes *per se*, but only because of the fact that they result from *voluntary agreement* among the participating individuals that the observing economist may conclude that exchange transactions or collective arrangements are welfare enhancing, as judged by the participants themselves. Accordingly, the analytical focus of the constitutional economist's procedural normative judgment has to be on the issue of whether or not the outcome-generating process can reasonably be assumed to be based on voluntary agreement of the parties involved.

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<sup>6</sup> The argument spelled out above is, of course, little more than a restatement, albeit from a somewhat different perspective, of the well known Wicksell-Buchanan charge that welfare economists act as if they were proffering policy advice to an imaginary benevolent despot (Buchanan 1999d: 456).

<sup>7</sup> Buchanan (1999b: 204): „Whereas the ‘social welfare function’ approach searches for a criterion independent of the choice process itself ..., the alternative approach evaluates results only in terms of the choice process itself.”



In fact, if examined more closely, the economist's standard assumption that market exchange is mutually beneficial or "efficient" can be shown to ultimately rest on nothing other than the claim that it is based on voluntary agreement of the trading parties. In other words, it is not because of attributes to be found in market outcomes per se, but only because of attributes of the process from which they result that economists can infer their "efficiency." By market exchange economists do not just mean any kind of exchange transaction, no matter what the circumstances are under which the traders make their choices. Instead, by market exchange they mean trades that are carried out under conditions which can be assumed to assure the voluntariness of the transaction.<sup>8</sup> Even if this is not necessarily reflected in the way they are described in standard text books, in the economist's understanding markets are not just places where demand and supply meet, whatever the conditions may be that prevail in these places. Markets are institutionally secured arenas for voluntary trade and voluntary cooperation, arenas within which rules are enforced that aim at preventing the use of coercion and fraud. It is ultimately only on the assumption that markets are, in this sense, arenas for voluntary exchange that economists can base their efficiency claims for market outcomes.

In effect, constitutional economics simply seeks to generalize to all levels of cooperative arrangements the procedural logic that, even if rarely made explicit, is systematically implied in the economist's standard notion of efficiency in market exchange, by consistently extending it from the level of market transactions to the level of collective-political action and, in particular, to the constitutional level at which the rules for the socio-economic-political game are defined.<sup>9</sup> The constitutional economist's central tenet is that a consistent normative individualism requires one to regard voluntary agreement among the parties involved as the ultimate criterion on which alone efficiency claims can be based, in the case of collective action and constitutional choice no less than in the case of ordinary market exchange.<sup>10</sup> What is true for market outcomes is, he insists, equally true for political outcomes: Whether or not they are welfare enhancing cannot be judged in terms of attributes of the outcomes per se, but only in terms of attributes of the processes from which they result, namely the extent to which they can reasonably be assumed to result from voluntary

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<sup>8</sup> Buchanan (1999a: 38): "The 'market' ... is ... the institutional embodiment of the voluntary exchange processes that are entered into by individuals in their several capacities."

<sup>9</sup> Buchanan (1999a: 39): „The task of the economist includes the study of all such cooperative trading arrangements which become merely extensions of markets as more restrictively defined."

<sup>10</sup> Buchanan (1999c: 248): "One of the great advantages of an essentially economic approach to collective action lies in the implicit recognition that 'political exchange,' at all levels, is basically equivalent to economic exchange. By this we mean simply that mutually advantageous results can be expected from individual participation in community effort."

agreement among the individuals involved – if not their agreement to the outcomes themselves, at least their agreement to the decision rules that produce them.

As Buchanan has repeatedly noted, there is an apparent affinity between the constitutional economist's approach to politics and the *contract theory of the state* in that both derive the legitimacy of the coercive power of government from the voluntary consent of those who are subject to such power. It is in reference to its emphasis on the legitimizing role of voluntary consent that constitutional economics can be justly described as a "voluntary exchange theory of government." Such label is not meant at all to negate the coercive nature of governmental power. It is meant to indicate that a government can claim legitimacy for its power of coercion only if, or to the extent that, such power is granted by, and exercised within the limits of a constitution its citizens voluntarily agree to. The reason for individuals to voluntarily submit to such a constitution is that by their joint commitment to the respective set of rules they can expect to realize benefits that otherwise could not be had or, stated differently, to play a "better game" than they would in the absence of such joint commitment.<sup>11</sup> In this sense, the label "voluntary exchange theory of government" is simply supposed to point to the fact that, just as they can realize mutual gains from ordinary market exchange, individuals can realize mutual gains through voluntary exchange of commitments to rules at the constitutional level.<sup>12</sup> And just as efficiency claims for market exchange are contingent on the voluntariness of the traders' choices, efficiency claims for "constitutional exchange" are equally contingent on whether or not the individuals involved voluntarily submit to the rules in question.

The contractarian perspective that constitutional economics shares with the social contract tradition in political philosophy can be given, and has been given, different interpretations, three of which are of particular interest in the present context because they differ markedly in the line of inquiry that they suggest constitutional economics should pursue. A quite common interpretation of the contractarian perspective, prominently exemplified by John Rawls' *Theory of Justice*, centers around the notion of a *hypothetical* contract. Authors who adopt this version of contractarianism direct their attention to the issue

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<sup>11</sup> Buchanan (1999b: 204): „Since it is carried out only after general agreement, collective action is essentially voluntary action. State or governmental coercion enters only insofar as individuals, through collectively imposed rules, prevent themselves from acting as they would in the absence of such rules.” – On this issue see also Buchanan (1999a: 39).

<sup>12</sup> Buchanan (1977: 136): "Economists ... are specialists in exchange ... . When they observe a social interaction, they interpret the results in exchange terms, as possibly emerging from voluntary action. To the extent that results can be fitted into the exchange pattern, economists can infer that *all* parties secure gains, as these gains are measured in terms of the participants' preferences and not those of the observer. ... This explanatory-evaluative task for the economist may be extended from the simplest to the most complex institutional structures."

of what kinds of rules a group of self-interested individuals can be expected to agree upon if they were to make their choice among potential alternative rules under ‘ideal’ conditions, conditions that are presumed to assure that the contractual agreement is reached in a voluntary, informed and fair manner. In the case of Rawls’ theory it is the conceptual construct of constitutional choice “behind a veil of ignorance” that is meant to describe ideal conditions under which the contracting parties can readily arrive at a voluntary agreement on mutually advantageous rules because they are, both, informed and uninformed in ways that eliminate potential sources of disagreement. On the one hand, they are assumed to be perfectly knowledgeable about the *general working properties* of potential alternative rules such that, in this regard, disagreement because of differing expectations is ruled out. On the other hand, they are supposed to be perfectly uninformed about any *particulars* that would allow them to anticipate any specific and differential effects that the chosen rules may have on themselves by contrast to other persons, such that conflicting interests in differentially advantageous rules are excluded as a potential source of disagreement.

Whatever insights the inquiry in what people can be expected to agree upon under ‘ideal’ conditions – whether what counts as ‘ideal’ is defined in Rawlsian or in other terms – may generate, it is obvious that they can be of limited value only to constitutional economics as an applied science that seeks to provide advice for how real people may solve their constitutional problems. As noted earlier, advice that an applied science provides will be of relevance only if it informs the addressees of how they may solve a problem they are *interested in solving*. And the question must be asked of whose problem-solving interest may be served by information about what persons would agree upon under ideal conditions. The hypothetical contract approach has been criticized for quite some time that the insights it produces are of no consequence. And, surely, if constitutional advice is to be of relevance it needs to inform addressees who know who they are about changes in rules that promise to make them better off, relative to where they are, and not about what would be in their interest if they would not know who they are and were placed under hypothetical conditions.

The hypothetical contract construct can be contrasted to two alternative lines of inquiry that one may pursue from a contractarian perspective, lines of inquiry that, as I suppose, promise to lead an applied constitutional economics onto a more productive research path. Instead of conjecturing about what might be agreeable under hypothetical conditions the constitutional economist may seek to advance conjectures about potential factual agreement, i.e. conjectures about what changes in rules would promise mutual gains for all parties involved, compared to the status quo, rule-changes that should be agreeable to the parties

concerned, given the conditions in which they actually find themselves. Such conjectures are conjectures about constitutional interests that the individuals involved actually have in common, as opposed to conjectures about constitutional interests that they would share under hypothetical conditions. While conjectures of the latter sort hardly qualify as relevant constitutional advice, by providing conjectures of the first kind constitutional economists inform the addressees about how they may come to “play a better game” among themselves, for the benefit of everybody involved.

Whether the constitutional economist’s conjectures about mutually beneficial constitutional changes are in fact true or not depends not only on the correctness of the underlying hypotheses about the factual working properties of rules. It also depends on the addressees’ subjective evaluation of the consequences that the rules under consideration are predicted to have. However correct the constitutional economists hypotheses about the factual working properties of rules may be, if his expectations about what kinds of consequences the addressees themselves regard as beneficial are wrong his conjectures about welfare-enhancing rule-changes will be falsified. In this sense the addressees themselves are the ultimate judges on what can count as ‘welfare-enhancing’ in matters of constitutional reform, and their agreement to suggested constitutional changes is the ultimate test of the constitutional economist’s conjectures about mutually beneficial reform.<sup>13</sup>

The emphasis on “in this regard” is important for two reasons. First, because the addressees can, of course, not be considered to be the ultimate judges on the truth or falsehood of the constitutional economist’s conjectures about the factual working properties of rules. And to the extent that their rejection of suggested reforms is based on incorrect expectations about how the reforms will actually work, their rejection of the constitutional economist’s advice does, of course, not falsify his conjecture that the suggested reform, if adopted, would work out in ways that the addressees would consider mutually beneficial. In such cases, lacking agreement would point to the fact, that additional ‘constitutional information’ may be needed to allow the addressees to make a better educated choice. The second reason why the emphasis on the “in this regard” is important is that a failure to find agreement may not be due to the falseness of the constitutional economist’s conjectures but to ‘blockages’ in the existing decision making procedures that prevent the addressees from reaching an “agreement”<sup>14</sup> on suggested rule-changes that what would in fact be in their

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<sup>13</sup> Buchanan (1977: 137): “The observing economist can suggest ways and means through which improvements may be made by agreement among all parties, and the test of his hypothesis lies only in agreement itself.”

<sup>14</sup> “Agreement” is put in quotation marks here because it is meant to denote not only unanimous group decisions but any kind of collective decisions that are made according to decision making rules that themselves are based on voluntary agreement among the members of the group.

common constitutional interest, ‘blockages’ that may exist because of strategic behavior or for other reasons.

I noted above that there are two alternative lines of inquiry that a contractarian constitutional economy may pursue by contrast to the construct of a hypothetical agreement. The above remarks on ‘blockages’ in the existing decision making procedures point to the second of these alternative lines of inquiry. Like the first it is concerned with the addressees’ *factual* constitutional interests as opposed to constitutional interests that they might have under hypothetical ideal conditions. Yet, while the first line of inquiry is concerned with the issue of which rules may promise to be mutually beneficial and can, therefore, be predicted to be agreed upon among the relevant parties, the second is concerned with the quite different issue of how well potential alternative rules or procedures for choosing rules are suited to enhance the prospects for those rules to be actually chosen or established that serve, in fact, the common constitutional interests of the parties involved. In other words, the applied constitutional economist who pursues this line of inquiry is interested in identifying potential changes in the rules for choosing rules, or in the procedures for establishing rules, that may enable the individuals concerned to more readily and more reliably select and establish among themselves rules that are in their *common* constitutional interests, whatever these constitutional interests may be in substance.

The distinction between, on the one hand, conjectures about which rules may be in the common constitutional interest of a group of persons and, on the other hand, conjectures about which rules for choosing rules enhance the prospects for common constitutional interests to prevail is an important distinction even if it may appear somewhat subtle. By contrast to the former, the validity of the latter conjectures does not depend on the substantive content of persons’ constitutional interests, i.e. on what kind of rule-regime they wish to adopt. They are purely factual conjectures about what procedures for choosing rules make it more likely that rules will be chosen which serve the *common* constitutional interests of the persons concerned, as opposed to constitutional interests that they may harbor individually and separately but that are in conflict with each other. Whether these conjectures are true or not is to be decided on theoretical and empirical grounds. The persons to whom the constitutional economist addresses his advice may, of course, reject to adopt rules which he supposes favor the choice of mutually beneficial rules. But such rejection does not prove that the constitutional economist’s conjectures are wrong, it only indicates that the addressees of his advice prefer, for whatever reason, other procedures for constitutional choice than those

which, according to his conjecture, would improve the chances for their common constitutional preferences to prevail.

### 3. Democratic Polities as Citizens Cooperatives

In the remainder of this paper the general arguments that have been made above about constitutional economics as an applied science and about the advisory role of constitutional economists will be applied to the case of democratic polities. Before turning to this issue, though, it is useful to briefly discuss in more explicit terms the distinction between different levels of collective-political choice – and, accordingly, between different levels of political advice – that has been implicit in the above analysis.

With his distinction between “the order of rules and the order of actions” Hayek has drawn attention to the systematic interrelation that exists, in terms of the game-metaphor, between the ways in which the rules of a game are defined, i.e. the “order of rules,” and the kinds of moves that the players will choose in playing the game, i.e. the “order of actions.” With his distinction between “the constitutional and the sub-constitutional level” Buchanan has pointed to the fact that “the order of rules” may consist of several layers of rules such that in addition to the *rules of the game per se*, i.e. the rules that define what the players may do or not do in playing the game, there are *rules for choosing rules* and even *rules for choosing rules for choosing rules*. The former I propose to call *operating rules*, the latter *constitutional rules*, “constitutional” here understood in the sense of “rules for choosing rules.” Applied to the collective choices that the citizens-members of a democratic polity may make the Hayek-Buchanan scheme suggests as distinction between three principal levels of choice. There are, first, choices at what one may call the *allocational level*, in the sense of policy choices that directly intervene into the “order of actions” or the playing of the game, policy choices that seek to correct directly outcomes of the game by correcting allocational choices the players have made. By and large the attention of traditional welfare economics may be said to mainly focus on this level. Its principal ambition is to provide advice for how “government” may improve social welfare by correcting “inefficient” allocational choices of private economic agents. Constitutional economics, by contrast, focuses attention on the second and third level of political choice. Its principal tenet is that, again in terms of the game metaphor, the more adequate strategy for correcting (systematically and not just incidentally occurring) undesirable outcomes of a game is to seek to improve the *rules* of the game rather than intervening into the playing of the game. This can be done directly by changes in what I have proposed above to call *operating rules*, i.e. the rules that define how the game is to be played,

and it can be done indirectly by changes in the *constitutional rules*, i.e. the *rules for changing rules*. In what follows I shall refer to constitutional choices of the first kind as *constitutional choices type I*, and to those of the second kind as *constitutional choices type II*. The ultimate purpose of political choices at all three levels is, of course, to contribute to a desirable “order of actions,” i.e. to make sure that the ways in which the game is played, and the outcomes it produces, serve the interests of the persons involved. Constitutional choices of either type are, in this sense, no less than policy choices at the “allocational level” *ultimately* targeted at improving the resulting “order of actions.” They differ with regard to the level at which they “intervene” in order to achieve this ultimate purpose.

As has been said before, advice that an applied science provides must, if it is to be of any practical relevance, be directed at an addressee who has an interest in solving the problem for which the advisor suggests a solution. In case of democratic polities the citizens are, quite obviously, the natural addressees for constitutional advice that seeks to inform about potential mutual gains from trade. Democratic polities can be best described as *citizens’ cooperatives* or, in John Rawls’ (1971: 84) terms, as “cooperative venture(s) for mutual advantage.” Just as the members of co-operative enterprises or voluntary associations are the owners or principals of their joint venture, the citizens of democratic polities are the “owners” or principals of the polity as a territorially based association. They are the “sovereigns” with whom the ultimate authority to decide on the polity’s affairs resides.<sup>15</sup> There are, to be sure, important differences between democratic polities on the one side and “ordinary” co-operative enterprises or voluntary associations on the other, among them, in particular, the fact that a polity is not only a *territorial* but also an “*inter-generational*” organization in the sense that new member are typically “born into the polity” rather than admitted by an express act of voluntary entry. Such differences do, however, not alter the fact that in a democratic polity no less than in any other co-operative enterprise the members-citizens are the sovereigns with whom the ultimate authority to decide upon common affairs rests.

As far as constitutional choices of type I are concerned, i.e. the choice of operating rules, contractarian reflections on what rules of the game citizens would agree upon under hypothetical, ideal conditions can, for reasons discussed above, not be expected to result in constitutional advice of practical relevance. Neither the citizens as members-principals of democratic polities nor politicians as their agents can be plausibly assumed to find such information on hypothetical agreements helpful for solving problems they are interested in solving. If constitutional advice is to be of interest for citizens who know who they are and

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<sup>15</sup> Rawls (1999: 577) describes “democratic citizenship in a constitutional democracy” as “a relation of free and equal citizens who exercise ultimate political power as a collective body.”

who can anticipate how they, personally, will be affected by suggested rule changes, it has to provide information on how mutual gains may be realized by all parties involved compared to the status quo and given their actual (not their hypothetical) constitutional interest. In other words, if he wants his advice to be of practical relevance the constitutional economist must suggest changes in the rules of the game that, as he conjectures, promise mutual gains for all parties involved, in terms of their own judgment, given their actual interests. Or, stated in yet another way, he has to suggest rule-changes that he conjectures to serve the common constitutional interests of the members-citizens of the polity.

The constitutional economist's task as advisor is to examine the existing operating rules for potential "defects" that prevent citizens from realizing mutual gains that could be had, and to suggest constitutional reforms that may correct for such "defects." The ultimate judges on whether or not the rule-changes that the constitutional economist suggests do in fact allow for mutual gains are the citizens themselves. Their voluntary and informed agreement is the *ultimate* test of whether his conjectures about what is in citizens' common constitutional interest are correct or not.<sup>16</sup> Failure to find such agreement proves the constitutional economist's conjectures wrong, if not his conjectures about the working properties of the suggested rules at least his conjectures about what kind of constitutional environment the citizens themselves consider desirable.<sup>17</sup> That the citizens' voluntary and informed agreement is the *ultimate* test for what is in their common constitutional interest must be emphasized for two reasons. First, even where the relevant decisions are made under unanimity rule *factual*, *observed* agreement, or *factual*, *observed* failure to reach agreement, need not be perfectly reliable indicators of what is and what is not in citizens' common constitutional interest but may be due, instead, to insufficient information, strategic behavior and other reasons. Second, collective choices in democratic polities are typically not all made by unanimity rule. As J.M Buchanan and G. Tullock have argued in their foundational contribution to constitutional economics, *The Calculus of Consent* (1962), there are prudential reasons why citizens-members of a democratic polity – as, in fact, members of any cooperative enterprise – may voluntarily choose to give up the veto power that a unanimity rule grants and to agree to

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<sup>16</sup> Buchanan (1999b: 207f.): "In a sense, the political economist is concerned with discovering 'what people want.' The content of his efforts may be ... summed up in the familiar statement: *There exist mutual gains from trade*. His task is that of locating possible flaws in the existing social structure and in presenting possible 'improvements.' His specific hypothesis is that mutual gains do, in fact, exist as a result of possible changes (trades). This hypothesis is tested by the behavior of private people in response to the suggested alternatives. Since 'social' values do not exist apart from individual values in a free society, consensus or unanimity (mutuality of gain) is the only test which can insure that a change is beneficial."

<sup>17</sup> As noted earlier, the citizens as the addressees of constitutional advice can, of course, not be considered the relevant judges on whether or not the constitutional economist's conjectures on the factual working properties of alternative rules are true. Such conjectures have to be judged on empirical and theoretical grounds, not in terms of preferences.



decide, instead, their common affairs by majority rule, or even to delegate decisions to representatives or agents whom they authorize to make political choices on behalf of the polity, at either of the three noted levels. In this sense a careful distinction must be made between unanimity as the *ultimate legitimizing principle* in democratic polities and unanimity as a *decision rule* for ongoing policy choices. Or, in other words, one must distinguish between the *source of legitimacy* of a democratic polity's constitutional rules and the *content* of these rules. While the constitutional rules of a democratic polity can ultimately derive their legitimacy from no other source than the voluntary agreement among its members-citizens,<sup>18</sup> in terms of their content they may very well allow for non-unanimous decision or the delegation of decision making authority.

The test of whether or not the constitutional economist's suggestions for constitutional reform find acceptance by the actual decision making procedures that the citizens of a democratic polity have established among themselves can only be a *proximate* but not the *ultimate* test of their validity. Such procedures may well allow for the rejection of rules that are, in fact, in citizens' common constitutional interest, and they may allow for the acceptance of rules that are not. Accordingly, if the constitutional economist's proposals for reform fail to find acceptance by the existing decision making procedures this must not be taken as the final verdict on the validity of his conjectures on what serves the common constitutional interests of a polity's citizens. It may also be due to shortcomings of, or 'defects' in, the decision making procedures, i.e. in the rules for choosing rules, that prevent reform proposals from being accepted even though their acceptance would be in citizens' common interest. There are reasons, therefore, for the constitutional economist to examine whether there might be such shortcomings or defects in a polity's rules for choosing rules, i.e. its *constitutional rules*, and to look for ways in which they may be corrected. This points to the second level of constitutional choice, namely of constitutional choice type II, at which the constitutional economist may play a role as advisor.

#### **4. Constitutional Rules and Citizen Sovereignty**

In terms of the distinction between *operating rules* and *constitutional rules* the institutions of democracy must be classified under the latter category. Democracy as a system of government is characterized by *particular procedures* for making policy choices and for

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<sup>18</sup> As D. Mueller (1998: 173) notes with regard to the unanimity principle: "It provides a normative underpinning to the constitution in that the assumption of unanimity combined with that of individual rationality implies that the institutions of the constitution must be expected to advance the interests of *all* citizens. The basic institutions of the polity are not designed to allow one group of individuals to exploit another."

choosing the operating rules of a polity, namely procedures that are supposed to promote the common interests of the citizens and that derive their legitimacy from citizens' voluntary consent. This is what the characterization of democratic polities as "citizens' cooperatives" or as "cooperative ventures for mutual advantage" is meant to express. Democratic institutions may, therefore, be examined, in particular, with regard to their capacity to actually enhance the prospects for a "citizens' cooperative" to come to adopt mutually beneficial operating rules. And, how well democratic institutions perform as procedures for choosing rules may, accordingly, be measured in terms of their capacity to promote citizens' common constitutional interest. This criterion for judging the performance of democratic institutions can be called, as I suggest, *citizen sovereignty*. To "improve" democratic institutions means, in terms of this criterion, to make them better instruments for citizen sovereignty, i.e. to change them in ways that better enable citizens to realize mutual gains from joint commitment to rules that are in their common constitutional interest, whatever these common interests may be in substance.<sup>19</sup>

The criterion of *citizen sovereignty* is central to the second capacity in which constitutional economists may serve as advisors in democratic polities, namely in providing information on potential changes in a polity's *constitutional rules*, i.e. in the rules for choosing rules, that enhance the prospects for citizens' common constitutional interests to prevail and, thus, increase the chances for the polity to actually operate as a "cooperative venture for mutual advantage." Proposals for reform that the constitutional economists may submit in this regard are, to be sure, subject to the "test" of whether or not they will be accepted by the citizens to whom they are addressed, or, more precisely, of whether or not they pass the existing decision making procedure by which a citizens' cooperative changes its constitutional rules. But this test is an "acceptance-test" only, not a test of the validity of the constitutional economist's conjectural advice. Whether or not the constitutional reforms that he suggests are in fact suitable to further citizen sovereignty is to be judged on empirical and theoretical grounds. As the polity's sovereigns citizens are, of course, entitled to opt for other constitutional rules than those which, according to the constitutional economist's conjecture, would allow for more citizen sovereignty. But their refusal to follow the constitutional economist's advice does not prove his conjecture wrong. It only proves that, for whatever reason, the citizens prefer not to follow his advice.<sup>20</sup>

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<sup>19</sup> Buchanan (1999d: 461): "Improvement in the workings of politics is measured in terms of the satisfaction of that which is desired by individuals, whatever this may be, rather than in terms of moving closer to some externally defined, supra-individualistic ideal."

<sup>20</sup> Because it would not add anything of systematic relevance, I do not discuss here the fact that such refusal may be due to 'defects' in the actual procedures by which a democratic polity chooses its constitutional rules and that,

The constitutional economist's advice for how to "improve" democratic institutions in terms of *citizen sovereignty* can actually come in two versions, a "weaker" and a "stronger" version. As the "weaker" version I consider advice about potential changes in the procedures for choosing rules that – by comparison to the existing procedures – promise to improve the chances for choosing rules that serve individuals' common constitutional interests, relative to the status quo. Such advice takes the *existing* constitutional rules as the benchmark against which "improvement" is measured. By "stronger" version I mean advice on how the existing procedures for choosing or establishing rules ought to be changed if the aim is to create more conducive conditions for *voluntary and informed consent* in constitutional choice. As subtle as it may appear, the distinction between the two kinds of constitutional advice is of significance. As noted, in the first case the *constitutional status quo* is taken as the benchmark against which it is to be judged whether or not suggested constitutional changes promise to allow for more citizen sovereignty. In the second case the constitutional status quo is itself judged against a normative criterion, namely in terms of the extent to which it can be reasonably assumed to be based on voluntary and informed consent of the persons concerned. And constitutional advice of the "stronger" version is advice for how the procedures by which rules are chosen and established may be changed in ways that facilitate not just the reaching of *factual* agreement on mutually beneficial rules, but that promote *voluntary and informed* agreement in constitutional choice.

The relevant analogy here is with the notion of voluntary market exchange discussed above. As noted there, the normative quality or 'efficiency' that economists attribute to market exchange is based on their, explicit or implicit, assumption that markets are institutionally secured arenas for *voluntary* cooperation. It is because – or, more precisely, to the extent that – the institutional framework within which they take place assures (as far as this can be assured under real-world constraints) their voluntary and informed nature that market transactions can be assigned the normative qualities that the gains-from-trade paradigm emphasizes. Analogously, 'efficiency' may be attributed to constitutional agreements or agreements on rules if – or, more precisely, to the extent that – the conditions under which they have been reached justify the presumption that they are based on voluntary and informed consent of the contracting parties. And just as the constitutional economist can inquire into how the institutional framework of markets may be 'improved' by creating more

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therefore, one may ask for these procedures, in turn, whether they could not be improved in terms of their capacity to promote citizen sovereignty. Following this line of reasoning would mean that the constitutional economist may have to shift his attention to the level at which the 'rules for choosing rules for choosing rules' are chosen.

suitable conditions for voluntary and informed exchange, he may likewise inquire into how at the level of constitutional choice more favorable institutional conditions for voluntary and informed agreement may be created.

The “weaker” and the “stronger” version of the constitutional economist’s advice for how to promote citizen sovereignty differ in terms of the reasons why the addressees to whom the advice is given, i.e the citizens of a democratic polity, may want to listen. Advice of the “weaker” version directly appeals to citizens’ constitutional interests, given the constitutional status quo. It informs citizens about potential changes in the existing procedures for choosing rules that will improve the prospects for mutually beneficial rules to be chosen. Citizens who believe such advice to be correct have prudential reasons to agree to the suggested constitutional changes because they promise to make them better off, jointly with their fellow-citizens. In this sense the “weaker” version of the constitutional economist’s advice can surely be expected to be of practical relevance. It informs about possibilities for solving a problem that its addressees, the citizens, presumably have an interest in solving. Apparently, the same cannot be said about advice of the “stronger” version. Advice of this kind does not appeal to citizens’ given constitutional interests but refers, instead, to the normative standard against which the constitution of a citizens’ cooperative should be measured, namely that it is legitimized by the voluntary consent of the citizens-members of the polity. It suggests changes in the procedures for choosing rules that one should adopt if one wants to create more suitable conditions for voluntary and informed constitutional choice and, thus, conditions that can lend more credence to the claim that a democratic polity’s constitution is based on voluntary and informed acceptance on part of its citizens.

Since advice of the “stronger” version does not appeal to *interests* of its addressees but to a *normative principle*, namely the legitimizing force of voluntary and informed agreement, it may perhaps seem as if advice of this kind is subject to a similar charge as the welfare economist’s advice, namely not to be tuned to the interests of real persons but to be directed to an imaginary, benevolent dictator who is interested in the normative principle as such. I do not consider this charge to be justified, nor would it be justified, in my view, to charge the inquiry into suitable conditions for voluntary and informed constitutional choice with committing the same mistake as the “hypothetical contract”-approach, namely to speculate about what hypothetical people would agree upon under hypothetical conditions instead of conjecturing what may be mutually beneficial for real people, given the situation they are actually in. To start with the latter charge, there is a fundamental difference between speculating about the content of hypothetical contracts and seeking to identify institutional

provisions that may, under real-world constraints, create more conducive conditions for voluntary and informed constitutional choice. While information on the content of hypothetical agreements is, presumably, of little interest to people who know who they are, information on what may enhance voluntariness in constitutional choice may well be of interest to real citizens, to the extent, at least, that they are interested in living in a polity that can claim to be based on voluntary and informed consent of its citizens. And, this brings me to my answer to the first charge, for citizens of democratic polities there are indeed, as I suppose, good reasons for having an interest of this kind.

With advice of the “stronger” version the constitutional economist reminds citizens of democratic polities of the normative foundation on which their polity as a citizens’ cooperative is based. He informs them about possibilities for constitutional reform that, as a matter of normative consistency, they should consider if they want to secure better pre-conditions for their polity to actually operate as a cooperative venture for mutual advantage. Such advice is not at all directed at an imaginary benevolent dictator but at the citizens themselves. It tells them what provisions they may jointly adopt if they wish to enhance voluntariness in matters of constitutional choice, provisions that – in terms of A. O. Hirschman’s (1970) classification – may strengthen their voice-options or their exit-options.<sup>21</sup> Apart from reasons of normative consistency, a prudential reason for citizens to follow such advice is that a democratic polity can be expected to be more stable and robust against changing circumstances the more its constitutional foundations can be assumed to be based on the voluntary and informed consent of its citizens.

## 5. Conclusion

As an applied science constitutional economics inquires into how people may realize mutual gains from joint commitments or, in other terms, how they may come to play “better games” among themselves by “exchanging” commitments to suitable common rules. The citizens of democratic polities as “cooperative ventures for mutual advantage” are the natural addressees for the kind of advice that such an applied constitutional economics may be able to provide. The focus of the above analysis has been to draw a distinction between two different levels at which constitutional economists may provide advice to citizens of democratic polities in matters of institutional-constitutional choice. The first level concerns, as I have called them, the *operating* rules and the second level the *constitutional* rules, i.e. rules for choosing rules. Advice on operating rules is based on conjectures about which among alternative rules are

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<sup>21</sup> These are, for instance, institutional provisions that fall under the rubric of “competitive federalism” (see e.g. Vanberg 2000 and 2001, pp. 7ff.).

better suited, in terms of their working properties, to result in mutual advantages for the members-citizens of a polity. Such conjectures have two kinds of components, namely hypotheses about the factual working properties of rules on the one hand and, on the other hand, assumptions about what, in terms of final outcomes, the citizens concerned will find preferable. While the citizens to whom advice for reforms in operating rules is addressed are, to be sure, the ultimate judges on the latter, they cannot be considered the competent judges on the validity of the constitutional economist's conjectures on the factual working properties of rules. Advice on constitutional rules is based on conjectures about which among potential alternative procedures for choosing rules provide better chances for citizens' common constitutional interests to prevail. The validity of such conjectures is to be judged in terms of empirical and theoretical arguments, not in terms of citizens' preferences, even though, of course, it is up to citizens as the sovereigns of democratic polities to decide upon whether or not they wish to follow the constitutional economist's advice in such matters.

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