



Small-Group, Multi-Level Democracy: Implications of Austrian Public Choice for Governance Structure

FRED E. FOLDVARY

ffoldvary@scu.edu

Department of Economics, Santa Clara University, 500 El Camino Real, Santa Clara, CA 95053, USA

Abstract. This paper examines the process of mass democracy as the fundamental cause of transfer seeking and the centralization of governance, using Austrian-school theory and methodology such as decentralized knowledge, disaggregated phenomena, and the structure of capital goods. The alternative of decentralized, small-group governance reduces the demand for campaign financing and makes more effective use of decentralized knowledge. In addition, when public revenues originate in the local districts and are passed on to higher levels of governance, it provides incentives for revenue sources which do not have an excess burden on production. The governance structure of cellular, bottom-up, multi-level voting, with public revenue flowing up from the lower to the upper levels, provides a contrast for a comparative systems analysis that can yield insight into the transfer seeking endemic in mass democracy.

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1. Public Choice and Austrian Economics

Dennis Mueller (1979:14) states that “the properties of public goods provide the *raison d’être* for collective choice” (emphasis in the original). Public choice consists of choosing for others as well as oneself. Public choice also involves voting, collectively-made social choosing.

A key principle of public-choice theory is that where benefits are concentrated and costs are spread thinly, the incentives are present to obtain knowledge and to organize to obtain transfers via the political process, to the detriment of the market process and of public well being, since the incentives to counter the special interests are lacking for both voters and consumers. This conclusion is based on the supply and demand characteristics of the political process. As Gwartney and Wagner (1988:8) put it, “The public choice theorist postulates that pursuit of votes is the primary stimulus shaping the behavior of political suppliers” of governmental goods and transfers. To reach a mass of voters, the politician requires substantial amounts of funds: “Politicians must also have an eye for how their actions will influence their campaign coffers” (1988:9). This demand is met by special-interest suppliers whose concentrated benefit provides them with an incentive to invest in political capital, whereas the typical consumer or voter, bearing a small cost for any particular program, lacks the incentive to make similar investments, since the net benefit of reducing the cost of such legislation is less than the cost of attempting to prevent it. The voter is therefore rationally ignorant: “Since one vote is not going to decide who is

elected, why should an individual study the issues and research the positions of alternative candidates?" (1988:11).

Gwartney and Wagner (1988:10) express the public-choice conclusion thus: "This *bundle purchase nature* of representative democracy substantially reduces the ability of voters to register their preferences on specific issues. It also increases the ability of government to extract taxes" (italics in the original). Government is able to practice fiscal discrimination, transferring resources from those with little clout to those that have influence, with not just losses to one party but also damage to society as a whole, as "the substitution effects will bring about economic waste and excessive government" (1988:18). Charles Rowley (1994:291) notes that the rent seekers (transfer seekers) include not just the special-interest beneficiaries but also "those departments of government and those government-dependent private contractors whose budgets" are augmented. "Rent" in the context of "rent seeking" as a commonly used term in the public choice literature refers to the "economic rent" or gains beyond those necessary to put resources into productive use.

Austrian theory complements this public-choice conclusion, as it invokes knowledge, uncertainty, time, and subjectivism. Indeed, Austrian theory intersects public-choice theory to create an Austrian version of public-choice theory that in some aspects can enhance and in other aspects may substitute for a neoclassical approach to public choice.

Austrian concepts that can be applied to public choice include the decentralized nature of knowledge, the subjective nature of values and preferences, the use of interpretive understanding (*Verstehen*), the disaggregation of phenomena, an emphasis on process over time rather than an equilibrium at a moment in time, the analysis of spontaneous order, the productivity of roundabout investments, and the methodology of axiomatic-deductive reasoning. Other Austrian methods, those of marginal analysis, methodological individualism, and the role of the entrepreneur are more widely shared to various degrees by the neoclassical and some other schools of economic thought.

Austrian insights can enhance not just the positive analysis of public-choice but also the constitutional analysis of alternative political regimes. Mainstream public-choice theory has focused on constitutional remedies: "*substantive constraints* designed to limit the scope of the ordinary legislative process and protect freedom of contract and private property from all intruders" (Wagner and Gwartney 1988:37) (italics in the original). Mainstream policy urges a greater appreciation for existing constitutional provisions, e.g. that the "time has come for the Court to recognize the Constitution's full protection of economic liberties" (Aranson 1987:310).

Historical experience has been such that while constitutional constraints such as the specification of powers, the division of branches of government, federalism, and the election of officials have generally acted to prevent the most extreme types of tyranny, the central governments of industrialized countries have nevertheless grown substantially during the past century. Peter Aranson (1985) notes that scholars in various fields have recognized the inability of current constitutional arrangements to suppress rent seeking. Federalism, for example, can formally divide power, but actual power becomes de-facto united if the structural incentives are such that the federal government dominates taxation and then programs such as conditional revenue transfers to the States centralize power in practice as the States must comply with regulations to receive the funds.

Hence, analysis that delves deeper into the epistemic and institutional aspects of public choice can help generate analysis of more fundamental remedies. This constitutes what Wagner and Gwartney (1988:37) call “the procedural design approach” that analyzes alternative institutions that change the outcomes.

Interests having high expected benefits along with some knowledge of the impact (e.g. ultimate incidence) of the benefits have an incentive to invest in roundabout political capital in the form of relationships and funds to seekers and holders of political office. These higher-order political capital goods include a knowledge of the political process by the transfer seekers and the provision of knowledge to the political officials by the seekers. The political capital also includes the establishment of personal relationships and the instillation of sympathy by the office seeker and holder for the special interest. It includes the rationalization by the official in statements to the public and even to himself that the transfers are in the public interest. This “false knowledge” propagated to the public is a political capital good for the transfer seeking special interest or faction, although a public bad for the general public.

Voters, consumers, and workers in general are rationally ignorant when the cost imposed by each special-interest transfer is low. Voters also tend to be apathetic on many issues, “apathy” consisting of an absence of either sympathy or antipathy toward some activity. For example, the federal government provides loan guarantees to some exporters, and studies have shown that these subsidies shift resource but do not increase output (Slivinski 2001:13). If voters and taxpayers knew about such subsidies, they might become outraged, i.e. have antipathy to the program. But due to their lack of knowledge about this specific program, they are apathetic, having no strong feelings against it.

Ignorance therefore complements apathy, as the lack of motivation to organize to prevent the transfer is complementary to the lack of motivation to obtain more knowledge about the specifics of the transfer. Since values are subjective, and different persons have different values, there will be some individuals whose preference for obtaining knowledge of corporate welfare is such that they are antipathetic to such transfers (and possibly have more knowledge about it, which complements their antipathy), hence these individuals do organize and join taxpayer or consumer organizations such as the 335,000-member National Taxpayers Union. Since the financial benefits of joining an organization such as the NTU, which advocates lower taxes and less government spending, is almost all an external benefit to others now and in the future, joining the NTU is evidence of sympathy for the cause of lower taxes or more efficient government, or antipathy to their opposites, and the fact that only a small percentage of US taxpayers have joined such organizations indicates the extent of apathy among taxpayers, not to paying taxes, but to fighting the system.

The uncertainty of whether organizing and fund-raising will be sufficient to overcome the power and finances of the transfer-seeking special interests also inhibits organizing by the public, unless they can be aroused out of their apathy by a civic entrepreneur who creates and leads a mass movement. Uncertainty reduces the perceived benefit of organizing and obtaining knowledge, hence turns the cost/benefit ratio to the degree where the anticipated cost exceeds the personal benefit for the typical victim of the transfer.

The branch of political economy known as “constitutional economics” is based on Knut Wicksell’s concept that, as James Buchanan (1988:104) put it, looks “to the structure within

which political decisions are made.” As noted by Peter Boettke (1994:255–256), the above public-choice outcome “might present a serious problem for the traditional classical liberal faith in democracy.” However, a rent-seeking outcome such as export loan guarantees is not a result of the democratic process as such, but of the particular institutional structure that exists in contemporary democratic countries. The problem is not the traditional belief in democracy but the belief in traditional democracy. The model inherited from the parliament in the United Kingdom and other influences is that of mass democracy, where a large number of individuals vote for a representative with whom they are not personally acquainted.

In earlier times, the population was smaller and the vote more restricted, providing a lower ratio of voters to representatives, and there was also a limited scope for mass media. But today, the ratio of voters to representatives is in the thousands and millions, and mass media has expanded in both scope and cost. This has reduced the cost-effectiveness of resisting transfers while increasing the effectiveness of transfer seeking by those with concentrated benefits, since the electorate receives messages by several mass media from newspapers to billboards to television and mass mailing and now e-mail. Candidates for office have a high demand for campaign financing, since they need the mass media to influence the voters, and the special interests have an incentive to supply the funds, since the centralization of political power into a top-down system provides the means to extract the revenues from the public via taxation, revenues which can then be channeled to the transfer seekers.

Given the structure of mass democracy, campaign financing can also serve a beneficial end of protecting an interest group from legislated restrictions and costs. For example, an association of gun owners might finance campaigns in order to prevent legislation that outlaws guns. Campaign financing is also associated with the freedom of speech, since the dissemination of ideas is costly. Restrictions on campaign financing therefore can infringe on the freedom to propagate ideas as well as attempts to protect a group from infringement on their liberties. Campaign finance reforms that attempt to limit funding of political campaigns only treat the symptoms of the problem rather than the cause, and in doing so, may prevent the protection of liberties while attempting to limit corruption.

The institution and model of mass democracy has been replicated around the world as various countries have transformed their political process from dictatorship to mass democracy. The different variations, such as the British-style parliamentary system versus USA-style president and Congress, or representation by geographic district versus proportional representation by party, do not greatly affect this basic outcome of mass democracy. The reason for the adoption of this mass-democracy model is not the public weal but partially a general ignorance of alternatives and partially the realization by powerful interests that this model preserves their privileges.

There has been some recognition of the problem of centralized governance and an analysis of decentralized structures. Donald Chisolm (1989), for example, has challenged the proposition that centralization promotes efficiency, arguing that decentralized organizations create methods of informal coordination. He notes as an example the San Francisco Bay Area transit systems, which do not have a unified hierarchy.

But while informal coordination uses local knowledge, the government agencies themselves are elected by mass democracy, and so simply decentralizing some programs and operations may not substantially reduce the problem of special-interest influence. Since

the fundamental cause is mass voting, it is fruitful to analyze the alternative, small-group voting.

2. Cellular Bottom-Up Multi-Level Governance

As Buchanan (1988:109) has noted, the improvement of the political process requires an “institutional change that will allow the operation of politics to mirror more accurately that set of results that are preferred by those who participate.” The constitutional alternative to large-group or mass democracy is small-group democracy. The variant which will be designated here as “cellular democracy” has the following features.

1. All jurisdictions are divided into small neighborhood districts, each electing its own council. The population should be sufficient so that there are usually enough volunteers to serve on the council, but not so large that it becomes infeasible to personally meet most voters and distribute literature at low expense. A population of about 500 may suffice in many cases; this is the population of the village of Arden, Delaware, which is built on a land trust and governed by town meetings and volunteer committees. Another community of similar population is the Fort Ellsworth condominium in Alexandria, Virginia, with 169 dwelling units; it elects a board of directors and also has several volunteer committees (Foldvary 1994). A somewhat larger or smaller size could be established, but based on these examples, the order of magnitude sufficient for a viable council seems to be less than a thousand residents or members. At any rate, the borders of the districts should be flexible, so that at the option of the members, the jurisdiction may be adjusted to suit the local circumstances. Often, already established borders and institutions such as voting precincts or residential associations would provide ready-made jurisdictional areas.

Each of these districts elects a council, including one or more alternate council members. The neighborhood council is designated as the level-1 council, level zero being the individuals or households. The council members may be recalled at any time by petition and vote. Individuals only vote for this neighborhood council. Confining the vote to just one local council limits the epistemic problem that voters face when casting votes for representatives; in this case, the knowledge would be local, personal, and easily accessible, consistent with Friedrich Hayek’s (1945:522) analysis of “the knowledge of the particular circumstances of time and place.”

2. Groups of neighborhoods and their councils form a region, or the level-2 governance. A suggested number of level-1 neighborhoods forming a level-2 region is around 10 to 20, which would also equal the number of representatives in the level-2 council. A larger number of representatives would dilute the voting power of the agent, reduce the personal acquaintanceship of the representatives, and induce factions and parties. At any rate, the number would be flexible and determined by the choices of the level-1 councils of their level-2 membership, as described in (4) below.

The optimal number of representatives to a higher-level council is most likely lower than that of the level-zero voters because the individual residents need not do more than vote, while the representatives are responsible for policy and the public finances.

Each level-1 council elects a representative and an alternate to the level-2 council. At level-1, an alternate council member replaces the member elected to level-2. A level-1 council may recall and replace its representative to level 2 at any time.

3. Groups of level-2 regions and councils in turn form the next higher level area, level-3, where again each level-2 council elects a representative and an alternate to the level-3 council, recallable at will. The process is repeated until it reaches the highest level council, designated here as “level h .”
4. One or more level- i councils may secede from the next higher level ($i + 1$) jurisdiction (other than level h), and create a new $i + 1$ level. Thus, each council, other than h and $h - 1$, has an exit as well as a voice option.
5. Public revenues originate in level-1 councils and flow up to the higher levels, except possibly for royalties or extraction charges or rents on minerals, water, and other material resources, and for pollution charges. Any level may charge a user fee for a particular service, so long as it is a genuine voluntary fee and not a disguised excise tax. There can be higher-level laws on the assessment, distribution, and amounts of the revenues among the levels of governance, but the collection of revenues is confined to level 1. No individual or property owner at level 1 may be taxed or have an imposed charge other than by the level-1 council. Moreover, a council of level higher than 1 may not require the level-1 council to implement any taxation of income, sales, value added, transactions, buildings, or personal property.

With this constitutional structure, all voting is done in small groups. The governance structure consists of federated multi-level cells, hence the designation “cellular democracy.”

3. Public Choice with Cellular Democracy

One of the conclusions of Buchanan and Tullock (1962:114–115) in their landmark work *The Calculus of Consent* was that “where possible, collective activity should be organized in small rather than large political units.” Mancur Olson (1971:63) had also theorized that in large groups, the incentive is lacking to avoid transfer seeking, but that incentives could be present in a federal grouping, i.e. with smaller groupings.

Cellular democracy, as described above, not only breaks the electorate into small units, but also provides constitutional rules which further minimize transfer seeking as well as the wasteful or abusive exercise of power by higher-level governments. With the individual voter only directly electing the neighborhood (level 1) council, the candidates do not require the mass media to reach the electorate. The voting jurisdiction is small enough for face-to-face meetings with the voters, either in meetings or door-to-door, and the distribution of the candidate’s publications is inexpensive. With a small jurisdiction, those who seek office and are well regarded by their local neighbors can most likely obtain a position as a level-1 council member.

In mass democracy, one incentive to run for office is the power and fame that can be wielded by the office holder, as well as the financial rewards of the office as well as from those seeking to influence legislation who provide gratis travel and other favors. With cellular democracy, ambitious political entrepreneurs could seek to rise up the council levels

to become a member of the highest level councils, with the associated fame and prestige. But even those with less ambition have incentives to volunteer for the lower-level positions, as in fact communities such as condominiums and residential associations have volunteer boards and committees. Motivations can vary from personal gains such as experience that can be included in a resume, social reasons, the desire to be useful to others, and sympathy with the community, the “fellow feeling” that Adam Smith (1982) describes as being a human motivator along with self interest.

There can still be some scope for political parties in a cellular voting structure. Candidates can identify themselves as belonging to a party, with the hope of having that party represented at the levels of government. There can therefore be mass advertising by political parties as well as by interest groups promoting various issues and the candidates favorable to those issues. But a candidate who is not a member of a dominant party or who takes a different stance from such interests can still easily contact the electorate and present his views. Hence, the demand for campaign funds is much reduced, severely limiting the power of special interests to influence the voters. There need not be any legal limits to campaign financing, since the very structure of the governance will limit the advantage of money.

Special interests can attempt to influence legislation at a higher level council. But the next lower level, $i - 1$, can monitor the level i council and recall representatives when the level $i - 1$ council members think they are no longer acting in the interest of the $i - 1$ districts. The secession option further strengthens the lower levels, since a wasteful or abusive level i could find itself with no lower-level members if they withdraw and regroup.

Cellular democracy would also facilitate the privatization of governance, where the local community can easily become a contractual association. New communities could then arise to cater to particular purposes (such as the retirement communities common today) and to various cultural preferences. This could be facilitated by bringing the secession option down to level zero, the individual household, wherever the physical structure of the community makes it feasible.

4. Fiscal Implications

With public revenues flowing from the lower to the higher levels, even if the amounts of revenues are set by the higher levels, there would likely be little demand top-down transfers of funds, or “revenue sharing.” This eliminates the ability of higher levels to impose conditions on the lower levels for obtaining revenue. The bottom-up flows of revenues complements the bottom-up voting to prevent the concentration of power at the highest levels.

The rules for electing and recalling representatives reinforce the decentralist incentives. The representatives at all council levels have been elected by all the lower levels, since the level h representative is elected from level $h - 1$ representatives, and these are elected from those of level $h - 2$, and so on down to level 1. If level-1 recalls its representative that was elected all the way up to level h , he is also recalled from all the higher level councils. Each representative is thus accountable to all the lower levels which elected him, all the way down to level 1.

Roy Cordato (1994:379) has pointed out that Austrian economists have exerted “little effort” to analyze “the effects of different types of taxation on economic behavior.” A

comparative analysis of mass versus cellular democracy will show that the institutional change will lead to a change in the tax base. With most public revenue originating at the level-1 district, the base of the revenue will tend to fall on inelastic and immobile sources due to competition among communities. Industry and residents will flee, or not migrate to, neighborhoods with high taxes on incomes, sales, transactions, and goods unless many neighborhoods form a tax cartel. Even then, like with cartels of producers, those districts which don't adhere to the rules can profit from reducing the tax burden, so any tax cartels will likely break down.

The main resource amenable to local taxation or revenue collection is land, which is both immobile and inelastic in supply. The collection of the site rents is also more efficient, not imposing an excess burden relative to elastic supplies such as labor, capital goods, and financial assets. The costs of raising revenue are also lower for land rent than for production and transactions, which have to be audited and involve complex rules.

Anthony de Jasay (1994:276) claims that for collective goods, marginal rates of substitution are not revealed by the market process, nor "do public goods have prices." But the typical collective works and services provided by local government, such as streets, parks, security, recreation and schooling mostly impact those in the vicinity and are thus territorial. These increase the demand to be located in the territory, capitalizing and increasing the rentals and prices of sites. Hence, these public goods do have prices: the site rentals that residents are willing to pay to be located there, exclusive of the value of the buildings. In paying such rentals, residents do indeed reveal their marginal rates of substitution between sites and other goods.

Cordato (1994:380) also noted that Austrian theory could shed light on taxation's effect on the time structure of production. Unlike the taxation of capital goods, a tax on land rent does not affect the time structure, since the rent is there regardless of who collects it. A tax on rent also does not skew the price and profit market signals that Austrian theory recognizes as vital. (See Tideman (1994) for an analysis of rent-based public finance.)

Indeed, privately owned communities do not normally use transaction fees or charges based on personal income, but in effect are based on rental fees and assessments (Foldvary 1994). Hotels, marinas, mobile home parks, industrial parks, condominiums, resorts, and residential associations typically have one assessment based on the value of the real estate if not the site. Even where shares of gross revenues are used, it is not clear whether, in the absence of income and sales tax forms providing the data, shopping center owners would still collect a percentage of the revenue rather than have a fixed rental for some time interval.

With each local neighborhood free to determine its own method of raising public revenues, a variety of methods could arise, but the tendency would be to avoid taxes that inhibit enterprise, residency, and investment, unlike centralized taxation where the cost of exit, leaving the country, can be rather high.

5. Austrian Economics and Cellular Democracy

The epistemics emphasized in Austrian theory are the decentralized nature of knowledge, based on particular times and places, and the uncertainty of the knowledge, especially of

the future. Decentralized governance brings decision-making to the lowest feasible and effective levels.

With the decentralization induced by cellular governance, governance would tend to be located where the knowledge is. The uncertainty leading to unintended consequences inherent in policy outcomes becomes less damaging as the scope of the policy is reduced. When government becomes decentralized, negative outcomes become localized. Learning from errors is also enhanced as the various localities attempt different policies and learn from the outcomes of others.

Decentralized policy also facilitates the expression of local and individual values. The subjective nature of values makes centralized policy an imposition on those with different peaceful values. The privatization of local communities into civic associations would further facilitate the ability of people to live in accordance with their values. Some communities, for example, could be based on a religious practice, something that would otherwise violate civil liberties if adopted on a global scale.

The Austrian concept of *Verstehen* or interpretive understanding contributes the insight that our knowledge of human behavior, unlike that of physical objects, is based on an interpretation of their purposeful action based on our own self-knowledge as well as knowledge of the culture. But people interpret phenomena in different ways, hence the understanding by individuals is based not on objective facts but on reality as perceived and filtered by knowledge and values. When private choices are made on the basis of misunderstanding or of interpretations from one particular viewpoint not shared by others, the damage or imposition is confined to oneself or one's business. But when public choices are made on that basis, the results can be far-reaching, even catastrophic. Hence, the cellular structure that limits transfer seeking has even more profound implications in limiting the scope of arbitrary and harmful public choices.

Austrian theory disaggregates phenomena, as for example when the money supply is increased, where the neoclassical approach focuses on the general price level, Austrian theory also hones in on the "Cantillon effects," i.e. of the changes in relative prices rather than just the average price level. An increase in the money supply is not evenly spread but has a particular path. Demand and therefore prices rise where money is first injected, and also, some prices are more sticky than others, and so slower to change.

Likewise, an Austrian public choice approach should regard public choice outcomes as a disaggregated process. Disaggregation enlarges the universe of policy positions. Rather than a fixed one-dimensional spectrum with a median voter whose views determines the stances of the political parties, there is a multi-dimensional universe of political spectra such as civil liberties, economic policy, and foreign policy. A voter can be median in one dimension and not in others, and the views of voters and decision makers are dynamic, evolving and changing over time. While minor political parties have an ideological focus, the major ones are a mish-mash pulled both by voter preferences and by organized special interests, often making outcomes of elections unpredictable and surprising.

Moreover, Austrian public choice theory should disaggregate the outcomes of public choices. Just as injection of money by the central bank does not just affect the general price level but also distorts relative prices, an injection of government power replacing private arrangements does not simply increase the relative size of government but also distorts

social arrangements. David Beito (2000) has described how due to political pressure and governmental substitutes, fraternal societies that provided mutual health insurance were replaced by governmental provision and corporate insurance. The impact of such programs as well as the centralization of education and programs such as social security is not just on the relative size of government versus private activity but also on the family, social relations, and savings rates. These are not just external effects of public choices but unintended consequences that are unknowable to the decision makers.

Austrian theory also disaggregates capital goods, in contrast to the homogenous treatment of K as a factor variable by neoclassical economics. It analyses goods of differing order, the higher order goods taking a longer time to fruition in profit, such as trees that take longer to mature. Likewise, Austrian public choice can analyze higher orders of investment in political capital, long-term investments by transfer seekers, in contrast to lower-order capital investments that turn over faster. Just as lower rate of interest induces more investment in roundabout higher-order capital goods, so too a more stable institutional structure, which does not “turn over” so frequently, induces a greater investment by special interests in political capital with a longer-run payoff. Frequently changing political-party controls can induce the special interests to treat both parties as one system and invest in contributions to both parties so that there are returns no matter which party is in power.

Since political capital is a capital good, the rate of interest can also affect investment in political capital, since high real interest rates induce investments in capital goods with a quicker turnover and may induce less long-term investment in political capital, those which do not have a quick payoff. The relationship between real interest rates and campaign spending on political capital may thus be a fruitful avenue for Austrian research, since political capital competes with private capital goods as investments.

The Austrian emphasis on process rather than outcomes also provides an alternative standard of optimality and efficiency. As stated by Jack Wiseman (1994:126), “the Austrian response is to change the focus of interest, from the efficient outcome of the resource-allocation process to the efficiency of the process *per se*.” Cellular democracy provides for a more market-like, more decentralized process which is thus a more efficient process with respect to what individuals desire.

A shift from mass to cellular democracy recalculates consent by changing the parameters. At the neighborhood level, the culture is more homogeneous, and the many local councils can represent a wide spectrum of policy views. Rather than a mass electorate having to make one choice at one moment in time, the dynamic and multi-faceted nature of preferences are better represented both by the geographical fragmentation of the voting cells and by the ability of representatives to be recalled at any time, thus offering dynamic flexibility in the representation of local views. Various councils can be electing representatives at different times rather than the whole population having to vote altogether at one time. Cellular democracy implements the dynamic nature of choice rather than confining voting to fixed points in time. It provides for continuous democracy rather than democracy only centrally-planned election days, with a fixed representation between elections.

The recent national political trauma of the impeachment of the president, for example, would be played out quite differently where the executive of the federal government is elected by the level- h council and may be removed at any time by the council, rather than

being elected by all the people for a fixed term of four years. The chief executive or president becomes much less of a king-like figure, and the level- h Congress need not be concerned with having to alter the “will of the people.” The calculation of consent of cellular democracy makes it easier to remove an official gone awry.

Ludwig von Mises (1981) in his critique of socialism concluded that central planning was inefficient because it lacked economic calculation, the determination of market prices that reflected scarcity and demand. Likewise, centralized democracy, with mass voting and power concentrated at the national level, lacks political calculation for what Buchanan and Tullock (1962) called the “calculus of consent.” Small-group voting is analogous to the market’s role in the private sector, providing a market for legislation based more on popular consent and less on moneyed interests.

Finally, cellular democracy provides a less costly political market for social entrepreneurs. They require a much lower investment to enter the political process, so they do not start out being beholden to special-interest investors. An activist can more easily run for and obtain membership in the level-1 council when the voting base is tiny and there is less competition for office. The political entrepreneur can promote ideas locally within his level-1 district, and the ambitious leaders can then climb up the council levels as each level elects the representatives to the next higher levels. The parameters of the cellular process give more power to the entrepreneur and less to factions and special interests than does mass democracy.

Most importantly, cellular democracy enables a civic entrepreneur to initiate innovative new communities. Tiebout (1956) competition among communities, where residents choose among communities with different rules and public goods, works at its best when new communities can be created. It is not enough that residents may choose among existing communities; if none of these are fully satisfactory, there needs to be the opportunity to innovate to create ever better communities, just as the economy advances as entrepreneurs innovate in goods and services and marketing. Buchanan and Goetz (1972) conclude that with such mobility the internalization of fiscal externalities also requires tax shares to be related to locational rent and also works with proprietary ownership arrangements.

Having small units which can dynamically change their membership and boundaries creates more of a spontaneous order in the political process than the rigid organizational order of the top-down mass-democracy model. This dynamism also alters the political time-discount rates of special interests. A rigid centralized structure makes long-term investments profitable, while a fluid, dynamic, ever-changing cellular structure requires a quicker return on political investments, resulting in less political investment by the special interests.

6. Examples of Cellular Structures

While there is no national government currently organized in cellular or other small-group structures, the concept of higher-level representatives chosen by the lower-level council rather than directly by individual voters is widespread. Many labor unions and political parties use some multi-level representation, and government councils often select representatives to regional or global organizations rather than have the electorate vote. For example, the US representative to the United Nations is not voted on by the people, but selected by

the President and Congress. City councils often select their representative to regional bodies such as transportation boards.

Clearly, it is more efficient for the UN representative to be selected by the national government than by the public, and also the UN representative will much more closely represent the interests of the national government if it is selected by it and not by the people. The president and Senate can also monitor the activity of the UN representative more closely than the people. The US Senate originally was to be elected by the State legislatures, and only later was the Constitution amended to provide for direct election.

Several cities in the United States have organized neighborhood councils. St. Paul, Minnesota, is organized into 17 neighborhood planning councils to promote citizen participation and also some neighborhood governance. For example, the Merriam Park Community Council's activities include park and street improvements, and it has committees that review city legislation that affects the neighborhood (City of St. Paul 2001). Portland, Oregon, has one of the most active systems of neighborhood councils. The city began creating neighborhood associations during the 1950s.

Most neighborhood councils are not the lowest level of government but are established to help provide a "voice" for the local community. Typically, the city provides financing for a paid staff and for some local projects. The concept is spreading; the new charter adopted by the City of Los Angeles in 1999 established such councils, along with a city Department of Neighborhood Empowerment.

Seattle has 13 district councils and a Department of Neighborhoods. The councils are made up of representatives of neighborhood organizations. They are also Neighborhood Service Centers, "little city halls" which serve as staff to the district councils and also provide services to the local residents and have magistrates that try minor offenses (City of Seattle 2001).

With respect to city governance, these councils only have an advisory function, but they do demonstrate a recognition of the value of local governance both for input into city policy and for the local provision of services. Two basic elements of cellular democracy, the local councils and the election of higher-level councils by lower-level ones, exist in practice. This provides an opportunity for civic entrepreneurs who would attempt to combine them.

7. Conclusion

The policy of decentralized governance has been analyzed by scholars of various schools and social sciences. Robert Putnam (2000:412), decrying the "empty public forums of our democracy," proposes that government be "decentralized as far as possible to bring decisions to smaller, local jurisdictions."

Gordon Tullock (1994) theorizes that many services can be devolved to the neighborhood level, which could become a predominant level of government if policy permits. He notes that small-scale government is more in accord with individual preferences. Robert Nelson (1989) suggests that a neighborhood association could have the option of selling part or all the neighborhood, retaining flexible responses to changes in the real estate market and enabling the neighborhood to profit from new development. John Dewey (1927) wrote that democracy begins in the neighborhood community, with face-to-face associations.

Decentralist ideas go far back in history to times even when government was not nearly so centralized. Thomas Jefferson (1816 [1984]) suggested that counties be divided into wards of sufficiently small size that every citizen could attend to public business and “act in person.” De Tocqueville (1981) stated that local civic activity in America was the heart of American democracy, since people more closely identified their own interest with local affairs.

However, these proposals and analysis concern only the decentralization of governmental functions without also providing the neighborhood with the political power of also electing the higher-level governance. Thus, the rent-seeking character of the public-choice process of mass-electing the municipal through national levels of government are left untouched. Cellular democracy provides a more radical change of the parameters of consent from contemporary mass democracy than the mere decentralization of administration.

First, it greatly simplifies the public’s voting choice by confining it to the candidates to the neighborhood level-1 council rather than voting for mayors, city councils, state legislatures, governors, Congress, president, and various local and state propositions. The greatly reduced cost and the personal acquaintance of the candidates reduces the incentives for voter ignorance and apathy.

Second, the rules of cellular democracy, such as council members being recallable and lower level councils able to secede from the jurisdiction of higher levels, provide incentives to decentralize governance to economically optimal levels. Third, the decentralization harnesses the localized knowledge, preferences, and entrepreneurship, and reduces the need for costly media messages. Fourth, by inducing local competition, cellular democracy provides the incentive to eliminate taxes with high excess burdens and shift public finance to user fees and site rents, similar to the financing of private communities.

The secession option, along with the small size of the councils, reduces the inefficiency of democratic governance. Collective governance has inherent inefficiencies relative to a rule by one person, but there are offsetting benefits. Democratic governance can foster community spirit, induce volunteer effort, and provide members with a voice. These benefits are more effective when the size is small. The Village of Arden, referred to above, is an example of a small community with democratic governance and much civic participation. At any rate, a cell in the structure can be a proprietary community run by a corporation, giving people a choice of living either in a democratic association or under one landlord.

The institutional concept of cellular democracy provides a basis for a comparative economic analysis of public choice in contrast to mass democracy. The knowledge and incentive aspects as well as the impact on the economy of mass democracy can thereby be better understood, Austrian theory offering additional insights due to its deeper investigation of the epistemics of rent seeking, its relationship to political capital, and disaggregated view of dynamic processes. The proposition that democracy, however flawed, has no better alternative, is insufficiently disaggregated, since democracy itself can have various structures, which impact outcomes in substantially differing ways.

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