

# **SYMPOSIUM ON HETEROGENEITY AND PUBLIC POLICY**

## **PART 1 of 2**

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### **ABSTRACT**

*It is a cliché to observe that modern democratic states are composed of citizens with diverse interests. Yet it seems fair to say that the formal study of how heterogeneity in an electorate - of incomes, preferences, political influence and in other dimensions - plays a role in shaping the policies that emerge in competitive democratic equilibria is, if not in its infancy, still far from mature. The purpose of this symposium is to call attention to the importance of explicitly addressing the role of heterogeneity in theoretical and applied research on public policy. And to contribute to this task.*

### **INTRODUCTION**

One way or another, the operation of the collective choice process in a mature democratic state leads to the balancing of opposing and heterogeneous interests. This is a messy process which those studying why governments do what they do try to simplify, for understandable reasons. It is easy to make a model of public policy complicated. It is much harder to produce an analysis of it that is relatively simple and yet still revealing.

Early formal models of public policy in democratic states, say those of 40 years ago, relied on the elegant median voter model of Duncan Black (1958). In this framework, the careful study of a single decisive voter was almost all that was needed. Understanding and empirically modeling the evolution of a particular policy required the identification of the key factors underlying the decisive voter's demands for public services, a task for which standard microeconomic theory was sufficient.

The median voter model remains a useful tool of analysis. However, it has become increasingly clear that it is desirable to consider more explicitly how diverse interests are represented in the sorts of policies that emerge in competitive political equilibria.

Almost three decades ago, Allan Meltzer and Scott Richards (1981, 1983) showed that (even) in a median voter framework, the evolution of government size depends importantly on the skewness, or third moment, of the distribution of income. As income becomes more skewed to the right, so that the median falls farther below the mean, the incentive for the decisive voter to use the public sector to effectively redistribute in his or her favor increases.

Heterogeneity of tastes for public services are also involved, as Dan Usher (1977) explained in an earlier contribution. When financed by progressive taxation, public provision of private goods may be evaluated by voters as a tradeoff between an implicit redistribution of income and the possibility of a mismatch between the amount of the good provided by the government and the amount each person would prefer the government to supply. There may or may not be a majority in favor of public provision depending on the relative strengths of these two considerations.

The seven papers in this symposium, which is divided into two parts, continue in the tradition of Usher and of Meltzer and Richards by identifying and studying particular aspects of heterogeneity in democratic societies which play key roles in determining the formation and evolution of public policies of various kinds. These papers cover a wide range of situations and types of policies, and emphasize different aspects of heterogeneity.

As a whole, the papers in this Special Issue are not intended to supply a comprehensive theory or approach to the study of heterogeneity in collective choice. Indeed, such a theory may never be possible or even desirable. The purpose of this issue is to call attention to the importance of explicitly addressing the nature and role of heterogeneity in the study of public policy, in both theoretical and applied work. And, of course, to contribute to this task.

The first two papers of Part 1 of the symposium are concerned with the impact of income inequality on public policy outcomes. In "The Distributive Implications of Indivisible goods", Dan Usher studies the interaction of income inequality and the indivisibility of goods or services. An indivisible good, such as a heart transplant, augments a person's utility when just the right amount is consumed, where more is superfluous or even harmful and less conveys no benefit at all. He derives several propositions about the relationship between the demand for such goods and the distribution of income, among them that indivisible goods are natural candidates for socialization, and that the burden of monopolization of indivisible goods can fall disproportionately upon the poor.

Philip Mohl and Oliver Pamp ("Income Inequality and Redistributive Spending: An Empirical Investigation of

Competing Theories") review the substantial body of empirical work on the relationship between inequality and redistribution, and then conduct a fresh battery of empirical tests of their own using data from OECD countries over a thirty year period.

Their key findings are that it is the inequality between the middle and top income groups that really matters for redistributive spending in these countries, and that such spending tends to be targeted at middle income groups. The latter result is reminiscent of, but different from Director's Law which holds that redistribution will occur from *both* ends to the middle.

The third of the four papers in Part 1 is "Strategic Consensus and Heterogeneous Voters When Voter Turnout is Uncertain", by Toke Aidt and Jayasri Dutta. The authors consider the conditions required for the existence of a competitive political equilibrium when the policy issue space is multi-dimensional and opposing and heterogeneous interests are ever present. They argue that a competitive political equilibrium is made more likely if the nature of voters' interests are uncertain from the perspective of politicians. Moreover, as a result of this uncertainty, politicians are forced to seek more consensus among opposing interests than they otherwise would. In effect, the uncertainty protects minorities (to some extent) from exploitation. They draw a key policy conclusion from this result, which is that election laws should not be drawn up so as to reduce uncertainty about electoral outcomes, for example by attempting to force voters to the polls.

The theoretical setup in the Aidt/Dutta paper has similarities with the setup of the probabilistic spatial voting model. (See, for example, Peter Coughlin, 1992). But it differs importantly by doing away with the requirement that

the indirect utility functions of voters in the expected vote function that parties optimize must be strictly concave. As they point out, it will be interesting to carefully reconcile their approach to the existence of a policy equilibrium with that of the probabilistic spatial voting literature.

In the last paper in Part 1, "Tax Complexity with Heterogeneous Voters", Paola Profeta and Emma Galli start right in with a probabilistic spatial voting approach to the balancing of heterogeneous interests in order to study tax complexity. Here complexity of the tax system - and it is usually very complex in reality - arises because competition forces politicians to address the varied interests of citizens in the pursuit of political power.

Profeta and Galli first formalize and then study the political costs and benefits of tax complexity in detail. They also relate their analysis to Italian experience over the last decade or so, which involves some swing of the pendulum back towards a simpler, though far from simple, taxation regime.

Part 2 of the Special Issue on *Heterogeneity in Public Policy* contains three papers, beginning with "Consumption versus Income Taxation: Three Moments in the Political Economy of Fiscal Choice", by Stanley Winer, George Warskett and Walter Hettich. This paper brings together in one model a number of aspects of heterogeneity that have been considered, usually one or at most two at a time, in various parts of the political economy literature. These are the three 'moments' in their title: the mean, variance and skewness of the distributions of skills or abilities and tastes for public goods, and the second and third moments of relative political influence. They investigate how these moments interact to influence the nature of the income-

consumption tax mix and the relative size of government in a laboratory political economy.

As in the Profeta and Galli paper in Part 1, Winer, Warskett and Hettich use a representation theorem to solve the simulation model that they explore. The theorem shows that policy outcomes in a spatial voting model may be replicated by maximization of a suitably defined political support function, which is a weighted sum of indirect voter utilities. Perhaps the most interesting results they uncover is the relationship between tax structure and heterogeneity in tastes for the public good. In particular, when income inequality is reduced and tastes for public services are on average high, consumption taxation rises relative to income taxation. The extent to which this result can be used to explain differences in reliance on consumption taxation, for example as between the U.S. (where it is relatively low) and the E.U. (with relatively high reliance on the VAT) remains to be seen.

Alexander Haupt and Silke Uebelmesser next analyze how heterogeneity in mobility and skills across the electorate affect labour market integration and education policies. In "Voting on Labour Market Integration and Education Policy When Citizens Differ in Mobility and Ability", Haupt and Uebelmesser are concerned with how these aspects of heterogeneity affect the equilibrium relationship between hard to change policies like labour market integration on the one hand, and easier to alter policies that are closely related, namely education.

The authors are thinking about situations in which (altruistic) parents of children can be expected to take a long perspective about opening borders to immigrants, because such hard to reverse policy has important implications for the future of their offspring and, in particular, for

the appropriate choice of education policy. In their model, voters (parents for example) of differing mobility and ability have differing incentives for strategic voting over the institutional or hard to change dimension of policy in order to influence the outcome of voting over education policies.

The last paper in the Special Issue, by Adam Martin and Richard Wagner, is "Heterogeneity, Voting and Public Policy". This paper explores the importance of the distinction between *organizations* and *orders* for the study of the role of heterogeneity in public policy, following Friedrich Hayek (1973). An organization – a political party for example, or even more generally a fiscal system in which voters agree on the necessity of its proper functioning – is one in which heterogeneity is only on the surface, so to speak. People disagree, but not about the overall purpose of their collective enterprise. On the other hand, they argue, in an order – a crowd of people for example where there is no apparent institutionalized coordinating mechanism – heterogeneity bites more deeply. In an order, people may disagree about basic purposes.

Martin and Wagner are attempting to provide room for what they refer to as deep level heterogeneity in the analysis of public policy – disagreements about the fundamental bases of society. In their view, public policy for an order must in large measure be constitutional in nature, for the heterogeneous interests that separate us can never be reconciled otherwise.

There is evidently a lot to digest in each of the two parts of the Special Issue on *Heterogeneity in Public Policy*. I hope that every reader will find something really interesting among the seven papers presented here.

To complete this Introduction, I would like to thank the contributors to this Special Issue as well as the anonymous referees of the papers. I would also like to thank Sophie Bernard and Peter van der Hoek for their editorial assistance.

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## **REFERENCES**

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