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Social preferences and voting on reform: An experimental study

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ABSTRACT

Debating over efficiency-enhancing but inequality-increasing reforms accounts for the routine business of democratic institutions. Fernandez and Rodrik (1991) hold that anti-reform bias can be attributed to individual-specific uncertainty regarding the distribution of gains and losses resulting from a reform. In this paper, we experimentally demonstrate that anti-reform bias arising from uncertainty is mitigated by social preferences. We show that, paradoxically, many who stand to lose from reforms vote in favor because they value efficiency, while many who will potentially gain from reforms oppose them due to inequality aversion.

1. Introduction

Efficiency-enhancing reforms[1] are often deemed difficult to implement in democratic societies, because of uncertainty regarding how the gains and losses from such reforms will be distributed among the electorate, together with the fact that those that benefit from the status quo are in a stronger political position than those who suffer (Fernandez and Rodrik, 1991; henceforth F&R). The aim of the present paper is to explore whether reforms do, nevertheless, end up being implemented because voters exhibit sociotropic preferences, that is, they do not only care for their own pocket-books but also are willing to put their own needs on hold for the well-being of society (Kinder and Kiewiet, 1981; Gomez and Wilson, 2001). In our laboratory experiment, the subjects vote on efficiency-enhancing reforms, some of which involve ex ante uncertainty over the ex post distribution of gains and losses. We show that voters pass many more reforms than predicted under the assumption of pocket-book voting (and more than what is explicable by noise), even though a majority expects to be worse-off following a reform. The presence of efficiency preferences in the subjects significantly raises the likelihood for a reform, whereas inequality aversion works in the opposite direction.

Our experiment is inspired by F&R's prominent paper in which they illustrate how individual-specific uncertainty can give rise to a bias against efficiency-enhancing reforms ("status quo bias" or "anti-reform bias"). F&R presuppose that in a democracy, reforms need support from a majority of the electorates. Under complete certainty, a reform will be accepted if

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[1] In line with the literature, we call a reform efficiency-enhancing if its monetary net benefits are positive, that is, the Kaldor–Hicks criterion is fulfilled.

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the majority gains from it, and rejected otherwise. The situation is different, however, if some voters from an ex ante perspective do not know whether they will gain or lose from a reform, but only know the probability distribution of possible outcomes. In this case, reforms that involve an expected loss to a majority may be rejected due to individual-specific uncertainty, although they would be enacted without uncertainty (Scenario *A*). Correspondingly, reforms from which a majority expects to gain may be accepted with uncertainty, although they would be rejected without uncertainty (Scenario *B*). Now, because uncertainty lifts only after the reform has been enacted (which is more likely to happen in Scenario *B*), whenever there is a "second vote or a chance to reconsider, the reform may be repealed" (F&R, p. 1149). Consequently, an important structural difference exists between these scenarios: Scenario-*A* reforms are unlikely to pass, in which case a majority would persistently fail to reap the gain from reform. Scenario-*B* reforms, in contrast, may be tried out; the majority therefore likely learns that they will in fact lose from the reforms.

F&R's ingenious analysis of political status quo bias rests upon two auxiliary assumptions: risk neutrality and pocket-book voting. In this paper, we are primarily concerned about the latter assumption, that is, we study the impact of sociotropic preferences on status quo bias.[2] Note that not all types of non-spiteful other-regarding or social preferences are sociotropic: efficiency preferences clearly are, but inequality aversion or Rawlsian maximin preferences can lead voters to vote against reforms that are to their own material advantage. It follows that, if the classes of reform gainers and losers are maintained at a constant size, the effect of social preferences on voting for a reform depends on the relative frequencies of different deviations from pocket-book voting in each class. This is a fundamentally empirical issue that lends itself to experimental testing.

Models and experimental tests of inequality aversion were put forward by Fehr and Schmidt (1999), Bolton and Ockenfels (2000), and others. The model by Charness and Rabin (2002) can also account for Rawlsian maximin preferences.[3] The literature on social preferences suggests that a significant number of people are potentially willing to sacrifice parts of their own income to help others even if their choices increase inequality, for instance, because they value efficiency or are altruistic (e.g., Charness and Rabin, 2002; Engelmann and Strobel, 2004; Fisman et al., 2007; Kerschbamer, 2013).[4]

While many contributions have studied social preferences in the context of markets and games (for surveys, see Camerer, 2003; Fehr and Schmidt, 2003; Sobel, 2005; Schmidt, 2011; Charness and Kuhn, 2011; Cooper and Kagel, 2013), few have dealt with their impact on the sphere of political decision-making. To our knowledge, Cason and Mui (2003, 2005) are the only ones who have experimentally examined the dynamics involved with voting on a reform. These authors extended F&R's model by allowing for costly voter participation, and found that uncertainty reduces the incidence of a reform even with costly political participation. In contrast, we conduct an experiment to explore the role of social preferences for voting on a reform and control for risk preferences.

While we are not aware of any study that accounts for the impact of social preferences in voting upon an efficiency-enhancing but inequality-increasing reform, the case can be thought of as the reverse of voting on efficiency-reducing but inequality-decreasing redistribution. From this viewpoint, we contribute a new perspective to a recent wave of research exploring voting on redistribution, including Beckman et al. (2002), Ackert et al. (2004), Tyran and Sausgruber (2006), Durante and Putterman (2009), Sauermann and Kaiser (2010), and Balafoutas et al. (2012). As their main result, these studies generally emphasize that voters are willing to sacrifice their own income to achieve a *more equal* distribution. In contrast, we investigate if voters are also willing to sacrifice their own income to implement an efficiency-increasing but *inequality-increasing* reform. So far, the literature provides an inconclusive picture of whether one motive outweighs the other. Höchtl et al. (2012) observed no evidence for voters to be efficiency-loving and showed that inequality averse voters may not matter for redistribution outcomes for empirically plausible cases. Bolton and Ockenfels (2006) investigated the tradeoff between equity and efficiency motives in a voting game with three voters. They found that twice as many voters were willing to give up their own income in favor of an equal distribution compared to a more efficient but unequal distribution. This observation suggests that social preferences hinder the enactment of efficient reforms. Messer et al. (2010) studied the impact of majority voting on the provision of a public good. They detected substantial concerns for efficiency in the subjects' behavior, but found little support for inequality aversion and maximin preferences.

In our experiment, we elicit the subjects' social preferences using the double price-list technique developed by Kerschbamer (2013) and applied, for example, in Balafoutas et al. (2012). We let the subjects vote on the four types of reforms discussed by F&R (majority better-off/worse-off vs. certainty/uncertainty about distribution of gains and losses). In addition, we elicit the subjects' risk attitudes using a standardized lottery-selection design (see Holt and Laury, 2002, 2005). The following were observed in the study's subjects: (i) efficiency preferences lead the subjects to support reforms that are to their own disadvantage; (ii) inequality aversion leads them to decline reforms that are at their own advantage;

[2] We do not challenge the risk-neutrality assumption; its violation would have a remote impact in any case. Risk-aversion would decrease the likelihood of reforms involving an expected gain of being enacted and thus reduce the asymmetry between the scenarios; risk-loving would symmetrically increase the likelihood of all reforms involving uncertainty to be enacted. For further discussion and examples of the role of uncertainty in the political economy of a reform, see Rodrik (1996) and Tommasi and Velasco (1996). A formal model of uncertainty and the adoption of economic reform was developed by Jain and Mukand (2003). Related time inconsistency problems were discussed by Dixit and Londregan (1995).

[3] Such motives seem to resemble observations from the political economy of reform literature, where it frequently appears unfair to consumers to make producers worse off in relation to the status quo (e.g., Summers, 1994).

[4] The fact that people value efficiency is also reported by a related strand of literature exploring preferences for principles of distributive justice (see Tausch et al., 2010, for a survey.)